

# THE STATE OF INDUSTRIAL: MARKET REMAINS ROBUST, BUT LABOR SHORTAGE A CONCERN

By Michael Hoban

As anyone even remotely familiar with the commercial real estate industry can attest, the industrial market remains red-hot, and despite historically low cap rates, the asset class continues to be a preferred target for American CRE investors. According to research by CBRE<sup>1</sup>, demand has exceeded supply for nine consecutive years by an average of 94.1 million square feet, driving the vacancy rate to a historic low of 4.3 percent at the close of 2018—even with new construction surpassing the 200 million-square-foot mark in 2018.

E-commerce is having an increasingly profound effect on logistics, with online sales requiring three times the square footage as traditional brick-and-mortar retail. E-commerce sales are expected to grow by \$75 billion in 2019, and CBRE researchers estimate that for each additional \$1 billion in e-commerce sales, an additional 1.25 million square feet of warehouse/distribution space will be needed to accommodate that growth, so demand will remain high for the foreseeable future.

Industrial specialist Brad Pope, SIOR, senior vice president with JLL Atlanta, used those eye-popping numbers to set the stage for an engaging panel

discussion on the “State of the Industrial Market” at the recent SIOR 2019 Spring World Conference in Washington, D.C. Moderated by Pope, the panel of industrial experts included Allen Gump, SIOR, executive vice president for the Dallas-Fort Worth office of Colliers International; Douglas A. Kiersey, Jr., SIOR, president of Dermody Properties; and John Van Buskirk, SIOR, founding principal of Lee & Associates of Eastern Pennsylvania.

While Pope’s stats bode well for continued growth in the sector, he cautioned that there are potential storm clouds looming on the horizon. The rate of growth for the economy has been slowing, (a little over 2 percent for the second half of 2019, predicts Bank of America | Merrill Lynch’s chief U.S. economist, Michelle Meyer); there are concerns over the long-term effects of tariffs and trade wars; a lack of developable industrial sites—particularly in the major metros—is hampering the delivery of new product; and the issue that seemed to weigh most heavily on the minds of the panelists: a shortage of labor.

“I don’t know if the old analogy of ‘What inning are we in?’ is even relevant anymore,” said Pope, acknowledging the havoc that e-commerce is wreaking upon

traditional logistics models. “Because I’m not sure we’re even playing the same game we’ve played in previous cycles.”

In July, the U.S. will surpass the record for the longest sustained economic expansion on record. Even with some signs that typically precede a recession (flattening yield curve, slowing home sales) beginning to emerge, growth remains slow and steady, and Kiersey feels that it would take an unforeseen calamity to derail the economy. “These expansions don’t die of old age, they die of some sort of animating event,” he noted, citing the savings and loan (S&L) crisis, 9/11, and the 2008 economic meltdown as examples. “But what we’re seeing right now is a great balance...and I don’t see that changing.”

Gump concurred, reporting that leasing demand in the North Texas market remains steady, as does the investor appetite for assets. “I’m not hearing any rumblings that ‘our business is off’ or ‘we’re going to have to pull back’ like we did in 2007-2008, when things started getting a little frothy. Everyone seems to still be doing well,” said Gump. He did express one potential concern, however, stating that the market may be “getting overbuilt in certain areas,”

and noting that Amazon has stopped taking million square foot buildings in his market.

The apprehension about overbuilding was seconded by Van Buskirk, who operates in the mid-Atlantic region (Eastern Pennsylvania, New Jersey, Baltimore, and the BWI corridor). He said the momentum in his market continues to be "incredible," citing rapidly escalating rents, a lack of developable land, historic high pricing, and an exceedingly tight leasing environment. But like North Texas, there may be some overbuilding in the less densely populated regions of Pennsylvania, with 16 one million square foot buildings either available or under construction in non-traditional locations.

"If you have 3-4 buildings popping up all at once in peripheral locations, and you don't have a real wind at your back from a labor standpoint, it will be interesting to see how these buildings resolve," he told the crowd.

With sub-four unemployment in many markets and continued upward pressure on wages, the lack of available labor was one of the dominant topics of the panel discussion.

"If you ask, 'what are tenants looking for?'—they're looking for labor," affirmed Kiersey. "They're looking at quantity, quality, and cost of labor...that's what's really resonated with me over the last 12 months. And I would say to every agency broker, please do the research on the labor and be ready to talk about that, because I guarantee you, your tenant is going to be doing the same thing."

The scarcity of workers is driving up wages to unprecedented levels in most markets, further complicating the picture for tenants. To illustrate, Van Buskirk

produced a slide showing a roadside trailer-mounted billboard on I-78, advertising wages of "up to \$19.70 per hour in the first year"—from July of 2018. "And for four or five years, they've been changing that billboard upwards like the leader board at the Masters," he quipped.

Gump conveyed that he had a prospective company looking to expand into the DFW region, with the expectation that they would be able to maintain their wage structure from other markets. "And I just told him, that isn't going to work here. We're past full employment, so you're just going have to pay more. And I think tenants are getting that now."

Despite the labor shortage and other impediments to continued growth, Kiersey reminded the 200-plus gathering that the overall outlook for industrial remains strong. "We are in the sweet spot and we have been for some time. The only question is, how long is it going to last?" ♡

1. <https://www.cbre.us/research-and-reports/2019-US-Real-Estate-Market-Outlook-Industrial-Logistics>

## CONTRIBUTING SIORS



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