

3Q23

Inland Empire Industrial Market Overview

An aerial photograph of an industrial facility, likely a water treatment plant, featuring large rectangular basins covered with metal grates. The perspective is from a high angle, looking down at the grates which create a strong geometric pattern of parallel lines. The lighting is bright, casting shadows that emphasize the texture of the metal.

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Market Observations

Economy

- The drop-off in ocean container spot rates from Asia to the U.S. West Coast since the second half of 2022, along with “return-to-normal” import volumes at Southern California’s ports, speak to more conservative retail spending outlooks.
- West Coast port operators and dockworkers signed a new six-year contract; this will help to restore a sense of operational stability at Los Angeles-Long Beach.
- Loaded import volume at the twin-port system totaled 5.3 million containers in the first eight months of 2023. This figure is on par with the same period in 2016
- Local unemployment across all industries reached 5.3% in August. Industrial-using sectors have shed jobs in recent months.

Major Transactions

- Only 10 leases over 100,000 SF were signed this quarter. This is a far cry from the third quarter of 2022 when 36 leases were inked.
- Brookfield Properties acquired just under 40 acres of land in Rialto for \$72 million. The site, which is situated less than two miles from The Renaissance Marketplace retail center, is intended for development into a logistics terminal.
- MUFG Bank carried out the largest single-property acquisition in over two years when it purchased the 1.3 MSF Watson Logistics Center in Apple Valley from Big Lots in a sale-leaseback.

Leasing Market Fundamentals

- Total vacancy increased for the sixth consecutive quarter, going from 0.7% in early 2022 to 3.9% in the third quarter of 2023. Net absorption over this period totaled 13.4 MSF compared with 36.0 MSF in new construction deliveries.
- Available sublease space totals 10.1 MSF, a record high, and a jump of 54.0% from three months ago.
- Most occupiers are focused on cutting costs amid still-high inflation and more-restrained retail spending. Shedding extra space is one way to reduce overhead.
- Lease term lengths are trending down as tenants adopt a more cautionary stance. Some may be biding their time as they wait for rents to further decrease.
- Only 26.7% of the 39.8 MSF under-construction pipeline has pre-leased.

Outlook

- Rising vacancy and muted (at best) net absorption gains are expected. Next quarter, for instance, 29.4 MSF in new construction is scheduled to deliver. Of this, only 9.5 MSF is pre-leased to date.
- Direct rents will soften amid a large pool of sublease space, new construction delivering vacant and cooler leasing activity.
- U.S. retail sales are closely being watched; a sharp pullback will further slow industrial leasing activity.
- The SCAQMD (the same organization that successfully implemented the [WAIRE Program](#)) has proposed legislation to reduce emissions at Southern California’s ports. Cargo volumes could be capped if the group’s initiative passes.

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Economy



Lower Ocean Container Spot Rates Are Indicative of Cooling Import Activity



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Loaded Imports in the First Eight Months of 2023 Were on Par with the Same Period in 2016

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Some West Coast Importers Diverted Cargo to Gulf and Eastern Ports in 2022

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The ILWU and PMA Reached a Tentative Labor Agreement in June 2023

Their contract was ratified in early September, restoring a sense of much-needed stability at U.S. West Coast seaports for the next six years. Longshoremen at East and Gulf Coast ports will soon negotiate their contract that is set to expire in late 2024; will conflict that potentially disrupts operations be avoided?

West Coast Ports Agreement Reached...Finally!

- The International Longshore Warehouse Union (ILWU) represents dockworkers at 29 ports from Washington State to California. The Pacific Maritime Association (PMA) represents ocean carriers and terminal operators.
- The prior contract expired on July 1, 2022.
- The ILWU has a history of work disruptions in prior negotiation periods, ranging from strikes, to deliberate work slowdowns to under-staffing shifts.
- These disruptions have cost major retailers billions of dollars in the past.
- In March, for instance, the ILWU did not stagger shifts during meal period.
- A tentative agreement was reached on June 15, 2023 for what became a new six-year contract. Longshore workers secured a 32% salary increase.
- Many Asian importers pushed inbound goods to East and Gulf Coast ports as talks dragged on. Some of this traffic will return since stability is now less of a concern.



Source: Newmark Research, City of Los Angeles, The Real Deal

East and Gulf Coast Ports Are Up Next

- The International Longshoremen (ILA) represents dockworkers at 36 ports from Maine to Texas. The United States Maritime Alliance (USMA) represents ocean carriers and terminal operators.
- Their contract will expire on September 30, 2024.
- Both parties will start discussions early in hopes of avoiding disruptions.
- West Coast ports will be seen as more stable until an agreement is reached.
- Higher pay and job security as it pertains to automating port operations were primary issues for the ILA in 2018/the last negotiation period.



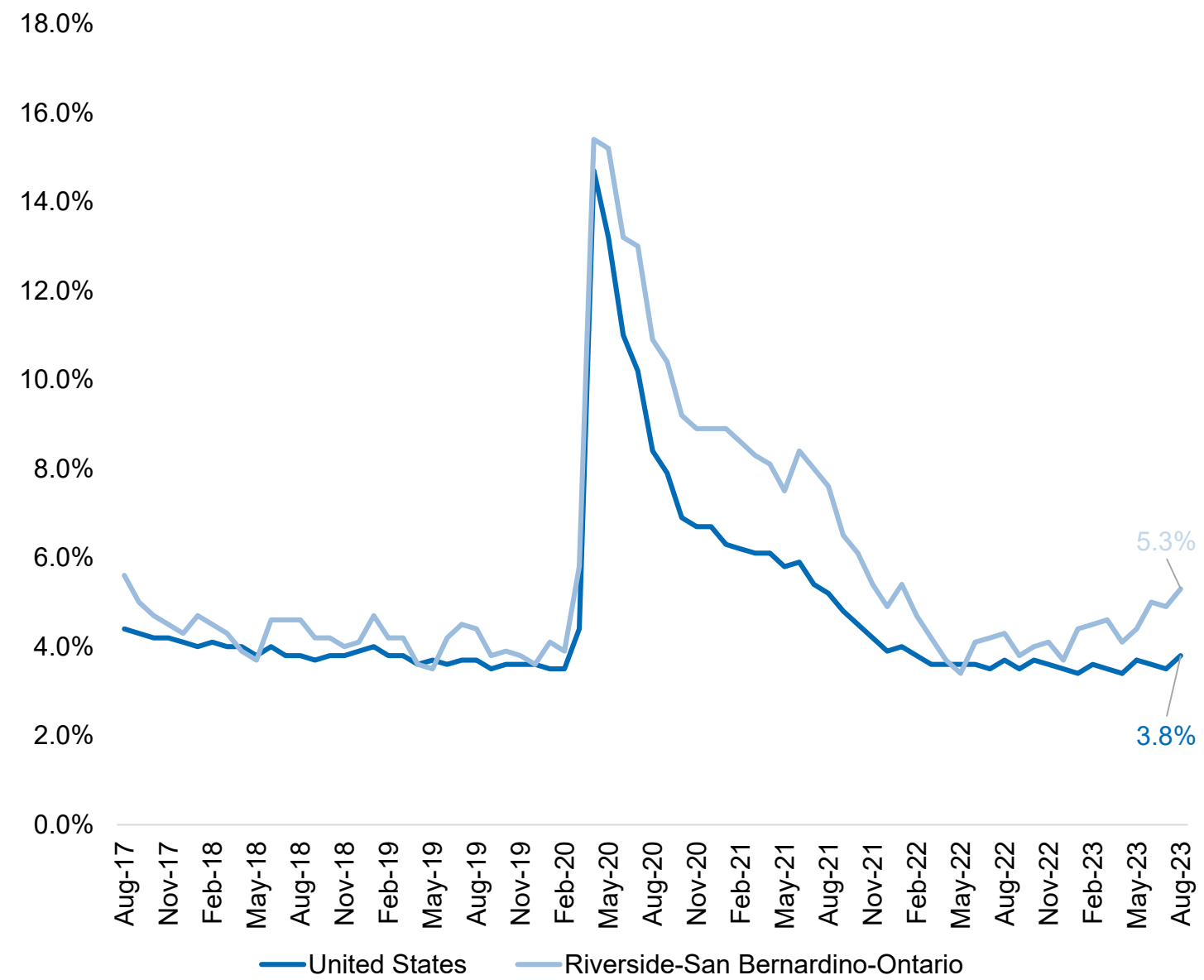
The Diverted Trend Continued to a Lesser Degree in the First Eight Months of 2023

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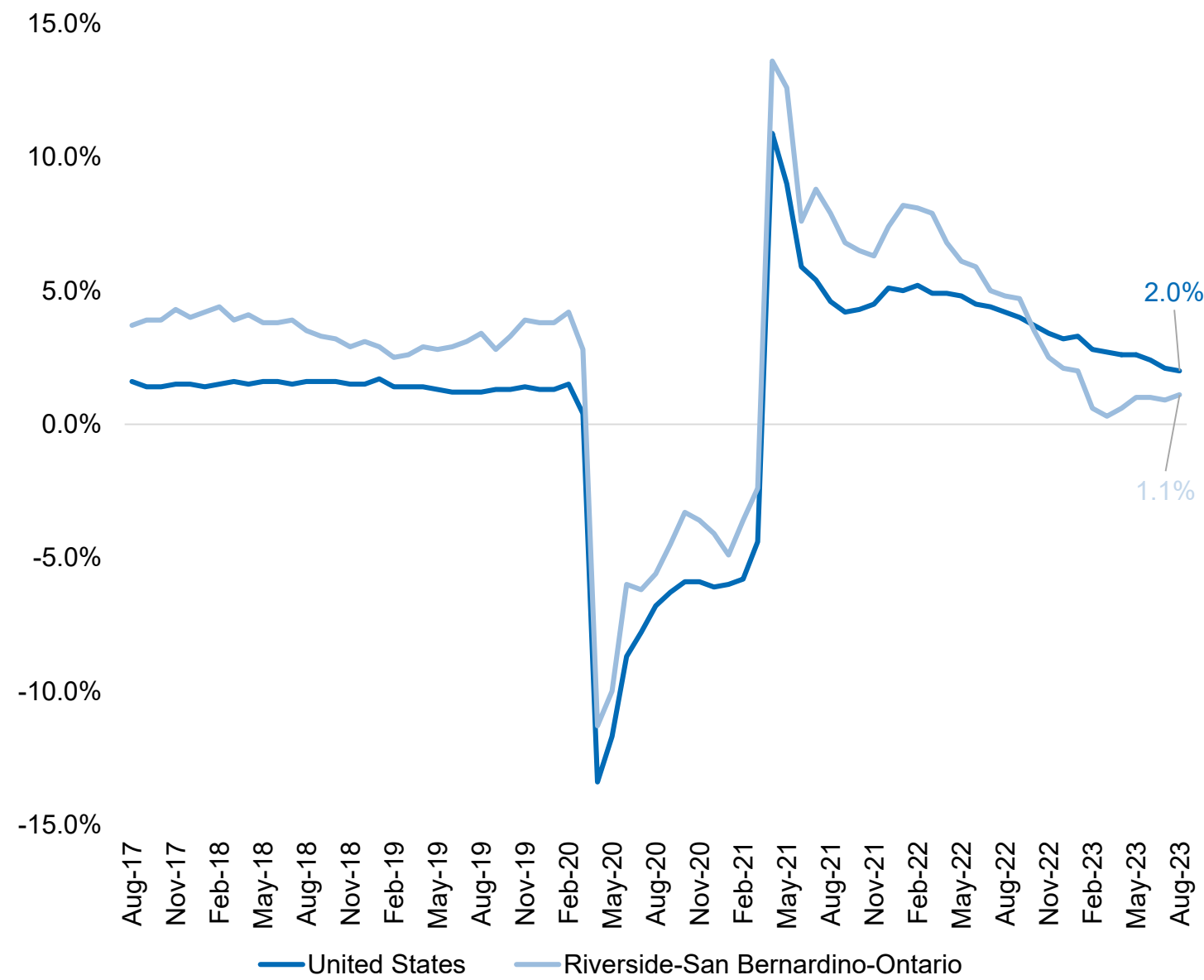
Local Unemployment Trends Upward; Overall Job Growth Slows

Local unemployment rate experienced an end-of-summer bump, despite modest nonfarm employment growth in August. Total nonfarm employment growth has stagnated over the past 15 months, largely from job losses in industrial-using sectors.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change

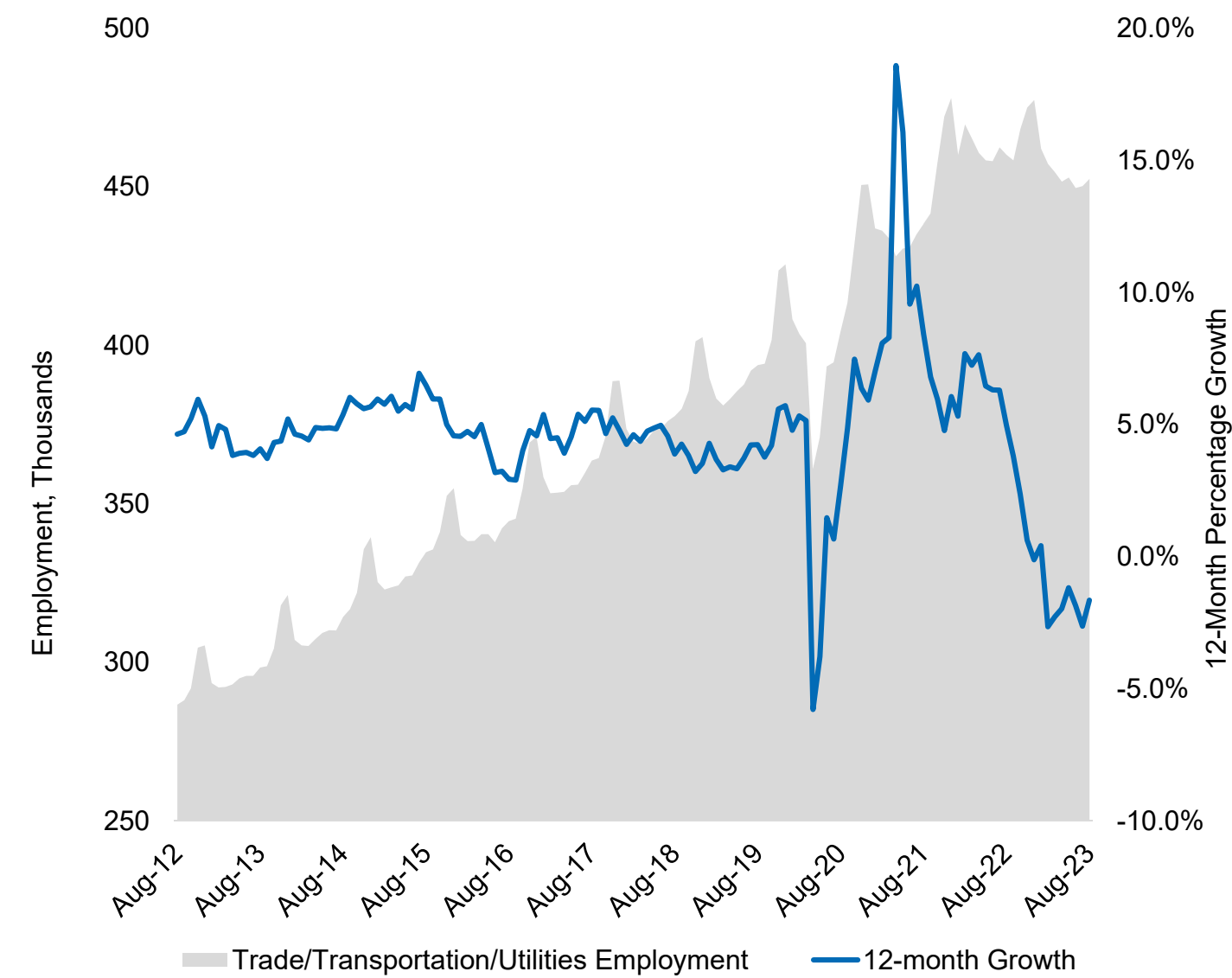


Source: U.S. Bureau of Labor Statistics, Riverside-San Bernardino-Ontario

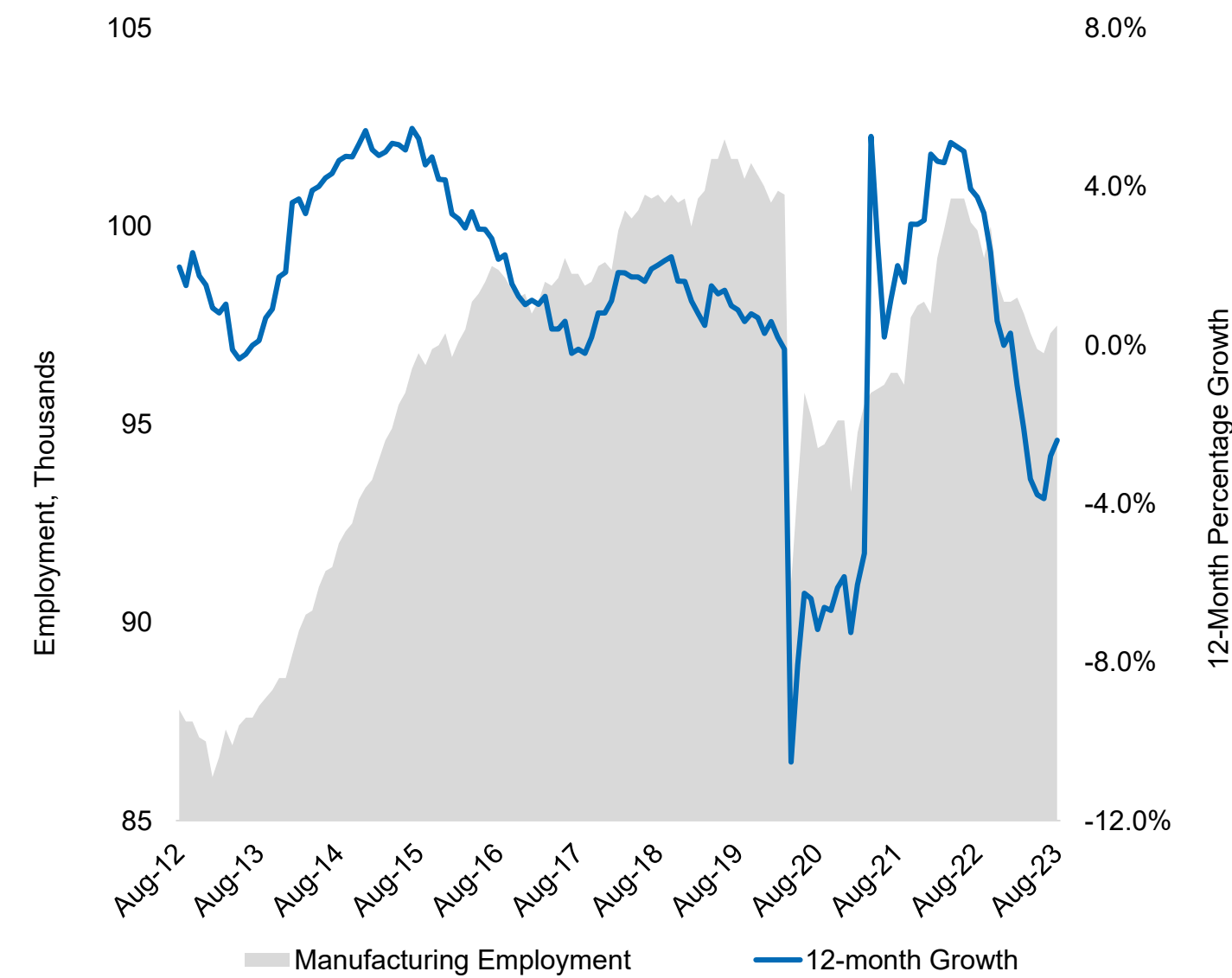
Industrial Employment Ebbs Over Past Year; More Projected Losses to Come

Amazon, which is the market’s largest employer, announced it was cutting 18,000 global employees earlier this year. This partly shaped the recent drop-off in trade/transportation/utilities employment in recent months. Local manufacturers, meanwhile, are facing slowing global demand and ever-rising domestic business costs.

Trade/Transportation/Utilities Employment and 12-Month Growth Rate



Manufacturing Employment and 12-Month Growth Rate



Source: U.S. Bureau of Labor Statistics, Riverside-San Bernardino-Ontario

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Leasing Market Fundamentals



Unprecedented Rent Growth Occurred from Early 2021 through Early 2023



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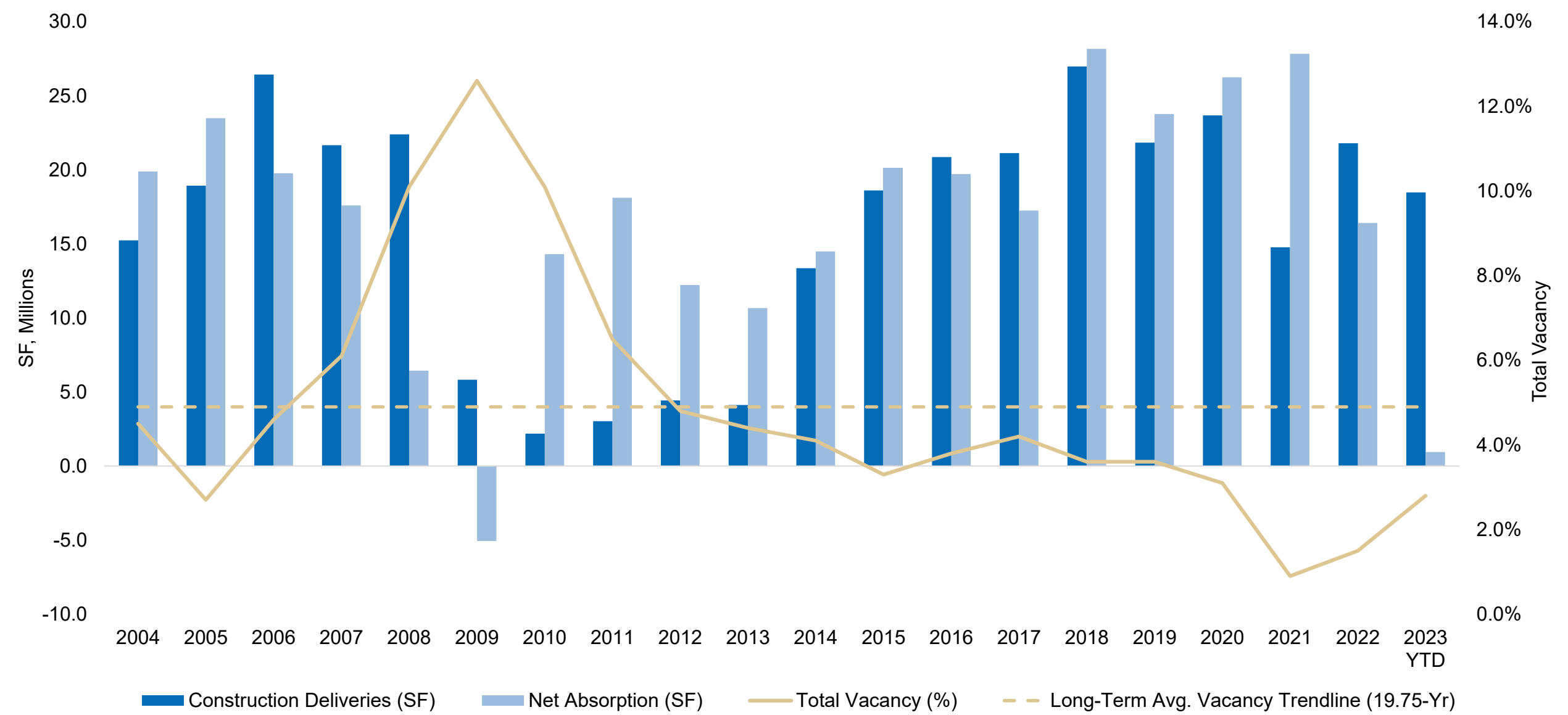
Average Weighted Lease Terms Are Declining

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Pre-leased Occupancies Counter Wave of Move-Outs; Vacancy Jumps

The market was able to avoid a significant net occupancy loss for the quarter due to the delivery of Amazon’s 4.1 MSF build-to-suit complex in Ontario and Target’s occupancy of the newly-delivered 1.2 MSF warehouse at Agua Mansa Commerce Park. Move-outs by tenants such as CJ Logistics (844,311 SF), Costco (800,000 SF), Skechers (643,263 SF) and Hillman Solutions Corp (609,888 SF) kept net absorption low. Vacancy (2.8%) is on the rise but remains well below the 19.75-year average of 4.9%.

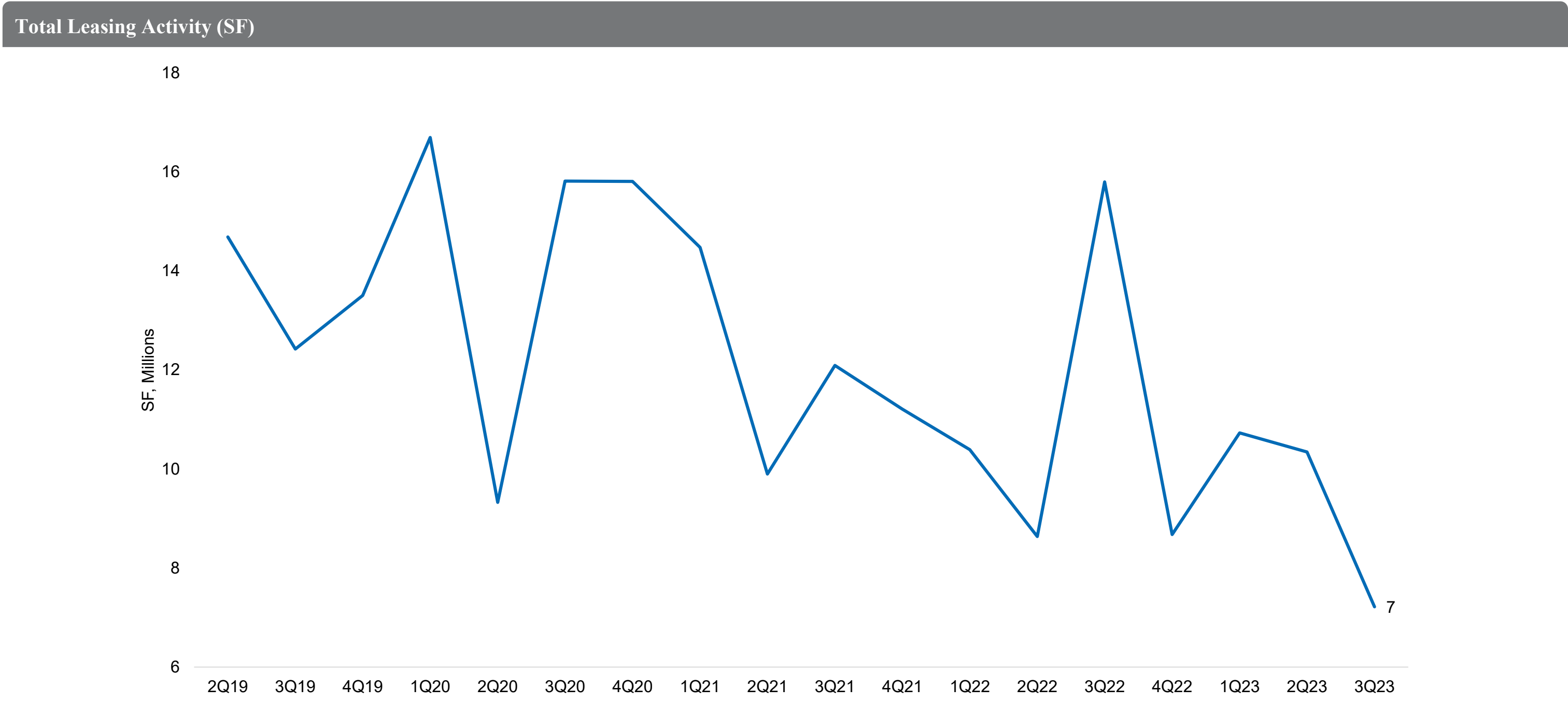
Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research

Quarterly Leasing Activity, Uneven Since Early 2019, Has Decelerated

The uneven factor is a function of how many mega-warehouse projects greater than 500,000 SF lease in a given quarter, coupled with macro economic conditions at the time (e.g., there was a great deal of uncertainty during the second quarter of 2020, the first full quarter after a national health emergency was declared). One trend is clear however: leasing activity is decelerating.

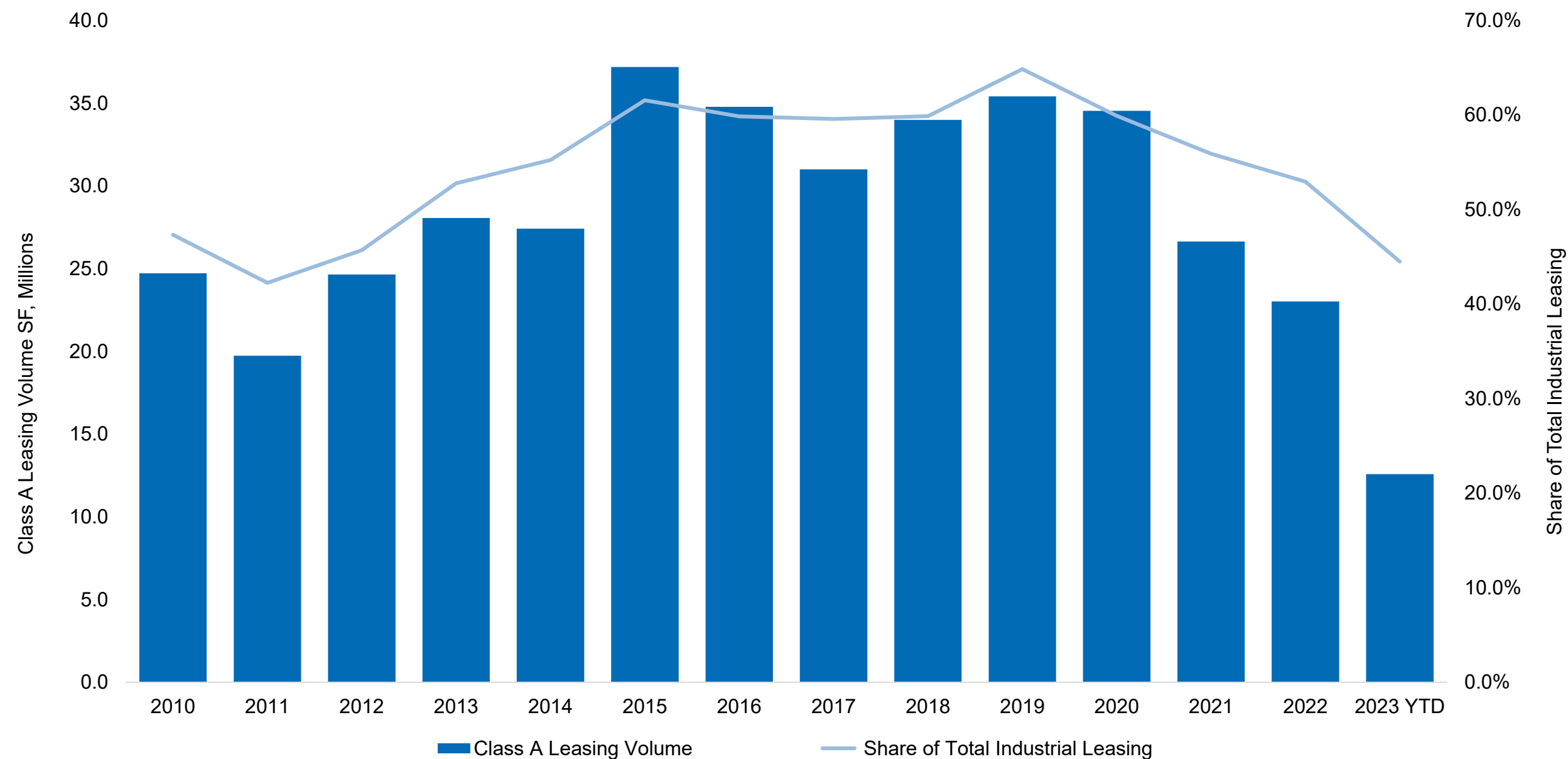


Source: Newmark Research, CoStar

Class A Warehouse Leasing Falls

Class A warehouse leasing accounted for 39.9% of total leasing activity in the first three quarters of 2023. This is below the 13.75-year average of 54.4%. Several tenants in the market are sitting on the sidelines and are waiting for rents to drop before committing to space. Pricing is the current issue, not demand.

Industrial Class A Leasing Volume and Percentage of Total Industrial Leasing Volume

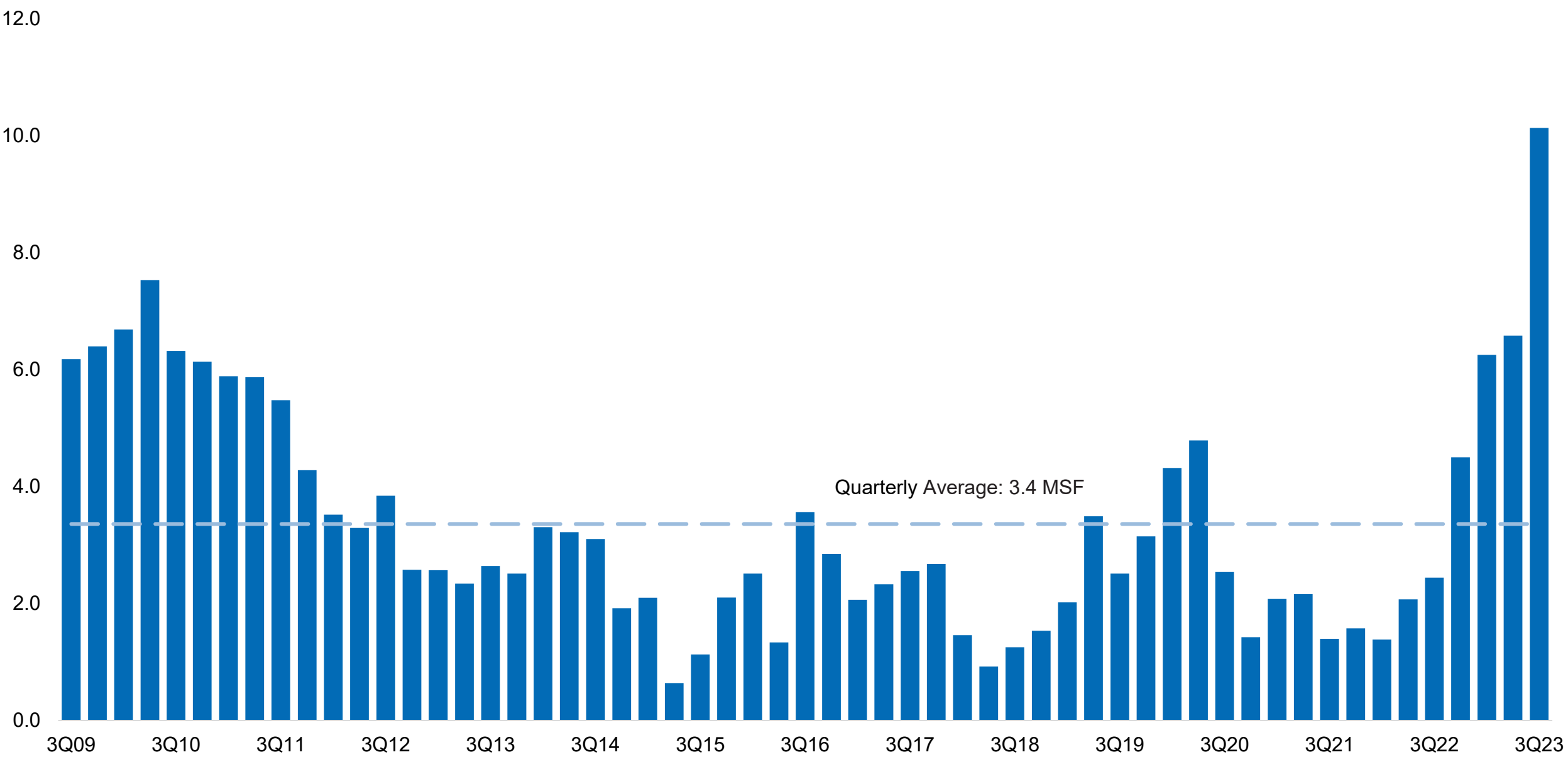


Source: Newmark Research, CoStar
Note: Class A is defined as 100,000+ SF warehouse/distribution facilities constructed since 2000 with a 30'+ minimum interior ceiling height.

Sublease Availability Explodes to Reach Record High

Sublease availability reached an all-time high of 10.1 MSF after jumping 54.0% from the previous quarter. Large listings by Costco (800,000 SF), Performance Team (468,139 SF), Goli Nutrition (422,432 SF), Studio RTA (238,321 SF) and Peloton Interactive (210,900 SF) contributed to this increase.

Available Industrial Sublease Volume (MSF)



Source: Newmark Research

Western Inland Empire Now Comprises Over 40% of Available Sublease Space

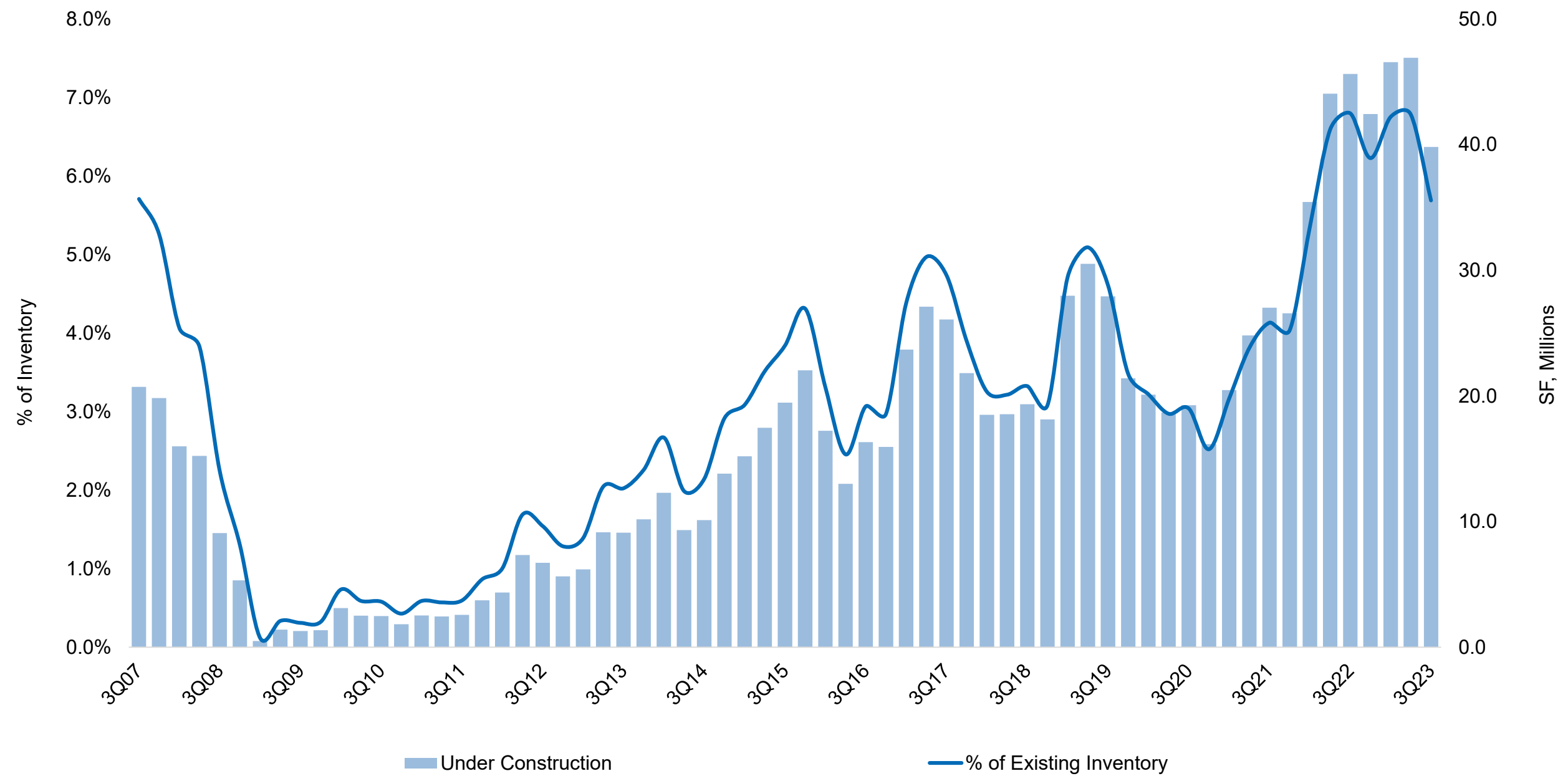


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Construction Pipeline Falls Below Prior Peak; Percentage of Pre-leased Space Falls

Underway construction totals 39.8 MSF, of which 26.7% is pre-leased. Market vacancy will further increase if this average does not improve.

Industrial Under Construction and % of Inventory



Source: Newmark Research

On a SF Basis, the 1 MSF+ Segment Predominates Underway Construction

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Notable 3Q23 Lease Transactions

No pre-leases over 30,000 SF were signed during the quarter. As pre-leases historically drive net absorption gains in the market, negligible activity could contribute to depressed net absorption gains and a rise in vacancy as new supply delivers in 2024.

Select Lease Transactions				
Tenant	Building	Submarket	Type	Square Feet
CEVA Logistics	12415 6 th Street	West-I.E.	Direct	752,497
Tenant leases entire building. Lease term expires in 1Q33.				
US Elogistics	1420 North Tamarind Avenue	East-I.E.	Sublease	677,225
Keeco is the subletter. US Elogistics' term expires in 3Q25.				
Armstrong Logistics Inc.	11618 Mulberry Avenue	West-I.E.	Direct	634,800
Tenant took space formerly occupied by LuLaRoe; Armstrong leases the entire building and has a term that runs through 3Q28.				
Ashley Furniture	2185 Lugonia Avenue	East-I.E.	Lease Renewal	500,602
Tenant has occupied the property since 2018. The five-year renewal had a starting rent of \$1.425 NNN with 4% annual escalations; the original lease had an initial rent of \$0.40 NNN with 3% annual bumps.				
Niagara	13032 Slover Avenue	West-I.E.	Direct	303,857
Tenant leases the entire building. Lease term expires 4Q28.				

WAIRE: Program Summary and Implications for Industrial

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Industrial Land Sales Volume in the High Desert Reached a New High in 2022

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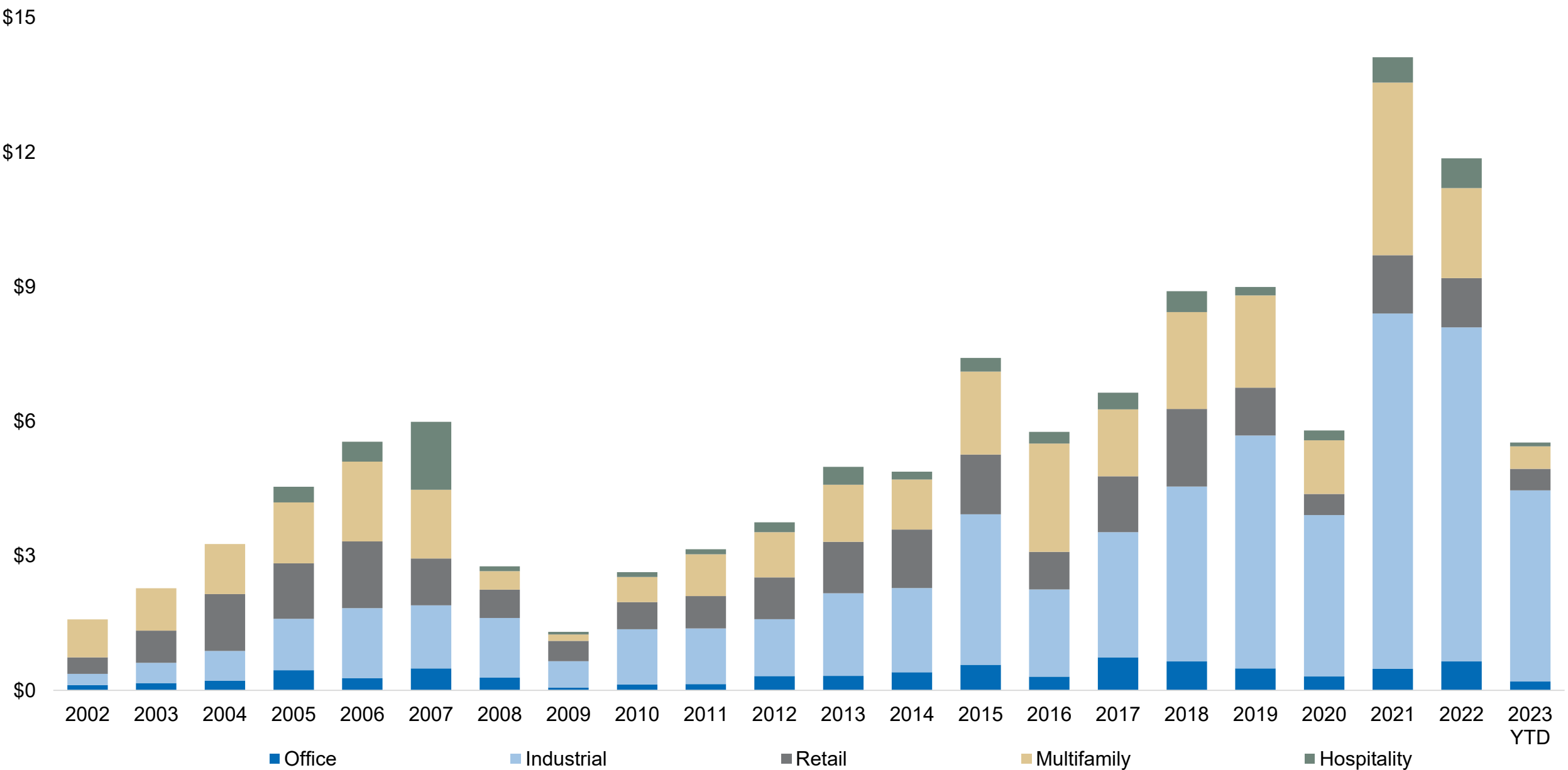
Sales Activity



Industrial Has Comprised an Unprecedented 77.0% of Total Sales Volume in 2023 YTD

77.0% vastly exceeds the 21-year average (2002 to 2022) of 39.3%. Heated rent growth in recent years favor the segment, with many investors targeting desirable buildings with credit tenants whose leases are up for renewal. What the tenant was paying (\$\$) is different than today's rent averages (\$\$\$\$).

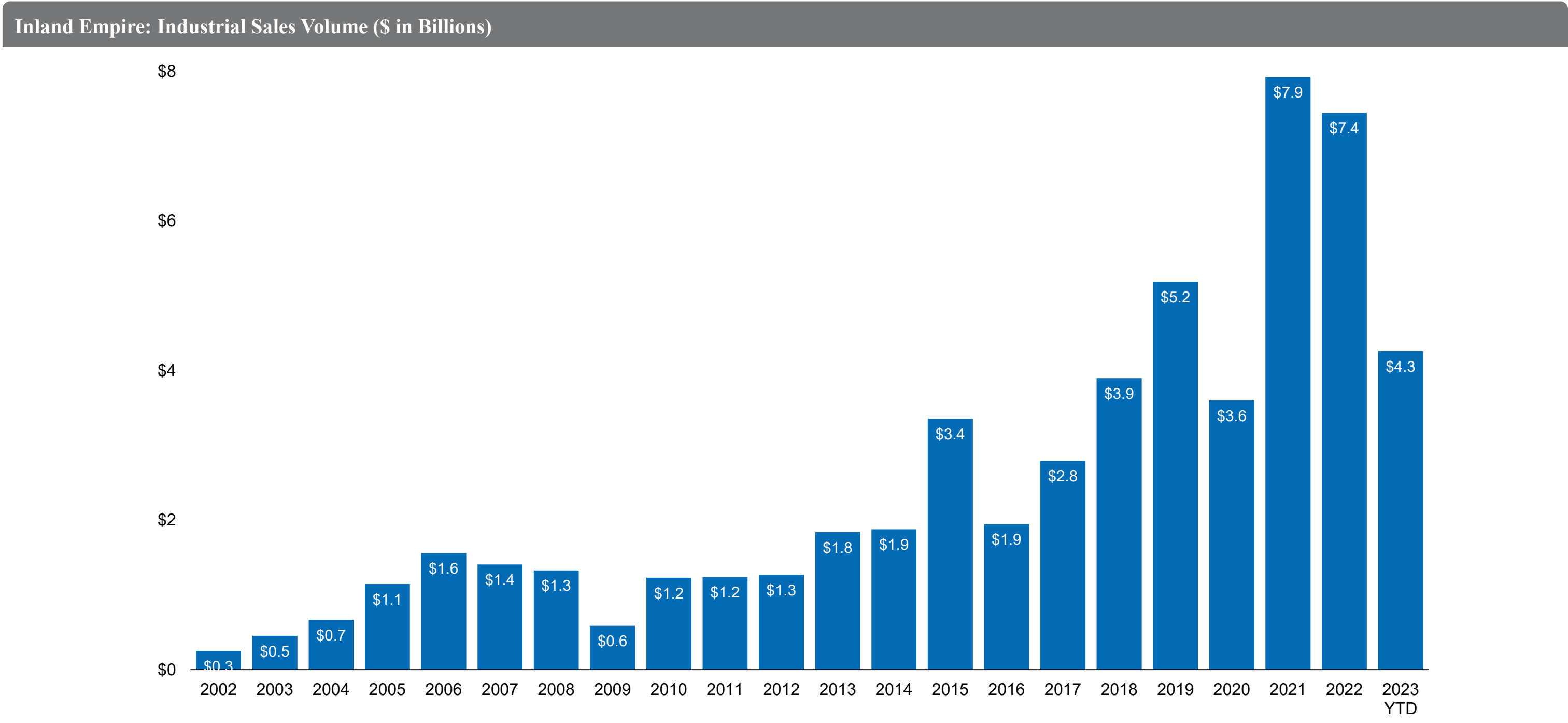
Inland Empire: Sales Volume Across Commercial Property Segments (\$ in Billions)



Source: MSCI Real Capital Analytics, Newmark Research
Note: Preliminary data is cited for the third quarter of 2023

Industrial Sales Volume: Up Close

Industrial sales volume totaled \$4.3 billion in the first nine months of 2023, and will fall short of 2022's total when the year is done. The higher cost of capital following multiple interest rate hikes is crimping momentum, in addition to cooling leasing fundamentals. Both will add downward pressure to pricing.



Source: Newmark Research, MSCI Real Capital Analytics
Note: Preliminary data is cited for the third quarter of 2023

Pricing Has Begun to Fall, While Cap Rates are Rising

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Share of Institutional Buyers Down Post-2021; All Other Investor Types Remain Active

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Appendix



Inland Empire Submarket Map and High-Level Statistics | 3Q23



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Inland Empire Submarket Statistics | 3Q23



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Inland Empire Statistics by Building Size Segment | 3Q23

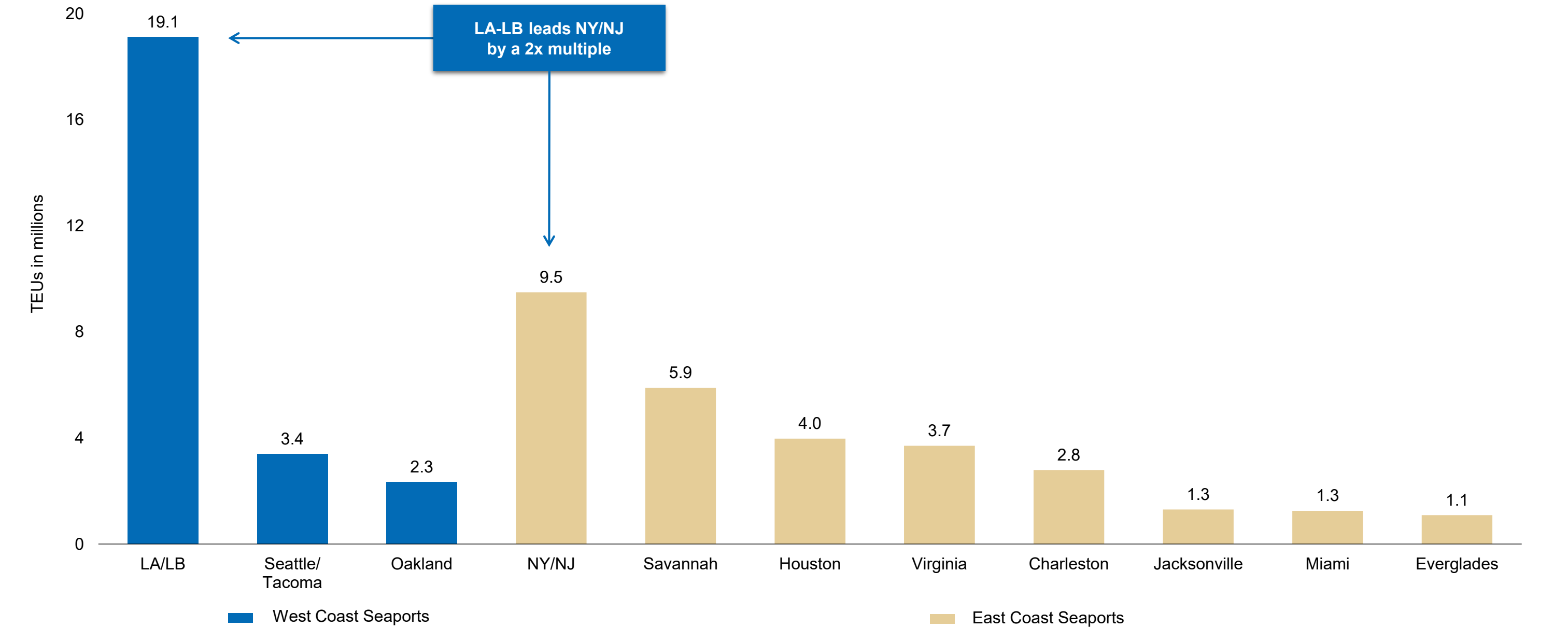


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Los Angeles-Long Beach is the Nation’s Dominant Port System

Los Angeles-Long Beach can accommodate 18,000 TEU vessels, which are too wide to traverse the new Panama Canal. Additionally, both ports have Class 1 freight rail connectivity to the nation’s major population centers.

Major U.S. Seaports: 2022 TEU Volume (All Containers: Loaded and Empty)



Source: Newmark Research, Individual Seaports
Note: Data is through February 2023 and is not adjusted for seasonality. Shaded areas indicate U.S. recessions

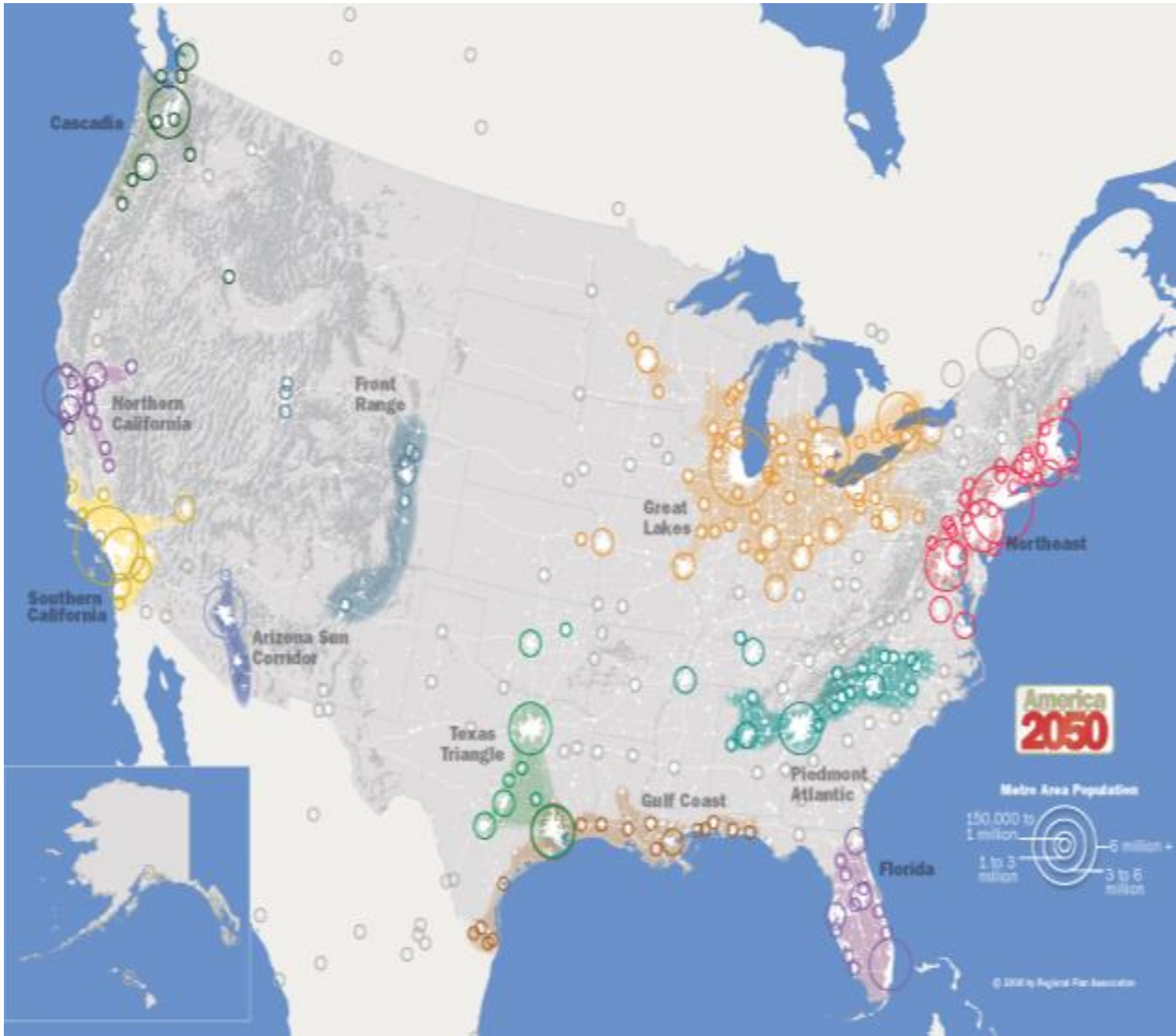
Why Los Angeles-Long Beach?



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Population of Megaregions: Past and Projected

Southern California benefits from its consumer base, ports and rail connectivity.



Megaregion	2010 Population	2025 Pop. Est.
Arizona Sun Corridor	5.7M	7.8M
Cascadia	8.4M	8.8M
Florida	17.3M	21.5M
Front Range	5.5M	7.0M
Great Lakes	55.6M	60.7M
Gulf Coast	13.4M	16.3M
Northeast	52.3M	58.4M
Northern California	14.0M	16.4M
Piedmont Atlantic	17.6M	21.7M
Greater Southern California	24.4M	29.0M
Texas Triangle	19.8M	24.8M

Source: U.S. Census Bureau

Transport Costs Are the Biggest Expenditure for Most Warehouse Occupiers



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Transport Costs Per TEU Container



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Amazon Is the Inland Empire's Top Occupier and Employer

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