An Office Sector Review
for the Pearl of the Orient

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Establishing a New Norm: An Office Sector Outlook

Research, May 2020

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The COVID-19 pandemic caused sudden adverse effects and high uncertainties to the global economy. Human mobility and business activities had to be limited in the short-term with the implementation of lockdowns. Essential work and businesses were what remained operational, resulting in a virtually inactive and stagnated economy. Ensuring the health and safety of the people became the main focus of both government and the private sector with the goal of "flattening the curve" as early as possible.

The economic uncertainties stemming from the spread of the disease greatly affected the commercial property sector. A number of office expansions and new space take-up were put on hold, others just cancelled outright, resulting in lower lease transactions in the short to medium-term. Companies are managing capital expenditures to maintain liquidity to prepare for sudden changes in the market. Occupiers are also reviewing their office space requirements as this may change as the outbreak progresses.

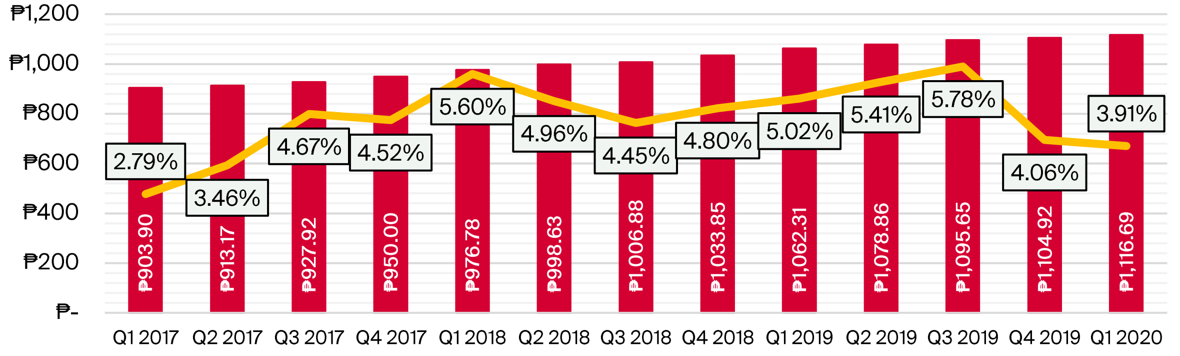
According to Bill Gates, in an article written in The Economist, life will return to normal when most of the population is vaccinated. With no vaccine in the immediate future, the effect of the pandemic may get even worse. It has been said that things will never go back to what they were prior to COVID-19.

The physical and psychological effects of the pandemic will change the way how people live, work, and interact. Out of this a 'new normal' will emerge. The pandemic has and is continuing to reshape the working landscape with social distancing becoming an integral part of the new normal. The work from home (WFH) strategy, which is being employed during the lockdown, may still be around long after. Occupiers are taking this opportunity to assess and re-evaluate their workspace requirements moving forward as well as their strategies for return to office when the time comes.

Tenant-Favorable Office Market

Based on the preliminary data gathered prior and during the early stages of Enhanced Community Quarantine (ECQ) imposed in the island of Luzon, the Metro Manila office sector somehow improved in Q1 2020. Despite additional supply of office space of more than 45,000 sqm, average vacancy rates in Metro Manila dropped to 3.91%, in comparison to the 4.06% average vacancy rating about a quarter ago. Average office rents in Metro Manila showcased a quarterly increase of 1.07% during Q1 2020, which translates to PHP 1,116.69/sqm. Rent relief was mandated in Memorandum Circular No. 20-12 of the Department of Trade and Industry (DTI),

FIGURE 1
Metro Manila Office Lease & Vacancy Rates Q1 2020



Source:
Santos Knight Frank Research

which grants businesses falling under Micro, Small, and Medium Enterprise (MSME) which have not been operational during ECQ, a grace period of 30 days (minimum) in their commercial rents. This is to alleviate the difficulty of MSMEs in paying their monthly rent as these businesses have been under financial distress during ECQ.

Despite the observed increase in Q1 2020, office rental rates are forecasted to contract during the course of 2020 as landlords will try to maintain cash flow while avoiding high vacancies resulting in a tenant-favorable office market. Several easing strategies will be seen from the landlords in order to retain low vacancy levels. For instance, landlords could provide flexible rental payment terms to their tenants and potential occupiers, in order to preserve the value of their rents. Flexibility in lease terms will become a new norm that may take effect in the short to medium term as businesses slowly start recovering their financial losses incurred during the ECQ. The relatively large office supply in the pipeline for Metro Manila, particularly in Quezon City and Ortigas Center, may pressure landlords to be more creative in packaging lease terms in order to attract potential tenants.

Office vacancies are seen to freeze and then gradually increase by the close of 2020 as most occupiers are expected to take a "wait and see" attitude due to the uncertainties caused by the pandemic. These occupiers will most likely take a conservative stance and carefully assess their office space requirements as the new normal sets in. This may cause a slowdown in the take-up of space in the newly constructed office buildings, particularly in Quezon City and Ortigas Center.

On the positive side, easing rents and rising office vacancy in Metro Manila are seen to be alleviated as the market presents an opportunity for international companies to offshore its operations in the Philippines as a way of managing costs. It maybe wise as reconsider lifting the PEZA moratorium as a means to jumpstart the industry.

Cleaner and Healthier Office Spaces

According to Asia-Pacific Knight Frank Occupier Services Commercial Agency (OSCA) head, "The workplace you left is the workplace you're going back to". The health risk posed by the virus is enough to remind everyone the importance of proper hygiene and sanitation. Regular cleaning and improved sanitation will be strictly imposed as well as possible rearrangements in the office space in compliance with the newly set regulations by the government to allow the resumption of operations once the lockdown is lifted. All this to control the spread of the virus and ensure health and safety in the workplace.


Zuellig Building (Makati)
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This new set of regulations will also include guidelines for people entering the building. Strict adherence to the guidelines should be followed to be allowed entry into the building. Wearing facemasks and being subjected to a body temperature check will be mandatory. Once inside, observance of proper physical distancing in elevators, common areas and workplace will be strictly enforced.

The increased emphasis on cleanliness and sanitation will provide greater opportunities for Facilities Management (FM) and Property Management (PM) services. Similar to any public area, office buildings draw in large crowds that increase the risk of contagion. FM and PM services will not only be useful in providing cleaning and sanitation services but will also provide protocols within the confines of office buildings as a preventive measure against COVID-19.

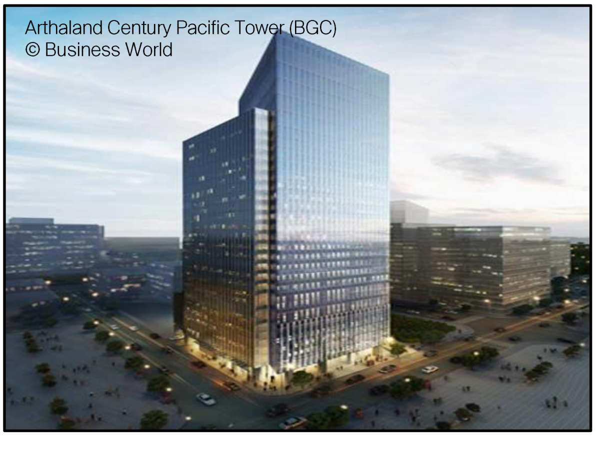
In China, the battle against COVID-19 has resorted to the use of modern technology. According to an article in South China Morning Post, Artificial Intelligence (AI) is being used in China to detect people who are not wearing masks in public and it also gives real-time updates about new COVID-19 cases and where it is located. Robotics were also being used for sanitation in public areas. It is seen that these practices can be adapted to the office setting in order to improve workplace safety. According to Facility Management Executives, sensors may be used to detect certain areas that need further attention in sanitation especially in places where employees usually gather. Touchless door entries as well as self-cleaning surfaces may also be installed in the workplace to minimize the direct contact with surfaces wherein the virus may linger.

In the medium to long-term, green buildings will gain a competitive advantage compared to traditional office buildings. Buildings accredited by US Green Building Council (LEED), Philippine Green Building Council (BERDE) and WELL Certified will be more sought-after. These buildings, by default, already put a premium on the health and well-being of its occupants. The design of the building provides large spaces which allows proper air circulation for better overall air quality. This is further enhanced by the use of state-of-the-art air filtration and ventilation systems to control and reduce the amount of carbon dioxide and harmful gases in the air as well as other airborne particles such as dust and microbes.

The design also calls for the increased use of natural light to illuminate the building to reduce the consumption of electricity. Natural light also serves as a natural disinfectant as some microbes have an aversion for it.

Workplace Redesigned

Due to government restrictions, companies were forced to implement work-from-home (WFH) and skeletal workforce schemes as part of their Business Continuity Plan (BCP). This is to ensure the safety of its employees and to secure the company's assets while continuing business operations. The global health crisis has also become an experiment to test if WFH set up is just as effective as working in the office. It is possible that WFH may continue even after the threat of COVID-19 has been eradicated.


Arthaland Century Pacific Tower (BGC)
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GT Tower
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The behavioral effect of the pandemic will force changes in the workplace environment. First, workplace density will become smaller. The events have shown that areas with a high density of people are more prone to the virus spreading rapidly. Limiting the number of people in the workplace on any day will be the standard. To do this, companies should implement a flexible work model wherein a smaller percentage of employees will be working onsite while the rest will be working remotely. Rotational schedules may be put in place to allow each employee to have access to the workplace when needed. Moreover, with lessened workplace density, the space allocation per employee will increase as workstations will be set further apart to maintain proper social distancing. Companies will be prioritizing the health and well-being of the employees and this will result into workplaces providing remote/solo-oriented type of work space as well as creating facilities that encourage responsible collaboration in the workplace.

Companies may also look into having a “core-flex” type of agreement with its landlord post-ECQ. The core-flex office solutions aim to provide potential occupiers with options to mix and match the space they are leasing between fixed (core) and flexible (flex), with corresponding modifications on the lease terms for each space. This enables the tenant to set the amount of office space needed on a long term basis, and at the same time, have space at hand used in the interim. This also allows the tenant the ability to thoroughly evaluate its space requirement and make a quicker decision on whether to scale-up or scale-down. This decision can likewise be executed quickly when the time comes.

Core-Flex solutions are also beneficial for tenants who are unsure of their expansion plans and do not want to commit to fixed term leases. Landlords would prefer that their tenants sign up for fixed term leases as this provides them added security. However, flex spaces are leased at a premium rate which compensates the landlord to some extent.

The outbreak of COVID-19 has become a multiple black swan event with its effects on an unprecedented global scale. The way of life, as we know it, will change, and together with it our attitude towards our day to day activities. Metro Manila office market poses opportunities despite the headwinds brought about by the pandemic. Immediate negative effects of the crisis to the industry will be felt within the remaining months of 2020 and are seen to slowly recover in 2021. Regardless of countless measures to mitigate the outbreak of COVID-19, offices and the workplace will be resilient and remain a key and integral part of economic recovery and progress.

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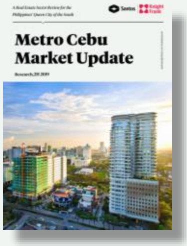

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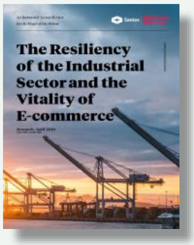

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