Strengthening Economy Boosts Industrial Demand; Performance Surge Pushes Values

The industrial landscape is being redefined by surging demand from e-commerce, traditional retailers, the manufacturing sector and third-party logistics providers. Rather than solely centering on ports and intermodal hubs, the emerging trends are fostering more inclusive demand for industrial real estate in a wide range of markets, including secondary and tertiary metros. These demand trends are supported by strong U.S. exports, totaling $2.0 trillion in 2013, 15 percent higher than the peak in 2008. Naturally, distribution and logistics centers in transportation corridors benefited and development has accelerated near maritime ports. As economic growth and rising trade lift demand for industrial space, vacancy rates in most metros will continue to tighten. Unlike past recovery cycles, however, this upswing has favored warehouse and distribution facilities more than the flex sub-sector. Demand has focused on the limited supply of quality, highly efficient assets, pushing rent growth for Class A warehouses well above the national average in many of the gateway and hub markets. Top-tier assets in late-recovery markets have also benefited, though to a lesser degree, as very tight development pipelines over the last few years limited competition and helped support rent growth. As the year progresses, flex space will gain momentum, particularly in markets with a locus of technology, such as Denver, Boston and San Diego.

Despite the slow, plodding nature of the recovery over the last five years, vigorous demand for industrial space persisted. Net absorption trended above historical averages for the past three years and the 8.1 percent vacancy rate at year-end 2013 represents a decline of 260 basis points from the peak. Rising consumer and business confidence, trade, housing and stronger consumer spending should boost economic growth in 2014, accelerating industrial demand. The convergence of these positive trends has, however, triggered a supply response, with an increasing number of build-to-suit and speculative projects to fulfill growing space requirements. Positive space fundamentals will support solid income growth, but the gains will be uneven, causing investors to remain cautious in their product quality and submarket selection.

2014 Annual Industrial Forecast

**Economy:** The economy is forecast to add 2.7 million jobs by year-end 2014, lifted by 2.5 to 3.0 percent GDP growth. Strong corporate profits, retail sales growth, improving international trade, and an accelerating construction cycle will combine to support economic momentum this year.

**Construction:** Approximately 120 million square feet of new supply is forecast to come online in 2014, an increase of 61 percent from last year. Much of the new supply has pre-committed leases or will be built-to-suit. Even with the steep rise in construction, total additions remain tame.

**Vacancy:** The national vacancy rate is forecast to recede by 100 basis points to a cyclical low of 7.1 percent by year end. Strong absorption of 239 million square feet in 2014 and still-limited construction from a historical perspective will support tightening vacancy trends.

**Rents:** Asking rents nationally are forecast to increase by an average of 5.1 percent, while concession reductions will boost effective rents. Rent gains for newer assets and in supply-constrained, gateway markets will exceed national averages.
Port and Hub Markets Dominate Top of Index

Major markets proximate to busy ports and those with links to multimodal transportation and distribution networks again occupy the top ranks of this year’s Index. Los Angeles (#1) and Houston (#2) claim the top two spots, supported by low vacancy rates and robust port-related activity and net absorption. Orange County (#3) and the Inland Empire (#9) each advanced two places. The latter benefits from the availability of entitled land for new development as well as spillover demand from the supply-constrained and more expensive metros. Los Angeles and Orange County. Denver’s low vacancy and brisk pace of job and rent growth advanced the metro two places to the fourth position in the NIR. Seattle (#5) and Miami (#7) slipped two and three places, respectively, despite dynamic growth in trade and transportation that is driving high levels of space absorption. Demand momentum in premier national distribution hubs Dallas/Fort Worth (#6) and Chicago (#8) supported these metros’ rise of two and four spaces, respectively, bypassing Salt Lake City (#10), which declined three positions.

Mid-Index Dominated by Smaller Port and Logistics Centers

The mid-tier markets represent a broad geographic mix of markets. Indianapolis’ intermodal transportation network and central location attracts e-commerce retailers and third-party logistics providers, advancing the metro three spots to #11. Despite leading the Index in rent growth, Minneapolis (#12) slipped three spots due to stronger momentum in other markets. San Diego (#13) advanced four places, buoyed by stronger income growth, venture capital funding and expansion in biotech and life sciences. Also on the West Coast, Portland (#15) receded five spots and Oakland (#18) fell three places as the limited supply of quality space will restrain demand and rent growth until new properties come online. Philadelphia (#14) and Harrisburg (#16) climbed five and four places. Tenant demand stemming from e-commerce, retail food and beverage products, and third-party logistics operators continues to overwhelm capacity, initiating a cycle of construction. Northern New Jersey declined four rungs to #17 as a lack of modern Class A space persists. However, several new and remodeled buildings are progressing through the pipeline in the high-demand port area. Atlanta’s (#19) ranking increased three places after posting a stellar year with the third-highest level of net absorption and fourth-highest job growth among markets in the Index. Vacancy will decline closer to the long-term average this year.
Lower-Ranked Markets Face Vacancy Hurdles

Most markets in the lower tier of the Index advanced or declined only marginally in the ranking, with the exception of two markets. Weak net absorption relative to other markets lowered Fort Lauderdale (#20) four spots and high vacancy dropped Tampa’s ranking six places to #24, despite improving fundamentals in both markets. Cleveland (#27) slipped two spots into the last position in the NIR due to weak job growth. Boston (#22), Washington, D.C. (#23), Detroit (#25) and Sacramento (#26) each edged up one rung, while Phoenix was unchanged at #21. These markets still post the highest vacancy rates in the Index but, with the combination of strong net absorption and low construction, the vacancy rates and rents in these markets should notch solid gains.

Index Methodology

The NII ranks 27 industrial markets based on a series of 12-month, forward-looking economic and supply-and-demand variables. Markets are ranked based on their cumulative weighted-average scores for various indicators, including forecast employment growth, vacancy, construction and rents. Weighing both the forecasts and incremental change over the next year, the Index is designed to indicate relative supply and demand conditions at the market level.

Users of the Index are cautioned to keep several important points in mind. First, the NII is not designed to predict the performance of individual investments. A carefully chosen property in a bottom-ranked market could easily outperform a poor choice in a top-ranked market. Second, the NII is a snapshot of a one-year time horizon. A market facing difficulties in the near term may provide excellent long-term prospects, and vice versa. Third, a market’s ranking may fall from one year to the next even if its fundamentals are improving. The NII is an ordinal index, and differences in ranking should be carefully interpreted. A top-ranked market is not necessarily twice as good as the second-ranked market, nor is it 10 times better than the 10th-ranked market.
Economy Gathers Momentum as Headwinds Abate; Fed Policy Could Be a Wildcard

Accelerating job growth, elevated consumer confidence, rising retail sales, and strength in energy, technology and trade continue to lend forward momentum to the U.S. economy. The severe winter clearly dampened productivity and economic activity in the first quarter, but personal consumption trends proved resilient and many components of industrial production remain in expansion. Recent reports on manufacturing, vehicle sales and construction spending reflect a broad-based rebound from weather-induced declines. Rising sales expectations and replacement needs for capital goods have driven capital investment plans in the manufacturing sector to post-recession highs. In addition, double-digit annual gains in residential investment confirm the recovery status of the housing sector, despite the short-term retreat in home sales and construction starts. The anticipated revival in residential and commercial construction should provide a significant lift to the economy in the second half of 2014.

The subdued pace of the economic recovery over the last five years has eased inflationary pressure and suggests that significant pent-up demand will be relieved once employment and incomes grow more vigorously. In addition, the Federal Reserve continues to normalize monetary policy by tapering its monthly purchases of long-term Treasurys and mortgage-backed securities, yet it remains supportive of economic growth. GDP posted 2.6 percent growth in 2013, and although the economy slowed in the first quarter of 2014, it should accelerate in the second quarter. Employers nationwide added 2.3 million jobs in 2013, and gains in the first four months of 2014 left payrolls just shy of their peak pre-recession level.

2014 Economic Outlook

Economic Productivity and Consumer Spending Drive Industrial Performance. GDP is forecast to trend ahead of its long-run pace, increasing by 2.5 to 3.0 percent in 2014 as consumption and incomes escalate, and residential investment grows. In addition, employers will add 2.7 million jobs in 2014, easing the unemployment rate to the 6 percent range. Homebuilding and commercial construction will gain momentum and lift hiring in areas that have been slower to recover, such as manufacturing, construction, and finance and insurance. Sustained home sales, double-digit home-price increases, and significantly diminished inventories, and new construction confirm that the housing sector is on the mend.

Steep Yield Curve Suggests Stronger Growth and Still-Accommodative Monetary Policy. A steady pace of tapering, tame inflation, and the deferral of a Federal Funds rate hike until mid to late 2015 will support consumer spending and private investment. However, as the economy gathers momentum, inflationary pressures could counter the current disinflationary environment.

Global Economic Recovery Still Fragile. The forecast for global economic growth remains positive, with Japan and most European countries in expansion. China’s slower pace of growth presents a downside risk, but the consensus forecast is a soft landing. Russia’s pre-eminence as a global energy supplier could weaken global productivity of G8 countries if the crisis in Ukraine escalates.
<table>
<thead>
<tr>
<th>MSA Name</th>
<th>Vacancy (Year-End)</th>
<th>Asking Rent per Sq. Ft.</th>
<th>Completions (000s of Sq. Ft.)</th>
<th>Employment Growth</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>13</td>
<td>14*</td>
<td>13</td>
<td>14*</td>
</tr>
<tr>
<td>Atlanta</td>
<td>11.4%</td>
<td>10.2%</td>
<td>3.36</td>
<td>3.50</td>
</tr>
<tr>
<td>Boston</td>
<td>9.5%</td>
<td>8.7%</td>
<td>6.11</td>
<td>6.25</td>
</tr>
<tr>
<td>Chicago</td>
<td>9.3%</td>
<td>8.5%</td>
<td>4.75</td>
<td>4.94</td>
</tr>
<tr>
<td>Cleveland</td>
<td>7.8%</td>
<td>7.4%</td>
<td>3.56</td>
<td>3.60</td>
</tr>
<tr>
<td>Dallas/Fort Worth</td>
<td>7.2%</td>
<td>6.5%</td>
<td>4.21</td>
<td>4.46</td>
</tr>
<tr>
<td>Denver</td>
<td>5.0%</td>
<td>4.9%</td>
<td>5.41</td>
<td>5.69</td>
</tr>
<tr>
<td>Detroit</td>
<td>10.4%</td>
<td>9.4%</td>
<td>4.11</td>
<td>4.20</td>
</tr>
<tr>
<td>Fort Lauderdale</td>
<td>8.6%</td>
<td>8.0%</td>
<td>6.58</td>
<td>6.93</td>
</tr>
<tr>
<td>Harrisburg</td>
<td>10.8%</td>
<td>9.9%</td>
<td>3.80</td>
<td>3.95</td>
</tr>
<tr>
<td>Houston</td>
<td>5.0%</td>
<td>5.2%</td>
<td>5.74</td>
<td>6.06</td>
</tr>
<tr>
<td>Indianapolis</td>
<td>6.9%</td>
<td>6.8%</td>
<td>3.41</td>
<td>3.38</td>
</tr>
<tr>
<td>Los Angeles</td>
<td>5.2%</td>
<td>4.7%</td>
<td>6.92</td>
<td>7.27</td>
</tr>
<tr>
<td>Miami</td>
<td>6.7%</td>
<td>5.9%</td>
<td>7.73</td>
<td>8.00</td>
</tr>
<tr>
<td>Minneapolis-St. Paul</td>
<td>6.7%</td>
<td>6.6%</td>
<td>5.86</td>
<td>6.22</td>
</tr>
<tr>
<td>Northern New Jersey</td>
<td>8.1%</td>
<td>8.4%</td>
<td>6.04</td>
<td>6.31</td>
</tr>
<tr>
<td>Oakland</td>
<td>8.4%</td>
<td>7.3%</td>
<td>7.80</td>
<td>8.26</td>
</tr>
<tr>
<td>Orange County</td>
<td>5.1%</td>
<td>4.4%</td>
<td>7.74</td>
<td>8.15</td>
</tr>
<tr>
<td>Philadelphia</td>
<td>9.3%</td>
<td>8.1%</td>
<td>4.68</td>
<td>4.82</td>
</tr>
<tr>
<td>Phoenix</td>
<td>13.0%</td>
<td>11.5%</td>
<td>6.4</td>
<td>6.75</td>
</tr>
<tr>
<td>Portland</td>
<td>6.6%</td>
<td>6.0%</td>
<td>5.11</td>
<td>5.19</td>
</tr>
<tr>
<td>Riverside-San Bernardino</td>
<td>5.2%</td>
<td>5.1%</td>
<td>4.46</td>
<td>4.70</td>
</tr>
<tr>
<td>Sacramento</td>
<td>12.2%</td>
<td>10.3%</td>
<td>4.57</td>
<td>4.69</td>
</tr>
<tr>
<td>Salt Lake City</td>
<td>4.5%</td>
<td>3.9%</td>
<td>4.62</td>
<td>4.76</td>
</tr>
<tr>
<td>San Diego</td>
<td>8.8%</td>
<td>8.5%</td>
<td>9.95</td>
<td>10.44</td>
</tr>
<tr>
<td>Seattle-Tacoma</td>
<td>5.7%</td>
<td>5.3%</td>
<td>6.73</td>
<td>6.96</td>
</tr>
<tr>
<td>Tampa</td>
<td>9.9%</td>
<td>9.0%</td>
<td>4.58</td>
<td>4.79</td>
</tr>
<tr>
<td>Washington, D.C.</td>
<td>10.0%</td>
<td>8.7%</td>
<td>7.77</td>
<td>8.21</td>
</tr>
<tr>
<td>U.S. Metro Average</td>
<td>8.1%</td>
<td>7.1%</td>
<td>5.38</td>
<td>5.65</td>
</tr>
</tbody>
</table>

* Forecast 1 See National Industrial Index Note on page 20.
The past 12 months proved stellar for the performance of industrial properties, with vacancy declining below its long-term average. In addition, surging rents and economic indicators foretell continued strength for the coming year. Healthy retail sales have stimulated space requirements for highly efficient warehouse and distribution space from e-commerce big-box users such as Amazon. Multi-platform retailers, such as Wal-Mart and Best Buy, and a plethora of third-party logistics providers, have also sparked demand. Markets with limited new construction, and/or a high degree of functional obsolescence in their inventory, lack suitable options for these users and have spurred build-to-suit development in many major transportation corridors. Expansion of the supply chain to enhance proximity to the consumer has resulted in distribution networks and new fulfillment centers near markets with large populations, and in intermodal transportation hubs, such as Dallas/Fort Worth, the Inland Empire, Phoenix, Atlanta and Chicago.

Net absorption of industrial space increased by 19 percent last year to 189 million square feet, far surpassing the 85 million square feet of new space delivered. As a result, the industrial vacancy rate dropped 90 basis points to 8.0 percent last year. Positive trends in net absorption and declining vacancy have persisted for 15 consecutive quarters, supporting a 6.2 percent surge in asking rents to $5.47 per square foot in the first quarter. The pace of new development has eased upward in response to vigorous tenant demand, tighter vacancy and solid rent growth, but the short industrial construction cycle can deliver new product to the market quickly. Risks of rapid speculative supply-side development overwhelming demand is not expected this year given the robust outlook for broadening economic growth in sectors that drive demand for industrial real estate.

2014 National Industrial Forecast

- Healthy Consumption, Trade Flows and Housing Benefit Broader Range of Properties. Growing consumption will expand space demand from small- to medium-size firms in secondary markets, as well as Class B properties in primary markets. The pace of recovery will also accelerate as markets that have lagged due to a higher proportion of flex space gather momentum.

- Construction Ramping Up, Though Conservative Underwriting Persists. Nearly every market has product under development and approximately 50 percent of the new construction is tied to pre-commitments. Increasingly comfortable with the industrial recovery thesis, a growing number of lenders now compete to provide construction loans. The size and nature of tenant requirements is shifting to smaller product, indicating that the improvement in property operations continues to expand beyond the big-box warehouse segment.

- Surging Demand Dwarfs New Deliveries and Lifts Sector Performance. Projected completions of 120 million square feet in 2014 represent a significant increase from the level recorded in 2013 but remain well below a forecast 259 million square foot increase in occupied space. As a result, the U.S. vacancy rate will plummet 100 basis points to a cyclical low of 7.1 percent. Asking rents nationally will increase 5.1 percent, with greater gains likely in supply constrained, gateway markets.
Industrial Sector's Value Proposition Hastens Flow of Investment Capital

The industrial sector's higher yields and discounted pricing in a period of improving space fundamentals and NOI growth continue to draw attention from well-capitalized investors. Overall sales volume of industrial properties still lags other major property types, but a shift of capital into industrial assets appears to be underway. Class A warehouse properties remain the preferred investment target and coastal areas the preferred regions, particularly the West. However, growing confidence in the national economy, together with the considerable price appreciation and cap rate compression in these markets, has compelled opportunistic investors to seek assets in recovering, high-growth metros such as Atlanta and Phoenix. In addition, industrial sales volume in smaller markets such as Reno, Nashville, Harrisburg/Central Pennsylvania and Fort Lauderdale more than doubled in 2013.

Industrial sales velocity jumped 15 percent over the past 12 months, totaling $55 billion. Retailers, distributors and logistics operators continue to locate near major population centers and multi-modal transportation hubs, driving demand for large bay, warehouse and distribution facilities, which accounted for 70 percent of sales volume last year. Conversely, sales of flex properties were virtually unchanged. The average price for warehouse assets rose 8 percent to $59.89 per square foot through the first quarter, while the average price paid in deals for flex space advanced 7 percent to $103 per square foot. The average price of warehouse and flex properties remains 12 and 29 percent, respectively, below peak levels. Overall industrial cap rates remained relatively subdued over the past year at 7.6 percent, although cap rates for warehouse properties in the six most preferred metros compressed 10 basis points to 6.7 percent during the year.

2014 Industrial Investment Outlook

- **Rising Trade, Housing and Consumer Spending Lift Space Demand, Drawing Capital to Sector.** The high level of industrial space demand has proven remarkably durable throughout the recovery, despite the slow pace of economic growth. Muted supply and surging demand will continue to support solid income growth in the industrial sector. Gains will not accrue to every asset, so investors will remain selective about product quality and submarket location. Key measures to consider include a low ratio of speculative construction relative to inventory and a significant discount in rents relative to peak values.

- **Supply Constraints and Competitive Pricing in Primary Markets Drive Investors to Class B Assets.** The significant spread of 150 to 200 basis points between Class A and B properties and improved NOI performance in a broader range of segments will attract opportunistic investors. The housing recovery and stronger hiring by small to mid-size businesses will lift demand for smaller, multi-bay warehouse assets and more affordable Class B multi-tenant properties over the year.

- **E-Commerce, Multi-Platform Retailers and Third-Party Logistics Operators Dominate Demand.** A sizeable pipeline of speculative and build-to-suit completions will add considerable new space to high-demand multi-modal transportation hubs with strong population and employment growth. Markets with balanced property operations and vibrant high-tech, trade or energy space demand drivers will more successfully assimilate new supply.
Elevated Port Activity Supports Strong Net Absorption; Rent Gains Follow

The growing national economy is driving the movement of goods through Atlanta, boding well for local industrial operators. The metro serves as a major distribution hub for the Southeast due to its extensive road, rail, and airport systems. Additionally, the region benefits from the nearby Port of Savannah, the second busiest U.S. container exporter. Last year, the port’s total container trade was 3.0 million TEUs, marking 29 percent growth from 2009. As plans move forward to deepen the Savannah Harbor to better accommodate larger container ships, the region will benefit from expanded cargo capacity. Improving operations at the port has attracted additional retailers and manufacturing and logistics companies to Atlanta, boosting space demand. McCaster-Carr, TJX Company, and Procter & Gamble are moving forward with build-to-suit facilities along the two freight railways that connect the port to the metro. The combination of heavily pre-leased new inventory and healthy net absorption has pushed down marketwide vacancy 440 basis points since reaching its peak in 2010. As demand for industrial space strengthens, vacancy will retreat further, making way for rent gains this year.

Transaction velocity will escalate this year as growing demand for industrial space draws investor interest to Atlanta. Over the past year, buyer composition shifted as private syndicates targeted warehouse facilities in northern areas of Atlanta along Interstates 85 and 75, outnumbering REITs and institutional buyers. Overall, well located stabilized assets typically command a cap rate range in the low-8 percent range while Class C properties initial yields begin in the mid- to high-8 percent area. Heightened buyer competition and the potential of rising interest rates will motivate property owners to list their assets, supporting increased sales activity in the coming months.

2014 Market Outlook

- **2014 NII Rank: 19, Up 3 Places.** Strong net absorption led to one of the nation’s largest drops in vacancy, pushing up Atlanta three spots in the index.
- **Employment Forecast:** After adding 63,900 positions last year, local employers will create 74,800 jobs in 2014, marking a 3.1 percent annual increase. This includes the addition of more than 16,200 workers in the trade, transportation and utilities sector.
- **Construction Forecast:** By year end, 3.3 million square feet of industrial space will come online, down from roughly 4.4 million square feet last year.
- **Vacancy Forecast:** Vacancy will tumble 120 basis points to 10.2 percent in 2014, building on the 130-basis point fall one year earlier.
- **Rent Forecast:** Asking rents will jump 4.2 percent to $3.50 per square foot in 2014, following a 3.7 percent climb in 2013.
- **Investment Forecast:** Class B/C warehouses measuring less than 50,000 square feet in Northeast and South Atlanta will remain a primary target of owner-user buyers.
Digital Manufacturing Institute Will Fortify Chicago’s Manufacturing Prominence

Chicago’s recent designation as the site of a digital manufacturing institute will further strengthen the metro’s manufacturing prominence and growing tech sector. The metro is already one of the biggest distribution hubs in the country, and its broad industrial base is proliferating as expanding companies generate additional need for large, efficient warehouse space. Three consecutive years of absorption above 10 million square feet has depleted the supply of top-tier space and pushed vacancy below pre-recession levels, spawning spec development along prime suburban distribution routes. Developers are especially active in the SW/I-55 Corridor submarket where more than 4 million square feet of warehouse space was delivered last year and at least 2 million square feet is expected this year. Also, rising land prices and higher tax rates are directing more development toward neighboring states. Amazon has two buildings underway in Kenosha, Wisconsin, that will add roughly 1.5 million square feet of warehouse space by early 2015. This year, metrowide vacancy will continue to tighten, allowing operators in many submarkets to post rent gains.

Investors are active at both ends of the quality spectrum, creating a bifurcated market. At the top, single-tenant net-leased properties with credited tenants and long-term leases are in strong demand throughout the metro at cap rates in the 6 percent range, but can dip lower for trophy assets. A lack of available properties has moved buyers to consider assets with shorter lease terms or properties in secondary and tertiary markets where initial yields are 50 to 100 basis points higher. At the other end of the spectrum, improving fundamentals have many investors seeking distressed properties for value-add plays that trade at cap rates above 9 percent. With investors focused elsewhere, many Class B/C facilities are languishing in the middle as slow rent growth has not yet produced yields high enough to attract buyers. As fundamentals strengthen this year, more of these assets should receive investor attention.

2014 Market Outlook

- **2014 NII Rank: 8, Up 4 Places.** A limited amount of new supply will help push down vacancy in this industrial market, lifting its spot in the NII.

- **Employment Forecast:** Local employers will generate 79,900 jobs in 2014, a 1.8 percent jump. This includes more than 4,000 manufacturing positions.

- **Construction Forecast:** After 7.8 million square feet was delivered in 2013, developers will bring 5.8 million square feet online this year. The largest project is a 1 million-square-foot building for Amazon in Kenosha.

- **Vacancy Forecast:** Vacancy will fall 80 basis points to 8.5 percent in 2014, following an 80-basis point drop last year.

- **Rent Forecast:** Rents will climb 4.1 percent in this year to $4.94 per square foot, up nearly 15 percent from the trough in 2011.

- **Investment Forecast:** Cap rates for well-located Class B/C assets are typically in the 8 to 9 percent range for suburban properties and may dip 50 basis points lower for comparable infill locations.
The Metroplex’s economy is running on all cylinders, which will boost industrial operations through the end of the year. Occupancy and rents are already above pre-recession highs, and further gains in the coming months are anticipated. In fact, developers were relatively slow to respond to improving conditions during the early stages of the current upcycle, which has enabled vacancy to dip below an equilibrium level. Supply-side pressure will return this year as speculative building has commenced, though little threat to the tightness of the market is anticipated until at least 2015. Several large distribution centers are underway and being met with sufficient demand at this stage. Prologis, for example, completed a distribution center for Pepsico’s subsidiary Quaker during the first quarter of this year. Trammell Crow recently announced a speculative project near the already underway Penn Distribution Center. Until more significant speculative space comes out of the ground next year, operators will enjoy strong rent growth and high occupancy in most areas.

Both local and out-of-state buyers are heightening their presence in the Metroplex in an attempt to ride the upswing in operations to higher NOIs. The market’s large size typically offers opportunities for buyers with an array of investment goals. However, most investors were chasing similar deals as 2014 began. Newer and larger is the prevailing sentiment among industrial buyers, which is opening up opportunities for owner/users and investors seeking older assets to acquire deals with fewer bidders. Average cap rates for properties at least 20-years-old are 200 basis points higher than newer assets, providing much healthier returns while conditions are tight. The downside risk of these deals, however, is the potential for overbuilding as developers elevated deliveries. Buyers will want to focus on infill areas where construction is challenging or along major transportation corridors to alleviate long-term risks.

2014 Market Outlook

- **2014 NII Rank: 6, Up 2 Places.** Robust employment and the solid recovery in operating fundamentals elevated Dallas/Fort Worth in this year’s NII.
- **Employment Forecast:** Dallas/Fort Worth will boast one of the strongest job-creating engines in the country again this year as 95,000 jobs are created, expanding payrolls by 3 percent. Last year, 72,700 positions were added.
- **Construction Forecast:** Speculative construction will begin in earnest in 2014, resulting in 17 million square feet of new space.
- **Vacancy Forecast:** The marketwide vacancy rate will retreat 70 basis points to 6.5 percent this year. In 2013, vacancy plunged 170 basis points.
- **Rent Forecast:** Asking rents will rise 6 percent in 2014 to $4.46 per square foot, following a 10.5 percent gain last year.
- **Investment Forecast:** Average cap rates dipped approximately 100 basis points last year, and further compression could materialize during the primary months of 2014 until the Fed’s tapering program is exhausted.
Developers Begin Speculative Construction as Demand Surges in Denver

Speculative industrial development is returning to Denver as technology, energy, and retail companies absorb space, boosting builder confidence. The market’s relatively central location and extensive transportation network is a lure for manufacturing and distribution company operations, creating healthy space demand. Additionally, Colorado’s legalization of marijuana has further increased the need for warehouse space as pot cultivation and manufacturing firms search for available facilities. In 2013, strong leasing activity drove net absorption of 4.2 million square feet, the largest annual rise in occupied space since 2007. Tightening conditions has made it difficult for companies to find available space, motivating builders to ramp up production. Completions will more than double this year, with speculative building representing roughly one-third of total deliveries. The largest project is a speculative Class A warehouse building, which will span 500,000 square feet. This development and several large facilities are being built along Interstate 70 near the Denver International Airport, a major high-tech corridor. New inventory will push up average rents in the metro, marking a second consecutive year for rent gains.

The performing local economy and improving fundamentals will result in heightened sales activity for Denver industrial assets this year. Intense buyer demand will outpace the number of for-sale listings, pushing up property values. Private syndicates are targeting warehouse facilities along Interstate 25 and I-70 in North Central Denver and in East Denver near the airport and major highways. First-year returns for these assets typically begin in the mid-7 percent range, while newer upper-tier properties trend 100 basis points lower. Due to the limited amount of Class A assets, REITs have been relatively inactive, though a wave of new inventory will provide these investors with more buying opportunities. Owner-user buyers will remain interested in Class B/C facilities measuring 15 to 80 thousand square feet with cap rates in the mid-8 percent area.

2014 Market Outlook

- **2014 NII Rank: 4, Up 2 Places.** Denver’s strong employment growth and low vacancy propelled the market into a top-five position in the Index.

- **Employment Forecast:** In 2014, 49,100 workers will be added to payrolls, expanding total employment 3.8 percent. Last year, 38,400 jobs were created.

- **Construction Forecast:** After completing 1 million square feet in 2013, builders will deliver 2.5 million square feet of industrial space this year.

- **Vacancy Forecast:** As new inventory comes online, vacancy will inch down 10 basis points, following a 180-basis point decline in 2013.

- **Rent Forecast:** Asking rents will climb 5.1 percent to $5.69 per square foot this year, building on a 7.6 percent surge last year.

- **Investment Forecast:** Investors with a higher risk appetite will target well-located distressed manufacturing and warehouse buildings with upside potential. These assets lie in the mid-8 to low-9 percent cap rate range.
Vigorous Houston Market Sparks Deals, Higher Prices

A high-octane economy is driving growth in most, if not all, industries in Houston, creating new space demand for warehouse, distribution and flex properties. An expanding port and the emergence of the Grand Parkway as a significant industrial corridor are also providing momentum, helping the market to record a drop in vacancy last year despite elevated completions. Bright spots appear in several segments of the local industrial market. Roughly 30 percent of the increase in occupied space last year came in large multi-tenant warehouse and distribution facilities built since 2008, even though those buildings represent only 3 percent of total stock. With additional available space remaining, tenants will continue to migrate to the newest buildings. In addition, small flex properties, which draw a diverse tenant mix, are also displaying vigor as numerous industries expand. Vacancy in these properties plummeted more than 300 basis points last year.

Growing businesses are also maintaining tight vacancy in properties ranging from 20,000 square feet to 100,000 square feet and enabling property owners to raise rents and withdraw leasing incentives. Properties listed for sale ignite keen bidding, and many assets trade for full asking price, or more in select instances. Cap rates here have settled in the 8 percent range, and investors continue to pursue both stabilized assets and properties that provide an opportunity to add value. Investors are also focusing on single-tenant properties but apply distinctions for assets located in the center of the metro and those located in the outer reaches. Buildings located far beyond the beltways typically require longer lease terms and strong corporate guarantees than closer in properties. Regular annual rent escalations are also desired.

2014 Market Outlook

- **2014 NII Rank: 2, No Change.** Impressive employment gains and robust space demand kept Houston in the index's second position.
- **Employment Forecast:** Employers will create 94,000 jobs in 2014 to expand payrolls 3.3 percent. More than 77,000 new hires were made last year.
- **Construction Forecast:** Developers will bring online 8 million square this year, outpacing last year’s total of 7.3 million square feet. Potential overbuilding in many submarkets where private developers are preparing projects will temporarily raise vacancy in these areas.
- **Vacancy Forecast:** Deliveries will offset a solid increase in space demand, yielding a 20-basis point uptick in vacancy to a still-tight 5.2 percent. The vacancy rate rose 10 basis points in 2013.
- **Rent Forecast:** After rising 3.2 percent last year, average rents in the metro will advance 5.5 percent in 2014 to $6.06 per square foot.
- **Investment Forecast:** Building features such as tilt wall construction and high clear heights remain prominent on the checklists of investors targeting the market for potential acquisitions.
Twin Ports Rush to Shore-Up Container Traffic, Supporting Long-Term Health of Market

The Los Angeles industrial market is highly dependent on the twin ports of Los Angeles and Long Beach, which are attempting to undergo infrastructure improvements to compete with a wider Panama Canal. Currently, the twin ports account for more than 40 percent of all the container traffic entering the nation. When the wider channel of the Panama Canal opens at the end of 2015, some dire estimates peg the loss of potential traffic as high as 20 percent. In an effort to maintain dominance in the segment, the Port of Los Angeles and Burlington Northern Santa Fe Railway are pushing for a $500 million rail yard near the port that would prevent the need for trucks to carry containers nearly 25 miles inland to Commerce before being loaded on trains. The scale of container traffic losses partially hinges on the ability to overcome legal challenges to the project, though the ability for post-panamax ships to reach Houston, Miami and the New Orleans port complex will certainly put a dent into operations in Southern California.

Uncertainty will be a large contributor to deal flow during the next several months as investors evaluate their risk tolerance and shuffle their portfolios. Owners with port-related tenants may consider divesting and moving into more secure assets. Although many tenants are likely to remain in the county, leases that expire in 2016 could potentially be renewed at lower rental rates as available space heightens competition. Changing conditions regarding the port aside, other opportunities are available for investors throughout the market. Interest rates on SBA loans are still low, which should support activity in the owner/user segment. Other investors can target properties with fewer than 100,000 square feet, which trade at cap rates in the low-7 percent range. Large, newer assets, meanwhile, remain the domain of institutional investors and change hands at first-year returns modestly above 5 percent.

2014 Market Outlook

- **2014 NII Rank: 1, No Change.** Investment in transportation corridors to the ports and a decline in construction support Los Angeles’ top ranking.
- **Employment Forecast:** Employers in the metro will expand payrolls by 2 percent this year as 81,000 positions are added. In 2013, 76,900 jobs were created in the market.
- **Construction Forecast:** The pace of development will slip to 1.7 million square feet in 2014, down from 2.9 million square feet last year.
- **Vacancy Forecast:** After a 40-basis point decline in 2013, vacancy will dip 50 basis points this year to 4.7 percent.
- **Rent Forecast:** As vacancy falls below the 5 percent threshold, operators will elevate asking rents 5.1 percent to $7.27 per square foot by year-end 2014.
- **Investment Forecast:** Redevelopment of the Warehouse District could gain steam as the new rail yard near the ports moves forward. Owners in the area may consider divesting to developers seeking to reposition assets.
Miami-Dade Market Pulses with Activity: 
Space Demand Growing, Capital Flowing

The Miami-Dade industrial property market strides confidently through the early stages of 2014, and growing space demand, modestly restrained construction, and a wave of domestic and foreign investment capital raise prospects for additional strengthening. Over all, several quarters of positive net absorption have slashed vacancy nearly 500 basis points from the peak, and demand is expanding throughout the field of space users. For example, the revival of residential construction is generating work for contracting trades and sparking the absorption of space in small multi-bay facilities, where vacancy plunged to the low-5 percent range over the past year. Additionally, several small multi-bay properties in the Design District and Wynwood are being converted to other uses, feeding a westward migration of tenants to business parks east of the airport. Vacancy in this area will tighten further in the quarters ahead.

Development, meanwhile, remains under control and is notably the domain of large builders and institutions who are readying properties for the anticipated surge in cargo volume ensuing from the expansion of the Panama Canal. Institutions are also acquiring large properties, often at cap rates in the mid-6 to 7 percent range. Small multi-bay assets, though, can trade from 8 to 10 percent depending on location, and the competition between investors here is intense. The pool of prospective buyers is diverse and turns over frequently. New buyers are crossing over from other commercial property types where yields have compressed below acceptable targets. In addition, as industrial property prices have risen, some local buyers are now casting an eye toward other metros in the state in search of higher yields. Owner/users are also active in this segment of the market, while foreign capital is present behind domestic entities.

2014 Market Outlook

- **2014 NII Rank: 7, Down 3 Places.** Despite improving operations, Miami slipped three slots into the bottom half of the top ten, as other markets have stronger forecasts.
- **Employment Forecast:** Payrolls will expand 2.8 percent in 2014 through the addition of 30,000 positions. In 2013, more than 34,000 jobs were added.
- **Construction Forecast:** Completions will total 1.8 million square feet this year, consisting of primarily properties measuring more than 100,000 square feet. Roughly the same amount of space came online during 2013.
- **Vacancy Forecast:** Behind net absorption of nearly 2.8 million square feet, vacancy in Miami-Dade will fall 80 basis points this year to 5.9 percent. A 30-basis point drop was recorded last year.
- **Rent Forecast:** The average rent in the county will increase 3.5 percent in 2014 to $8.00 per square foot, wiping out last year's decrease of 2.8 percent.
- **Investment Forecast:** Property owners contemplating a sale stand solid chances of capturing top value for their assets in the county's competitive bidding climate. A prevalence of all-cash deals will lead to quick executions.
Heavy Demand Triggers Spec Industrial Development in Minneapolis-St. Paul Metro

More than 17,000 manufacturing jobs have been created in the Minneapolis-St. Paul metro since the depth of the recession, helping to generate strong tenant demand for industrial space. Newer warehouse buildings in outer-lying suburbs near major transportation corridors are particularly sought-after; however, the lack of available space has generated spec warehouse development in these areas. In Rogers, for example, Liberty Industrial has a 227,000-square-foot spec building underway that signed a tenant before construction has been completed. In Shakopee, Opus has begun work on a 200,000-square-foot spec project and Shutterfly will move into a new 217,000-square-foot building midyear. Also, in Brooklyn Park, developers plan to begin construction on more than 350,000 square feet of spec warehouse space this spring. Fundamentals in older industrial buildings near the urban core and in flex space has been lagging, but demand is improving as more tenants expand and renew leases at current asking rents, boosting operators’ NOI.

Strengthening operations in industrial properties has attracted the attention of investors. A lack of available net-leased single-tenant assets at cap rates in the 7 percent range is motivating more buyers to consider net-leased multi-tenant properties, which trade 50 to 100 basis points higher. As demand for industrial space flourishes, some institutional investors are switching from buying existing industrial buildings to purchasing developable land that will be banked or built on for higher returns. These companies are re-evaluating portfolios and may list properties to capitalize new endeavors. Land investors are active in Brooklyn Park where the last segment of Highway 610 connecting Interstates 35W and 94 in the northern metro is underway. Ryan Companies has proposed a new business park on 150 acres in this area and in Hudson, Wisconsin, United Properties has tied up a 21-acre industrial site.

2014 Market Outlook

■ 2014 NII Rank: 12, Down 3 Places. Minneapolis-St. Paul fell three spots and out of the top ten due to a below-average vacancy decline.

■ Employment Forecast: In 2014, 42,000 jobs will be created, a 2.3 percent increase. This includes approximately 4,000 manufacturing positions.

■ Construction Forecast: Developers will complete nearly 2 million square feet in 2014, the majority of which is build-to-suit warehouse space.

■ Vacancy Forecast: After a jump in inventory pushed up vacancy 40 basis points in 2013, strong demand for large industrial space and steady construction output will lower vacancy 10 basis points this year to 6.6 percent.

■ Rent Forecast: This year, overall asking rents will rise 6.2 percent to $6.22 per square foot, following a 6.5 percent climb in 2013.

■ Investment Forecast: With tenant demand for industrial space escalating throughout the metro, value-add properties are garnering significant buyer interest at cap rates in the 9 to 10 percent range.
A multibillion dollar infrastructure expansion is currently underway in the Port of New York and New Jersey in order to accommodate larger container ships. Activity at the nation’s third largest port is expected to double in the coming decade, generating increased demand and rent growth for industrial properties in Northern New Jersey. In anticipation of elevated movement of goods, builders will escalate development nearly tenfold this year, including several speculative projects. The majority of construction projects are warehouses with large floor plates and high ceilings in order to satisfy tenant requirements. The biggest development scheduled for completion this year is an 880,000-square foot multi-tenant building in Jersey City. As large-scale developments come online, vacancy will move up by year end. Despite the uptick in available space, higher rents commanded by newer inventory will help lift regionwide asking rents for the third year in a row.

Future growth at the Port of New York and New Jersey is whetting investors’ appetite for industrial properties throughout the region, however, a lack of quality listings will move buyers away from primary locations. As property values rise, and buyer demand remains high, more owners will be motivated to bring properties to market, boosting transaction velocity throughout the area. A diverse pool of buyers is seeking smaller assets along major trucking corridors. Similar properties traded over the past year with initial yields in the 6 to 8 percent range. REITs and owner-users are often acquiring properties near shipping terminals and along major transportation routes, which sold during the past year with cap rates in the mid- to high-5 percent range. In particular, these investors are targeting a fresh supply of newer properties in the Meadowlands submarket due to the area’s strategic access to both New York City and other major U.S. and Canadian markets.

### 2014 Market Outlook

- **2014 NII Rank: 17, Down 4 Places.** A significant increase in construction and rising vacancy dragged down Northern New Jersey four positions.

- **Employment Forecast:** Employers in the region are expected to add 30,000 positions in 2014, up from the 27,100 jobs created in 2013.

- **Construction Forecast:** Developers will expand inventory by 1.1 percent this year with the addition of nearly 4 million square feet of space.

- **Vacancy Forecast:** The return of speculative construction projects to the area will push vacancy up 30 basis points to 8.4 percent.

- **Rent Forecast:** Asking rents will climb 4.5 percent this year to $6.31 per square foot. In 2013, rents reached $6.04 per square foot after a year-over-year gain of 3.8 percent.

- **Investment Forecast:** Projected increases in port activity are focusing buyer attention on warehouse properties throughout the region, for which financing is readily available. Last year, sales of warehouse properties jumped 25 percent.
E-commerce, Regional Economic Expansion
Jump-Start Industrial Market

The Phoenix industrial market is poised to strengthen on improving fundamentals in 2014 amid elevated construction. Builders will deliver more than 10 million square feet in 2013 and 2014, exceeding the previous four years’ combined total. Accelerating regional economic growth as well as relatively low building and labor costs have encouraged retail and tech company expansions within Valley distribution and manufacturing facilities. Macy’s is adding 360,000 square feet to its Goodyear distribution building this year in step with rapidly growing online sales, which rose 50 percent annually in 2012. Further east in the Valley, WinCo Foods will deliver an 800,000-square foot distribution center to better serve the grocer’s expanding footprint across western states. The largest project of the year is Intel’s 2.1 million-square foot Fab 42 manufacturing building, which delivered in Chandler early this year. Further expansion projects can be expected, supported by rising demand from e-commerce and growing nearby local economies as Phoenix remains a strategic location for company distribution operations.

Improving industrial operations are giving way to a more active investment market, boosting transaction velocity, particularly in the southeast and southwest areas of the metro. Investors are targeting warehouse and distribution assets, typically less than 100,000 square feet, along transportation corridors, with Tempe and areas west of the airport garnering increased investor attention. Deal volume of distribution assets is rising, as investors anticipate swelling space needs alongside improving economic growth. The number of these assets traded more than tripled last year, and transaction volume is off to a strong start in 2014.

2014 Market Outlook

- **2014 NII Rank: 21, No Change.** Strong net absorption of existing space will lower vacancy, yet Phoenix maintains one of the highest vacancy rates in the country, cementing its position in this year’s index.

- **Employment Forecast:** Employers will expand payrolls 2.6 percent with the addition of 47,100 jobs this year, following a 2.8 percent rise in 2013.

- **Construction Forecast:** This year, 4.9 million square feet of space will come online, with build-to-suit projects accounting for the majority of space. Last year, construction reached a five-year high of nearly 5.2 million square feet.

- **Vacancy Forecast:** Accelerating absorption will outweigh a consecutive year of nearly 5 million square feet of new space, pushing down vacancy 150 basis points to 11.5 percent. In 2013, vacancy rose 60 basis points.

- **Rent Forecast:** Marketwide asking rents continue a strong recovery from the 2011 trough and will advance 5.5 percent to $6.75 per square foot this year. In 2013, asking rents jumped 5.4 percent.

- **Investment Forecast:** Steady investor demand will maintain upward pressure on industrial asset prices. Chandler and Tempe will account for a large portion of deals, while investor interest picks up in the Northwest Valley.

### Market Forecast

- **Employment:** 2.6% ▲
- **Construction:** 300K ▼
- **Vacancy:** 150 bps ▼
- **Asking Rents:** 5.5% ▲

*Sources: CoStar Group, Inc.*
Construction and Tenant Demand Levels Begin to Merge, Creating Balanced Market

Vacancy in the Inland Empire industrial market has fully recovered from the downturn, though rents remain below the pre-recession peak. At the end of last year, vacancy was nearly 800 basis points below the peak rate due to an increase in space demand of nearly 15 percent. Developers have responded to the improved conditions by flooding the construction pipeline with projects. Industrial stock will climb by 3.9 percent in 2014, the highest completion rate since 2008, when builders were finalizing properties that broke ground prior to weakening operations. Although pre-leasing is soft at less than 30 percent, sufficient demand should emerge to absorb the speculative construction. In fact, the Inland Empire is anticipated to be among the nation’s leading absorption markets again this year. Much of the new demand will come from major firms opening distribution centers. Amazon.com, for instance, will open a 1.2 million-square foot distribution center in Moreno Valley in late 2014, adding about 1,000 jobs to local payrolls.

Sales activity stepped back last year as the market transitions from largely value-add plays to a more traditional investment climate. As the recovery in the investment market began gaining momentum in 2012, investors with a tenant-in-tow or those seeking highly vacant properties were challenged to find deals in Los Angeles and Orange counties. After turning to the Inland Empire, the number of distressed or deeply discounted properties available evaporated, while conditions had yet to improve enough to pull traditional operators off the sidelines. This year, more investors will move eastward as rising rents and some of the strongest tenant demand in the nation occurs in the metro. Deals with less than 100,000 square feet began the year trading at average cap rates in the mid-7 percent range, plus or minus 50 basis points depending on location. Larger deals, between 100,000 and 250,000 square feet, change hands at average first-year returns above 8 percent.

2014 Market Outlook

- **2014 NII Rank: 9, Up 2 Places.** Projections for strong absorption and rent increases propelled the Inland Empire into the top ten of the NII.
- **Employment Forecast:** After 44,100 jobs were created last year, employers will hire a net of 27,500 workers in 2014, expanding staff by 2.2 percent.
- **Construction Forecast:** Developers will be active again this year, adding 15.5 million square feet of space. In 2013, 10 million square feet came online.
- **Vacancy Forecast:** Vacancy will dip 10 basis points in 2014 as developers maintain pace with new demand. By year-end 2014, vacancy will rest at 5.1 percent. Last year, vacancy dropped 160 basis points.
- **Rent Forecast:** Asking rents will advance 5.4 percent to $4.70 per square foot this year, building on a 6.7 percent climb in 2013.
- **Investment Forecast:** Fewer value-add deals will be found, though high yields should support deal flow in the Inland Empire.
Strengthening Industrial Performance Brings Return of Speculative Construction

The Seattle-Tacoma industrial market is tightening on favorable demand drivers, prompting developers to ramp up construction. Durable employment and economic growth in the Puget Sound has pushed up demand for space among warehouse and distribution users. Overall vacancy is at nearly a six-year low heading into 2014, as builders undertake several speculative projects throughout the metro. The 650,000-square foot Coho building, underway in the White River Corporate Center in Puyallup, is slated to deliver in the third quarter. In the metro’s most active industrial area, Kent Valley, a 320,000-square foot multi-tenant warehouse delivered earlier this year, while in the same area, Amazon is slated to build its fourth Washington fulfillment center. The company announced plans in the first quarter for a nearly 1 million-square foot facility in the city of Kent. The market’s healthy condition will maintain robust absorption this year, further improving the outlook for operators, despite the recent return of speculative construction.

Investor demand is outpacing listings of industrial assets amid strengthening operations. Transaction velocity is growing throughout the metro, particularly in Auburn and Renton, as well as Pierce County. Institutional investors continue favoring Kent Valley due to its strategic location between the major ports and proximity to Sea-Tac Airport. Demand for warehouse and distribution facilities in this area with at least 30-foot clear heights is strong, as these buildings allow tenants maximum use flexibility. Cap rates in Kent Valley average from the mid-5 to low-6 percent range, while assets with larger floor plates can trade at initial yields below 5 percent. Investors seeking higher yields in outside areas such as Snohomish County will find cap rates in the 7 percent range and above.

2014 Market Outlook

- **2014 NII Rank: 5, Down 2 Places.** Steady payroll and rental growth coupled with limited supply-side threats kept Seattle in a top-five position.

- **Employment Forecast:** A steady pace of hiring in the private sector will underpin the addition of 45,800 jobs in the metro this year, marking a 2.5 percent employment expansion. Last year, 46,800 jobs were created.

- **Construction Forecast:** Developers will complete 2.8 million square feet of space this year, more than half of which will deliver in Puyallup and South Hill. Last year, builders brought nearly 2.7 million square feet online.

- **Vacancy Forecast:** Net absorption will total more than 3 million square feet for a third consecutive year, pushing vacancy down 40 basis points to 5.3 percent. In 2013, vacancy dropped 40 basis points.

- **Rent Forecast:** Average asking rents will rise 3.9 percent to $6.99 per square foot this year, following a 4.3 percent bump in 2013.

- **Investment Forecast:** Intense investor demand will maintain downward pressure on cap rates throughout the metro, particularly within Kent Valley.
Capital Flow to Industrial Investments Robust as Performance Escalates

Strong performance continues to fuel global investor demand for U.S. commercial real estate, particularly in sectors such as office and industrial properties where recoveries are gaining momentum. The industrial sector attracted keen interest from both private and cross-border buyers, but the biggest shift in buyer composition occurred in the well-capitalized listed REIT segment. REITs acquired $10.7 billion of assets in 2013, representing a 67 percent increase over 2012 and 21 percent of total sales volume. Cross-border capital flows into industrial properties increased 20 percent in 2013, totaling nearly $3.0 billion. Foreign capital sources thus far remain focused primarily on the safety of warehouse assets located in major metros and secondary markets, while listed REITs and private buyers dominate acquisitions in single-tenant properties and secondary and tertiary markets. The momentum in investor demand and improved property operations curbed the impact of volatility in the 10-year Treasury last year.

Industrial mortgage originations rose 52 percent year over year through the first quarter. National and regional banks cumulatively originated 54 percent of loans, followed by life companies at 21 percent. International banks accounted for 6 percent of originations, doubling their market share from one year earlier. Aggregate CMBS issuance increased 78 percent to nearly $90 billion in 2013, as conduits offered new and increasingly flexible products, yet market share for industrial loans fell 200 basis points to 13 percent as other lenders offered competitive terms. The delinquency rate of CMBS loans is declining, with industrial loan delinquency decreasing 350 basis points over the past year to 8.72 percent as of May 2014. An increasingly competitive marketplace has made lenders more willing to finance deals of greater complexity and geographic diversity, and additional investors are willing to take on challenged, capital-intensive assets. Banks and life companies remain constrained in the amount of leverage offered and the markets and acquisition strategies they can fund despite a general easing in CRE loan standards.

2014 Industrial Capital Markets Outlook

- **Debt and Equity Remain Active and Stable.** The environment is not without risk, and near-term interest-rate volatility should be expected. As the Fed tapers quantitative easing and the market decodes statements by a new Federal Reserve chief, volatility risks will remain.

- **The Industrial Cap Rate Spread Over 10-year Treasury Remains Higher than Long-Term Average.** With the cap rate for industrial properties at 7.6 percent, the spread of 500 basis points to the 10-Year Treasury stands near a historic high and already encompasses a 100-basis-point Treasury hike. The 6.7 cap rate for warehouse assets in the six “preferred” metros narrows the spread by 90 basis points, compared with a warehouse asset in a secondary metro at 8.1 percent.

- **Capital Flows to Broader Market Segments.** Institutional and foreign capital will maintain steady demand for core assets in primary markets. Risks of higher financing costs could erode some of the cap rate arbitrage of investing in secondary and tertiary markets or value-add assets, but lender competition and the pace of occupancy and rent growth will remain robust.

Note: Employment growth is calculated using seasonally adjusted monthly averages.

The information contained in this report was obtained from sources deemed to be reliable. Every effort was made to obtain accurate and complete information; however, no representation, warranty or guarantee, express or implied, may be made as to the accuracy or reliability of the information contained herein. Sources: Marcus & Millichap Research Services, Bureau of Labor Statistics, CoStar Group, Inc., Economy.com, Georgia Port Authority, Port authority of New York and New Jersey, Real Capital Analytics and The Port of Los Angeles.