4Q 2023

INDUSTRIAL MARKET REPORT

LOS ANGELES - LONG BEACH

LEE & ASSOCIATES
COMMERCIAL REAL ESTATE SERVICES

Introduction

The U.S. economy grew by 4.9% in the third quarter and is expected to grow by 2.5% in the fourth quarter according to the Atlanta Fed. For all of 2023, the Conference Board forecasts that the economy will have grown by 2.4%.

In terms of employment, the December jobs report from the BLS showed that companies added 216,000 workers to payrolls, below the 240,000 monthly average for the previous 12 months but above the 173,000 added in November. Unemployment was unchanged at 3.7%, signaling relatively good conditions for job searchers. Employment in transportation and warehousing declined by 23,000 in December and has decreased by 100,000 positions since reaching a peak in October 2022. Average hourly earnings for workers grew by 4.1% annually in 2023. Wage growth has outpaced inflation since March 2023.

With regard to inflation, although both headline and core inflation are trending downward, neither have reached the 2% target the Fed is seeking to achieve. Both metrics of inflation remain elevated. The Bureau of Labor Statistics reports that in December, the Consumer Price Index increased 0.3% month-over-month, and rose 3.4% over the last 12 months. The index for all items including food and energy (aka: Core CPI) increased 0.3% in December and 3.9% over the year.

Assuming inflation continues its downward path, the Fed has indicated it anticipates cutting the Fed funds rate at least three times in 2024. Consequently, because of the uncertainty and the continued fragility of the economy, most private and institutional investors remain on the sidelines and/or are slowly beginning to raise capital to deploy selectively. Investors continue to adopt a cautious posture, but it is generally believed that capital market activity will resume towards the second half of 2024.

In the immediate near term, the industrial sector will face unique and idiosyncratic headwinds throughout the start of 2024. As a consequence of piracy in the Red Sea, six of the top ten container carriers are diverting away from the Red Sea and the Suez Canal. This routing change is leading to higher costs for carriers using more fuel and more ships for the longer journeys around the south of Africa, and higher container rates for shippers. Asia - N. America West Coast rates have increased 74% to $2,713/FEU since mid-December, with reports that prices will climb to $5,000/FEU next week as shippers may be shifting volumes to the West Coast to avoid East Coast delays.

In the long term, however, relative to other asset classes, the industrial sector remains a prized property type and investment vehicle since underlying fundamentals in the economy bolster demand for the sector. Although nationwide demand for industrial space is below the highs experienced during the pandemic, current levels are above pre-pandemic norms. This is unsurprising since, as a percentage of total sales, e-commerce retail sales (one of the key drivers of the industrial sector) now stand at 15.6% – 0.8 percentage points higher than where it stood in Q4 of last year.

SOUTHBAY SUBMARKET

SOUTHBAY SUBMARKET Q4 TRENDS AT A GLANCE

Absorption
1,252,920 SF

NNN Rent Overall
$1.78 / SF

Sales Transactions
$163,022,500

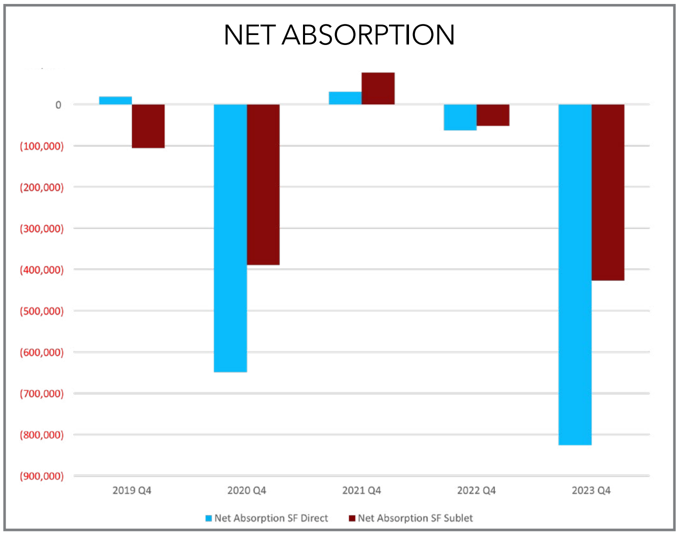
Vacancy
3.9%

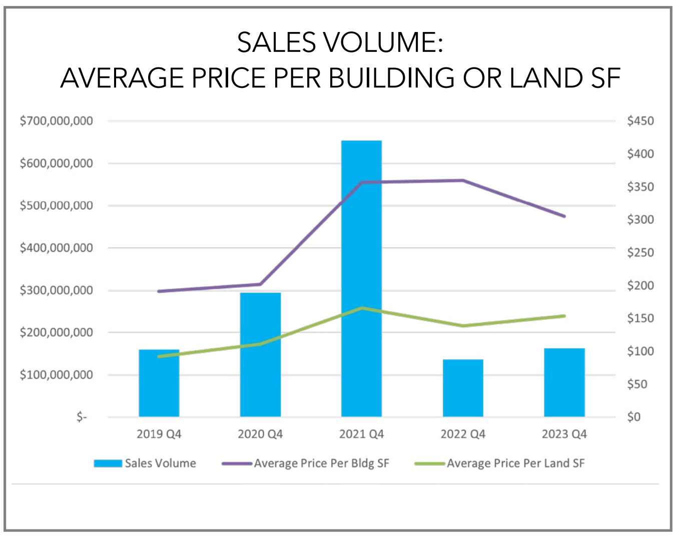
Under Construction
633,144 SF

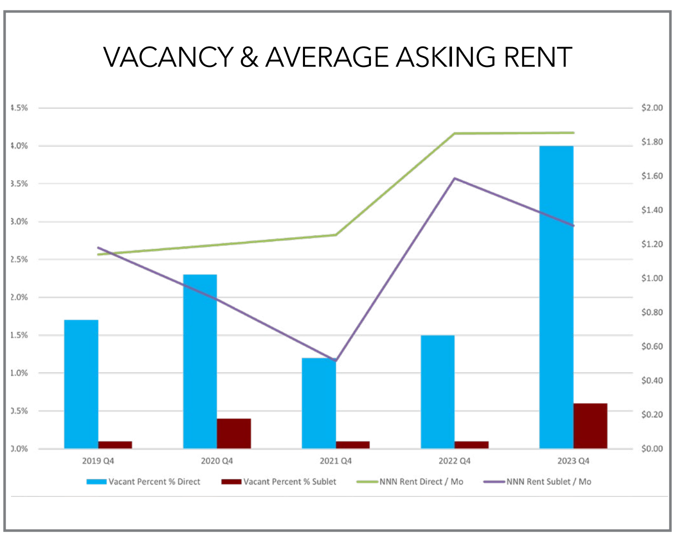
Average Sales Price
$305.23 / SF

Source: Costar Realty Information Inc.

SOUTHBAY SUBMARKET Q4 OVERVIEW







Source: CoStar Realty Information Inc & AIR

Currently in the South Bay, 7.9 million square feet or 3.9% of the base is vacant and available. Representing a 250 basis point increase in vacancy from a year ago, don't expect it to fall anytime soon. Excess space garnered during the extraordinary surge in industrial demand during the pandemic is now being returned to the market in the form of sublet space. Vacant sublease space now totals over 1.14 Million Square Feet (MSF). A year ago, by comparison, vacant sublease space totaled 202,166 square feet. 87 leases transacted this quarter and 15 (or 17.2%) of them were sublease deals.

Given the submarket's proximity to the ports, South Bay industrial space demand continues to be robust, however, most tenants have paused their warehouse search and opted to renew at their current locations rather than securing new leases. Rather than having the "build it and they will come" mentality, tenants are more opportunistic when securing a new location and learning to do more with less. As a consequence of these factors, the tenant pool is shrinking and landlords are facing significant downward pressure on leasing rates. While there is still a noticeable delta between asking and taking rates, year-over-year, overall leasing prices have declined by 3.2%. Currently, overall leasing prices are $1.79 per square foot NNN, while lease prices for direct spaces are now $1.85 NNN. On a quarter over quarter basis, overall asking prices have declined by 10.25% and asking prices for direct spaces have declined by 11.25%. Class A industrial buildings are still leasing at $2.00 PSF NNN+.

For the first time in a decade, landlords will need to make favorable concessions and adjustments in rent to attract tenants. We anticipate that this trend will continue throughout all of 2024.

Two buildings totaling 94,328 SF were added to the base this quarter. Additionally, 5 more buildings totaling 633,144 SF are under construction. While construction projects are set to deliver within the next 18 months, there are fewer projects being added to the pipeline as developers currently face high construction-loan and labor costs.

SOUTHBAY SUBMARKET Q4 OVERVIEW

This quarter only 18 industrial sales transacted. Of these 18, exactly half of them were investment sales. On both an average price per building square foot basis and median prices per square foot basis, the value of industrial buildings declined this quarter. Respectively, industrial buildings traded at $305.23 and $283.18.

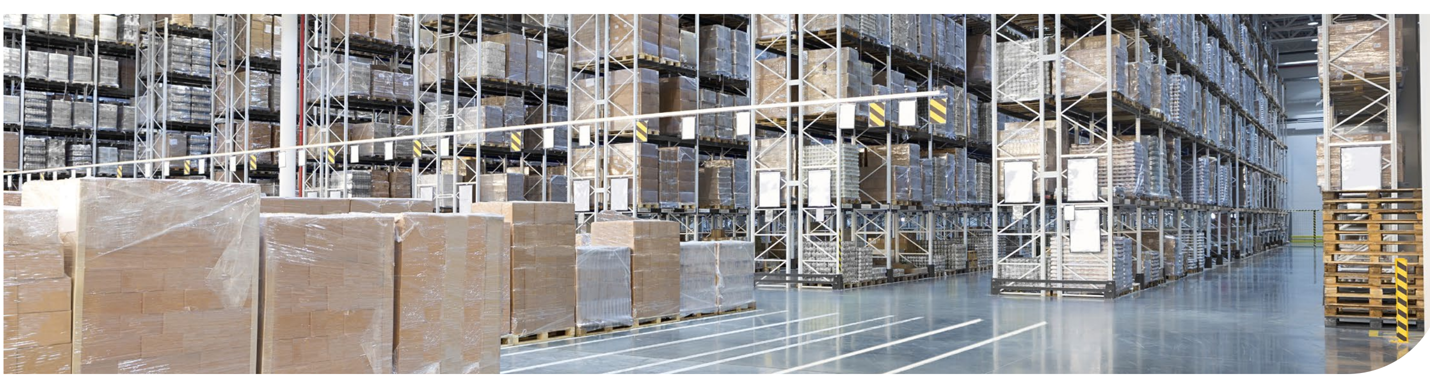
Since the first quarter of 2014, the number of sales transactions have averaged 20 per quarter Throughout all of 2023, the average was 13. There has been a total of only 50 industrial sales in 2023: 10 in Q1, 13 in Q2, 9 in Q3, and 18 in Q4. Anticipate sales transaction activity to remain at current levels throughout the first half of 2024 as investors in the industrial sector still face high borrowing costs and trepidation about the economy. Once capital market infusions resume, expect leasing activity to increase. For perspective, since Q1 of 2014, the South Bay has averaged 110 leases per quarter. In all of 2023, per quarter, it averaged 84 leases.

TOP LEASES FOR 4Q23

ADDRESS	CITY	TYPE	TENANT	EXECUTION DATE	SQUARE FEET
19200 Western Ave.	Torrance	Distribution	National Road Logistics, LLC	November	315,256 SF
444 Quay Ave.	Wilmington	Land	Pacific Green Trucking Inc.	December	218,471 SF
1640 W 190th St.	Torrance	Distribution	Bright Event Rentals	October	123,345 SF
1041 E. 230th St.	Carson	Distribution	Trinity II	December	119,668 SF
3555 Conant St, Bldg 23	Long Beach	N/A	Ford Motor	November	106,476 SF

TOP SALES FOR 4Q23

ADDRESS	CITY	TYPE	BUYER	SALES PRICE	SQUARE FEET
2411 Santa Fe	Redondo Beach	Investment	Terreno Realty	$45,700,000	112,363 SF
1217 W. Artesia	Compton	Investment	Artisan Ventures	$21,000,000	71,000 SF
18421 S Main St	Gardena	User	AIDS Healthcare Foundation	$20,000,000	53,978 SF
1215 W Walnut St	Compton	Investment	Bridge Investment Group	$15,900,000	57,671 SF
24310 Garnier St	Torrance	User	Hori (USA), Inc.	$13,517,500	33,253 SF



MIDCOUNTIES SUBMARKET

MIDCOUNTIES SUBMARKET Q4 TRENDS AT A GLANCE

Absorption
(550,910 SF)

NNN Rent Overall
$1.64 / SF

Sales Transactions
$82,109,506

Vacancy
3.5%

Under Construction
515,221 SF

Average Sales Price
$265.05 / SF

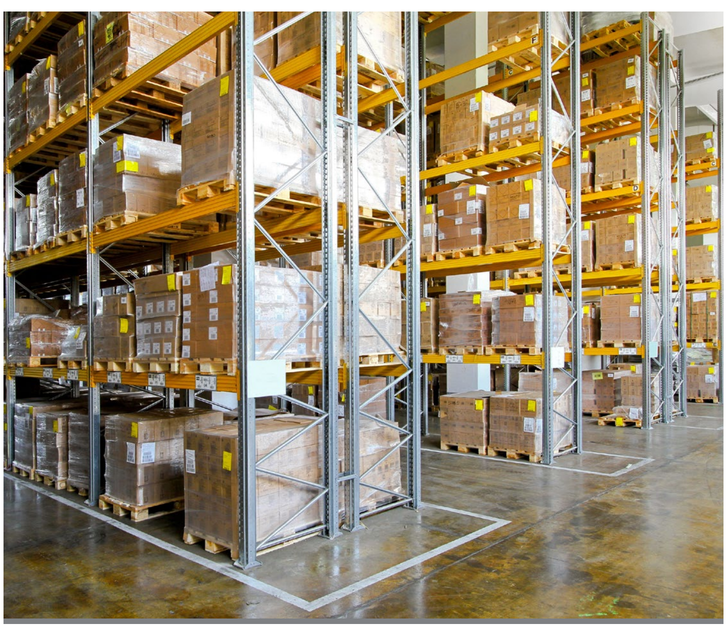
Source: Costar Realty Information Inc.

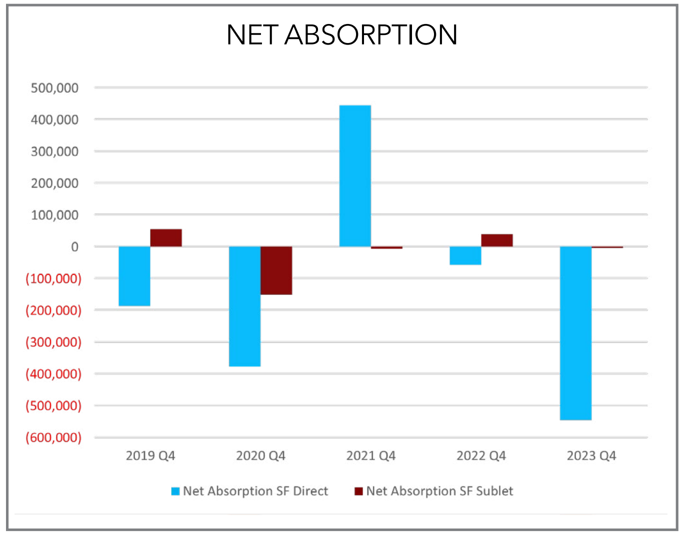
MIDCOUNTIES SUBMARKET Q4 OVERVIEW

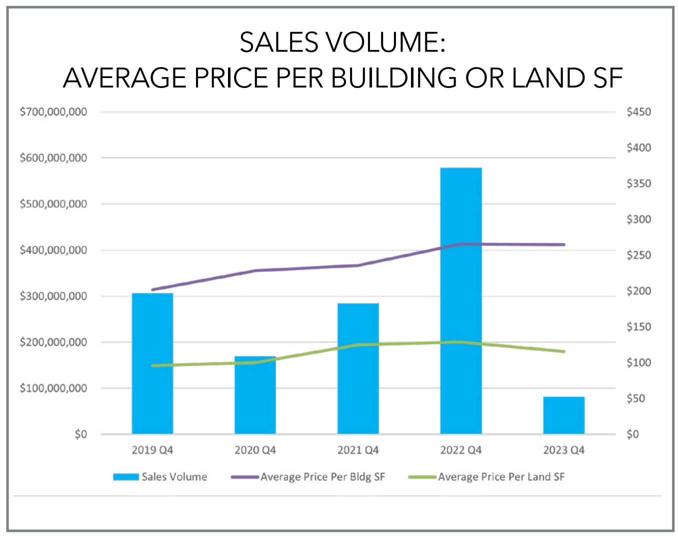
Mid-Counties continued to have the lowest vacancy rate of any major industrial submarket within Los Angeles at 3.5%. There is only about 2.9 MSF of direct vacant space on the market. As small as that number is, it represents an increase in vacancy for the submarket. Since Q4 2022, vacant space has increased by over 2.0 MSF.

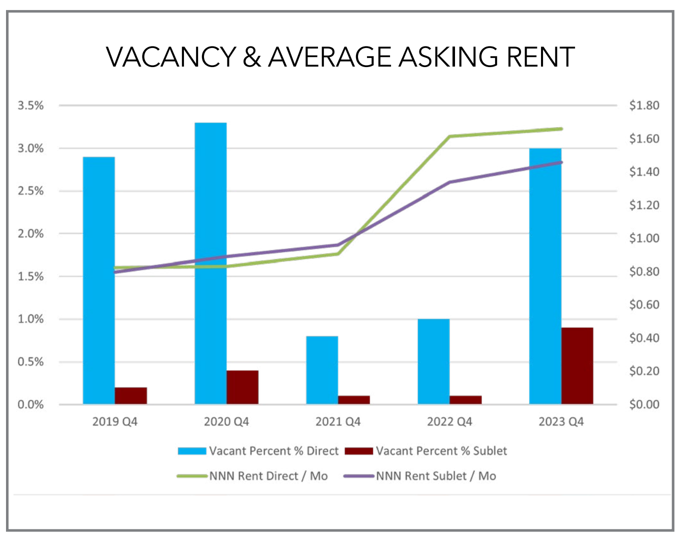
No new building delivered this quarter, and seven buildings totaling over 515,221 SF are under construction. In contrast to other submarkets, overall asking rents increased to $1.64 NNN PSF, a year over-year increase of about 5.12% from Q4 2022's rate of $1.56 PSF.

Tenants with leases up for renewal should be prepared for sticker shock as rents have nearly tripled over the past 10 years. Because of these tight conditions, tenants are opting to renew rather than relocate. Landlords, on the other hand, will either have to exercise patience in leasing their buildings or reduce lease rates to remain competitive. With that said, even with all these challenges facing the Midcounties, its clear demand for Mid-Counties industrial space remains strong. For any industrial tenant looking for an alternative to the South Bay, they will most likely turn to either the Inland Empire or Midcounties.









Source: CoStar Realty Information Inc & AIR

CENTRAL SUBMARKET

CENTRAL SUBMARKET Q4 TRENDS AT A GLANCE

Absorption
48,253 SF

NNN Rent Overall
$1.69 / SF

Sales Transactions
$99,629,045

Vacancy
4.6%

Under Construction
816,365 SF

Average Sales Price
$244.19 / SF

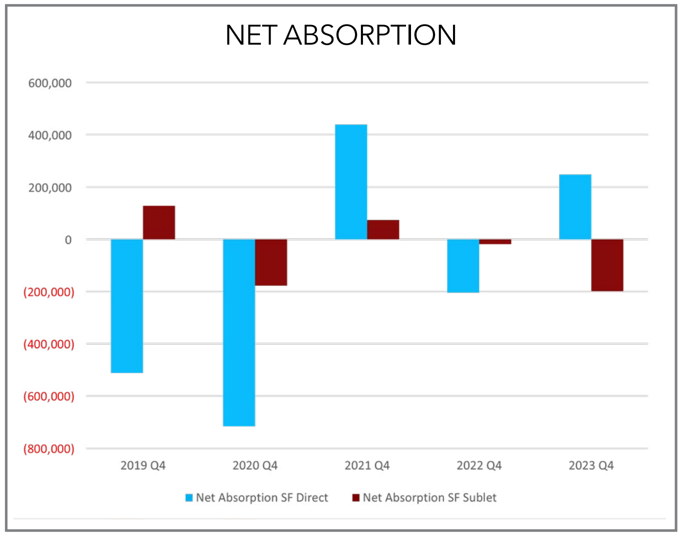
Source: Costar Realty Information Inc.

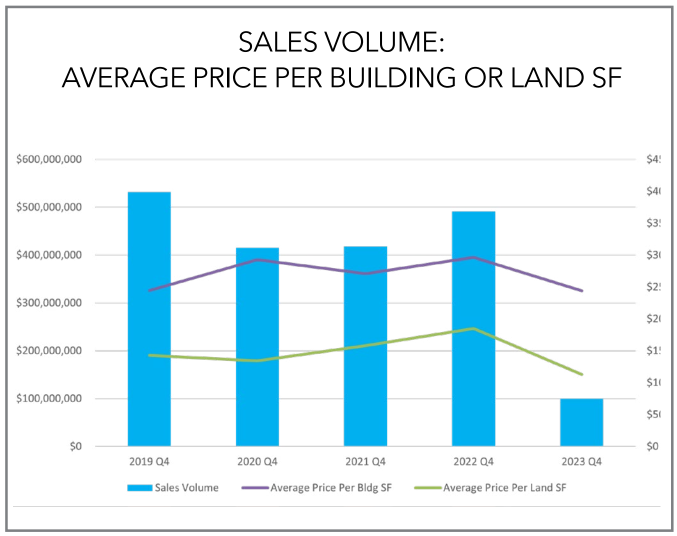
CENTRAL SUBMARKET Q4 OVERVIEW

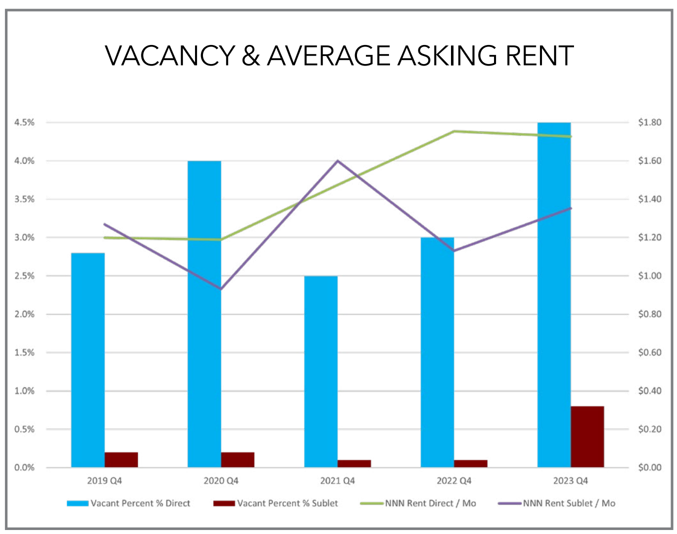
Nearly identical to what it was last quarter, the vacant rate in Central LA ended Q4 at 4.6%. There is now over 11.2 MSF of vacant space in Central LA. Contrary to what used to be the case for the past decade, Central LA has one of the highest vacancy rates among all the submarkets in the LA Basin now. Two new buildings totaling over 72,000 SF were delivered this quarter, and eight buildings totaling over 816,000 SF are still under construction. Unlike nearly all the submarkets across the L.A. basin this quarter, net absorption was positive, although net absorption of sublet space was nearly 200,000 square feet in the red. The amount of sublease space increased dramatically this quarter.

Year-over year, sublease vacancy increased by 60 basis points from 0.1% in Q4 2022 to 0.7% in Q4 2023. In terms of square footage, there is now over 1.53 MSF of vacant sublease space on the market. Sublet net absorption numbers notwithstanding, the demand for functional industrial space is nearly insatiable in the Central submarket, and asking prices are now extremely high – although they are easing up a bit. Average asking rental rates are now $1.69 per square foot (PSF). This represents a quarterly decline of $0.03 or 2.9%. Industrial demand is heavily concentrated in the Vernon and Commerce submarkets, where food production and apparel manufacturing are the top industries. Commerce has a large concentration of food manufacturing tenants. The spaces these tenants occupy come at a premium and will continue to drive up asking rents.

Although landlords have started to reduce their asking rents to placate occupiers who cannot afford to lease at current prices, the pace of reduction has been slower than expected. Nonetheless, expect the reduction in asking rents to continue over the next 18 months.







Source: CoStar Realty Information Inc & AIR

INLAND EMPIRE SUBMARKET

INLAND EMPIRE SUBMARKET Q4 TRENDS AT A GLANCE

Absorption
4,060,656 SF

NNN Rent Overall
$1.31 / SF

Sales Transactions
328,096,750

Vacancy
5.5%

Under Construction
27,130,313 SF

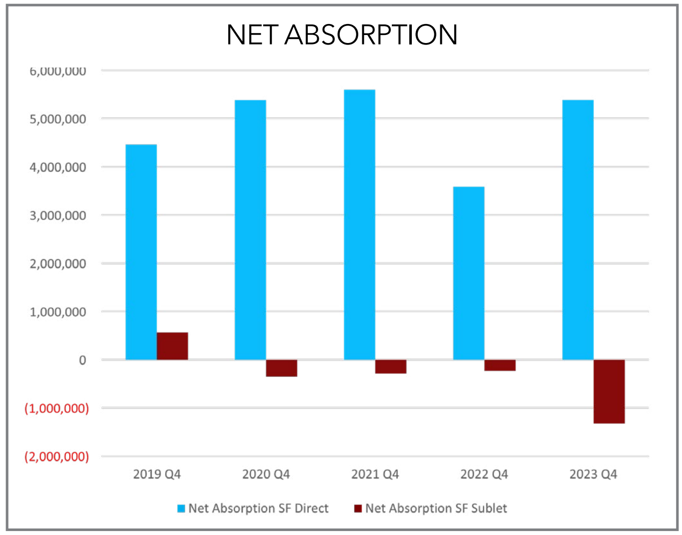
Average Sales Price
$295.57 / SF

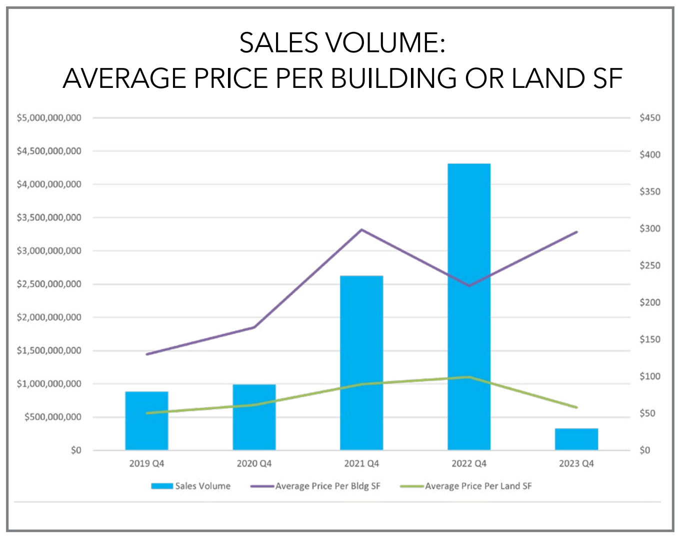
Source: Costar Realty Information Inc.

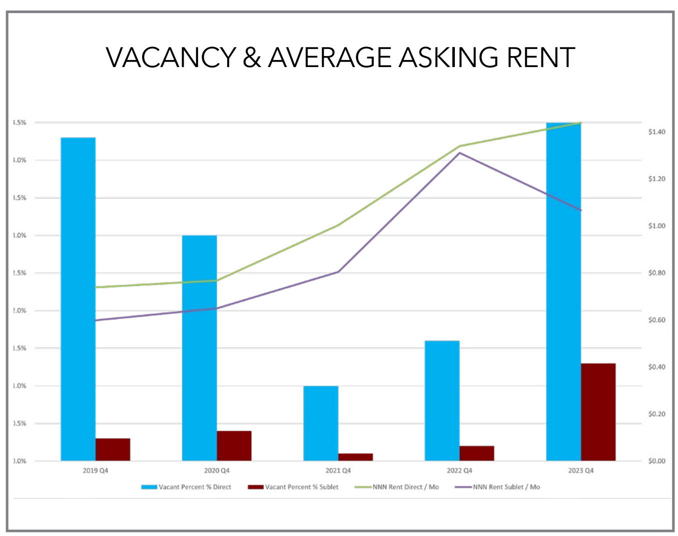
INLAND EMPIRE SUBMARKET Q4 OVERVIEW

The vacancy rate increased noticeably in the Inland Empire. By the end of Q4, more than 36.2 MSF of space was vacant and available. Compared to last quarter, the vacant rate grew by more than 140 basis points to reach 5.5%. The rise in the vacancy rate is attributed to 34 new buildings totalling over 12.4 MSF that were delivered in Q4 alone. A significant plurality of these buildings were not pre-leased. In the pipeline there are 140 buildings totaling over 27.1 MSF under construction. Overall net absorption for the quarter was positive and totaled 4.06 MSF. Net absorption of sublet space, however, was negative 1.32 MSF. This is unsurprising because companies that expanded their warehouse/distribution space during the pandemic to keep up with the pandemic-fueled e-commerce boom have started to reduce excess space. Currently, there is over 8.3 MSF of vacant sublet space on the market. In Q4 2022, by comparison, there was only 1.3 MSF of vacant sublet space. We anticipate that this trend will continue throughout all of 2024 and well into 2025. We are seeing a noticeable decline in overall asking rent. Currently, asking rents are $1.32 per square feet (PSF) NNN. At the start of the year, they were $1.34 PSF NNN and the trend is moving in a downward direction.

Historically, communities within the Inland Empire have welcomed growth and expansion of warehouse spaces. Warehouses increased from 234 in 1980 to more than 4,000 today, and the industrial and logistics sector became the largest job creator in the region. However, developers are now facing significant pushback against further warehouse development. Developers indicate that community resistance has given them pause on expansion. Beyond rising labor and construction costs, developers have to contend with issues such as development moratoriums, increased fees and taxes, and permitting delays.







Source: CoStar Realty Information Inc & AIR

A LOOK AHEAD

On a macro scale, although rate cuts are expected this year, investors still face elevated borrowing costs and feel insecure about the economy. As a result, expect capital market investment in the industrial sector to resume only after Q2 of 2024 with leasing activity following suit.

With regard to port activity, imports were down year over year and, after losing market share through much of 2022 and 2023 to their East and Gulf coast counterparts, U.S. West Coast ports are hoping to lure back imports after securing a new longshore labor contract. The following additional factors are likely to assist West Coast ports achieve this goal.

First, a variety of capacity expansion projects at the Ports of Los Angeles and Long Beach are years away from completion and are thus unlikely to impact cargo operations in 2024. The Port of LA, for example, is just starting the environmental review process for an 80-acre near dock chassis maintenance, repair, and storage yard. And the Port of Long Beach's Pier B on-dock rail facility, capable of building 20K foot trains, is scheduled for completion in 2032. Second, West Coast ports will benefit from drought-induced draft limitations at the Panama Canal, which is limiting vessel transits on all-water services from Asia to East and Gulf coasts. As of mid-December, shippers have shifted volumes to West Coast ports to avoid East Coast delays due to the piracy and violence experienced near the Suez Canal. And lastly, in addition to potentially testy longshore negotiations on the East/Gulf coasts, terminals in the Ports of LA and Long Beach are as fluid as they have been since prior to the pandemic.

On a local level, do not expect vacancies to decline in the South Bay's industrial market throughout the first half of 2024. A good majority of credit tenants are no longer in the market and if so, are contract dependent, thus the remaining tenants are more likely to secure renewals rather than pursue new leases. Landlords, consequently, should expect to feel continued downward pressure on lease rates and must be willing to negotiate if they wish to see their spaces leased quickly. Sales activity, moreover, will likely be subdued throughout the first half of the year and is unlikely to exceed levels seen this quarter.

1. BEA: https://www.bea.gov/data/gdp/gross-domestic-product
2. Atlanta Fed: https://www.atlantafed.org/cqer/research/gdpnow
3. Conference Board: https://www.conference-board.org/research/us-forecast. Official GDP numbers for Q4 will be published on January 25, 2024 by the BEA. https://www.bea.gov/data/gdp/gross-domestic-product
4. BLS: https://www.bls.gov/news.release/pdf/empsit.pdf
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7. Statista: https://www.statista.com/statistics/1351276/wage-growth-vs-inflation-us/ ; Atlanta Fed: https://www.atlantafed.org/chcs/wage-growth-tracker ; BLS: https://www.bls.gov/news.release/cpi.t01.htm
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9. CNBC: https://www.cnbc.com/2023/12/13/fed-interest-rate-decision-december-2023.html
10. Freightos Weekly Update January 10, 2024 by Judah Levine
11. St. Louis Fed: https://fred.stlouisfed.org/series/ECOMPCTSA
12. Freight Waves: http://tinyurl.com/57zknz8 "'Not-in-my-backyard' mindset threatens warehouse growth" by Mark Solomon

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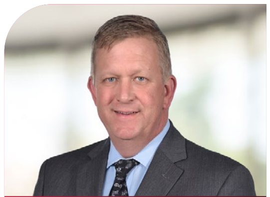

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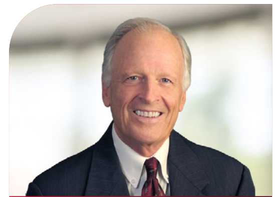

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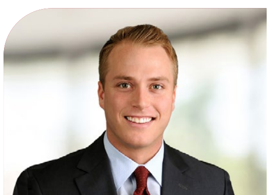

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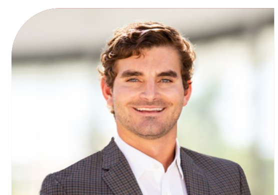

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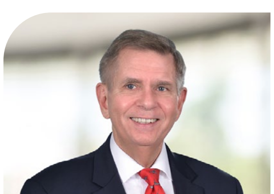

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