PINNACLE

market insight

JULY 2014

MARKET INTEGRATION IN STEP WITH ASEAN INTEGRATION

MACROECONOMY

The buzzword lately is the “ASEAN Integration” due to the planned Association of Southeast Asian Nations (ASEAN) Economic Community (AEC) by December 2015 of the ten nations, namely: Brunei Darussalam, Cambodia, Indonesia, Lao, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam. ASEAN Integration is still milled upon by the government, private sector and civil society; and is still subject to substantial information dissemination campaign. As an example, “ASEAN Integration” has four main pillars: political and security, socio-cultural, financial integration and economic integration. By December 2015, it is only the economic pillar that is being targeted, hence, the AEC.

To quote the ASEAN website: The AEC areas of cooperation include human resources development and capacity building; recognition of professional qualifications; closer consultation on macroeconomic and financial policies; trade financing measures; enhanced infrastructure and communications connectivity; development of electronic transactions through e-ASEAN; integrating industries across the region to promote regional sourcing; and enhancing private sector involvement for the building of the AEC. In short, the AEC will transform ASEAN into a region with free movement of goods, services, investment, skilled labour, and freer flow of capital.

Even with the economic leg, the Bangko Sentral ng Pilipinas (BSP) recently projected that the Philippines will achieve about 72% of its targets by December 2015. At any rate, BSP reiterated that the economic integration is “optional” and would depend on the capability of each national economy.

The Philippine economy remains to be vibrant. While the first quarter growth rate is a lower 5.7% than the initial target of 6.5%, the full year target for 2014 is kept between 6-7% level. The lower Q1 growth is diagnosed due to the delayed impact on the economy of the natural disasters last year. Nonetheless, it is third-best performing growth in Asia, next only to China and Malaysia.

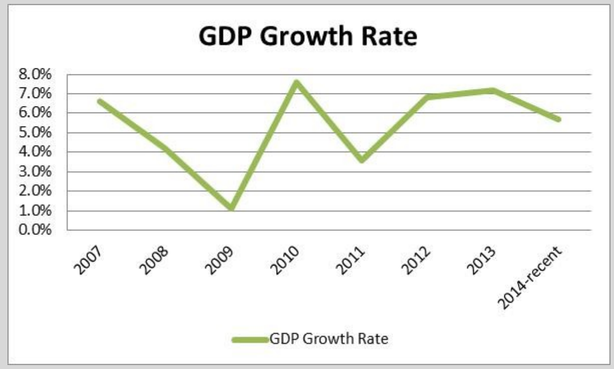
Based on Bangko Sentral ng Pilipinas statistics, the average bank interest rate continues to dip at 3.78% as of June compared to 5.19% as of February of this year. Inflation rate in June inched up to 4.5% compared to 4.1% in February. The Philippine Peso to US Dollar exchange shows a slightly weaker dollar from Php 44.9 in March to Php 43.64 in July. Dollar remittances from overseas Filipinos have been steadily increasing. For January to April of this year, remittances reached US$7.392 billion compared to US$6.986 billion for the same period last year, or an increase of 5.8%.

Foreign direct investment (FDI) from January to March of this year reached US$ 635.58 million, excluding reinvested earnings and debt instruments, due mainly to US$ 567.75 million investments in financial insurance activities. FDI for 2013, excluding reinvested earnings and debt instruments reached US$ 663.49 million. Philippines is in another banner year for foreign investments. For the first three months, investments in manufacturing account for US$ 23.94 million while investments in real estate activities account US$ 19.49 million.

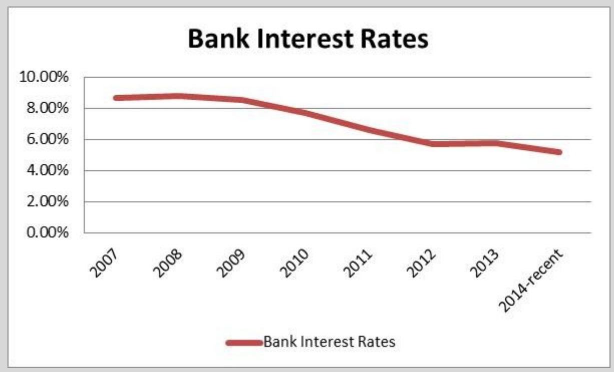
The total Visitor Arrivals for the first four months reached 1.697 million, which is 2.85% higher than the same period last year (Department of Tourism). Visitor from Korea and United States top the country of origin.

The above economic indicators show a sustained economic growth and sound investment environment for 2014. It is interesting to see how the real estate players are panning out, given these strong economic fundamentals and in preparation for the ASEAN economic integration by 2015.

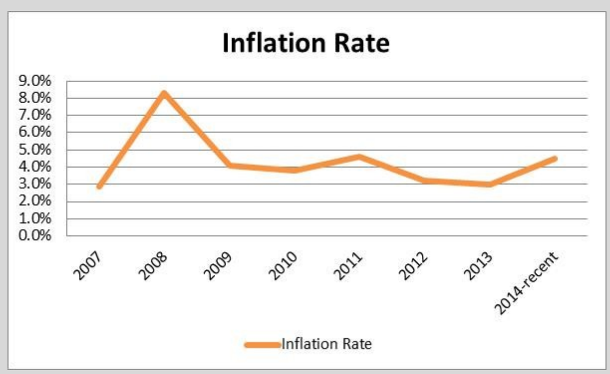
The top developers are increasing their capital expenditures (CAPEX) to fast track their projects. The SM Group allotted Php70.57 billion for its capital expenditures this year; of which 55% is for the shopping malls, 28% for the residential segment, and the balance for offices, hotels and convention



GDP Growth Rate
Source: Philippine Institute for Development Studies (PIDS) and NEDA



Average Annual Bank Interest Rates
Source: Philippine Institute for Development Studies (PIDS) and Bangko Sentral ng Pilipinas (BSP)

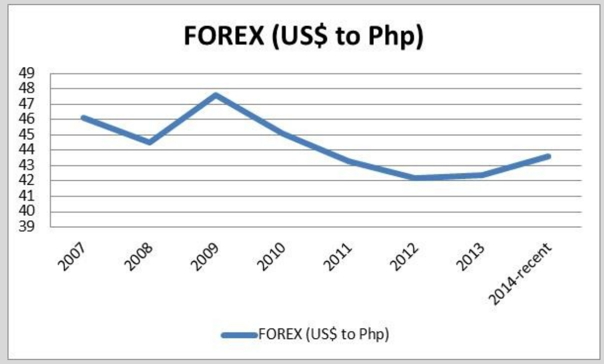


Inflation Rate
Source: Bangko Sentral ng Pilipinas (BSP), Philippine Institute for Development Studies (PIDS) and NEDA

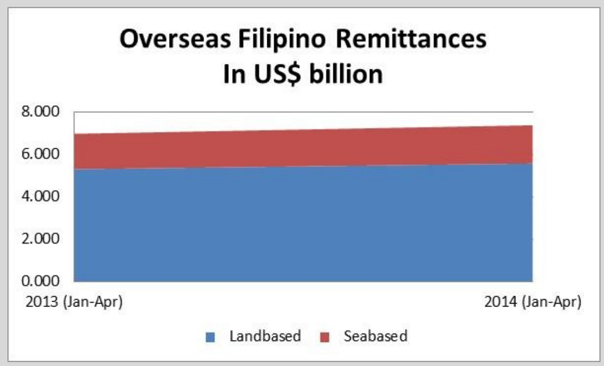
centers. This breakdown shows the variety of the projects of the SM Group and their priorities, malls and residences. It should be noted that the SM Group recently consolidated its various real estate vehicles to form the largest property group in ASEAN. The SM Group is clearly looking for opportunities in the forthcoming ASEAN economic integration.

Ayala Land allotted Php70 billion for its 2014 projects. True to its tradition of master planned developments, it is embarking on its 74-hectare Arca South project (recently acquired FTI Complex from the government) and its 1,125-hectare Alviera project in Porac, Pampanga. More importantly, the Ayala Group has launched its Seda hotel brand in Bonifacio Global City, El Nido and Vertis North, as well as its new retail platform “District” in Dasmariñas and Imus in Cavite, as well as in Talisay City in Negros Occidental.

The Megaworld Group earmarked Php 40 billion for expansion this year, excluding the CAPEX of Empire East which is reported at Php 25 billion in the next five years. It also consolidated its stake in Global-Estate Resorts, Inc. (GERI) from Alliance Global. This is to position the Group in the tourism industry, not only in Boracay, but also in its gaming jewel Resorts World/Newport, in Twin Lakes in Tagaytay, as well as in Cavite, Iloilo and Laguna. In addition, Suntrust Properties, its subsidiary targeting the affordable residential segment, has been launching a number of projects.



Foreign Exchange
Source: Bangko Sentral ng Pilipinas (BSP), Philippine Institute for Development Studies (PIDS) and NEDA



Overseas Filipino Remittances
Source: Bangko Sentral ng Pilipinas (BSP)

The Vista Land Group allotted P21.6 billion for its capital expenditures in 2014 given its massive expansion around the country. Its popular Camella brand has been providing houses-and-lots all over the country, and is typically the first mover in tertiary cities. More importantly, this Group is beefing up its Starmall Prima and Starmall Strip brands. It is currently operating Starmall Alabang, Starmall EDSA-Shaw, Starmall Las Piñas and Starmall Annex. It intends to expand its Starmall Prima in Taguig, Bacoor-Cavite, and Sta. Rosa-Laguna. The Starmall Strip is projected to open 22 branches by 2017. Thai mall developer Land & House is the foreign partner of Vista Land Group, and owns 11% of Starmalls.

In addition, the Villar Group is aggressively expanding its offices, malls and hotels businesses as part of its transformation into a complete real estate company. As a strategy, the Vista Land Group will be putting up BPO offices in their Starmalls.

Filinvest Land has earmarked Php 20 billion for its programmed spending this year, which includes at least Php 8 billion for residential development of residential projects. Apart from the residential segment, it is expanding its Festival Supermall River Park and as well as its hotel platform with the operation of Crimson Hotel. The Filinvest Group entered into a joint venture with the Singaporean-firm Archipelago International Pte. Ltd. (AIPL) for the formation of FilArchipelago Hospitality, Inc. (FHI). AIPL is an affiliate of Aston International, which manages hotels, resorts, residences, spas and villas under Crimson and other hospitality brands.

SNAPSHOTS

SECTOR	TREND	COMMENT
OFFICE	▲	Strong demand, sustained low vacancy, and slight rental increase
RESIDENTIAL	▲	Rents and prices for luxury residential remains high; socialized and affordable segment is underserved; mid-market is competitive, budding rental market
RETAIL	▲	Big players are expanding into various retail platforms and acquiring smaller players; rents are stable
HOTEL & GAMING	▲	The gaming industry is fuelling the influx of international brands; local players have been operating their own brands in secondary locations
INDUSTRIAL	▲	Occupancy has been increasing as more investments in manufacturing have been coming in, decline in available industrial spaces

FHI currently operates two hotels under the 5-star Crimson brand, one in Mactan, Cebu and another in Filinvest City, Alabang, and one hotel under the 3-star Quest brand in Cebu City. FHI is also responsible for managing the Grand Cenia Condotel and Residences in Cebu, and its Entrata Complex in Alabang, and the Crimson Resort and Spa in Seascapes Resort Town in Cebu.

Robinsons Land sets a budget of Php 16 billion as CAPEX for this year. This would go to the expansion of its shopping malls and hotels, mixed-use properties such as office buildings, residential condominiums, as well as land and residential housing developments in key cities and other urban areas nationwide. It has embarked on socialized housing projects in recent years as well. The Robinsons Group has years of experience in exploring various platforms and asset classes, including the creation of its local brand “GoHotels” in clear contrast to its partnership with Crown Plaza and Holiday Inn.

Rockwell Land Corp. of the Lopez Group has allocated Php 10 billion for its CAPEX this year, which 25% higher than last year. Rockwell is ramping up its first venture into the hotel and leisure business, Aruga Serviced Apartments. It is within Edades Tower, occupying six floors—from the third to the eighth floor, and is located within the Rockwell Center complex in Makati City. Aruga will offer 114 units for occupancy. Rockwell is targeting two other serviced hotels under the Aruga brand, one in Ortigas in Metro Manila, and another in Cebu.

The listed holding company of tycoon George Ty-Metrobank Group, GT Capital Holdings Inc., has set a capital expenditure budget of nearly Php 40 billion this year, mainly to expand its power generation and

real estate businesses. Federal Land Inc., its real estate development arm, is allocating Php 12.81 billion to develop residential, commercial and retail projects, as well as to finance land banking initiatives.

DMCI Holdings has allotted at least Php 20 billion for its CAPEX this year. Majority of that, Php 15 billion, is intended for its power plant expansion and the remaining Php 5 billion is for real estate. It is a known fact that the cash cow of the DMCI Group is its mining unit Semirara Mining Corp. DMCI Group is aggressively expanding its power plant portfolio with two 350MW plants. Being one of the largest real estate contractors in the past, the Php 5 billion expansion in real estate development is a testament to its commitment to provide quality and affordable housing units.

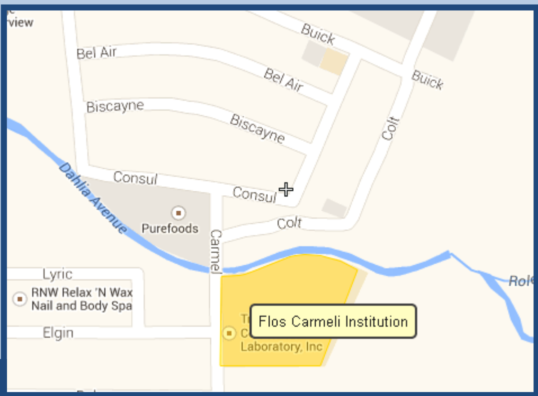
Cosco Capital, Inc., the listed holding firm of Lucio L. Co, more than doubled its CAPEX this year to around Php10 billion from Php 3.5 billion last year. Around Php 3 billion will go to its popular retail arm Puregold Price Club, Inc., which will open 25 additional stores this year. It also recently completed its Divisoria 999 Shopping Mall and a commercial building at the Fairview Terraces, joint project with Ayala Group.

S&R Membership Shopping, which currently has eight warehouse stores, opened stores in Davao City and Shaw Boulevard in Mandaluyong City last year, running ahead of its customary pace of one store a year.

Plans are underway for the development of its 2.3-hectare property in Urdaneta, Pangasinan, on which the first of its three community malls will rise. Cosco is also in talks for the acquisition of land in Laguna and Nueva Ecija for the two other malls, which will carry the brand Cosco Mall.

The Group recently partnered with the Japanese convenience store group Lawson, Inc. The partnership will open 20-30 stores this year, which will eventually accelerate to 80-100 stores annually in the succeeding years, with a 500-store target by 2020.

PROPERTIES FOR SALE



LOT WITH IMPROVEMENT Fairview, Quezon City (FORMER FLOS CARMELI INSTITUTION)
Carmel St., Regalado ave., West Fairview, Quezon City (Near FEU Hospital)
Lot Area: 14,066 sqm
Classified as medium density residential zone, previously used as school
Asking Price: PHP175,825,000

VACANT LOT Porac, Pampanga
Barangay Planas, Porac, Pampanga
Lot Area: 1,445,156 sqm
Located on the west side of Subic-Clark-Tarlac Expressway (SCTex) about 900 meters north east from Floridablanca Interchange, currently undergoing construction, approximately 10 kilometers southeast from Porac town proper, about 20 kilometers southwest from Diosdado Macapagal International Airport.
Asking Price: PHP500 per sqm

Bulk of the CAPEX is also intended for strategic acquisition such as the recently acquired NE Pacific Shopping Centers Corp., the largest mall operator in Cabanatuan City, Nueva Ecija; and the Office Warehouse chain, which has 47 stores.

Its wine and spirits business is projected to have double-digit growth this year, as the Group entered the low-priced imported segment with the launch in November 2013 of Spanish brand Excelente.

Cosco Capital, Inc., formerly known as Alcorn Gold Resources Corp., has 51% stake in Puregold, as well as 100% stakes in various commercial property developers and liquor distributors, and in oil storage company Pure Petroleum Corp, and mining. Its real estate units are Ellimac Prime Holdings, Inc., Fertuna Holdings Corp., 118 Holdings, Inc., Nation Realty, Inc., Patagonia Holdings Corp., and Pure Petroleum Corp. Other subsidiaries in the wine and spirits segment are Meritus Prime Distributions, Inc. and Montosco, Inc.

Lucio Tan's Eton Properties Philippines, Inc. is allotting Php 10 billion for its capital expenditures for the next two years to support its plans to focus more on generating recurring income rather than real estate sales. Eton currently has an inventory of 90,000 sq.m., with its five office buildings, with a sixth building, Eton Cyberpod Three, under construction bringing it to 156,000 by the end of the year. In the next two years, Eton will add another 60,000 sq.m. of leasable space, which is in accordance with Eton's thrust of targeting BPO industry and beefing up recurring income. Eton intends to complete six more office towers in Eton Centris in Quezon City by 2017.

Century Properties Group, Inc. (CPG), known for its flashy brands and products, earmarked Php 8 billion CAPEX this year as it unveils more projects and diversifies its portfolio. It recently opened its Century City Mall in Makati, and is building its office tower in Century City named as Century Spire. CPG is also unveiling its first tourism-related project this year, a hotel-serviced-apartment.

BUILDING EDSA, Quezon City
Along EDSA near GMA and Kamias
Lot Area: 1,442 sqm.
Floor Area: Approx. 16,000 sqm.
10-storey building with 2 basement parking
Asking Price: PHP420 Million
For Lease: PHP4.5 Million per month

BUILDING EDSA, Quezon City
Along EDSA near GMA and Kamias
Lot Area: 1,400 sqm.
Asking Price: PHP140,000 per sqm
(Net to seller)

The Group is also launching its 8-hectare, Php 20-billion, mixed-use development "Azure North" project in San Fernando, Pampanga, that boasts of the second "Paris Beach Club" with Paris Hilton designing it.

Another maverick developer is ABOITIZLAND Inc. which increased its CAPEX this year to Php 5.4 billion, a 35% rise from 2013 as it sets its sight on expanding nationwide. The Aboitiz Group is well known in the Visayas and Mindanao, and even partnered with other players such as Ayala Land in recent years. Nonetheless, AboitizLand is committed to enter the market nationally where more than half of the CAPEX budget is allocated for residential development, while the rest will go to industrial and commercial projects.

More importantly, AboitizLand is expanding its industrial offering in Batangas and Davao City. Further, the Group has been actively bidding in toll-roads, and other infrastructure projects such as airports and power plants.

The next two developers, Landco and Sta Lucia, are known for horizontal projects, and decades of experience. It is noteworthy that they are diversifying their offerings.

Landco Pacific Corp. (Landco) is allocating a CAPEX of Php 9 billion for the next five years to fund its expansion in upscale leisure and horizontal residential development. Its projects are Tribeca Private Residences in Sucat, Muntinlupa City; Playa Azalea in Samal, Davao del Norte; Nautilus, the first tower of its upcoming seaside condominium development called Playa Calatagan Residences. Three buildings are set to rise in Playa Calatagan Residences. Landco's beach resort amenity, Aquaria, is expected to rise in Calatagan, Batangas.

Sta Lucia Land Inc. (SLI) raised its CAPEX to Php 2 billion from Php 1.35 billion last year as it plans to launch 20 new projects. It is acquiring properties in Laguna, Batangas, Cavite, Rizal, Davao, among other places. Sta Lucia is also expanding its existing mall that will add a gross floor area of over 50,000 square meters to the existing shopping center's 180,000 sqm. SLI's other investments include a 12 percent stake in Philippine Racing Club

Inc., a horse racing operator and the joint venture partner of Ayala Land Inc. in Circuit Makati.

OFFICE MARKET

The Business Process Outsourcing (BPO) industry continues to drive the demand for office spaces in Metro Manila as well as the entire Philippines. Key industry players are projecting an additional of approximately 120,000 employees this year, and probably breaching the one-million mark, and to generate a total of US$ 18 billion revenue. In 2004, the BPO industry had only 100,000 employees and generated about US$ 1.55 billion of revenues.

With this strong demand, even with the introduction of new office buildings with a total leasable area of 400,000 sqm, such as Cyberpod Centris North and South Towers, CityNet 1, and V Corporate Center, RCBC Savings Bank Corporate Center, 8 Campus Place Tower 3 (Wells Fargo Center), and others; rents are expected to be stable and may even increase slightly. Many of these buildings are pre-committed and have signed up lease contracts even prior to completion. Vacancy of Premium Grade A and Grade A buildings is projected to stay below 5% across the major business districts by end of the year. Rents in Premium Grade A shall continue to command rates hovering around Php 1,100 per sqm per month, while rents in Grade A have an average of Php 765 per sqm per month. Small and old buildings in Makati are offering rents at an average of Php 550 per sqm per month.

RESIDENTIAL MARKET

The ongoing handover of various housing and condominium units to the individual buyers this year would show the depth of the residential market. Mid-market and affordable residential units are typically for “end-use”, although there is a marked sales pitch of “investment opportunity” in recent years.

In the past, only the high-end and upper-mid market segments have strong leasing activities. This will continue with rents between Php 50,000 to Php 100,000 per month for upper-mid condominium units, while rents of above Php 100,000 per month for high-end, depending on the sizes. Luxury condominium units would command rents north of Php 250,000 per month.

Given the low savings rate of the banks, condominium units have been marketed as investment opportunities with projected rental yields of 5-8%. The budding dilemma of the overseas Filipino buyers, who comprise a significant segment, is that they would typically want to use their units anywhere between one to six months when they are staying in the country, and only lease out their units when they are abroad. This would obviously impact on the potential income of their units, as well as the challenge of findings tenants during their “abroad time”. Some developers have been offering “serviced residences/units” or condotel operations to address this pattern.

The affordable and socialized segments are still underserved. It is noteworthy that the big players have been active in building in this segment, instead of just partnering with smaller players to comply with the 20%-socialized housing component as required by the Urban Development and Housing Act.

RETAIL MARKET

The retail market is still dominated by the big players. In recent years, there were a number of strategic mergers and acquisitions. The last quarter was dominated by the Puregold-Cosco Group, with its acquisition of the Office Warehouse, NE Pacific Shopping Centers Corp., and partnership with the Japanese-retailer Lawson Inc.

Major retailers still enjoy high lease rates and occupancy levels, as the economy and population continue to grow. Malls are generating the highest yields in the property market. To take advantage of the propensity to spend of the Filipino shoppers, major developers and niche players have been introducing various retail platforms.

HOTEL AND GAMING MARKET

Visitor Arrivals for the first four months reached 1.697 million, which is 2.85% higher than the same period last year that is touted as record-breaking. The gaming industry has been very active in attracting visitors to fill up their casinos. The major chunk of the hotel rooms that would be operation this year are in the PAGCOR Entertainment City area, such as Belle Grand-City of Dreams, Radisson Hotel and Tune Hotel. The City of Dreams is expected to be opened any time soon consists of 920 rooms.

In terms of room rates, five star hotels will continue to charge north of US$ 300 per night on the average. Four star hotels have breached the US$ 250 rate on the average. Existing hotels have been enjoying increasing rates due to record-breaking tourist arrivals the past years.

INDUSTRIAL MARKET

The manufacturing sector's growth of 10.5% in 2013 and 5.4% 2012 in 2012 is a testament to the revival of the industry. As earlier reported, even the massive Clark Special Economic Zone (Clark) and Subic Bay Freeport Zone (Subic) have a combined available industrial space of only 150 hectares by end 2013. Recently, it is reported that a Singaporean company will invest Php 7 billion for mixed-use development projects in a three-hectare area inside the Clark.

In an agreement with the Clark Development Corporation (CDC), Capilion Corporation Pte Ltd. said the mixed-use facility would be used for business process outsourcing, residential, commercial and retail companies. This is the biggest contract to be signed in recent years with a projected job generation of 75,000 in seven years. The Singapore firm presented to CDC a demand draft totaling US$4.9 million or approximately P215 million representing the corporation's advance lease, security deposit and performance security plus reservation for another 8,639 square meters adjacent to the property.

Based on reports, Taiwanese groups led by TECO Electric have proposed a US $250 million "Software Park" in either Subic or Clark to house IT companies, which are interested to locate in the Philippines. The proposed US$250 million Software Park will cover an initial land area of 15 hectares in Clark or Subic and is expected to employ a maximum of 21,000 people, and would generate a total revenue of US$10 billion worth of economic activities from rents, revenues from locators, and allied services.

In La Union, the Bases Conversion and Development Authority (BCDA) is set to bid out 14-hectare Phase 1A of Poro Point Freeport Zone, dedicated as industrial zone. Phase 1B is also industrial zone with an area of 70 hectares. The master plan for the development of the Poro Point Freeport Zone in San Fernando, La Union was approved by the BCDA last October. The entire Poro Point Freeport Zone has a total area of 146 hectares.

INTEGRATION

The top developers do not show any sign of slowing down, in fact they are even accelerating given their capital expenditure outlays. Likewise, foreign companies have been investing in the Philippines, especially with the recent rating upgrade of the Philippines to investment grade. It is noteworthy that investments are coming not only from the traditional partners of the Philippines like the US and Japan. Investments from Singapore and Thailand consist of the typical financial transactions, as well as operational integration in recent months.

It is also clear from the positioning of the top players that they are integrating their products and platforms to take advantage of the boom market, as well as the forthcoming ASEAN economic integration. Most of the players are exploring various market segments and asset classes to generate growth. As mentioned, most of the big players have teamed up with international and ASEAN partners, creating synergies and opportunities well ahead of the December 2015 integration.

ABOUT PINNACLE

Pinnacle Real Estate Consulting Services, Inc. provides a full range of services to buyers, real estate lenders and investors.
A team of experienced professionals is dedicated to enhancing the value of clients' investments throughout the Philippines.

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Asset Administration
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-Inspection
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-RPT Payments
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Performing Loan Collections
Structured Loan Management and Analytics

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