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DAVAO POST-PANDEMIC OFFICE RECOVERY

Occupiers and developers seize opportunities amid a lukewarm office market

Insights & Recommendations

Davao City is one of the most competitive outsourcing destinations in the Philippines, and one of only three Philippine cities that are in Tholons' Top 100 global sites¹ for outsourcing.

However, the COVID-19 pandemic will likely lead to slower office leasing all over the Philippines, including Davao City.

Despite the challenges, Colliers sees office leasing opportunities for urban hubs outside of Metro Manila including Davao especially when market sentiment starts improving early 2021.

Colliers encourages outsourcing occupiers to lock in space in integrated communities. Landlords, meanwhile, should highlight their property management capabilities and availability of PEZA-proclaimed space*



Demand

> Colliers believes that demand from both from traditional [†] and outsourcing firms will prop up office absorption as the market sentiment improves towards Q1 2021.

End 2019



Full Year 2020

2020-22
Annual Average

Supply

> We project about 53,200 sq metres (572,400 sq feet) of new office space in 2020. While we expect completion delays of up to two quarters, we project 2020's pipeline will still be completed this year.

4,300 sq m



53,200 sq m



17,700 sq m



Rent

> In 2020, Colliers sees a 10% decline in office rents due to slower leasing. Rents should bottom out in 2020 and then with increased leasing activity begin rising in 2021.

YOY/
End 2019

2.6%

PHP 480

YOY /
End 2020

-10%

PHP432

Annual Average
Growth 2019-22 /
End 2022

-2%

PHP450

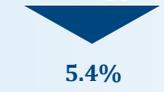


Vacancy

> Colliers sees vacancy rising to about 14.5% in 2020 due to slower leasing. The central bank is projecting a faster economic growth in 2021 and we see this anchoring a rebound in office leasing in Davao City during the year.

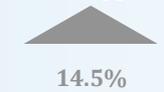
-17.1pp

5.4%



+9.1pp

14.5%



+0.9pp

8.0%



Source: Colliers International. Note: 1 sq m = 10.76 sq ft. *Philippine Economic Zone Authority (PEZA) proclaimed spaces where locators enjoy tax and non-tax incentives. [†]Traditional includes companies in various sectors such as legal, engineering and construction, government agencies and flexible workspace operators.

¹[Tholons Services Globalization Index 2019](#).

RECOMMENDATIONS

Lock in space in integrated communities

Colliers now sees occupiers looking for space in integrated communities to improve their business continuity plans. We see firms gravitating towards integrated communities to maximize the live-work-play amenities of these developments. In Davao City, about 43% of new space due to be completed in 2020 is within an integrated community.

Highlight property management and design requirements

The COVID-19 pandemic has highlighted property management capabilities. Moving forward, Colliers believes that occupiers are likely to be more discerning with design considerations (e.g. proper air circulation, more office space per employee, and glass ratio for natural sunlight) and property management protocols including sanitation (e.g. implementation of measures to avoid virus transmission) and emergency preparedness.

Highlight Davao's viability as a key hub ex-Manila

Davao remains a viable outsourcing hub outside Metro Manila. According to Tholons, an outsourcing advisory firm, Davao City is ranked as the 95th most competitive outsourcing destination in the world. Davao is one of three Philippine locations (along with Metro Manila and Cebu) to be included in the Top 100. Among the factors considered in the annual poll are quality of manpower; cost and infrastructure; risk and quality of life; and digital innovation. Davao's economy has also been expanding by 9.6% annually from 2016 to 2018, fastest among key regions in the country.

GDP Growth Comparison, 2016-2018

	2016	2017	2018
Overall Philippines	7.1%	6.9%	6.3%
National Capital Region (NCR)	7.5%	6.2%	4.8%
Davao Region	9.4%	10.7%	8.6%
Central Visayas	8.8%	5.2%	7.6%
CALABARZON	4.8%	6.7%	7.3%

Source: Latest data available from the Philippine Statistics Authority. Note: CALABARZON = Cavite, Laguna, Batangas and Quezon provinces, which, along with Central Visayas, are two of the fastest growing regions in the country.²[Cities and Municipalities Competitive Index](#).

Maximize Davao's skilled manpower

Colliers sees Davao as a competitive office site outside of Metro Manila due to its skilled manpower. The city produces about 15,000 college graduates every year with about 46% having degrees in Business, Math, Science, and Information Technology. The city is also considered an education hub for the entire Mindanao group of islands.

Accelerated adoption of modern technology

Colliers believes that occupiers in Davao should also be more aggressive in implementing modern technologies, similar to what their Metro Manila counterparts do. In our opinion, this is especially important for firms looking to improve their business continuity plans.

Highlight Davao's disaster resilience program

We believe disaster resiliency is likely to be among the major considerations of outsourcing firms when choosing alternatives to Manila. In this category, Davao will likely be a key option as it is ranked as the third most disaster-resilient city in the country according to the Cities and Municipalities Index 2019², only behind Iloilo and Cagayan de Oro.

Highlight PEZA availability

In our opinion, developers need to highlight their PEZA-proclaimed spaces especially if they want to capture the spillover demand from Metro Manila. Colliers projects about 41,300 sq metres (444,400 sq feet) of PEZA supply in Davao city in the next 12 months. Colliers believes that Davao remains on the radar of investors and leasing queries will likely materialize if there is adequate PEZA space.

Infrastructure-led development

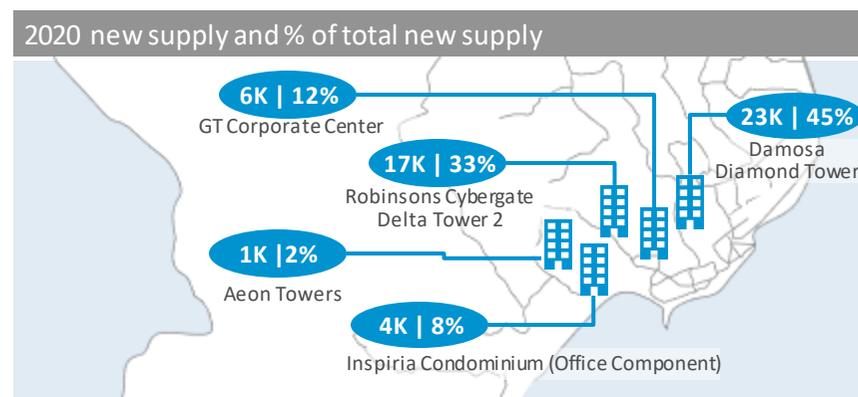
Davao is likely to be one of the major beneficiaries of the government's *Build, Build, Build* program. Colliers believes that developable land around the proposed Davao Coastal Road, Davao Monorail, Mindanao Railway Project (MRP), and the Davao Bus Rapid Transit (BRT) should further be assessed for their feasibility for township projects that feature malls, hotels, condominiums, and offices. These public projects due to be completed even beyond the term of the current administration should ensure the viability of adjacent township projects.

NEW SUPPLY IN TOWNSHIPS

Among the new office towers due to be completed in Davao in 2020 are Robinsons Cybergate Delta Tower 2, GT Corporate Center, Aeon Towers and Inspiria Condominium (Office Components).

Another building due to be completed during the period is Damosa Land's Diamond Tower at Damosa IT Park. The project is one of the largest office towers in the city with a leasable area of 22,900 sq metres (246,400 sq feet).

For 2020, Colliers projects the completion of about 53,200 sq metres (572,400 sq feet).



Source: Colliers International

OCCUPANCY TO RECOVER IN 2021

Colliers recorded about 44,500 sq metres (478,800 sq feet) of office space take-up in 2019. Similar to what we project in Metro Manila, we are likely to see a decline in leasing activities in 2020 due to the uncertainty brought about by the COVID-19 pandemic. Hence, we see 2020 vacancy reaching 14.5% from 5.4% in 2019.

Economic analysts and credit rating firms are projecting a rebound in 2021. The Philippine central bank, while projecting GDP to contract by 0.8% in 2020, is looking at a 7.8% rebound in 2021.

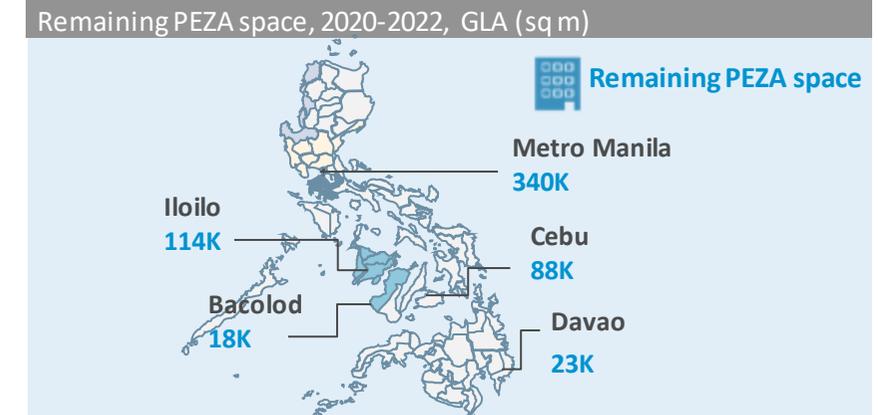
If this materializes, we are also likely to see a recovery in terms of office space leasing and this should spill over to key outsourcing outside Metro Manila including Davao city. In our opinion, a recovery in 2021 is likely to be

anchored by demand from traditional and outsourcing occupiers.

Colliers believes that outsourcing occupants that are currently Metro Manila-centric are likely to scout for viable sites outside the capital region.

Davao City is the center of commerce for the Davao Region, which was the fastest growing region in the country from 2016 to 2018, based on the latest available data from the Philippine Statistics Authority (PSA). Hence, we see traditional occupiers partly driving demand in 2021.

In 2019 prior to the COVID-19 pandemic, the IT and Business Process Association of the Philippines (IBPAP) noted that the growth in employment in the outsourcing sector is mainly attributable to more jobs created in outsourcing sites outside Metro Manila, including Davao. While investors take a wait-and-see stance due to uncertainty, we see the economic recovery in 2021 stoking office space demand in Davao during the period.



Source: Colliers International

RENTS TO DROP 10%

Due to slower leasing activities, Colliers projects office rents in Davao city declining by 10% in 2020. With an economic recovery in 2021, we see rents growing by about 2%. In our opinion, a recovery in office leasing is likely to be anchored by an expansion of traditional businesses in the city as well as a rebound in absorption from outsourcing tenants.

Colliers sees leasing activities gravitating towards office spaces within integrated communities once market sentiment improves. Hence, we see lease rate growth in offices within townships rising at a faster pace.

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About Colliers International

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OPPORTUNITIES FOR DAVAO RESIDENTIAL INVESTORS AND DEVELOPERS AMID COVID-19

How residential developers and investors should respond to market uncertainty due to COVID-19

Insights & Recommendations

Davao City is a residential hotspot in Mindanao and is a preferred site of both end-users and investors.

The sustained demand over the past four years has encouraged condominium and house and lot developers to invest in the city.

However, Colliers believes that the demand is likely to be curtailed by the COVID-19 pandemic while supply will likely be pared down due to quarantine measures.

Colliers believes that over the next few years, buyers are likely to prefer units within integrated communities and near infrastructure projects lined up by the government such as the Mindanao Railway. Aside from highlighting these features, developers should also look at alternative developable sites.

	2019	Full Year 2020	2020-22 Annual Average
 Demand <p>> In 2019, we recorded the highest number of units sold, surpassing the previous record of 5,500 units in 2018. From 2020 to 2022, we project about a 10% decrease in take-up due to the COVID-19 pandemic.</p>	 5,600 units	 5,000 units	 5,000 units
 Supply <p>> From 2020 to 2022, Colliers sees the delivery of about 8,100 units or 2,700 units annually, lower than our initial estimate of 2,900 units factoring in the work stoppage and construction delays due to the lockdown.</p>	 2,200 units	 2,000 units	 2,700 units
 Capital Values* / Yields <p>> The average price of condominium units increased by 5.5% from PHP104,500 in 2018. Given the impact of the pandemic, we expect developers to give a 3% to 7% discount on selected pre-selling projects.</p>	YOY / End 2019  5.5% PHP110,200	YOY / End 2020  3.0% PHP113,500	Annual Average Growth 2019-22 / End 2022  3.0% PHP120,400

DAVAO CONDOMINIUM SUPPLY TO SLOW DOWN

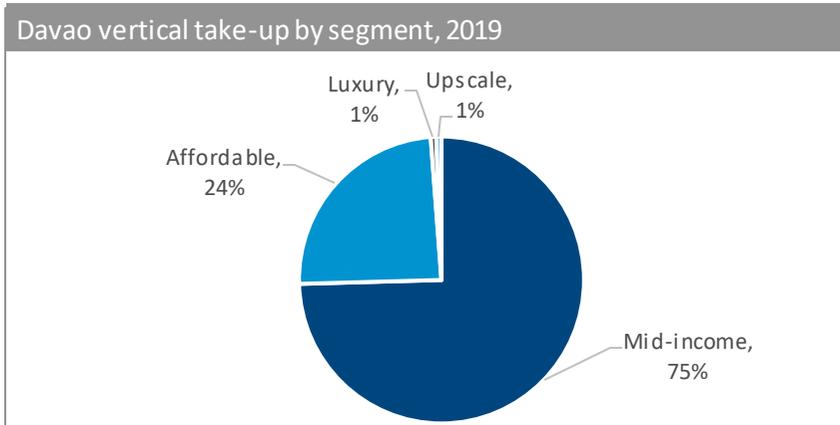
Davao's condominium stock reached 14,100 units by the end of 2019, about 19% higher compared to its 2018 stock of 11,900 units. More than 55% of the new completions were mid-income projects which have a total contact price (TCP) of PHP3.2 million to PHP6 million (USD62,700 to USD117,600). Affordable and mid-income units remain as the most popular segments, but overall demand is likely to slow down in 2020 due to the pandemic. We see demand recovering in 2021 anchored by a rebound in economic growth and low mortgage rates.

Source: Colliers International. Note: USD1 to PHP51 as of the end of 2019. 1 sq m = 10.76 sq ft.
Note: Demand, supply, and capital values represent vertical residential market only. Capital values indicated are average price per sq metre.

RECOMMENDATIONS

Highlight residential projects in integrated communities

The COVID-19 pandemic has highlighted the need to be in an integrated community. In our opinion, Davao City will likely remain an attractive residential option for both end-users and investors in Mindanao post-pandemic. But the demand for residential projects, whether house and lot (H&L) or condominium units, will likely hinge on integrated features, i.e. unit owners can easily access essential goods and services. Hence, we encourage developers to highlight the integrated features of their residential projects as this will likely be among the major considerations of unit owners even after the lockdown and COVID-19 pandemic. Townships currently make up 16% of Davao’s existing condominium stock and we expect that 35% of the upcoming supply from 2020 to 2022 would likely come from these integrated communities.



Source: Colliers International

Explore alternative sites for lot only and (H&L) projects

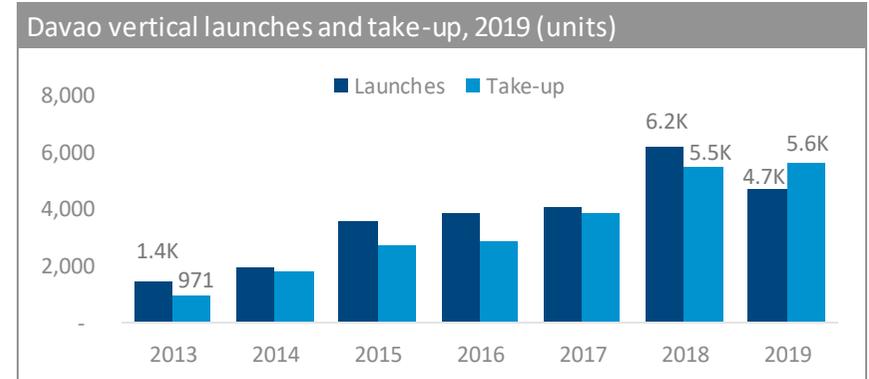
Colliers believes that lot only and house and lot projects will likely remain attractive among Overseas Filipino Workers (OFWs) from Davao. Those from the fringes of Davao City are likely to continue investing in horizontal projects. We see a resurgence of demand in 2021 and this should be supported by OFWs’ demand for housing. The Davao region is the fifth largest source of OFW deployment among the Visayas and Mindanao regions¹.

Bank on infrastructure projects

In our opinion, developers should highlight the price appreciation potential of land and residential projects that are planned near key public projects, including Davao Coastal Road, Davao Monorail, Mindanao Railway Project (MRP), and the Davao Bus Rapid Transit (BRT). These projects are likely to help spur demand for residential projects even beyond the COVID-19 pandemic.

Convert and repurpose old facilities

Developers should be on the lookout for old facilities in the city that can be redeveloped including in Davao’s Chinatown. In our opinion, some old structures can be redeveloped into mixed-use integrated communities featuring mid and high-rise residential towers complemented by office and retail space. Developers should also highlight the area’s historical background.



Source: Colliers International

Vertical and house and lot price segment, (PHP)

Segment	Average Total Contract Price (TCP)
Luxury	8 million and above
Upscale	6 million to 8 million
Mid-income	3.2 million to 6 million
Affordable	1.7 million to 3.2 million
Economic	580,000 to 1.7 million
Socialized	Below 580,000

Source: Colliers International. ¹Philippine Statistics Authority

PARED DOWN SUPPLY

Colliers sees slower condominium completion in 2020 due to construction delays. Like Metro Manila, Davao City was also placed under lockdown which affected the construction of condominium projects all over the city.

In our opinion, the city and national governments as well as private developers are likely to implement physical distancing measures through the end of the year and we see these delaying a number of residential projects. Hence, from our initial estimate of 2,940 units, we see a delay of close to 1,000 units or a third less compared to our original forecast.

PREFERENCE FOR VERTICAL

Colliers has recorded an annual average take-up of 4,500 units for condominium projects in Davao City from 2016 to 2019. Launches during the period were at 4,700 units per year. Demand in the city practically matches annual condominium supply.

Colliers believes that Davao City has become a viable residential hub in Mindanao due to its competitiveness. The 2019 Cities and Municipalities Competitiveness Index ranked Davao as the third most competitive in the country based on economic dynamism, government efficiency, infrastructure, and resiliency. Former Davao Mayor Rodrigo Duterte's election as Philippine president further raised interest in the city and has transformed Davao into a preferred residential haven of investors and end-users from nearby cities and provinces. In our opinion, Davao will likely sustain its attractiveness as a property investment hub even beyond the term of President Duterte.

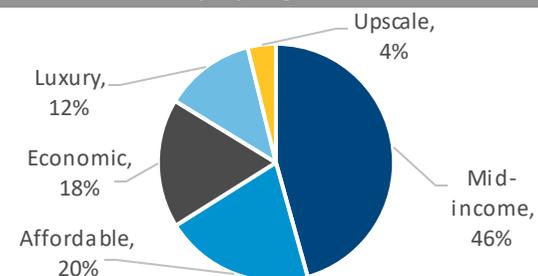
At present, the major concern is the economic impact of the COVID-19 pandemic on both investor and end-user appetite for condominium units. In our opinion, the slower leasing of office space in the city is indicative of businesses' wait-and-see stance and this cautious outlook is likely to spillover to the condominium market.

Davao vertical residential supply forecast, (units)

	As of 2019	2020	2021	2022	Total end-2022
Davao	14,100	2,000	2,700	3,400	22,200

Source: Colliers International. ²Department of Trade and Industry, Cities and Municipalities Competitiveness Index, 2019 ³BusinessMirror, Virus, oil price plunge to cut 400-k OFW jobs, 2020.

Davao house and lot take-up by segment, 2019



Source: Colliers International

COVID-19 TO AFFECT HOUSE AND LOT DEMAND

The mid-income and affordable H&L segments recorded strong take-up in 2019. These are the house segments that command an average price of between PHP1.7 million to PHP6 million (USD33,300 to USD117,600). In 2019, both segments combined for 66% of total demand in Davao City.

Colliers believes that one of the major reasons behind the strong take up of horizontal projects in 2019 is the sustained inflow of OFW remittances. The latest available data from the Philippine Statistics Authority (PSA) shows that the Davao region is the fifth largest source of OFW deployment among the Visayas and Mindanao regions.

Colliers believes that demand for H&L will likely be affected by the slowdown in OFW remittances. Some government officials and economic think tanks³ are forecasting a drop of between USD3 billion to USD6 billion (PHP153 billion to PHP306 billion) in remittances in 2020. In our opinion, this is likely to derail residential take up for both H&L and condominium segments. We see a greater impact on the H&L segment as this is primarily end-user demand driven. Anecdotally, OFWs looking for larger lots are among the major drivers of this residential segment.

Meanwhile, the central bank's projected 7.8% economic growth and recovery in OFW deployment in 2021 are likely to help revive residential demand in the city. This is likely to be supported by mortgage rates which currently hover between 5.0% and 7.0%, much lower than the Asian Financial Crisis levels of between 20% and 23%.

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