*Metro Manila Retail Market Update*

# Beyond the Pandemic: The Integration of Digital and Traditional Retail

**Q2 2022**

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# General Overview

Metro Manila's vibrant retail sector was negatively impacted during the peak of the COVID-19 pandemic. Despite the Omicron Variant outbreak and heightened alert levels at the start of the year, the retail sector saw a resurgence in the first half of 2022. The eventual lowering of alert levels has caused a revitalization in the retail market, feeding primarily off families, with children in tow, visiting malls and other retail facilities. Furthermore, this resurgence can also be attributed to the rise in vaccination rates, increased consumer spending, and improved mobility. With Metro Manila in Alert Level 1, all businesses and establishments are allowed to operate with minimal restrictions.

The increase in vaccination rates spurred consumer spending and confidence significantly. Based on the latest government data, around 70.8 million people are fully vaccinated and 15.1 million individuals have received their first booster. Given this, people are now more confident in leaving their homes, visiting major shopping malls, and eating in restaurants.

Overall domestic consumption similarly persisted during the first quarter of the year. Household Final Consumption Expenditure (HFCE) expanded by 10.1% from a decline of 4.8% in the same period of the previous year. Consumption of food and non-alcoholic beverages grew by 9.9% and covers a total of 36.2% of household spending. Further reflecting the resurgence, restaurants and hotels as well as miscellaneous goods and services make up close to 28.8% of household consumption. However, with unemployment rates and commodity prices rising, including fuel and transportation, consumers may shift priorities when it comes to their spending. It is important to note that transport, utilities, and fuel already makes up 22.6% of household consumption.

Mobility has also slightly improved in the first half of the year, but faced many challenges. As lockdowns eased people were free to travel with minimal restrictions. However, just as the country emerged from the Omicron variant surge, the conflict in Ukraine arose. As a result, fuel prices sharply rose. This was further exacerbated by sanctions against Russia, a major supplier of oil and gas. To combat rising fuel costs, the government introduced the "Libreng Sakay" transport program which offers free public transportation rides. This not only helped commuters going to work, but also allowed individuals and families to go to their destinations, including retail establishments, with minimal cost.

Since the alert level in Manila allowed for a relatively relaxed quarantine, commerce flourished and prompted a significant increase in consumer spending, paving the way for businesses to thrive. Retail establishments were allowed to operate with fewer restrictions, presenting the consumer with a wide array of options to spend their money saved. Foot traffic continues to improve as Alert Level 1 continues to be in effect and companies steadily transitioning back to office working. Though some companies have adopted a hybrid working set-up, the few days when the workers are back in the office, in a way contribute to improving foot traffic to the malls and other retail facilities. The lingering fear in going out of their homes by the general public is slowly fading, and a proliferation in the retail environment of the metropolis is now being observed.

# Upcoming, New Launches, and Expansions

As of the second quarter of 2022, there were at least 165 upcoming stores in the Metro Manila retail sector. Food & Beverages and Clothing & Apparel closely match in terms of their share of upcoming stores. There will be 54 upcoming Food & Beverage stores amounting to 32.73% of the total, while 53 Clothing & Apparel stores are expected to be introduced into market this year amounting to 32.12% of the total.

Among the upcoming brands, is the American based Olive Garden which will be brought in by the Bistro Group. The group plans to establish their first two branches in SM Mall of Asia in Pasay, and in Glorietta 3 in Makati. Furthermore, the Bistro Group will also be bringing in Fogo de Chao, an American based Brazilian steakhouse. Haidilao International Holdings Ltd, China's largest hot pot restaurant chain, is set to open its first branch in the coming year. With over 1,000 stores worldwide, it will not only offer their famous Sichuan-inspired spicy soups, but they also plan to incorporate Filipino tastes into their menu.

For Clothing & Apparel brands, Chinese fast fashion brand Urban Revivo is set to open their flagship store in SM Mall of Asia in July; with further stores opening in Glorietta and Rockwell in Makati, SM Megamall in Ortigas, and Trinoma and SM North EDSA in Quezon City. With over 360 stores globally, Urban Revivo, in partnership with Suyen Corporation, is set to showcase its runway-inspired, ready-to-wear designer and high street fashion looks to the Philippine market. Aside from clothing & apparel, American retailer Bath & Body Works is set to open in SM Megamall in Ortigas. They aim to offer their world-renowned selection of lotions, candles, body sprays, and ahnd sanitizers to Filipino consumers.

In partnership with the Bistro Group who also brought in Denny's and Hard Rock Café, Los Angeles' based Randy's Donuts opened its first branch last April at Uptown Parade in Bonifacio Global City; with plans to open 2 more branches in Mall of Asia in Pasay and Robinsons Magnolia in Quezon City. Additionally, Japanese company MUJI opened its first MUJI Coffee in their newly re-opened MUJI store in Bonifacio Global City, their second-largest store in the country. It is intended to be a small space where shoppers can enjoy and experience Japanese-inspired snacks and a cup of freshly-brewed coffee.

Reflecting the positive outlook that retailers and business owners have on the retail market, expansion plans are moving full steam ahead. Just in this quarter Skechers and Under Armour opened their biggest stores in the Philippines in SM Mall of Asia and Power Plant Mall respectively. Additionally, Nike opened the biggest Nike concept store in Southeast Asia in Bonifacio Global City. The store boasts a whopping 14,000 sq. ft in space and offers a range of Nike sports and lifestyle products. This is on top of the launch of IKEA's biggest store globally in Pasay which opened in the last quarter of 2021 and Uniqlo's biggest store in Southeast Asia in Makati which opened in the last quarter of 2018.

In terms of shopping malls, the Araneta Group's Gateway Mall 2 in Quezon City is set for a soft launch by the last quarter of 2022. It will add 190,000 square meters of floor space to the city's retail market and will offer eleven floors worth of retail and dining stores. Similarly, Ortigas Malls recently announced the groundbreaking of the Greenhills Mall annex which is also set to open in the last quarter of 2022. The annex building will be three storeys tall and will house over 120 retail and dining options. SM Mall of Asia is also undergoing expansion.

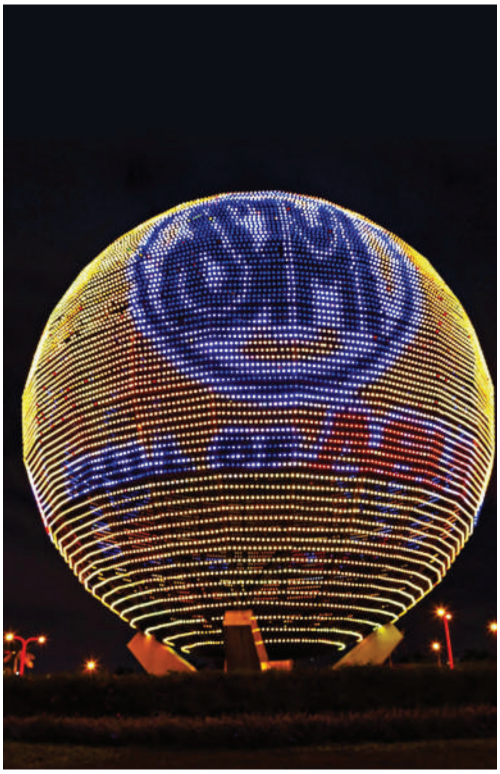
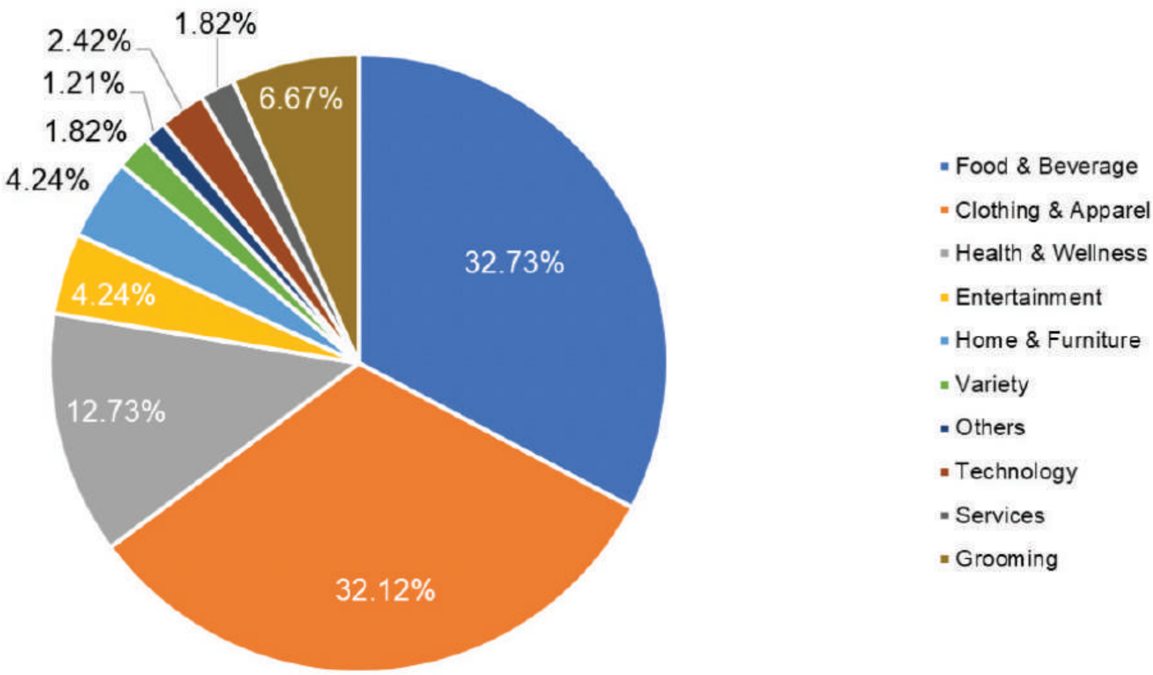


Figure 1. Upcoming Retail Stores in Metro Manila




Source: Santos Knight Frank Research

# Trends in the Retail Sector

Metro Manila consumers are not only returning to malls, but are doing so with a vengeance. Having continuously maintained Alert Level 1 status, more Filipinos are returning back in droves to physical shopping. Given the lack of outdoor nature parks and the relatively humid and hot temperatures, shopping malls still remain as the predominant destination for social gatherings. Unlike during the height of the pandemic, more Filipinos now have a stable income to draw from as more get back to work and to the office.

This has been reflected by the retail sales in the food and beverage sector. According to Euromonitor International, in 2021 Philippine F&B sales expanded to $24.36 billion from the $23.75 billion registered in 2020. Latest data from the Philippine Statistics Authority (PSA) shows the gross value added in retail trade grew by 8% or around PhP 605 billion in the first quarter of 2022 compared to PhP 559 billion in the first quarter of the previous year. The PSA further reported a 10% increase in household final consumption expenditure in the first quarter of 2022 compared to the previous year. April also saw the jobless rate hitting its lowest level since the pandemic at 5.7%.

It is a well-known fact that the Philippines is ranked as one of the most active internet users in the world. With a population of over 111 million people, the Philippines has over 92.05 million social media users who spend an average of 10 hours and 27 minutes on the internet. A study by Google, Temasek, and Bain & Company reports that the Philippines' internet economy in 2021 was worth $17 billion. According to the government this makes up 5.8% of the country's GDP. Additionally, the government recorded a total of 2 million new e-commerce enterprises. This was mostly driven by the mass digital adoption of the population as a result of the pandemic.

Online shopping has become even more prevalent as more Filipinos have access to the internet. Websites such as Shopee, Lazada, and Zalora continue to dominate the internet retail space. According to a report by the government, with data gathered from Statista, Shopee had 76.86 million site visits in the first quarter of 2021 alone, while Lazada garnered a total of 39.02 million site visits. Additionally, the Statista report on weekly online shopping activities of internet users in the Philippines as of the third quarter of 2021 show that 62.5% of Filipino internet users purchased a product or service online, while 24.6% said they had ordered groceries via online stores. With the growing popularity of e-Commerce, retailers are reaching people in their homes through large investments in digital marketing and outreach. This shows that Filipino consumers and retailers are both shifting and adding on to traditional retail methods with modern ones that offer more convenience and diverse supply through e-commerce.

Adding on to this, retailers continue to adopt methods that were spurred by the pandemic. These include cashless payment or transactions through the use of online money transfer applications and online banking such as GCash or PayMaya, as a mode of payment. Retailers also continue to adopt not just online purchases, but also online order and store pick-up. These methods continue to be sustainable as they are both safe and convenient in a still health-cautious market.

As a consequence of the pandemic, more clothing & apparel stores have been shifting to online transactions and customer interactions. With this transition, some of the freed up mall spaces are being occupied by new restaurants and other F&B establishments. This is evident in some malls like Shangri-la, Podium, and Uptown Mall as the space occupied by F&B establishments close to the space being occupied by non-F&B stores. It is also noted that establishments catered to children like play areas and child-centered barber shops are opening as more families become comfortable going to the malls with their children.

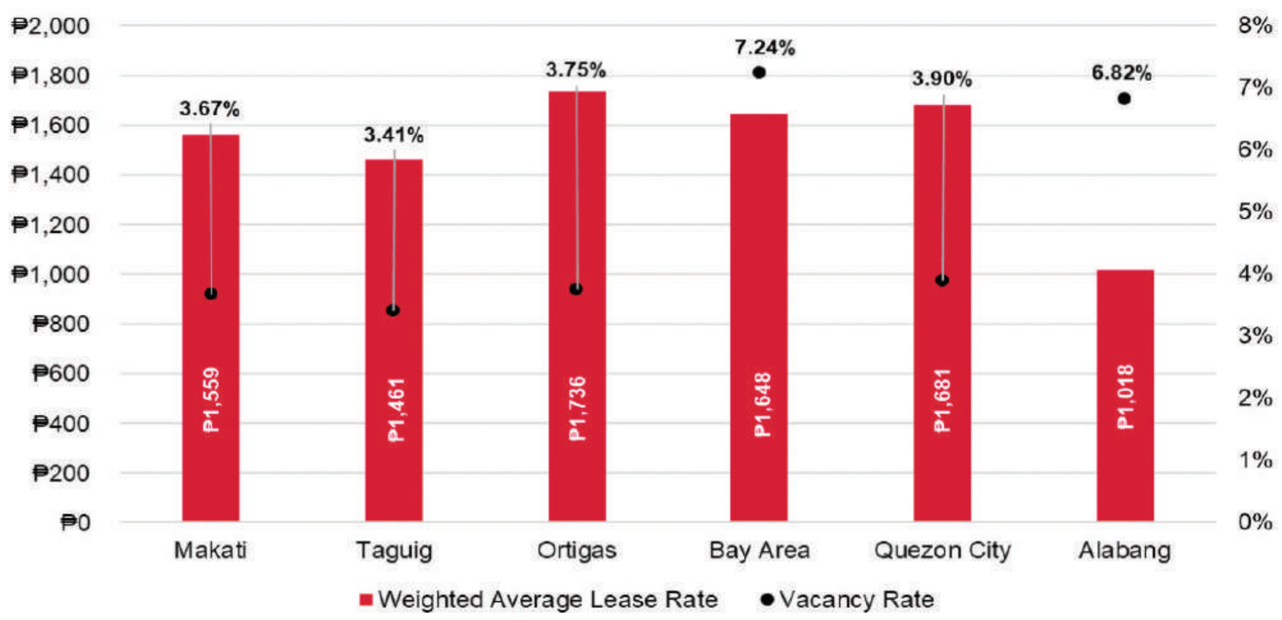
## Vacancy and Lease Rates

Mall vacancies levels have not only improved since the pandemic, but continue to reflect the positive direction of the retail environment. With vacancy levels at 4.62%, demand for retail space, especially in Malls located in strategic areas, remain high. Taguig City posted the lowest vacancy rate among all business districts at 3.41% with Makati following close by at 3.67%. This can be attributed to Alert Level 1 being maintained and workers slowly returning to the office. Schools are expected to resume classes on campus in the coming school year, and this is expected to generate more foot traffic in malls and other retail facilities. Likewise, the Bay Area posted the largest vacancy rating at 7.24% as the stores scheduled to open in some of the malls that became operational just before the pandemic did not push through.

Despite the positive direction of the retail sector, foot traffic remains low in shopping malls located in the fringes. Malls in Ortigas is one such example. Although Ortigas houses multiple commercial business districts and residential developments, malls like Tiendesitas, Estancia, and Ayala 30th are still experiencing low foot traffic. Given the lack of access to convenient transportation and the oversaturated nature of shopping malls within the area, consumers may bypass these malls for bigger and newer shopping establishments. Malls, like SM Megamall, Trinoma, SM North EDSA, and SM MOA, that are centered around transportation hubs and are easily accessible are the ones that have the highest foot traffic. Instead of just attracting consumers from the neighboring areas, these malls are visited by consumers from all around Metro Manila.

The monthly average lease rate for retail space this quarter stands at PhP 1,567.32 per sqm, a figure similar to that of pre-pandemic lease rates. Lease rates generally have an escalation rate of an industry standard of 10% and utilities are generally excluded from the price. Additionally, some malls may ask for an average 3% commission on sales on top of the lease rates. This may mean that mall operators are seeing stronger demand and a positive outlook for the retail sector. Additionally, inflation and the rise of commodity prices may have pushed lease rates up as malls become more expensive to maintain. It should be noted that in major shopping malls, a typical 5-10% discount rate can be negotiated. If demand is high, these malls tend to lower their discount rates to 5% or less. However, in a mall with lots of vacant spaces, a tenant, through negotiations, can have a discount rate of 20-25%.

Figure 2.Metro Manila Retail Average Lease and Vacancy Rating Per CBD




Source: Santos Knight Frank Research

# Retail Sector Outlook

Foot traffic is only expected to increase in the coming months as more people get vaccinated and boostered and as restrictions further ease. Mall operators are seeing not only a resurgence, but a potential for further growth in the retail sector as seen through the lease rates and occupancy levels. Although the pandemic has pushed retailers online, the physical shopping experience will always remain popular to the Filipino consumers and families. Recent and future launches show that Food & Beverage and Clothing & Apparel stores are almost neck and neck. Although some malls are converting their shopping sections into food hubs, it can be said that traditional retail is not going anywhere and that retailers are now focusing on harmonizing, integrating, and complimenting both their online and onsite stores. This can possibly create a new system or structure for future retail developments.

This positive outlook however, will not be easy to achieve. The sector faces headwinds with rising fuel prices, construction costs, and the further depreciation of the peso. As the peso continues to depreciate imported construction materials become more expensive. According to the PSA, the NCR's construction materials retail price index (CMRPI) rose by 6.1% in April year-on-year, compared to a 1.3% increase in April 2021. Retail prices of construction materials are anticipated to rise further in the coming months as the external challenges persist. This may force retailers to pause or delay their expansion plans.

As e-Commerce continues to expand its reach, mall operators must continually seek to update and modernize to remain significant. Developers should also be strategic when it comes to repurposing viable space to minimize the interim losses and for recovery in the long term. As previously mentioned, e-commerce has changed the way Filipino consumers shop and it will most definitely change the way the retail sector operates. This will hopefully spur innovative designs and configurations to better complement and integrate the online with the onsite. It is up to developers to find new and innovative ways to meet the everchanging challenges and demands of the market. The growth and resiliency of the retail market remains bright and will continue to be driven by both online and onsite shopping experiences.

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