Metro Manila Office Market Update

Changing Tides
The shift towards new trends

Q1 2022

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General Overview

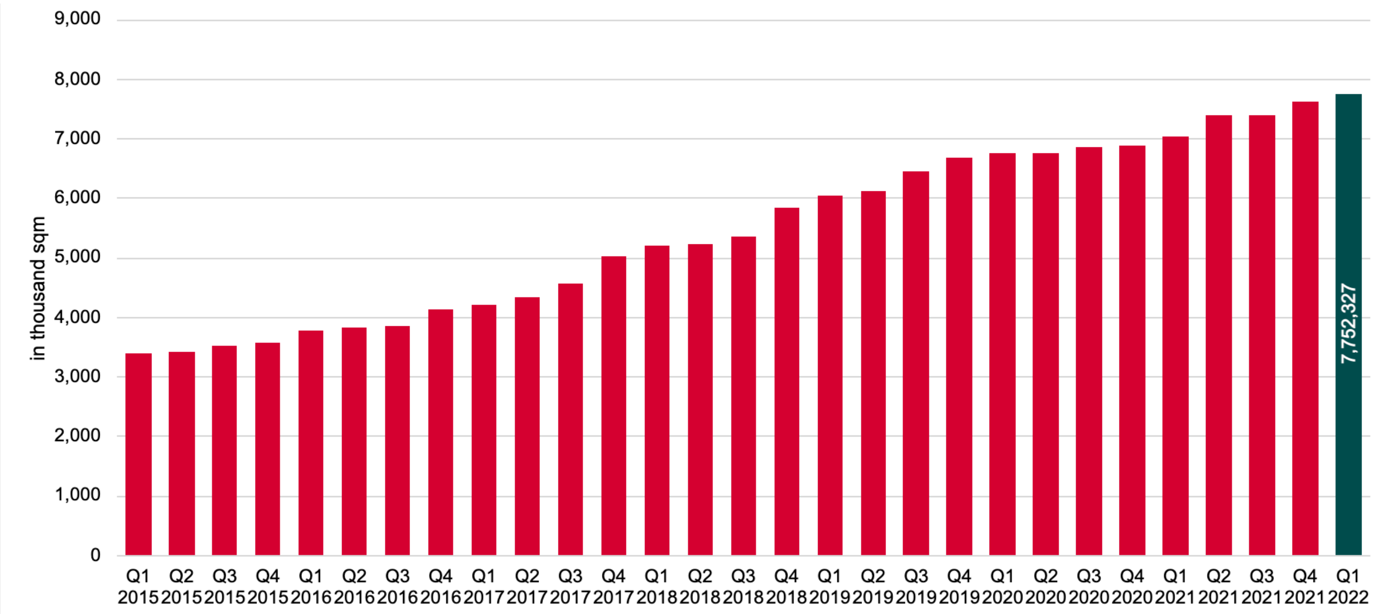
One thing remains certain, the effects of the pandemic endure. The Metro Manila office market for the first quarter of 2022 continues to reflect the realities of the enduring pandemic and the shifting mindset of employees and employers. Although quarantine measures throughout the metropolis have been alleviated and downgraded to COVID Alert Level 1, the office market remained on its downward trajectory.

Despite the trajectory of the market, new office buildings were completed this quarter. The office supply grew by 127,374 sqm coming from the different business districts across Metro Manila with the biggest additions coming from the Bay Area. With this, the overall office supply in Metro Manila increased to a total of 7,752,326 sqm.

With supply growing in the market, overall vacancy rating rose with it. As of Q1 2022, the office vacancy rating pushed, yet another record, upward to 21.21%. The factors that contributed to this uptick of vacancy remains the same as previous quarters. Offshore gaming operators underwent a massive exodus and Philippine Offshore Gaming Operator (POGO) licenses were revoked due to the pandemic. As PAGCOR reports, revenue from POGO licenses fell from PhP5.28billion in 2020 to Php3.47 billion in 2021. PAGCOR further estimated a decline to PhP1.67 billion for 2022. Work-from-home or hybrid working arrangements are also a primary factor for the increase in vacancy. Even with the recent 70%-30% ruling by PEZA which went to effect during the latter part of the year, IT-BPO operators have chosen to forgo their incentives and continue their work-from-home arrangements to meet employee demands and cut overall operational costs. Close to 100,000 sqm of office space were freed up during the quarter, thrusting the total available space to 1.64 million sqm.

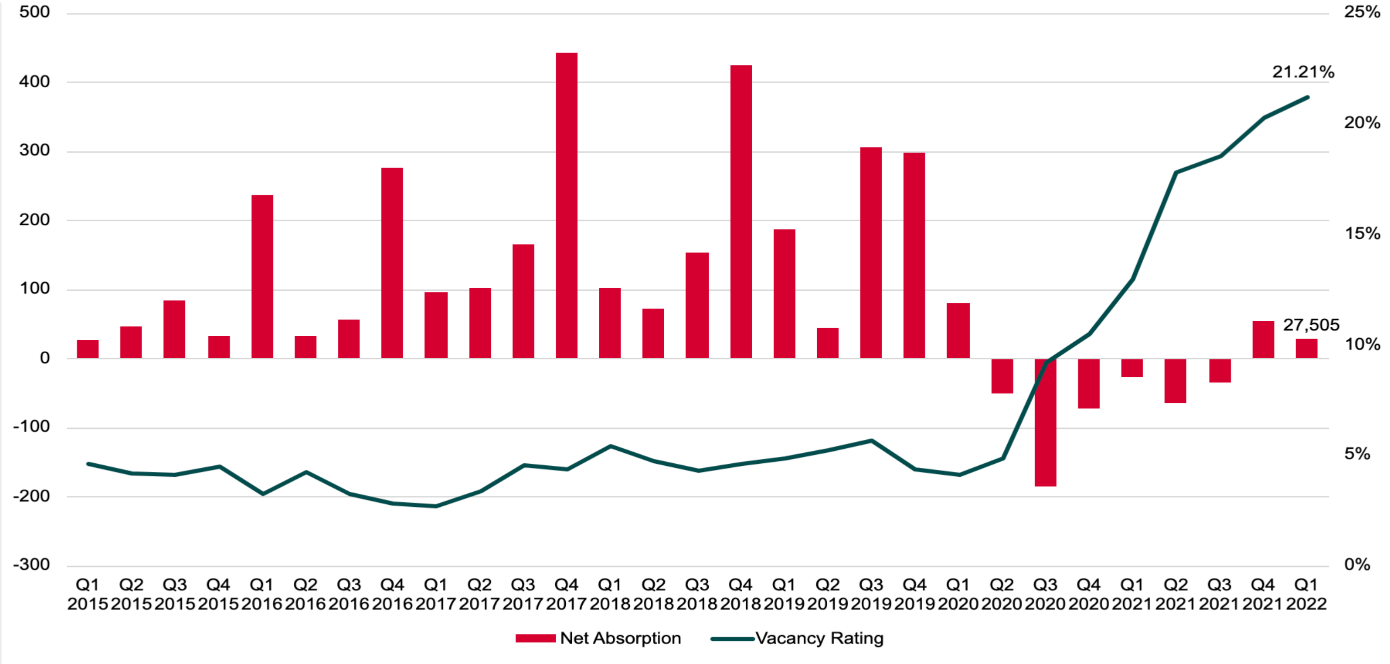
Lease rates in Metro Manila further dipped this quarter with the average asking lease rates standing at PhP1,081.85 per sqm per month. Lease rates contracted by 1.81% year-on-year (y-o-y). With prices decreasing, this further shows that the market is tenant-driven, with landlords taking into account the needs of potential locators to be flexible as well as stiff competition in the market.

Figure 1. Metro Manila Historical Office Supply



Source: Santos Knight Frank Research

Figure 2.Metro Manila Historical Net Absorption and Vacancy Rating



Source: Santos Knight Frank Research

Makati

Makati still bears the brunt of the effects of the pandemic with vacancy rates rising to a record high of 22.84%. New supply of about 42,500 sqm as well as tenants still assessing whether there is a need for office spaces have contributed to this growth. There are signs that tenants are slowly making their comeback as net absorption for the quarter grew by 6,459 sqm.

Despite the current environment, Makati remains the highest in terms of lease rates in Metro Manila. The average asking rental rates in the district stood at PhP1,350.14 per sqm per month. Rental rates have increased slightly by 0.14% y-o-y with prices remaining competitive to attract potential tenants and occupy vacant spaces.

Today, Makati holds about 1.3 million sqm of working space. The current environment has not stopped developers from pushing through with their projects with a whopping 323,618 sqm being added within the next three years. In 2022 alone, the district is expected to have an additional 250,000 sqm of Grade A and Prime office space reflecting the positive outlook of developers and the embracing of the “new normal.”

Taguig

Fort Bonifacio in Taguig remains the largest in Metro Manila in terms of office supply. It comprises close to 30% of total supply in the metropolis or around 2,134,505 sqm of Prime and Grade A offices. With the addition of about 24,595 sqm of office space, the vacancy rates in Fort Bonifacio grew to 15.45%. With more supply being introduced in the metropolis, landlords seek to remain competitive. Average asking rents in the area fell to PhP1,263.99 sqm per month, decreasing by 1.49% y-o-y.

The district remains an attractive area to both international and domestic corporations with its open spaces, technologically advanced and green buildings, city layout, and competitive prices. The expected new supply reflects this argument as a total of 852,070 sqm of Prime and Grade A of office space will be added in the next three years. Furthermore, approximately 344,000 sqm of the new supply will be coming from the neighboring Arca South, a 74-hectare lifestyle and business district currently being developed.

Bay Area

It cannot be denied that the Bay Area had been hard hit by the pandemic. Prior to the lockdowns it was the main district that hosted the POGO industry. With tightened regulations, income tax being imposed on the industry, as well as the Chinese nationals fearing equal local health treatments, offshore gaming operators started ceasing operations. This massive exodus led to office landlords finding ways to fill up empty spaces while remaining competitive.

However, the Bay Area is showing evident signs of recovery. Vacancy ratings have decreased by 0.95 to 25.09% from the preceding quarter. Net Absorption for the quarter grew by a massive 55,704 sqm. Rental rates have also improved with average prices this quarter standing at PhP1,098.46 per sqm per month, increasing by 1.50% y-o-y. Additionally, with access to both current and future available and developable land, developers are still interested in investing in the district. Around 534,947 sqm of spaces are expected to be introduced to the market within the next three years. This further shows not only the recovery, but the resilience of the demand and outlook for office spaces in the Bay Area.

Ortigas Center

Ortigas continues to have the highest office vacancy rate in Metro Manila this quarter. Vacancy rates, however, have improved with a recorded 24.91%, down 1.42% from the previous quarter. Additionally, net absorption for the district stood at 20,338 sqm this quarter. This shows that despite the vacancy rating, things are starting to look brighter for the district.

Competition remains intense amidst the high-quality offices in the area with lease rates averaging PhP 809.41 per sqm per month, down by another 0.29% y-o-y. Lease rates in Ortigas remain the lowest among the various districts in Metro Manila. This further reflects the tenant driven nature of the district. Developers are still expecting their projects to push forward to boost supply in Ortigas. The district is expecting approximately 480,636 sqm of new Grade A and Prime office spaces in the next three years. This massive supply is the result of delays caused by the lockdowns and cut in demand from the pandemic. Furthermore, the foreseen increase in supply combined with the enduring effects of the pandemic, may cause vacancy levels to increase, which in turn create downward pressure on office rents.

Quezon City

Signs of recovery are also being felt in Quezon City with vacancy ratings decreasing to 20.89% from 21.49% of the preceding quarter. The positive net absorption of 7,321 sqm reflects the recovery and improvement of the office market in the district. Similar to other districts, lease rates continue to go down. The average lease rate for this quarter stood at PhP876.33, decreasing by 5.19% y-o-y.

At 1,202,436 sqm, Quezon City makes up for approximately 15% of total office space in Metro Manila. This will further be added upon as 521,277 sqm of Prime and Grade A office space will be added in the next three years. Although the market seems to be recovering, it may be short-lived as historically the district has never gone below 6.5% since Q2 of 2014. With the additional supply coming in, expected lower net absorption, and the enduring effects of the pandemic, prices will remain on a downward trend.

Alabang

The quarter saw vacancy ratings in Alabang expanding to 22.59% from 21.90% of the preceding quarter. Additionally, net absorption saw a negative trend this quarter freeing up 3,320 sqm of office space. It is also important to note that Alabang is a major host for the IT-BPO and POGO. Adding on to the exodus of offshore gaming operators, these negative downtrends can be attributed to yet again the pandemic as industries, like the IT-BPO sector, remain in a work-from-home or hybrid set-up.

Average asking rates continue to decrease with landlords trying to attract prospective locators. Average lease rates hit PhP827.52 per sqm per month this quarter, contracting by about 2.27% y-o-y. However, with about 228,835 sqm of Prime and Grade A office space being added in the next two years and the country opening up economically to domestic and international players, Alabang still remains to be a potential investment hub.

Figure 3. Metro Manila Lease and Vacancy Rates per CBD

Source: Santos Knight Frank Research

Office Outlook

The lightening of restrictions and lockdowns during the first quarter of 2022 have seen a slight improvement in several districts in terms of vacancy ratings and net absorption. However, when looking at the office market performance as a whole, it still remains on a down trend. Vacancy ratings remain high with a record 21.21% with current surplus in supply pushing it further upwards. While lease rates are also decreasing to a weighted average of PhP1,081.85, decreasing by 1.83% y-o-y.

Real Estate Investment Trusts (REITS) have also gained popularity over the pandemic as it not only augments developer's working capital, but provide investors with an alternative investment option. This is further evident as 5 REITS have been introduced to the market over the course of the pandemic with an additional REIT from Vista Land expected to join this year.

Office demand continues to have room for improvement even as 70%-30% PEZA ruling orders the BPO sector to return to work. Some BPOs, like Concentrix, even choose to forego their incentives so that their employees can remain at home. Companies are reassessing the need to pay rent and the need to lower operational costs. Employees themselves are influencing corporate thinking as demand for a work from home or hybrid setup gains ground as fuel costs increase, inflation rises, and public transportation remain disorganized.

Given this trend however, demand for office buildings, specifically green buildings, remain as more BPOs, data centers, and foreign investors come in. The trend towards a preference to green buildings is one of the byproducts of the pandemic as locators are inclined to take up spaces that have features that benefit and protect the physical and mental health of employees as well as lower overall operational costs. Developers and landlords must also reassess the way offices are built and designed to accommodate the need for less space and the adoption of a permanent hybrid set-up.

Additionally, with the recent economic liberalization laws passed by Congress, foreign investors are expected to pour in. Given our low labor costs, the Philippines remains an attractive market for international corporations. The recovery of the office market will be driven by these new trends as the market continues to recover and with businesses returning to the office workplace.

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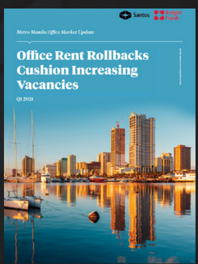

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