

Philippines Real Estate Report Q3 2012

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Abstracts

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The Philippines real estate sector is on the up. After a year of outperformance in 2011 and a strong start up until Q112, the outlook for the remainder of 2012 is looking increasingly rosy.

Since our last quarterly update, we have seen a number of positive developments in the sector. Energy World Corporation (EWC) and its partners InterOil and Pacific LNG Operations have announced plans to establish a liquefied natural gas (LNG) terminal and a natural gas power plant in Quezon, the Philippines. In February 2012, the Philippines National Economic and Development Authority (NEDA) Board announced that it had approved three new road construction projects. Next up the Philippine Department of Trade and Industry has announced that two seaports in the province of Davao del Norte are to be expanded. Hijo Resources will expand the port at Tagum City, with the project complementing its ongoing PHP50mn (US\$1.17mn) construction of six villas and six casitas adjacent to the site, while San Vicente Terminal and Brokerage Services will in turn develop a PHP2.7bn (US\$63mn) container handling facility at Panabo City. What is more, a number of the sector's leading local players have also won new construction contracts over the past three-month period.

More broadly speaking, a recent pledge by the Philippine government to boost infrastructure spending throughout the remainder of 2012, as well as to improve monetary conditions suggest that a sustained uptick in construction activity is on the cards in the short- to medium term. This will surely have positive repercussions for the industry, in the form of increased demand and most importantly a spur in supply. As a result, we recently revised upwards our forecasts for the Philippine construction sector, with real growth expected to reach 6.5% in 2012 (up from the prior forecast of 5.7%). Beyond 2012, we believe that construction activity in the Philippines could improve

further still, with real growth for the sector forecast to average 7.5% per annum between 2013 and 2016. Within this, we see rents in H112 remaining at their H211 levels for all cities, which while not as high as 2011's peaks, is healthy on 2010 levels.

Improvements in H212 can be expected as government spending starts to bear fruit and trade begins to find a stronger footing. The same can be presumed for yields, which we see ultimately remaining buoyant at healthy levels for all cities.

What is more, BMI believes that 2012 could well be the year when the much-touted Public-Private Partnership (PPP) scheme takes off. There are as many as 13 infrastructure projects in the initial phase of the PPP programme, which are all set to complete their tendering process before the end of 2012. These projects would require time to reach financial closure, as well as complete land acquisition and equipment procurement procedures.

BMI cautions, however, that there may be a bump in the roadmap towards ongoing growth in the sector.

And that bump comes in the form of the present macroeconomic backdrop. Given the government's continued inability to promote growth-positive initiatives, we continue to see the Philippine economy growing well below potential over the medium term. Our forecast for 2012 headline GDP growth remains a lacklustre 3.9%, as private consumption continues to lead the way forward in the face of weak exports, and is a standout bright spot in the Philippine economy. Overall consumption should expand by 5.0% in the year as consumer spending continues to be supported by strong remittances and government consumption accelerates after not growing at all in 2011. The outlook for exports remains challenging with key trade partners China, Japan, the US and eurozone all set for weaker growth that will likely keep a lid on demand for Philippine products. Still, following a year in which total exports fell by 4.2%, we do see the sector bouncing back into expansionary territory with modest 2.2% growth. In particular, we will be keeping an eye on electronics exports, which make up nearly 50% of total exports and put in a particularly weak performance in 2011.

Some of the key opportunities in the real estate market are:

The Philippines is one of the fastest-urbanising countries in East Asia. With an English-speaking and relatively low-cost workforce, it is ideally placed to participate in high-demand services such as business process outsourcing.

Many residents of cities in the Philippines continue to experience poverty, environmental degradation and live in slums or other inadequate housing arrangements. Economic development has created rural-to-urban migration.

Some key risks to the real estate market are:

Political unrest in the Middle East and North Africa causing a decline in overseas remittances.

Economic difficulties in the US and eurozone, and commodity price fluctuations, pose risks to private consumption growth.

Despite President Benigno Aquino III's pro-foreign direct investment (FDI) policies, the changes in the law affecting REITs mean developers that had planned to set trusts up have stopped. In August 2011, mall developer SM Prime Holdings dropped its plans to raise US\$500mn via a REIT and Ayala Land dropped its plans to raise US\$400mn following the tax rises by the BIR and the tax agency.

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