Industrial Insight

When It Rains, It Ports

Supply Chain Disruptors to Influence U.S. Industrial Market Activity in 2H 2024

NEWMARK

At the 2024 halfway mark, industrial occupiers see a U.S. consumer still positioned to spend, compelling normalized levels of inventory replenishment after a protracted period of destocking, which will support continued net positive industrial absorption. This summer, import volumes are expected to hit their highest levels since 2022[1].

With the persistent global disruptions over the past four years, supply chain managers have adopted strategies that address both systemic and situational risks to their networks. The major ongoing investment to expand North American manufacturing, as well as many firms diversifying ports of entry and transport modes for flexibility, are examples of how firms are looking to meet domestic demand and preempt disruption.

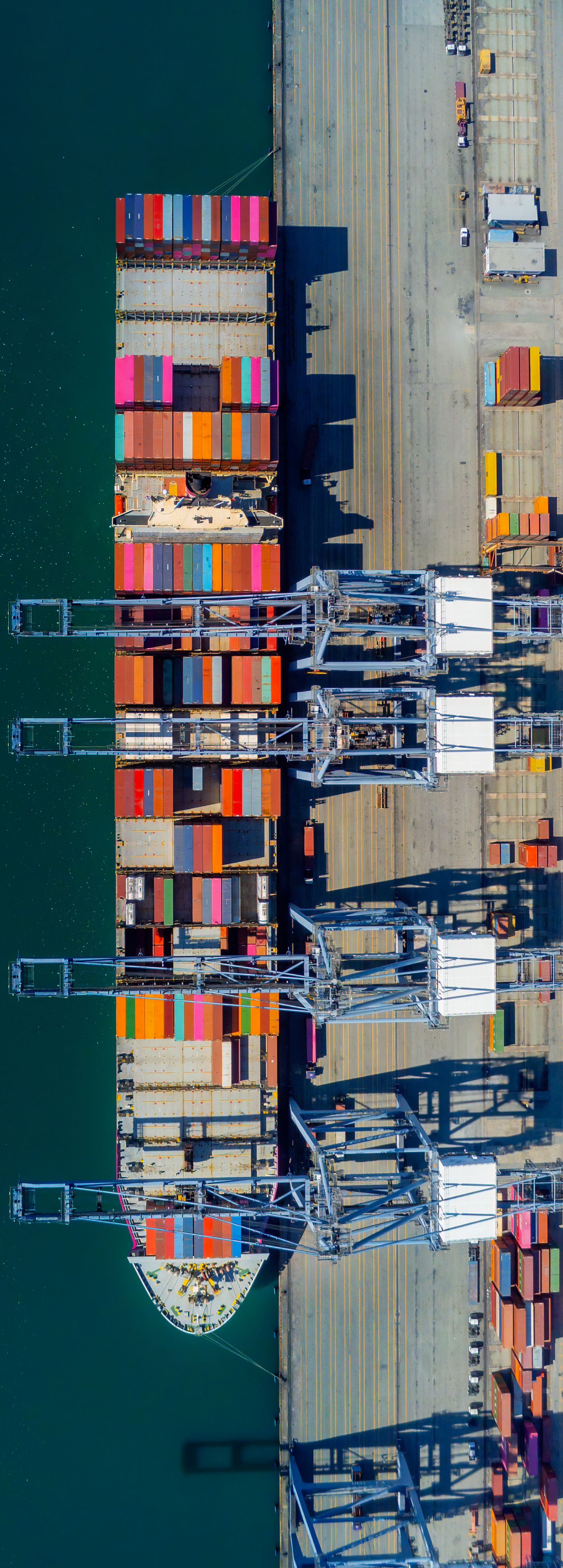
Already, those "optionality" levers have been pulled in response to the latest set of global disruptions (chokepoints at the Suez and Panama canals). As those existing challenges may be easing, the latter half of 2024 is poised to deliver a new wave of supply chain disruptors closer to home, potentially deepening industrial demand trends observed this year in some markets and driving new requirements in others.

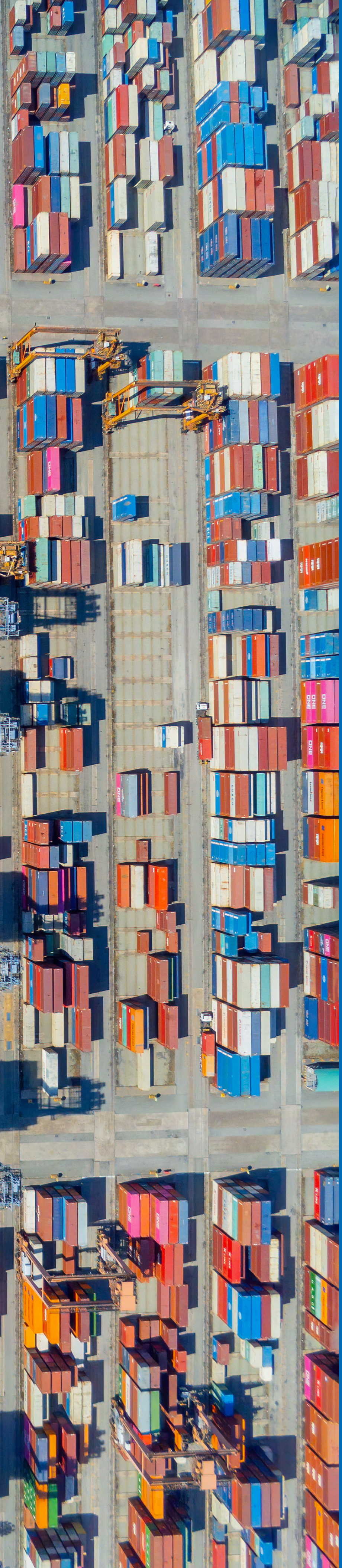
Domestic challenges on the horizon profiled in this report are threefold:

ENVIRONMENTAL

LABOR-RELATED

GEOPOLITICAL





Environmental

The National Oceanic and Atmospheric Administration (NOAA) forecasts a record Atlantic hurricane season, threatening East and Gulf coast ports. Weather-related port disruptions can be short but sharp, potentially affecting multiple ports simultaneously (e.g. Hurricane Sandy caused port closures from Virginia to New York in 2012). Impacts to cost and timeliness of freight transit extend past the ports; for example, private trucking capacity diverted to disaster relief could impact regional freight operations

Labor-Related

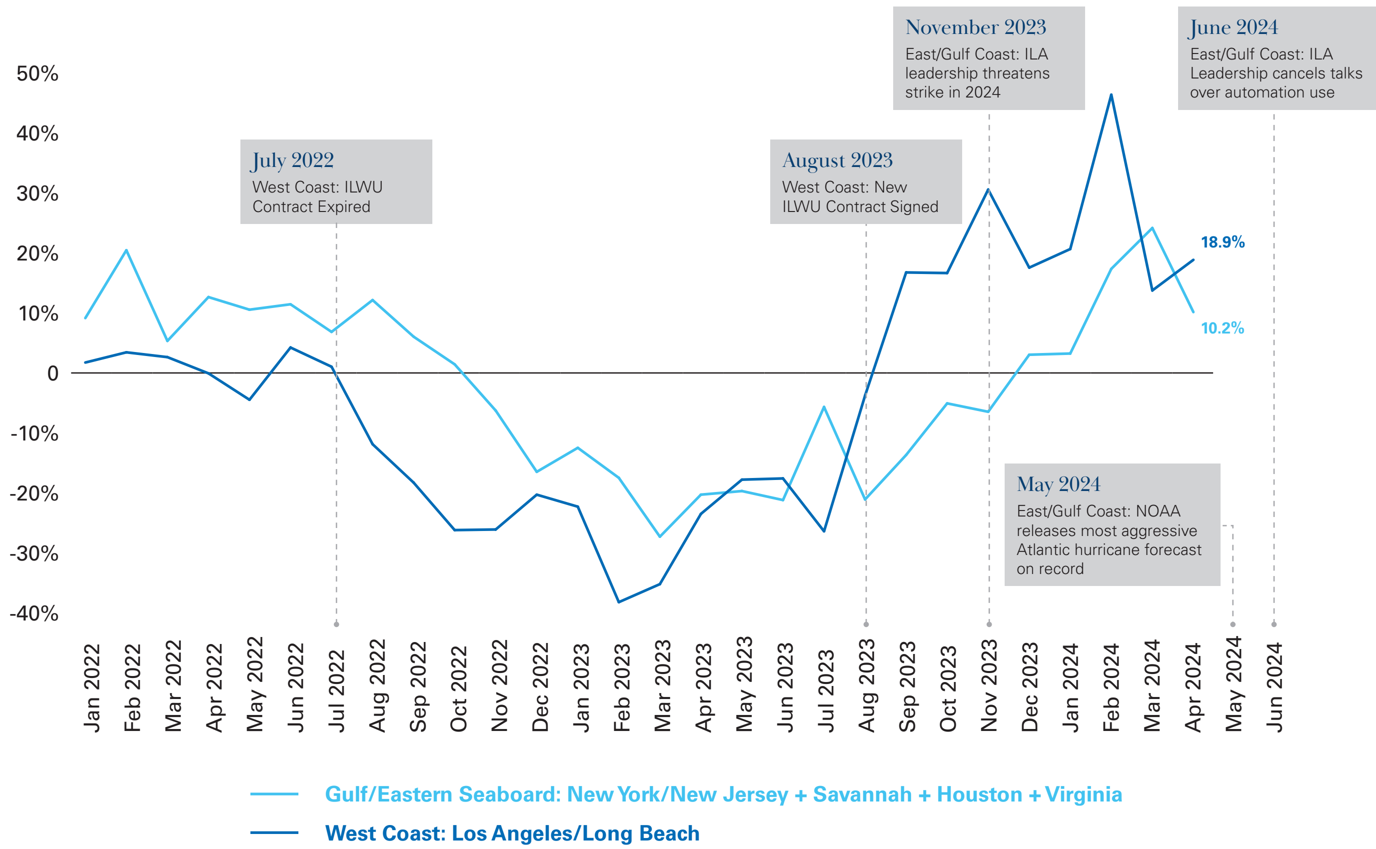
Compounding possible East/Gulf coast environmental challenges is looming port labor unrest. The International Longshoremen's Association (ILA), representing port workers from Texas to Maine, recently suspended scheduled contract talks. This contentious start recalls the International Longshore and Warehouse Union (ILWU) contract negotiations on the West Coast from 2022 into 2023. During the ILWU's contract negotiation period, the East/Gulf coast port share grew by nearly three percentage points, a record annual shift in historical context, as many shippers rerouted cargo to avoid delays. Year-to-date port data signals a seesaw effect as some cargo shifts back West – more will likely follow if talks drag past ILA contract expiry in September.

Geopolitical

Globally, China accounts for 31% of manufacturing output but only 13% of consumption[2]. With weakening domestic growth, new Chinese export orders have grown for five consecutive months, contributing to higher U.S. import volumes[3]. Concerns over cheaper Chinese products flooding markets, in part, prompted new tariffs enacted by the Biden Administration, including a 100% tariff on EVs. Concurrently, market participants note increased Chinese third-party logistics (3PL) industrial requirements in numerous primary markets, but particularly in the Southern California markets that support the largest U.S. port complex (and by extension, largest port of entry for Chinese imports). With inventory replenishment resuming, Chinese 3PLs may be expanding to support regional consumption, and the proliferation of Chinese e-tailer entrants to the U.S. market. This activity may also be motivated by getting product into the States before tariffs go into effect, including those announced this year, or potential new announcements. While geopolitical tension may spur some industrial expansion, some firms are cautious about making capital expenditures considering the potential for new or countermanded policies, or macroeconomic fluctuations, especially with a U.S. presidential election pending.

Potential East/Gulf Coast Port Disruptors Likely to Further Boost West Coast Port Volumes Amid Overall Import Growth

Major U.S. Seaports: Annual Change in Loaded Imported TEUs
By Month



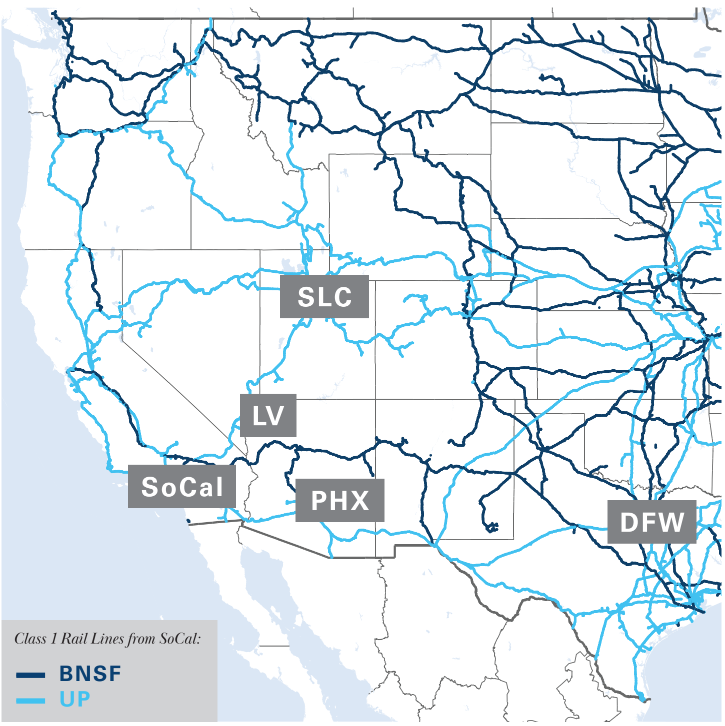
Sources: Newmark SoCal Research, WSJ, NOAA, Individual Seaports

Taken altogether, these factors are likely to increase warehouse utilization (depressing sublease additions) and industrial requirements in Southwest intermodal markets that are within a one-day drive cycle or rail-connected from Southern California ports. The pricing gap between Southern California and "the extended SoCal Port universe" - Las Vegas, Salt Lake City, Phoenix and others, remains substantial. It is simply more cost effective to house longer dwell-time inventories not meant for the Southern California population base, outside of the region. Rail connectivity allows distributors to reach a wide network of markets with a lower carbon footprint, an important consideration for SoCal importers. For time-sensitive goods, air cargo – already seeing double-digit volume growth this year – will continue to be a critical transit mode, positively impacting warehouse utilization and occupancy in air-cargo hubs[4]. While the current economic environment is not conducive to ramping up inventories more than necessary, and there is still slack in warehousing utilization as seen in the amount of sublease space on the market, an eventual return to net industrial expansionary activity will grace Southern California markets as well. The ramp up in Chinese 3PLs noted above could be a bellwether of that return.

While these shifts are likely to be most acute over the latter half of this year and into next, diversification of industrial operations (e.g. committing to sites in strategic markets) for greater supply chain resiliency will continue to drive new requirements for space across the country, especially for the most modern, efficient space. Onshoring, nearshoring and domestic manufacturing expansion will also continue to drive requirements in both the manufacturing and logistics sectors, as the cascade of global interruptions to supply chains continues to underline the attractive attributes of a make-where-you-sell strategy, especially for critical industries.

Shifting Cargo Points of Entry Contributing to Greater Leasing Volumes in Key Southwest Intermodal Markets

Industrial Fundamentals in Select Southwest Markets



Market	Leasing Vol. 4Q Rolling Sum (MSF)	% Change From Annual Leasing Volume,'17 - '19	1Q24 Average Industrial Asking Rent
Phoenix	30.9	32%	$11.20
Salt Lake City	13.7	23%	$10.45
Las Vegas	12.7	10%	$14.24
Dallas	62.7	0%	$9.62
SoCal (LA + IE)	82.0	-22%	$18.31
USA	**750.4**	**-9%**	**$10.14**

Source: Newmark Research, CoStar. 4Q Rolling Sum Between 2Q23 and 1Q24.

References:

1 National Retail Federation

2 Carnegie Endowment for International Peace

3 Wall Street Journal, Caixin, S&P Global PMI

4 Xeneta

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