Metro Manila Office Market Update

The Last Battle of the Pandemic

1H 2023

The last battle against the pandemic

The COVID-19 pandemic exerted a profound influence on global economies, instigating widespread disruptions and engendering heightened levels of economic uncertainty. Governments worldwide responded by implementing health measures aimed at curbing the virus's spread, subsequently resulting in restrictions on human mobility and substantial limitations on business operations.

In the Philippines, stringent measures were enforced, permitting only essential services to sustain their operations. Industries catering to these essential services constituted the sole entities allowed to operate, leading to a significant contraction in the overall economy and contributing to a period of stagnation.

The commercial real estate sector bore substantial repercussions as a consequence of the economic uncertainties stemming from the pandemic. The disease's spread prompted businesses to defer or cancel plans for office expansions, lease renewals, and other commercial real estate transactions, precipitating a decline in lease transactions within the market.

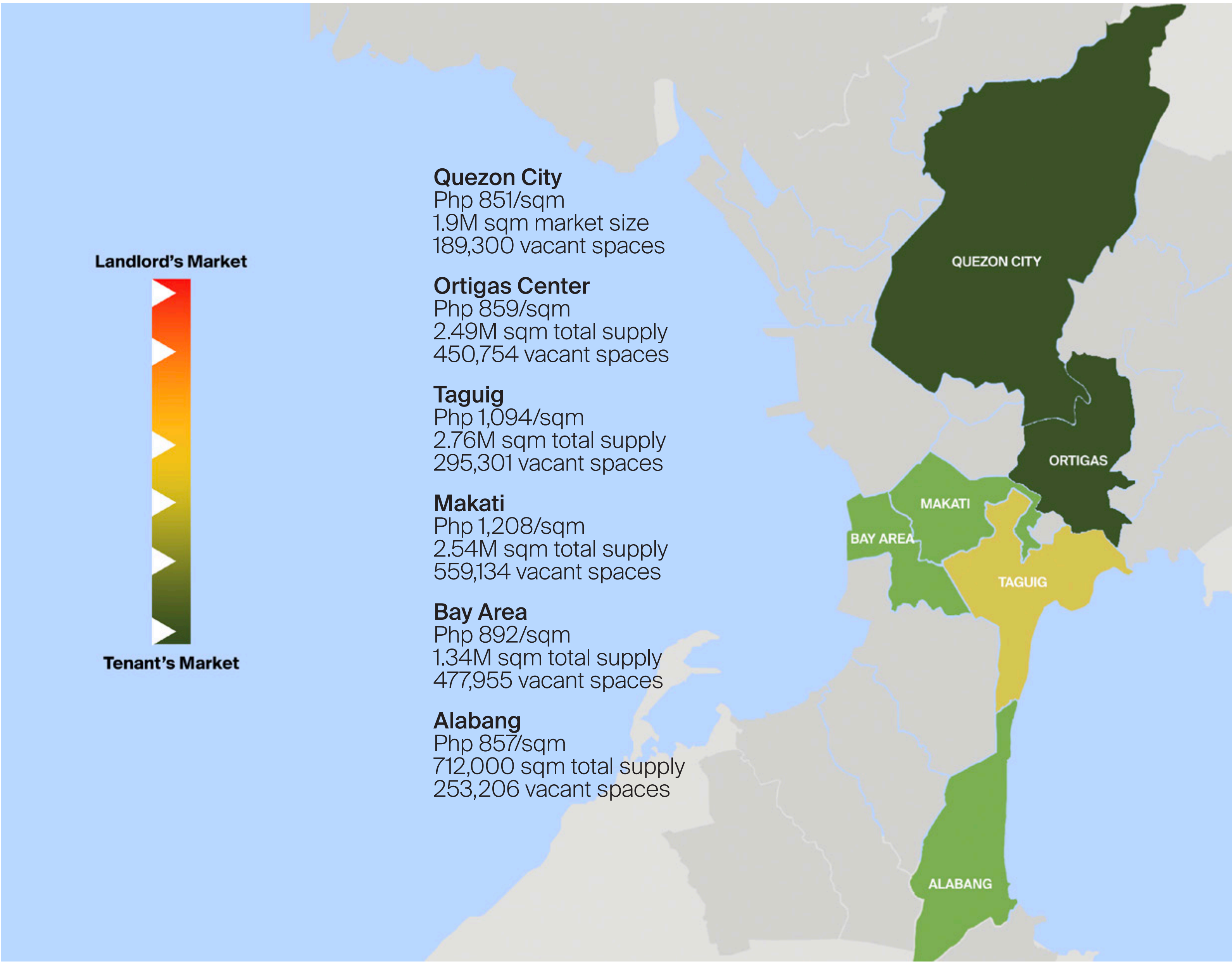
To navigate the challenges posed by the pandemic, global occupiers have implemented strategies to manage their variable expenses and maintain financial stability. This has involved a reassessment and review of office space requirements, with a strong emphasis on optimizing rental costs, and workplace mobility.

Occupiers explored ways to enhance mobility within their workforce, enabling remote work options and implementing agile working arrangements. This approach not only promoted employee safety and well-being but also contributed to cost savings by reducing reliance on traditional office spaces.

The advent of the pandemic instigated a substantial shift in work dynamics, particularly with the sudden adoption of remote work, a concept previously deemed unfamiliar and met with resistance. However, as the pandemic's impact unfolded, organizations and individuals were compelled to embrace remote work as an imperative response to the crisis.

Even subsequent to the World Health Organization's declaration that the COVID-19 pandemic has concluded, the remaining significant challenge does not center around masks, vaccines, or government policies. Instead, it revolves around reintegrating individuals into office spaces.

Metro Manila office market maintains tenant favorable conditions



The Metro Manila Office Sector faced challenges in maintaining its vibrancy even as the COVID-19 pandemic concluded. The adoption of hybrid modality led to a sluggish uptake of office spaces. According to Santos KnightFrank's data, the office sector in Metro Manila experienced a slow-down in office transactions, with nearly 7.793 million square meters of transacted space in the first half of 2023, compared to 7.686 million square meters in the last half of 2022.

The weighted average lease rates in Metro Manila witnessed a bi-annual decline of 10%, dropping from Php 1,000 per square meter in the last half of 2022 to Php 900 in the first half of 2023. This downward trend in lease rates can be attributed to landlords offering competitive packages to attract occupiers, creating a favorable leasing environment.

Makati City, the country's first established business district, maintains its position with the highest rental rates in Metro Manila. The strength of Makati's status is evident in its improved vacant spaces, decreasing from 567,831 square meters in the last half of 2022 to 559,134 square meters in the first half of 2022.

Despite this improvement, rental rates in Makati remained unchanged at Php 1,208 per square meter per month, solidifying its position with the highest rates among all business districts in Manila.

On the other hand, Taguig experienced a market deceleration with an increase in vacant spaces from 280,000 square meters in the last half of 2022 to 295,301 square meters in the first half of 2023.

Despite having the largest supply share in the Metro Manila office market, approximately close to 3 million square meters, downsizing activities and the ongoing adoption of hybrid work arrangements by tenants in Taguig contributed to the slight increase in vacancy rates. Lease deceleration was observed in Taguig as a result of these factors.

The available office spaces in Ortigas Center gradually decreased from 490,783 square meters of vacant spaces to 450,574 square meters of vacant spaces.

This notable movement in the Ortigas Center office market can be attributed to favorable leasing activities by virtual office service providers, supporting the ongoing occupancy momentum in the area. The affordability of rental rates in Ortigas, averaging at Php 859 per square meter per month, makes it an attractive option for office expansion, providing a viable alternative market.

Not far from Ortigas Center, Quezon City has shown a gradual improvement in its office market performance. The number of vacant spaces in the city decreased from 213,366 square meters in the last half of 2022 to 189,380 square meters in the first half of 2023. This decline in vacant spaces can be attributed to increased lease activities by business process outsourcing companies. As a result of this positive trend, rental prices have risen from Php 812 per square meter per month to Php 851 per square meter per month.

Moving southward. The Bay Area's, office sector continues to sustain the impact by the exodus of the POGO industry, resulting in a sideways movement in both demand and lease rates. The available space increased from 477,955 square meters to 619,930 square meters, with an average lease rate of Php 892 per month in the first half of 2023, compared to an average of Php 911 per month in the last half of 2022.

Meanwhile, Alabang CBD, exhibited a positive performance in vacancy during the first half of 2023, with available space from 258,739 square meters in the last half of 2022 to 253,206 in the first half of 2023. Despite this positive performance in office vacancy. Lease rates have decreased from Php 863 per square meter per month to Php 857 per square meter per month, in the same comparative period.

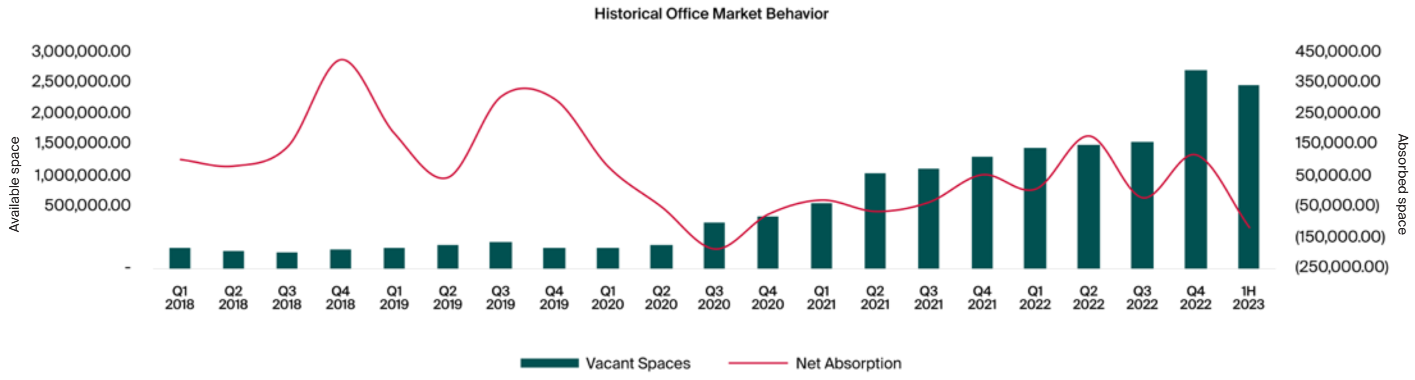
Workplace reimagined: hybrid to buoy demand

The implementation of restrictions in March 2020 led to the widespread adoption of the hybrid work modality, as the default work experience across the country. Despite initial resistance, the transition to remote work was relatively smooth for the majority of individuals, given their familiarity with computer-based work and internet connectivity, which enabled them to work from anywhere. Remote workers proved to be productive, leveraging creativity to set up home offices in various parts of their residences and eliminating the need for daily commutes.

The significant shift towards the hybrid work modality has had a noticeable impact on the office market, particularly reflected in the sequential increase in available office space. During the last period of 2019, the available office space was recorded at 291,000 square meters, which then rose to 721,794 square meters by the end of 2020. This substantial increase in available space indicates a decline in leasing activities during that period, as businesses adjusted their strategies in response to the changing work landscape.

Upon the cessation of the pandemic, a significant number of businesses enforced a mandatory return-to-office policy, requiring employees to resume on-site work at full capacity. However, after experiencing nearly two years of productive remote work, a considerable portion of the workforce resisted these demands to return to the office. Remote workers demonstrated that work can be effectively accomplished from any location, eliminating the need for lengthy commutes and offering greater flexibility.

In the corresponding period last year, the Philippine government actively promoted the return of employees, particularly those in the business process outsourcing sector, to on-site work as a means to revitalize economic growth. However, the response from employees revealed resistance, underscoring the shifting attitudes and preferences towards remote work. These changing perspectives have been influenced by the lessons learned and the increased efficiency experienced during the pandemic, resulting in a greater inclination towards remote work arrangements.

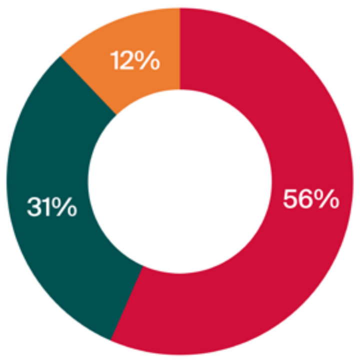


Taking all these factors into consideration, the concept of a hybrid workplace has emerged as an alternative approach. Recognizing the advantages of both remote work and in-person collaboration, organizations are exploring the possibility of creating a hybrid work environment that combines the benefits of flexibility and remote work with the value of face-to-face interactions.

According to Knight Frank's (Y)ourspace report, a substantial number of international multi-market businesses have embraced hybrid work arrangements. Out of the 350 surveyed companies, 56% have chosen to adopt a hybrid modality, allowing employees to work both remotely and in-office. This approach provides flexibility and a balance between the benefits of remote work and the advantages of in-person collaboration.

Preferred Work Modality of Top Multinational Firms

- Hybrid
- Office first
- Remote first



On the other hand, 31% of the surveyed businesses remain committed to an "office-first" policy. These organizations prioritize the physical office environment and prefer their employees to work predominantly on-site. They believe that face-to-face interactions and a centralized workspace are essential for their operations and company culture.

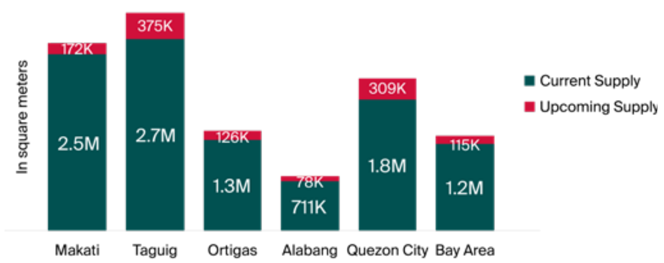
In contrast, 12% of the companies have adopted a remote-first or remote-only setting. These organizations have fully embraced remote work as their preferred mode of operation, with employees primarily working from home or other remote locations. This approach recognizes the benefits of remote work in terms of flexibility, reduced commuting time, and increased work-life balance.

The findings in Knight Frank's (Y)ourspace highlight the diverse approaches that businesses are taking regarding hybrid work arrangements. This allows them to leverage the advantages of remote work, such as increased productivity and employee satisfaction, while still recognizing the importance of in-person collaboration and connection.

The transition to hybrid work models has undoubtedly affected the dynamics of office leasing. Some companies have opted to downsize their physical office footprint or adopt flexible work policies that reduce the need for dedicated office spaces, which may result in a temporary decline in demand for office rentals.

While hybrid work arrangements have introduced significant changes to the traditional office setup, allowing employees to have flexibility in working remotely or in-office, it is important to acknowledge that the demand for office spaces may encounter certain obstacles. Despite these challenges, Santos Knight Frank foresees that there will be 1.1 million office spaces to be introduced in the market until 2025.

Metro Manila Office Supply



It is empirical to recognize that the need for office spaces will not completely disappear. Certain industries and businesses will continue to rely on physical work environments to foster collaboration, host meetings, and provide a centralized hub for their operations. Additionally, some employees may prefer working in an office setting to maintain separation between work and home, or for access to specialized equipment and resources.

These preferences of specific needs that cannot be met by remote work, and hybrid modality, will continue to drive the demand for office spaces to remain constant, irrespective of the prevailing work modality, ensuring a continued and essential role for office spaces in the future.

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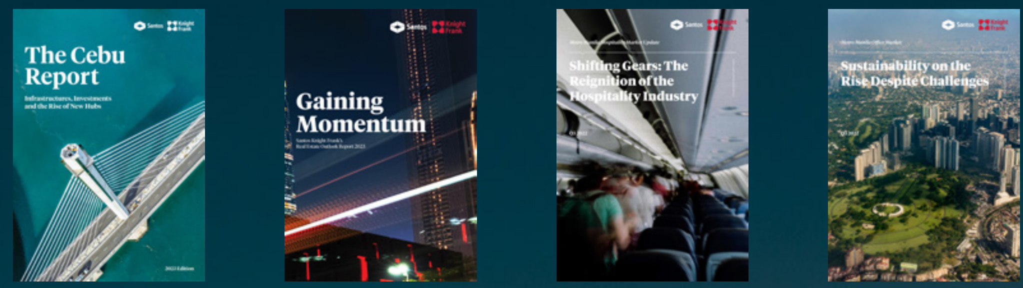

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