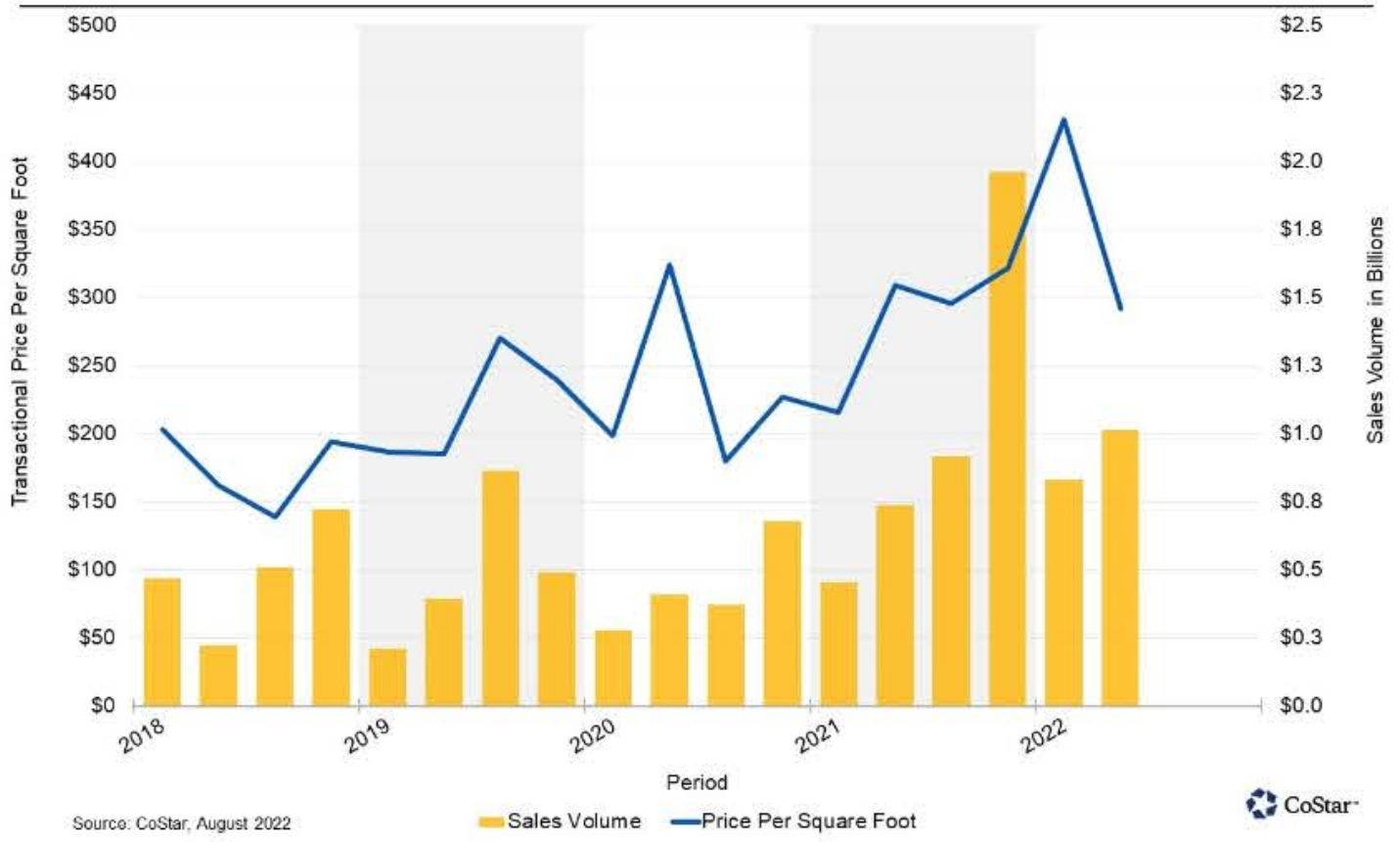


# San Diego's Industrial Investment Market Remains Heated Recessionary Fears, High Interest Rates Could Lead to Uncertainty

## Investment Volume Remains High in San Diego as Pricing Slips



By Joshua Ohl

San Diego's industrial investment market saw more than \$1 billion invested in the region during the second quarter, for only the second time in the past decade.

Investment volume will likely tick up even further as CoStar researchers gather more deals from the second quarter, but the San Diego industrial market has a long way to go to eclipse last year's cumulative sales haul of \$4.9 billion.

Unlike the other property sectors, the local industrial market is characterized by large industrial campus sales. Those include sprawling distribution centers and flex buildings that are likely to be retrofitted with lab equipment and space attached to developable land.

One such deal closed at the start of the second quarter. Investment manager BentallGreenOak

acquired a North County portfolio consisting of the Vista Distribution Center along with four freestanding buildings from Link Logistics Real Estate. The portfolio sold for \$205.5 million and totaled more than 600,000 square feet.

Transactional capitalization rates have averaged 5.1% since the start of 2021, and during the second quarter the average capitalization rate was only 4.8% on investment deals in San Diego. Properties trading at sub-4.5% rates, too, have become more routine.

Given the swiftness and magnitude of the recent rise in interest rates, levered buyers may find that buying properties at such a low capitalization rate has led to the cost of debt eclipsing the year-one rate of return, an untenable position for many.

The average price paid for an industrial asset fell to \$292 per square foot during the second quarter, down from more than \$400 per square foot during the first quarter of 2022. The second-quarter transactional price was the lowest it has been since the start of 2021, when the average price was less than \$225 per square foot.

Buyers received an average discount of 2% off the asking price during the second quarter. That was a smaller adjustment than what was seen in the first quarter, but typical of the asking price versus sale price trend over the past two years.

Lenders across Southern California have noted that fewer deals are crossing their desks, while many of those that do are simply passed upon. The number of sales fell below 100 for the second straight quarter, lower than the sales levels seen here in 2021.

At this point, it may be too early to tell if high interest rates will impact deals, although redevelopment opportunities are likely to continue to be an attractive investment vehicle here. Similarly, fears of a recession could also sideline some investment activity.

And while annual rent growth reached the midpoint of 2022 at an all-time high of 12.9%, it's probably not realistic for investors to bake double-digit rent growth into their proformas, as rent growth is anticipated to begin moderating toward the historical average by 2024, according to CoStar's base-case forecast.