More Industrial Supply Is Coming But It Still Won't Meet Demand

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By Lynn Pollack

A record amount of new industrial product is expected to come online this year, following another banner year in 2022, but it likely still won't be sufficient to blunt demand.

In the 118 markets covered by CommercialEdge, more than 450 million square feet were delivered last year and 713 million square feet are under construction. An additional 698.4 million square feet are currently in the planning stage of development. But "despite historic levels of new supply, it was not enough to keep up with demand," analysts note, adding that the average vacancy rate for the top 30 markets fell steadily throughout the year and now sits at 3.9%.

CommercialEdge analysts predict that supply chains will further normalize this year, leading to less need for inventory stockpiling. However, import flow will continue to plague tight port markets, leading to likely increased demand for industrial space along the East Coast in markets like New Jersey, Houston and Savannah-Hilton Head.

E-commerce will still likely be a driver of space demand decisions, but "there will be less demand for multimillion-square-foot distribution centers this year than during the first two years of the pandemic," analysts say. However, they also predict that demand for last- mile distribution facilities will grow, "especially for well-located facilities in high-growth markets."

The supply shortage is going to be further compounded by an expected pullback in warehouse development: according to Prologis, warehouse development starts will drop to a 7-year low, as rent growth exceeds 10%. The firm blames the rapid rise in the cost of capital for the pullback, and says starts will fall by 60% to less than 175 million square feet this year.

In a third quarter earnings call, Prologis CFO Tim Arndt said the firm would shift away from speculative projects in certain markets, reflecting what he called "a more cautious approach." Prologis expects the overall industrial pipeline to drop from over 500 million square feet in Q3 2022 to 275 by year-end 2023.

Adam Roth, executive vice president of industrial services at NAI Hiffman and director of NAI Global Logistics, agreed, noting that "the combination of higher capital cost and record construction pricing will greatly reduce the development of speculative industrial space."