Inland Empire Industrial Market

Frenzied Leasing Activity Causes Rents to Soar

- Vacancy is now on par with Los Angeles' 1.5% average.

- Desirable buildings that come to market can attract up to 10 offers; bidding wars ensue.

- Many tenants are agreeing to landlord terms when their leases are up for renewal; no negotiations.

- Restoration Hardware, Geodis Logistics, Skechers, Amazon, Subaru of America and FedEx all took occupancy of spaces greater than 500,000 square feet.

- Occupiers have taken 87.8% of the 20.9 million square feet of new supply delivered over the last 12 months.

- Loaded inbound volume at the ports in the first five months of 2021 was up 47.1% from the same period in 2020.

- Domestic distributors are trying to replenish inventories amid global supply chain disruptions, which is leading to severe congestion at Los Angeles-Long Beach.

- A total of 13 container ships were anchored, awaiting entry into the twin ports on June 24.

- Some companies are relying on air freight (up to 10x more expensive than ocean transport) to get product into the U.S.

The Just-In-Time (JIT) Inventory Model is Changing

Prior to the pandemic, JIT was a popular strategy for distributors to increase efficiency and decrease waste by receiving goods only as they are needed, thereby reducing inventory costs. Today's environment challenges the model.

China dealt with its first COVID outbreak in early 2020, which ground its factory operations to a near halt. The initial outbreak was eventually contained, China's economy reopened and, beginning in May 2020, a backlog of imports flooded U.S. ports. Import volume has not let up since. To compound matters,

Market Analysis

VACANCY AND ASKING RENT

Average Asking Rent (per SF/NNN) — Vacancy (%)
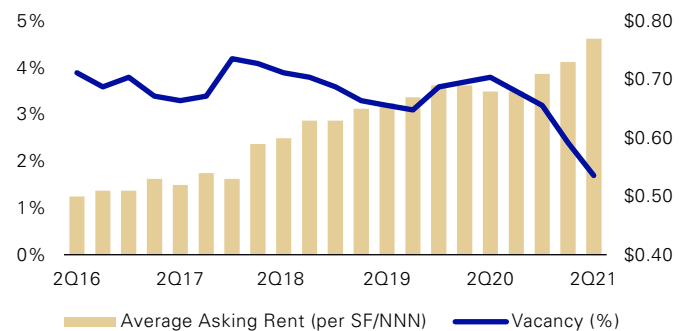
NET ABSORPTION, CONSTRUCTION DELIVERIES AND VACANCY

Net Absorption (SF) — Deliveries (SF) — Vacancy (%)
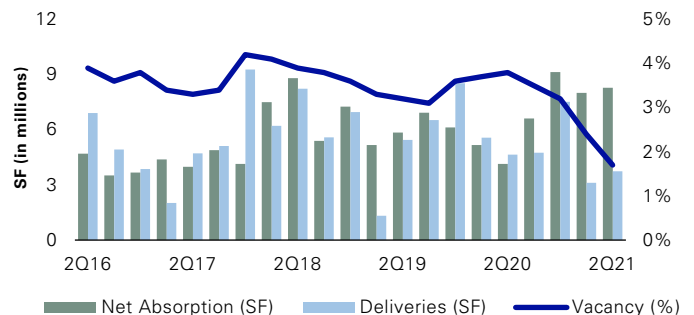
Market Summary

	Current Quarter	Prior Quarter	Year Ago	12-Month Forecast
Total Inventory (SF)	648.6M	644.8M	626.2M	↑
Total Vacancy Rate	1.7%	2.4%	3.8%	→
Quarterly Net Absorption (SF)	8.3M	8.0M	4.1M	→
Average Asking Rent/SF/Month	$0.77 NNN	$0.73 NNN	$0.68 NNN	↑
Deliveries (SF)	3.7M	3.1M	4.6M	→
Under Construction (SF)	22.6M	19.8M	18.7M	→

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there are growing concerns of another outbreak, this time from the Delta variant, in Southern China.

Global supply chain disruptions, whether in the form of a pandemic, port strike, raw material shortages or the blockage of a major trade route (e.g. the Suez Canal in March 2021) have serious repercussions on the costs (far higher) and timeliness (far longer) of goods entering the U.S.

The JIT model strains distributors in such periods and accounts for why many are shifting to more of a just-in-case model. By having excess inventory on hand, distributors can help mitigate against future disruptions.

Growing domestic inventory capacities leads to more demand for warehouse space, which favors a big-box market like the Inland Empire. When paired with pre-pandemic conditions, such as rising e-commerce sales, balanced development activity, healthy consumer spending, proximity to major consumer populations, access to multi-modal transport and demand for

modern facilities, then it is apparent why today's leasing activity is frenzied.

Contract Rents are Skyrocketing

Warehouse contract rents for direct leases and renewals over 100,000 square feet in spaces with a 30-foot and greater ceiling height had a weighted average of $0.71/SF/month in the first half of 2021, up 29.2% from the same period in 2020.

As of late, however, pricing benchmarks are being set on a deal-to-deal basis. There is also the time gap between recently signed leases and those in active negotiations. In the western half of the market, for instance, some leases were being negotiated north of $1.00/SF/month in late June.

Outlook

Landlord-favorable conditions abound, and very aggressive rent growth will follow. This is based on contracting vacancy and escalating land costs, which, in addition to pricy raw materials, will drive up replacement costs for new construction.
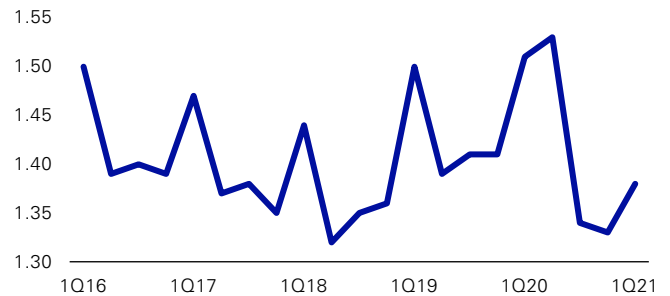
YTD Import Volume

Loaded Inbound Cargo
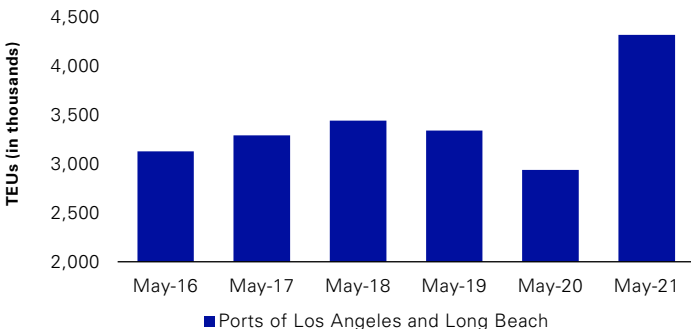
Source: Port of Los Angeles, Port of Long Beach

U.S. Total Business: Inventories to Sales Ratio

Quarterly Averages

Source: US Census Bureau (not seasonally adjusted); based on the most current data available

Lease Transactions

Tenant	Building	City	Lease Type	Square Feet
Mars Petcare	Phantom West & Nevada Avenue	Victorville	Build-to-suit	819,964
Noble House Home Furnishings	3655 E Philadelphia Street	Ontario	Renewal	741,458
Amazon	1895 Marigold Avenue	Redlands	New	699,350

Sale Transactions

| Buyer	Building(s)	City	Sale Price (PSF)	Square Feet
Costco	5600 E. Airport Drive	Ontario	$345,000,000 ($214/SF)	1,613,290
The Blackstone Group Inc.	3994 & 3996 S. Riverside Avenue	Colton	$231,200,000 ($166/SF)	1,396,495
Duke Realty Corporation	2151 S. Vintage Avenue	Ontario	$184,170,000 ($240/SF)	766,235

Submarket Statistics

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Net Absorption (SF)	YTD Net Absorption (SF)	Wh/Dist Asking Rent (Price/SF)	General Ind Asking Rent (Price/SF)	Total Asking Rent (Price/SF)
East I.E.	247,321,988	11,753,209	2.1%	5,393,492	7,989,714	$0.74	$0.75	$0.75
High Desert	14,249,066	843,544	3.8%	-97,854	-97,854	-	$0.51	$0.51
South I.E.	18,235,677	501,796	1.9%	-24,813	-41,345	$0.70	$0.85	$0.73
West I.E.	368,780,489	9,530,203	1.3%	3,015,304	8,446,510	$0.89	$0.94	$0.91
Market	**648,587,220**	**22,628,752**	**1.7%**	**8,286,129**	**16,297,025**	**$0.77**	**$0.77**	**$0.77**

Submarket Breakdowns

	Cities
East I.E.	Banning, Beaumont, Bloomington, Calimesa, Colton, Glen Avon, Grand Terrace, Highland, Loma Linda, Mentone, Moreno Valley, Perris, Rialto, Redlands, Riverside, Rubidoux, San Bernardino, Yucaipa
High Desert	Adelanto, Apple Valley, Barstow, Desert Knolls, Helendale, Hesperia, Lancaster, Lenwood, Lucerne Valley, Phelan, Silver Lakes, Victorville
South I.E.	Hemet, Lake Elsinore, Menifee, Murrieta, San Jacinto, Sun City, Temecula, Wildomar
West I.E.	Chino, Chino Hills, Corona, Eastvale, Fontana, Jurupa Valley, Mira Loma, Montclair, Norco, Ontario, Rancho Cucamonga, Upland

Net absorption is the change in physically occupied space. A hypothetical vacant and available space could lease this quarter with the tenant set to take occupancy six months later; positive absorption is not recorded until this physical move-in occurs. The space will remain vacant, but not available, until occupancy.

The total asking rent is the weighted average across warehouse, manufacturing, flex, incubator and general industrial properties.
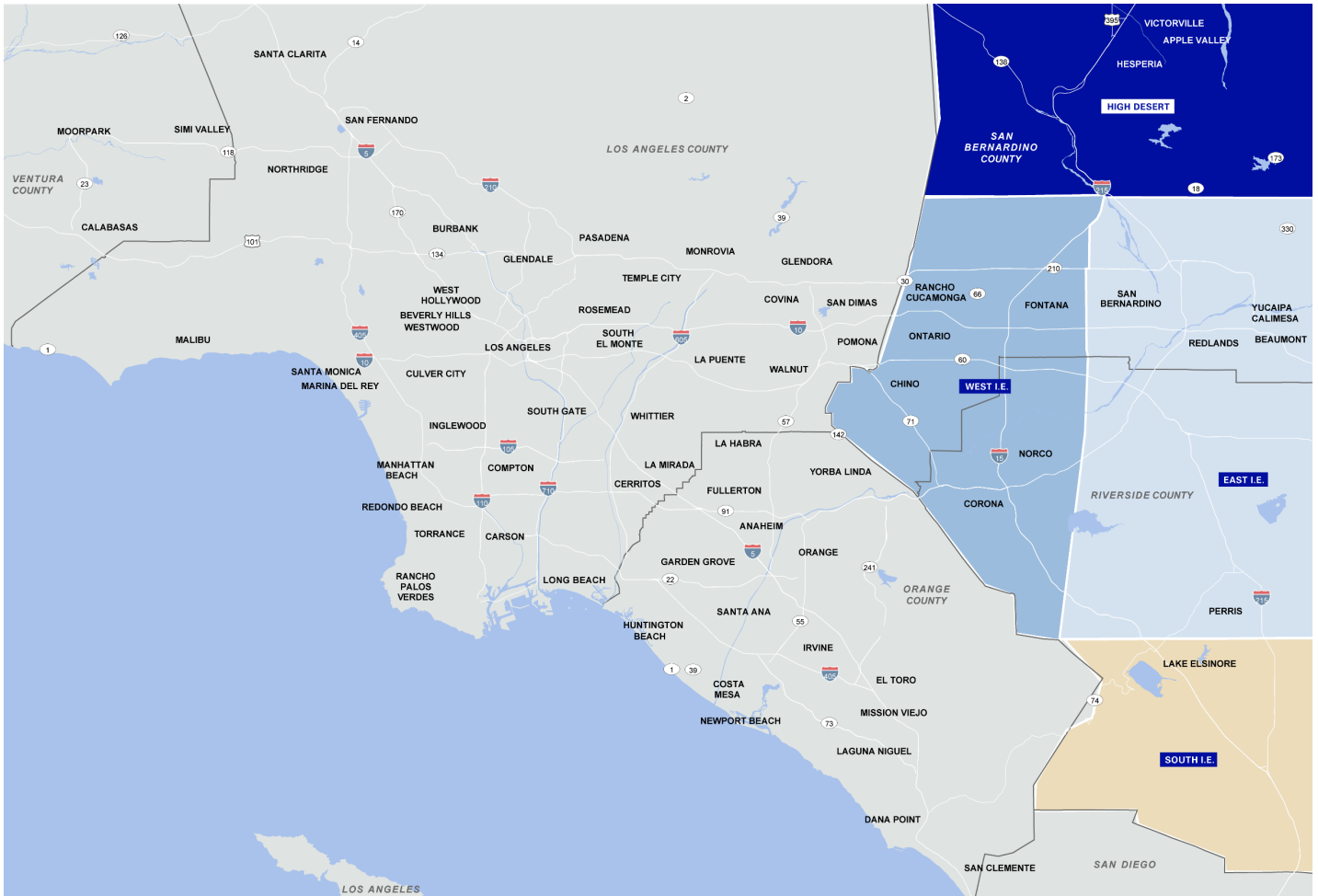
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