Sperry Van Ness
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INDUSTRIAL Market Outlook

Consumer demand for same-day delivery has changed the way retailers look at distribution. In order to minimize the distance required to ship goods from a warehouse to the customer, sellers are establishing multiple distribution centers across the country, each located in or near a major population center that it serves. The need for highly efficient, modern industrial space has inspired developers to build millions of square feet in those densely populated markets, generally meeting only a portion of the growing demand for these mega centers. Ideally, distribution centers should be proximal to the markets they serve, but a scarcity of vacant tracts in places like Los Angeles tends to push new construction to the perimeter or to nearby, developing markets like the Inland Empire. In town, much of the existing industrial stock may be functionally obsolete due to low ceilings and other restrictions, but some markets may offer opportunities to replace older warehouses with modern product. The pending opening of an expanded Panama Canal is putting additional pressure on port markets that hope to capture a portion of the international trade carried by shipping companies operating the largest container ships. Houston, Miami, Port Everglades, FL., Port Newark, NJ and other major seaport operators have been racing to complete dredging and infrastructure improvements that will clear the way for massive container ships. The Gulf and East Coast ports that do secure shipping agreements will undoubtedly see increased demand for distribution centers as the Canal's completion in 2015 approaches, but some promoters may be overstating prospective container traffic volumes. On the West Coast, port authorities are also completing upgrades in hopes of retaining trade volumes. Finally, manufacturing is making a surprising comeback in some U.S. markets, owing to a combination of low U.S. energy costs and increasing labor costs in China.

ATLANTA, GEORGIA

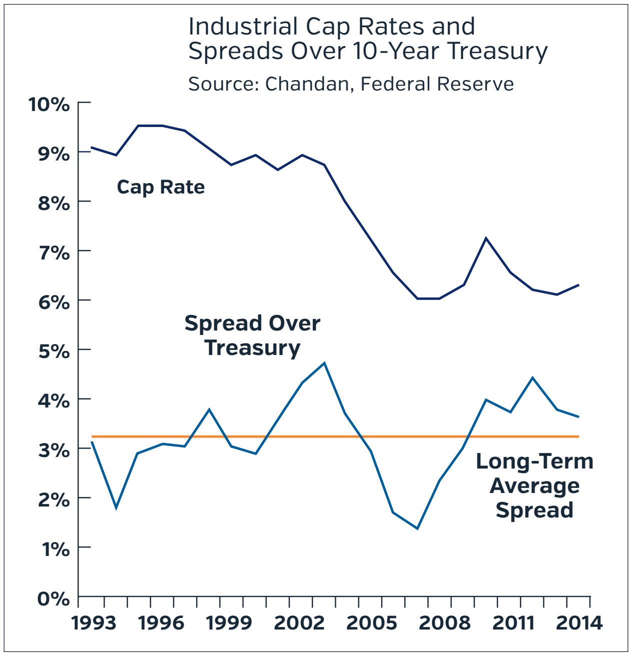
Construction pumped more than 4.5 million square feet of new space into Atlanta's industrial market in 2013, the largest addition since 2008. Build-to-suits accounted for more than three-fourths of the new space, however, and the additional speculative construction paled in the face of ravenous demand. Absorption hit a post-recession high of nearly 11 million square feet, driven chiefly by small and midsized companies. The vacancy rate plummeted 120 basis points from the previous year to end 2013 at 12 percent. The surge in construction and an increasing average rental rate both reflect the difficulty that tenants face in seeking modern, well-located space for growth. Although massive deals such as Home Depot's 1.3 million-square-foot e-commerce center and a 1 million-square-foot project for Procter & Gamble tend to dominate Atlanta's real estate headlines, investors will find numerous opportunities catering to the small and midsized businesses that accounted for nearly 80 percent of the market's industrial absorption in 2013.

10 INDUSTRIAL MARKETS TO WATCH

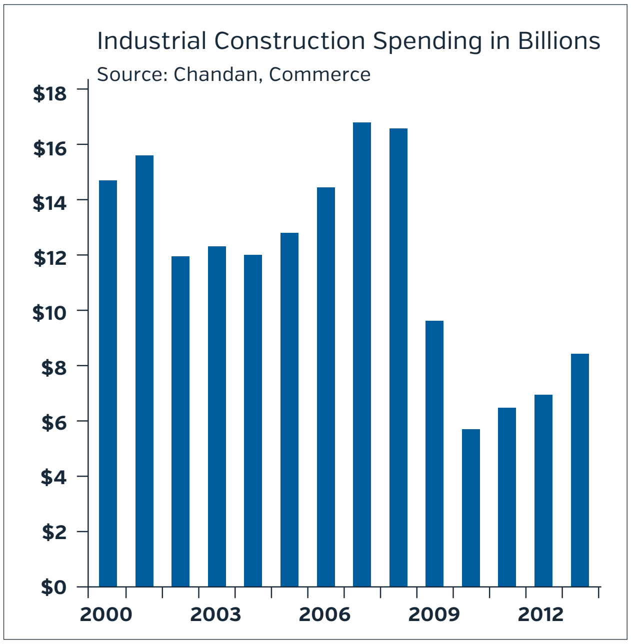
- ATLANTA
- INLAND EMPIRE
- LOS ANGELES AND LONG BEACH
- MIAMI AND PORT EVERGLADES
- NORTHERN NEW JERSEY
- PHILADELPHIA
- SEATTLE AND TACOMA

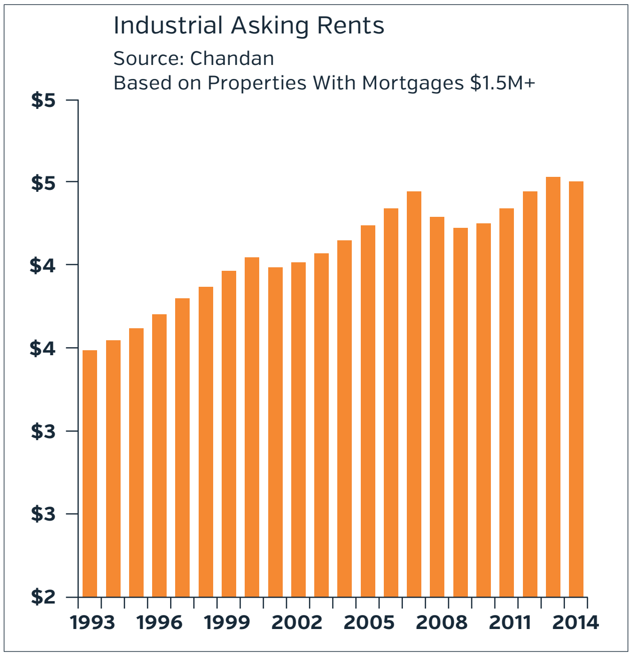
Key Industrial Market Trends in 2014

Industrial property cap rates increased slightly in mid- and late-2013, responding to the abrupt upward adjustment in broader interest rates. As of early 2014, the spread between industrial cap rates and the 10-year Treasury yield was close to its long-term average level. Logistics properties are bucking the trend, however, with cap rates declining over the same period.



Rental and occupancy rate trends have diverged for modern, well-located assets and other properties in less desirable locations. The overall trend shows a slight decline in rental rates, owing to large drops for functionally obsolete spaces. In urban areas and along logistics channels, rent trends will build momentum as the economy improves.





Industrial property development has been restrained for several years, dominated by build-to-suit construction for specific tenants. The thin pipeline and lag in new deliveries will support higher occupancy and rental rates.

INLAND EMPIRE, CALIFORNIA

Demand is mushrooming in this vital industrial market. Companies absorbed nearly 15 million square feet of space in 2013, almost double the roughly 8 million square feet of absorption in 2012. Construction introduced almost 6 million square feet of new supply in the past year, and another 16 million square feet are nearing completion in 2014. Users have already committed to more than a third of the buildings currently under construction. The Inland Empire's vacancy rate of a little more than 4 percent, although tight, offers greater flexibility and lower average lease rates than users can find closer to the ports of Los Angeles and Long Beach. Developers are depending on those competitive advantages to help lease the tremendous volume of new space in the works. As new projects come online, however, the average lease rate of will increase, narrowing the rent rate differential that has helped to offset the added cost of transporting shipped goods between the ports and distribution centers in the Inland Empire.

LOS ANGELES AND LONG BEACH, CALIFORNIA

Moves by two shipping companies from the Port of Los Angeles to the Port of Long Beach in late 2012 contributed to an 11.3 percent year-over-year increase in cargo traffic at Long Beach in 2013, while LA's volume for the year declined by only 2.6 percent. The twin ports have invested billions of dollars in capital improvements to avoid losing shipping volume to East Coast ports following the opening of the expanded Panama Canal in late 2015. Nearer on the horizon, the West Coast longshoremen's labor agreement will expire in June 2014, bringing elevated risk levels for port-related industrial users until the sides forge a new agreement. Nearly four years of positive absorption have filled portions of the Los Angeles Basin industrial market, with a vacancy rate of less than 3 percent in the San Gabriel Valley, Central L.A. and the South Bay submarkets. Other submarkets offer only slightly more vacancy, with Orange County topping the list at just over 4 percent. Average rents have been on the rise since the first quarter of 2011 and now top 50 cents per square foot in most submarkets, with landlords in the South Bay and Orange County quoting rent of 60 cents or more per square foot. More than half of the developed space in Los Angeles County and Orange County is 20 years old or older, creating some redevelopment opportunities, while a dearth of large, Class A distribution buildings is accelerating rent growth for that segment. Development activity is brisk with more than 20 million square feet under construction, but is unlikely to fully satisfy the growing demand for industrial space due to the limited availability of buildable sites and a faster pace of absorption.

MARKETS TO WATCH

NOT THE LARGEST or the most actively contested markets, the 2014 Industrial Markets to Watch are each at an important juncture that presents unique opportunities for investment. Together, they reflect the diversity of trends that is driving the economy and commercial real estate performance in markets across the country.

MIAMI AND PORT EVERGLADES, FLORIDA

As a gateway to Latin America and the Caribbean, Miami's port and intermodal hub is a center of growing demand for modern industrial space. Miami's overall vacancy rate of 6 percent is down almost 100 basis points from a year ago, but with 1.5 million square feet added to the market in 2013 and a similar amount under construction, monthly rents have been flat at around 70 cents per square foot. The Port of Miami is investing $2 billion to service the largest container ships that will pass through the expanded Panama Canal when it reopens in late 2015. Improvements include dredging channels to a depth of 52 feet, installing massive dock cranes, and building a tunnel under Biscayne Bay to connect the port with nearby highways. Heated transaction volume has compressed cap rates on assets around the port to near 6 percent. Port Everglades, on the other hand, may present interesting opportunities for acquisition or development. Located 23 miles from Miami in Fort Lauderdale, Port Everglades handled approximately 1 million ten-foot equivalent units (TEUs) of containerized goods in 2013, trumping the Port of Miami's volume by 50,000 and making Everglades the state's busiest cargo port. The port is dredging its channels to a depth of 50 feet to handle larger ships, and an intermodal container transfer facility under construction will soon enable ships to unload cargo directly onto railcars.

NORTHERN NEW JERSEY, NEW JERSEY

Following a net contraction in 2011, industrial absorption turned positive in 2012 and then increased fourfold last year, amounting to almost 2.5 million square feet. Users have steadily soaked up available space, pushing the vacancy rate to approximately 7 percent in early 2014. Monthly rents have risen modestly in each of the past several quarters and averaged about 50 cents per square foot at the start of this year. More than 1.6 million square feet of new space is under construction, five times the amount of space added in 2013, as developers bet that the opening of a widened Panama Canal in 2015 will boost cargo volume through the ports. Demand for high-quality warehouse space in the East Coast's largest port complex is growing, but infrastructure investments in Baltimore, Virginia and elsewhere have enabled those markets to complete for shipping volume from New York and New Jersey. The local ports are making ready to handle the largest container ships by increasing channel depths, adding intermodal hubs and raising the Bayonne Bridge by 65 feet. The port's proximity to the densely populated North East makes it an ideal point of entry for consumer goods and gives investors good prospects for stable asset values.

PHILADELPHIA, PENNSYLVANIA

The Philadelphia industrial market has been overshadowed by peers with more rapidly accelerating growth in the by its faster-growing peers but to its advantage, the market's fundamentals remain largely unchanged and stable in 2014. Philadelphia County's more than 360,000 square feet of absorption in 2013, in the absence of major construction, helped to push down the industrial vacancy rate to near 8 percent, on par with the Philadelphia suburbs and lower than the vacancy rates in most of the region's other markets. Companies seeking space for their own use have taken out more buildings here in the past few years than those leasing space. The population count has decreased by more than 14,000 since 2008 but is back on a moderate growth track. Investors that see Philly's lack of growth as stagnation may be willing to sell at attractive prices, and those sellers will find potential buyers attracted to the market's incrementally improving industrial fundamentals.

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SEATTLE AND TACOMA, WASHINGTON

Seattle's port handled 3 million TEUs of containerized cargo in 2013, placing it among the nation's top five ports for finished goods. The port is PPMX-ready, meaning it has the required channel depth and cranes to handle the largest, fully loaded cargo ships that will be in common use following the reopening of the expanded Panama Canal in 2015. The nearby Port of Tacoma, too, has been PPMX-ready since 2011, after having dredged its channels to the necessary depth and adding massive gantry cranes. Tacoma's containerized cargo volume has surged to more than 1 million TEUs per year as a result, and helped to fuel additional demand for industrial space. Falling market-wide vacancy is nearing 5 percent and demand for space is generating build-to-suits as well as accelerating absorption, which spiked to 1.5 million square feet in the fourth quarter of 2013 alone. The market added more than 1 million square feet of new space in 2013 and has more than twice that amount under construction. A strong employment base, rooted in energy and technology and enjoying a boost in aerospace manufacturing, has helped Seattle to more than recover the number of jobs it lost in the Great Recession. Projected household growth near 5 percent bodes well for the market's distribution centers. While the newly refitted Port of Tacoma is expanding its market share of cargo traffic, Seattle is also feeling increased competitive pressure from Prince Rupert, a Canadian seaport in British Columbia that is also PPMX-ready following recent upgrades to its facilities.

Noteworthy
DETROIT, MICHIGAN

A steady recovery since 2009 has soaked up available industrial space in the Motor City, driven not only by automakers and their suppliers but by major expansions in textiles, furniture production, food and beverage suppliers and regional distribution operations. With an occupancy rate above 90 percent and rental growth accelerating, the first significant speculative construction of the recovery cycle is underway at the corner of Broadmoor Avenue and 36th Street. The 43,000-square-foot building adds to a wave of construction and expansions that began in owner-occupied buildings. Investors are buying up well-located development sites and a ramp-up in industrial construction appears imminent. Lenders remain cautious, however, frequently demanding as much as 50 percent equity on mortgages for industrial properties. That gives equity-rich investors a strong advantage in vying for properties and developable sites.

IT'S A DIFFERENT WORLD OUT THERE.

It requires a different kind of commercial real estate firm working on your behalf in order to be successful. The Lipsey Company has ranked the Sperry Van Ness® organization as one of the most recognized commercial real estate brands in the US for a reason–we know how to deliver a certainty of execution for our clients. Sperry Van Ness International Corporation is one of the largest commercial real estate franchisers with more than 180 locations in 200 markets.

TOP TRENDS AND MARKETS TO WATCH REPORTS

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Industrial Trends and Markets to Watch

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Retail Trends and Markets to Watch