COLLIERS FLASH

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OPTIONS FOR PHILIPPINE PROPERTY PLAYERS IN RESPONSE TO WEAKER GROWTH

Philippine developers and investors re-align strategies amid slower growth in economy, property

Insights & Recommendations

Due to the spread of COVID-19, the Philippine economy will grow at a lower rate in 2020 than originally expected. In response to this situation, Colliers recommends:

> **Landlords** should target traditional* and outsourcing tenants considering our expected decline in demand from POGOs**; communicate early with tenants regarding flexible lease terms; and emphasise wellness features and certifications.

> **Occupiers** should take this opportunity to negotiate long-term deals with landlords and look for new buildings in business hubs' fringes offering discounts.

> **Condominium developers** should highlight property management as it is crucial to building health.

> **Mall and hotel operators** should line up marketing campaigns to recapture demand as COVID-19 issue wanes.

Sharper GDP growth in 2021

Oxford Economics is projecting the Philippine economy to grow by 3.9% in 2020 from its original estimate of 5.9%. Despite this, Oxford Economics is expecting a sharper recovery in 2021, with the country's GDP estimated to grow by 7.3%.

Retail to recover in 2021

The retail sector has felt the immediate pinch brought about by COVID-19. Oxford Economics expects private consumption to grow by a slower 3.6% this year but with a rebound to 7.1% in 2021. This should benefit retailers and mall operators.

Office relies on non-POGO segments

Colliers sees office vacancy in Metro Manila rising due to slower office space absorption from POGOs. But this should be tempered by take-up from outsourcing and traditional occupants especially once market sentiment improves by H2 2020. Vacancy should be around 6.5% in 2020 assuming leasing activities pick up in H2 2020.

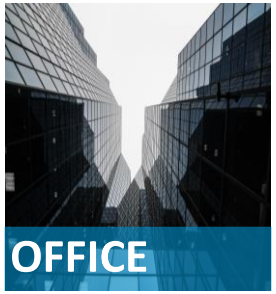
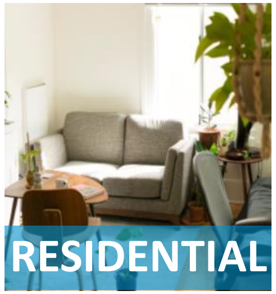
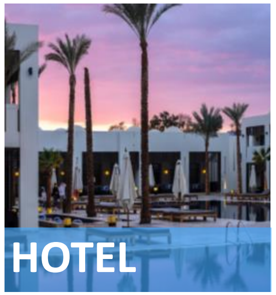
Condominium developers recalibrate

Colliers projects the completion of about 14,720 new condominium units in Metro Manila in 2020. With significant completion, developers should highlight property management as it is crucial to the health and safety of occupants and buildings and offer more flexible terms to attract buyers.

PROPERTY PLAYERS RETHINK STRATEGY TO MAXIMIZE ECONOMIC RECOVERY

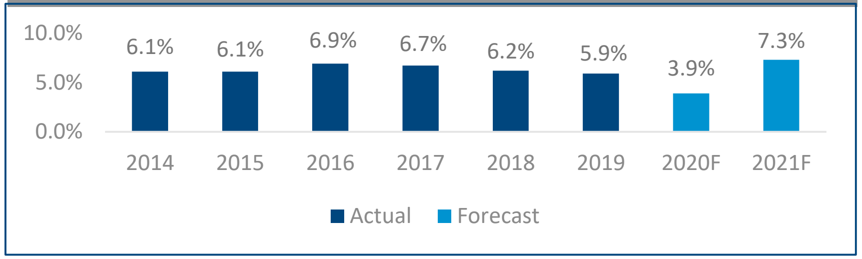
The Philippines' GDP grew by 5.9% in 2019, the slowest pace since the 3.7% recorded in 2011. The economic growth potential for 2020 will be clipped by the impact of COVID-19. In our opinion, a coordinated policy and monetary response from the Philippine government and central bank is likely to instill confidence in the property market before the end of 2020, assuming the outbreak peaks in H1 2020. Office landlords should maximize wellness features of buildings and strengthen property management capabilities while occupants should use this as an opportunity to negotiate long-term deals. Condominium developers should offer more flexible terms to investors and note that developers able to respond well to the pandemic are likely to be remembered by buyers once market conditions normalize. Meanwhile, residential investors should cash in on better pricing due to lower interest and mortgage rates while mall operators should strengthen their e-commerce strategies.

Economic data: Philippine Statistics Authority. [1]Krshnan, T. (March 23, 2020). Country Economic Forecast Philippines. *Oxford Economics.* *Traditional includes companies in various sectors including legal, engineering and construction, government agencies and flexible workspace operators. **Also known as Philippine Offshore Gaming Operators (POGOs), primarily offshore gaming firms from China.

Sector	Impact on real estate market	Recommendations
 OFFICE	> Inspection activity is likely to decline which should result in lower take-up in H1 2020. > A slower macroeconomic environment is likely to hinder traditional occupants' expansion plans;, we expect demand will recover in H2 2020 at the earliest. > Slower expansion from POGOs and traditional occupants due to travel bans imposed by Chinese and Philippine governments and Luzon quarantine.	> Occupiers – look at new buildings in fringe locations where rents are cheaper than in major CBDs; the time is right to negotiate long-term leasing deals. > Landlords – proactively attract traditional or outsourcing tenants for space vacated by POGOs; target likely resilient sectors such as pharmaceuticals and technology; work with existing tenants to provide flexible lease terms while maximising wellness features and prioritising wellness certifications.
 RETAIL	> Luxury retail to feel the immediate pinch due to decline in tourist arrivals, especially those coming from China and South Korea, the Philippines' major source markets. > Domestic consumption is likely to weaken in the near term. Recovery in demand likely to depend on any government stimulus. > Online retailers including those with F&B deliveries and pharmacies should benefit during this period.	> Retailers – implement online-to-offline strategy; smaller tenants should maximise their tie-ups with ecommerce operators and platforms; target senior citizens who are embracing online shopping. > Landlords – provide short-term rent concessions to support retailers and ensure and highlight hygiene standards in malls through good ventilation and adequate sterilisation.
 RESIDENTIAL	> Softer demand due to increasing unemployment or declining remittances from Filipinos abroad. > Depending on the duration of the Luzon quarantine, prices in the secondary market will likely soften to their pre-selling levels. > Demand in business districts that mainly house offshore gaming companies from China (e.g the Bay Area) are likely to decline particularly if the travel ban continues.	> Developers – highlight property management as it is crucial to the health and safety of buildings and unit owners; offer more flexible terms to attract buyers. > End-users and investors – take advantage of the opportunity presented by better pricing for both the pre-selling and secondary markets. Look for units in fringe areas where there is still potential for capital value appreciation and where price increases have been due to end-user demand.
 HOTEL	> The hotel sector is immediately impacted, with occupancies of only 35% according to our contacts from various hotel operators, down from 71% occupancy at the end of 2019. > This is even lower than our initial estimate of hotel occupancy of 63% factoring in a significant drop in Chinese and Korean tourists in 2020 due to the travel bans. The MICE[2] and banquet businesses are affected due to community quarantines imposed across Luzon.	> Operators should start lining up marketing efforts to recapture foreign and domestic tourists as the COVID-19 epidemic wanes. > This is likely to be the first sector to benefit from a government-initiated stimulus package. Hotel operators, retail establishments, and allied services should closely monitor developments related to the proposed financial package from the government.

[2]Meetings, Incentives, Conferences and Exhibitions

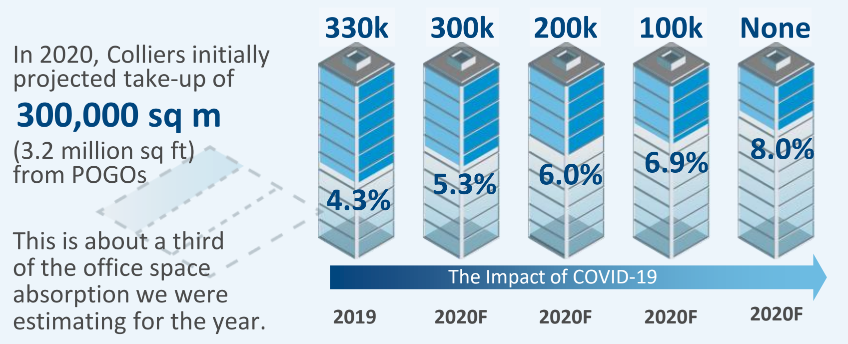
Philippines, historical GDP growth, 2014-2021F



Source: Philippine Statistics Authority, Oxford Economics

OFFICE: VACANCY TO RISE

Metro Manila office vacancy forecasts, 2020 POGO take-up scenarios



We expect an upside coming from outsourcing and traditional firms recovering in H2 2020. If the duration of the community quarantine in Luzon is limited, these firms could bridge the gap left by POGO firms, limiting vacancy to increasing to below 7% this year.

However, should the pandemic take a more significant toll on demand, then we expect vacancy to rise closer to 8% in 2020. In terms of lease rates, Colliers has been recording a two-tiered rental scheme since the entry of POGOs in Q4 2016. Traditional and outsourcing occupants are paying at a discount (20% to 30%) compared to POGO tenants.

For the first two months of 2020, we saw POGO firms pre-leasing nearly 54,000 sq metres (581,000 sq feet) of office space in two business districts in Metro Manila. But these buildings have yet to be completed and the POGO companies have yet to commence actual operations, as they face a shortage of employees amid the travel ban.

HOTEL: RATES TO DROP FURTHER

We see 2020 foreign arrivals likely to be lower than 2019 figures due to the COVID-19 outbreak. We expect average occupancy rates for H1 2020 to decline below 50% (down from our initial forecast of about 63%) due to substantial new hotel room supply as well as the adverse impact of a travel ban in China, the Philippines' second largest source of tourists after South Korea. Some hotel operators in Metro Manila have already reported lower occupancies of about 35% as of the end of February 2020.

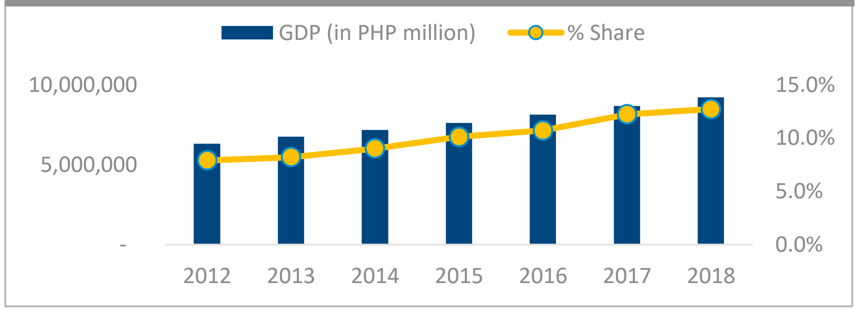
Colliers notes that the daily rates of several hotels declined by about 30% at the end of February 2020 compared to rates in December 2019.

RESIDENTIAL: SLOWER TAKE-UP

Colliers sees the completion of about 14,720 units in key districts in Metro Manila. Colliers estimates that about 79% will likely be in the Bay Area or about 11,590 units. These units were previously sold and developers were able to book these at their peak price. The concern is on the secondary lease and re-sale market, especially in the Bay Area where demand has primarily been driven by POGOs. In our opinion, if prices soften, developers are likely to stop launching.

In the event that the COVID-19 situation worsens, we project a drop in demand and slowdown of take-up in selected business districts in Metro Manila. Factoring in a slower take-up from Chinese investors especially in business districts where demand is POGO-driven, Colliers sees Metro Manila vacancy increasing to close to 20% from 11% in 2019.

Share of Tourism to Philippine GDP, 2012-2018



Source: Philippine Statistics Authority

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