

From Strength to Strength: Industrial Real Estate's Red-Hot Streak



If there's one way to summarize the start of 2023 it's: "market uncertainty." There's been an ongoing push and pull in the commercial real estate (CRE) narrative, with some sources saying we should brace for a crash and others insisting things are much better than they seem.

One of the factors pointed to as a life preserver for CRE in these rough waters is performance in the industrial sector. Unlike the woes we've seen in office, industrial has been on a more-or-less unstoppable red-hot streak since 2020.

But as the whole market starts to cool down, can this sizzling sector keep its momentum going?

Performance in Perspective

To understand the answer to that question, we first need to look at exactly how industrial has performed in recent years. Data from the Commercial Real Estate Development Association (NAIOP), shows that actual industrial absorption has outperformed forecasts since 2020, indicating the strong market appetite for industrial space.

2021 also saw the sector hit historic highs in asking rent, along with all-time lows for vacancy, as the National Association of Realtors (NAR) reported at the end of that year.

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Though things started to slow in the second half of 2022, industrial was still noted as the “highest-performing major real estate sector” in terms of deal activity for the year in McKinsey’s “Global Private Markets Review 2023.”

All of which means that the past three years have seen industrial real estate rocketing to new heights, even during massive economic uncertainty.

The Trend in 2023

As the data starts to flow in from the first quarter of 2023, the good news is that the run seems to be far from over – but it is slowing.

NAIOP’s prediction for industrial space absorption for 2023 is 310 million square feet (SF), while they estimate a further 323 million in 2024. And while those figures are lower than the demand we saw in 2021-2022 (433 and 413 million SF respectively), they’re still far higher than the pre-pandemic figures NAIOP shows for 2015-2019 (~200-250 million SF per year).

Additional data from Yardi’s April 2023 “National Industrial Report” sheds light on other metrics for the sector. Yardi notes that industrial in-place rents were up 7.1% year-over-year in March (\$7.15 per SF), and that vacancy was still at an extreme low of 3.9% across the US.

Even more impressively, the report notes: “[W]hile transactional activity has slowed similarly to other property sectors, the price per square foot for industrial sales reached record levels in the first quarter of 2023.”

Taken together, those numbers paint a picture of an industrial sector that, while evening out, is still strongly buoyed by ongoing demand.

Steady Tailwinds

Returning to our original question of whether the momentum will continue in the coming years, it’s worth having a look at the tailwinds driving the sector.

For starters, there is ongoing demand for logistics and last-mile delivery services. Increasingly, businesses need to optimize their supply chain to meet the stringent time and service demands of their customers.

Another factor in some markets is the lag between supply and demand for industrial space. As NAIOP noted back in March: “Supply chain issues that hindered the delivery of construction materials through western ports have been mostly resolved, but demand for industrial space around these ports continues to exceed supply, contributing to the demand for space in inland markets.”

Add to that manufacturer reshoring trends, the growing need for logistics hubs and flex facilities for eCommerce and blended retail models, and the case for industrial going from strength to strength seems clear.

As always, however, for investors looking to enter the space, our top advice remains to keep a firm eye on the fundamentals of the market, and to seek out local advice when contemplating your next big deal.