

## **Is The Tide Shifting for Industrial? Well, Maybe** **But softening demand may prevent a bubble, and prospects for long-term growth remain optimistic**

By Lynn Pollack

Is the tide shifting for the white-hot industrial sector? Depends on who you ask. Rents are soaring, vacancy is at historic lows (especially in desirable port markets) and cap rates have compressed dramatically. But according to one industry watcher, downside risk may be building, despite sunny baseline predictions.

In an analysis published in Scotsman Guide, Moody's senior economist Thomas LaSalvia points to a few overarching trends to note: mounting recession risk, potential "overexuberance" among investors and logistics companies over long-term growth expectations, and changes in consumer spending, which is shifting to food services and drinking.

"Moving forward, it is likely that some of the excitement for this sector will subside, and that certain acquisition and development deals will garner an additional layer of scrutiny," LaSalvia says. "But this is not necessarily a bad thing for the overall health of the sector. Slightly softer demand, along with delays in speculative inventory growth due to supply chain issues and higher interest rates, may serve to prevent a bubble."

LaSalvia predicts "at least a moderate decline" in consumer and business spending, which historically has correlated with the performance of the industrial sector. He also notes "conflicting performance" on manufacturing and industrial production, citing near-term space demand headwinds for the sector. And while e-commerce has been viewed over the course of the pandemic as a major tailwind for industrial, he says recent data suggests the impact of COVID-19 on enduring e-commerce habits "may be more transitory than permanent." E-commerce sales as a share of total retail sales has declined from a second quarter 2020 peak of 16.4% to 14.3% at the end of Q1 2022, "not the trend of acceleration many had anticipated," LaSalvia says.

But despite that, "overall, the long-run fundamentals are solid for industrial real estate," LaSalvia writes. "The U.S. logistics network still needs to evolve and grow to prevent future supply chain issues, but competition within retail will only serve to promote development that will reduce shipping times. Toss in a movement back toward just-in-case inventory management, along with a revived domestic advanced manufacturing industry, and the prospects for long-term growth in industrial real estate look bright."