February 2017

Americas Industrial & Logistics Trends Report

Summary

Despite some global and domestic economic uncertainty, the industrial real estate market continues to expand in most parts of the Americas.

- User demand in the Americas industrial & logistics market slowed slightly in Q4 2016, down from near-record highs earlier in the year.
- Although net absorption in the U.S. decreased both quarter-over-quarter and year-over-year, the vacancy rate fell by 10 basis points (bps) to 4.9% and availability was flat at 8.2%. As has been the case each quarter since Q3 2010, leasing demand (as measured by net absorption) outpaced new construction, though the gap between the two has narrowed considerably.
- As a result of the tight supply, the net rent index increased by 1.5% in Q4 and 6.6% year-over-year to $6.14 per sq. ft. —the highest level since CBRE began tracking this metric in 1980.

- The Canadian markets have become bifurcated with record-low vacancy rates in Toronto and Vancouver being offset by rising availability rates in markets like Calgary and Edmonton.

- Latin America has seen a similar pattern with the core Mexican markets showing strong user demand and positive fundamentals, while the Brazilian markets have experienced a slowdown in leasing, resulting in rising vacancies and declining rents.

Perspectives

This report reflects current observations and sentiments from more than 950 CBRE Industrial brokerage and investment professionals in the Americas.

U.S. TENANT / USER PERSPECTIVES

- E-commerce, third-party logistics and food & beverage tenants continue to dominate user demand in most markets.
- With extremely low unemployment rates across the U.S., occupiers are concerned about the availability and cost of labor. Access to high-quality and dependable labor has become a major factor in location decisions.
- There have been 27 consecutive quarters of positive net absorption, pushing occupancy to 95.1%—the highest level since CBRE Econometric Advisors began tracking this metric in 2002.
- Class-A distribution space has become extremely tight, with many markets reporting less than 2% vacancy in this segment.
- Activity in smaller light industrial infill properties has increased as users look to add a last mile element to their supply chain.

U.S. LANDLORD / OWNER PERSPECTIVES

- New development totaled 49.6 million sq. ft. in Q4 2016, down 9.1% from Q3 and 2.0% from Q4 2015.
- Deliveries are expected to increase in 2017, with 198 million sq. ft. under construction in Q4. While deliveries and under-construction totals continue to rise, oversupply is not a near-term concern because vacancy rates are at all-time lows in many key markets and users are actively looking for new space.
- Due to the unique needs of large e-commerce and distribution users (higher clear heights, excess car and truck parking, and increased power), Class-A big-box supply has become extremely tight. Speculative construction has become common, representing the majority of new deliveries and projects under construction in most of the key distribution markets.

U.S. CAPITAL MARKETS PERSPECTIVES

- U.S. industrial investment totaled $17.3 billion in Q4, the highest quarterly volume of 2016 and bringing the full-year total to $59.2 billion—the second highest since 2007, but 24% below 2015's record levels.
- 2016 was the strongest year on record for individual asset acquisitions, totaling $41.3 billion—a 7% increase from 2015.
- The overall decline in volume from 2015 was attributed primarily to a smaller number of megadeals, measured by portfolio and entity-level transaction volumes totaling $17.9 billion—down 55% from the prior year.
- The flex segment of the market grew 7% year-over-year on sales of $18.6 billion, while deal activity in the warehouse segment posted a 33% year-over-year decline on sales of $40.6 billion.
- Investors continued to prefer major markets in 2016, which accounted for more deal volume than did non-major metros.
- 2016 deal volumes reached all-time highs in five large markets: Miami/Dade County, St. Louis, Westchester County, N.Y., Denver and New York City.
- Los Angeles had the highest level of investment with $4.4 billion in 2016, followed by Chicago

U.S. CAPITAL MARKETS PERSPECTIVES (CONT.)

($3.5 billion), Dallas ($2.5 billion), Seattle ($2.3 billion) and San Jose ($2.3 billion).

- Industrial acquisitions by foreign investors totaled $3.4 billion in 2016, the second highest year on record after 2015's record levels. Cross-border activity increased by 72% between Q3 and Q4. Canada, China, Singapore, Switzerland and Germany were the top five sources of inbound capital.
- Industrial sales prices rose 14% year-over-year, according to preliminary estimates of the Moody's RCA CPPI (index based on repeat-sales transactions). Despite rising interest rates in Q4, cap rates rose marginally by 20 bps—a trend corroborated by CBRE's H2 2016 Cap Rate Survey. Average cap rates for the year were 6.8%.
- Industrial was the only property sector with double-digit annual total returns in 2016 (12.3%) and outperformed the overall NCREIF Property Index.

REGIONAL PERSPECTIVES

U.S. NORTHEAST AND MID-ATLANTIC REGION

- **Pittsburgh:** Significant new supply was added to the market in 2016, which pushed the vacancy rate up 40 bps to 7.6%. However, development is expected to slow in 2017, which should push up rents and lower the vacancy rate. High-tech robotics and energy users are notably active.
- **Harrisburg:** Going into 2017, users are looking very carefully at the labor pool before making any decisions. Occupiers in high-headcount industries and those with seasonal surges are reporting rising costs and difficulty in hiring.
- **Lehigh Valley:** Large users continue to flood the market, showing preference for new development but also leasing several properties that have had long-term vacancies. Occupiers currently seeking space include food & beverage, tire, retail, e-commerce and logistics companies. Land is scarce and is selling for $20 to $30 per sq. ft., which will put pressure on new development.
- **Northern New Jersey:** Users seeking locations near Port Newark have driven demand for Class-B space and have pushed rents in this segment up nearly 25%. Food & beverage companies, in particular, are seeking this space.

U.S. SOUTHEAST REGION

- **Charleston:** The Port of Charleston's growth has brought a variety of users to the market, particularly those in the automotive, logistics and petroleum industries. The growing auto manufacturing sector is expected to draw new parts suppliers and distributors to the market.
- **Miami:** The market has seen 18 consecutive quarters of positive net absorption, which has lowered the vacancy rate to 3.0%. Deal velocity has been strong, with almost 200 transactions in Q4 2016. However, deal size is somewhat small relative to other Tier I markets, with only three tenants leasing space of more than 100,000 sq. ft. Users looking for space include e-commerce, distribution, building materials and logistics companies.
- **Jacksonville:** Vacancy stands at 7.0%—down 280 basis points (bps) year-over-year. The market is seeing more e-commerce and distribution deals as port volumes and regional population both grow. The market is expected to see future benefits from infrastructure projects and a deepening of the channel to attract larger post-Panamax ships.
- **Atlanta:** Demand remains strong with 2.6 million sq. ft. of positive net absorption in Q4. Big-box development remains prevalent with some 30 users looking for spaces of 100,000 sq. ft. or more. Bulk development is moving farther out and the market is seeing a trend of one-off multi-tenant redevelopments closer to the urban center. Third-party logistics, e-commerce and consumer goods companies remain the most active users in the market.

REGIONAL PERSPECTIVES (CONT.)

U.S. CENTRAL REGION

- **Chicago:** Demand continues to outpace supply as the market enjoyed its 26th consecutive quarter of positive net absorption in Q4. More than 16 million sq. ft. of space was under construction in Q4. Land has become scarce in the I-55 corridor—a key big-box market and primary location choice for many distribution users. Active users include food, logistics, e-commerce, distribution and construction companies.
- **Minneapolis:** Demand remains strong with more than 4 million sq. ft. of net absorption in 2016. Active users include distribution, manufacturing, consumer goods and food companies. Developers responded to the demand with approximately 3 million sq. ft. delivered in 2016. However, with an additional 2 million sq. ft. under construction in Q4, there is some concern about overbuilding of bulk product in some submarkets. Speculative development is expected to slow in 2017.
- **Kansas City:** E-commerce, logistics, food and consumer products are among the most active industries looking for and leasing space. A number of key expansions have driven development, with 7.5 million sq. ft. under construction in Q4. Demand, particularly for large blocks of space, is expected to remain strong and quickly absorb new deliveries in 2017.
- **Dallas/Ft. Worth:** The market continues to lead the nation in job growth. The industrial market has added approximately 200 sq. ft. of warehouse space for every new job added to the economy. More than 19 million sq. ft. of space was under construction in Q4, with 28% pre-leased. A number of big-box developments are underway, however supply in the 900,000-sq.-ft. to 1 million-sq.-ft. range exceeds demand, which will increase vacancy in 2017.

U.S. WEST REGION

- **Denver:** The market has enjoyed 27 consecutive quarters of positive net absorption, which has kept the vacancy rate below 5% for the past four years. There was 3.5 million sq. ft. of space under construction in Q4, with nearly half of that pre-leased. Active tenants looking for and leasing space include e-commerce, food & beverage and consumer-goods companies.
- **Oakland:** With a 1.7% overall vacancy rate (lower in the Class-A segment), new users have had a difficult time finding space. The market has seen some of the fastest-growing rents in the country, with another 10% or more of growth expected in 2017. Developers have responded with 2 million sq. ft. under construction as of Q4. There are more than 40 users in the market looking for spaces of more than 100,000 sq. ft.
- **Inland Empire:** Although the market is known for its big-box transactions, activity has been strong for spaces of less than 100,000 sq. ft., especially in Inland Empire West. Active tenants include e-commerce, distribution and logistics firms, all of which are looking for access to the ports of Los Angeles and Long Beach and to the large regional population. User demand is expected to remain strong in 2017, which will push rents up between 3% and 6%.
- **Los Angeles:** Vacancy is at 1.2%, contributing to slow activity levels due to the limited amount of available space. Rental rates have peaked at more than $8.70 per sq. ft. NNN. Given the intense competition for Class-A space, most new developments have been pre-leased. Active tenants include cold storage, packaging, furniture and e-commerce.

REGIONAL PERSPECTIVES (CONT.)

CANADA

- Demand for Canadian exports increased slightly in Q4 and is expected to increase further in 2017.
- Demand for space in Toronto and Vancouver will remain competitive in 2017 due to a lack of available product, putting increased pressure on already high sale prices and rents.
- Increasingly, there is a distinct mismatch between available product and user needs in primary markets. For example, in Vancouver there is very little mid- and large-bay product despite user demand for such product. Developers are increasingly marketing small-bay product as flexible industrial and office space to appeal to a broader base of users and are getting higher rents more in alignment with the office sector.
- In Alberta, there is a bifurcation between building classes. While Class-A industrial product remains in demand by a variety of users, the demand for Class-B buildings has significantly softened. Bullish developers are looking to repurpose Class-B buildings for other uses.
- The Canadian manufacturing market has improved, but not to the degree expected given historically ideal conditions. The low Canadian dollar has not been nearly as impactful as originally anticipated. According to the IHS Market PMI index, business confidence for Canadian manufacturers grew slightly to 51.8, as new orders and volumes grew modestly.

LATIN AMERICA

- Mexico's manufacturing output increased 2.1% in November. Electronics and food & beverage industries are driving growth in the manufacturing sector with 6.0% and 5.8% growth respectively in November. Automobile production fell in 2016 (-0.1%) due to less demand in the U.S.
- Mexico City reported strong industrial demand in 2016, with record-high absorption by logistics and distribution users. The market recorded 8 million sq. ft. of net absorption in 2016, and closed the year with a vacancy rate of 4.2%.
- Bajio, the largest of Mexico's regions with an inventory of 95 million sq. ft., recorded 15 million sq. ft. of positive net absorption in 2016 and a vacancy rate of 6.9%. Completions in the Bajio region reached 12 million sq. ft. in 2016.
- Asking rents remained stable in most Mexican markets, where Class A/A+ rates were flat at an average US$0.38 per sq. ft. Mexico City and Queretaro were the only markets that recorded an increase in asking rents, mainly due to strong demand and second-generation spaces coming back to the market with higher rents.
- Risks for the Mexican economy and industrial real estate market include possible changes in U.S. international trade policy and in foreign investment flows. A devaluation of the Mexican peso could lead to increasing exports to the U.S. and other international markets.
- Due to a rather severe economic downturn, demand for industrial & logistics parks in Sao Paulo has been somewhat stagnant with just 100,000 sq. ft. of net absorption in Q4 2016. Despite sluggish demand, supply grew by 3.9 million sq. ft., bringing the vacancy rate to 28.0%—a 760 bps year-over-year increase.
- The most active tenants for prime logistics space in Sao Paulo are third-party logistics and food & beverage users. With vacancies quite high, landlords are offering concessions and net asking rents have declined to R$19.25 per sq. m. per month, down 5.7% year-over-year.

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