SMALL BAYS, BIG OPPORTUNITY
INDUSTRIAL REAL ESTATE'S NEXT POWER PLAY

The industrial sector has undergone remarkable shifts in recent years. Once dominated by the rise of bulk warehouses and expansive distribution centers, today's narrative is increasingly shaped by small-bay industrial assets. These under-the-radar properties are becoming more sought after for their sustained demand, resilient fundamentals, and compelling investment potential.

While national vacancy rates for large-scale industrial properties have climbed significantly, now hovering around 7.4%, small-bay vacancy remains notably lower at approximately 4.2%. Further, Corebridge Financial reports that small-bay industrial rents have jumped more than 40% since 2020, significantly outpacing broader industrial rent growth.

That growth is no accident. It's powered by reshoring, supply chain decentralization, and growing demand for local, last-mile logistics. These smaller-profile operators are helping leasing activity remain steady, even as big-box absorption slows.

Unlike large logistics users that chase national footprints and cost efficiencies, small-bay tenants operate close to their customer bases. That proximity gives them staying power. It also gives landlords dependable occupancy. Small-bay leases also tend to be operationally sticky: tenants often expand or contract within a park rather than relocate, reducing turnover costs and enhancing retention.

Operationally, these assets offer stable tenant profiles, shorter lease terms that allow for more frequent rent adjustments, and relatively low maintenance costs. Compared to larger single-tenant facilities, small-bay portfolios are easier to scale, quicker to reposition, and better insulated from tenant turnover, making them increasingly attractive in a market that values flexibility and risk diversification.

THE SMALL-TENANT ADVANTAGE

Small-bay industrial's most powerful advantage is right in its name: small spaces, small leases, small tenants. These local and regional businesses—ranging from HVAC and electrical contractors to niche manufacturers and e-commerce startups—represent a massive but fragmented segment of the U.S. economy. According to the Office of Advocacy, there are over 36 million small businesses in the U.S., responsible for nearly half of private-sector employment.

These tenants aren't just surviving; they're aligned with secular trends: domestic production, regional distribution, and urban logistics. Together, they help provide owners with durable, diversified income streams and a buffer against macro volatility.

And what do many of these users look for in their spaces? While specifics can vary based on location and use case, Lee experts broadly report high demand for suites in the 2,000- to 10,000-square-foot range with standard TI packages including robust power, modern lighting, refreshed storefronts, and shared amenities. Functional spaces with good clear heights, ample electrical capacity, dual dock-high and ramp-to-grade access, and outdoor storage are particularly valuable given rising construction costs.

And with operational costs in warehousing and fulfillment, such as minimum monthly spends, storage fees, and fulfillment expenses, on the rise, disciplined, cost-effective TI strategies emphasizing operational efficiency and location over extensive amenities are crucial. The Fulfillment Advisor's 2025 Warehousing and Fulfillment Costs Survey points out that these escalating costs are driving tenants toward flexible industrial solutions that offer lower overhead and improved operational efficiency, making right-sized footprints even more valuable.

As the spotlight on the sector grows, strategically positioned markets across North America are emerging as small-bay hotspots.

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MAPPING THE MOMENTUM

As with many property sectors, small-bay demand tends to follow migration and population growth, making these positive trends evident across markets from the Pacific to the Atlantic.

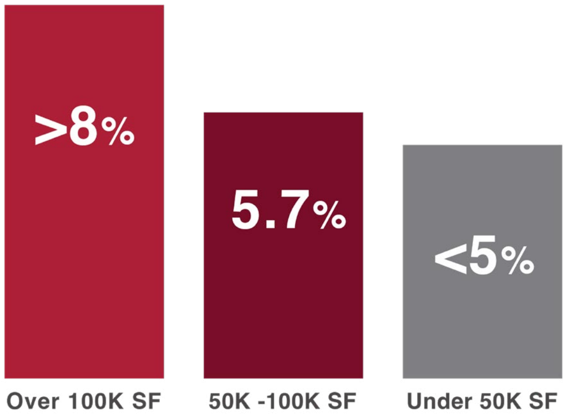
In longstanding industrial hubs like Phoenix and Denver, resilient tenant demand for small and mid-sized spaces continues to drive steady absorption, with some landlords even subdividing larger facilities to capture smaller users. In California, Fresno, Bakersfield, and Ventura County remain small-bay standouts with vacancy below the national average, while San Luis Obispo's 2.4% vacancy ranks among the tightest in the nation.

Secondary Western markets, including Reno, the Salt Lake City outskirts, Boise, and Phoenix's East Valley, are emerging as cost-effective alternatives to expensive coastal areas, attracting tenants seeking value and operational efficiency.

In Vancouver, demand for small-bay space across the Fraser Valley and Tri-Cities remains strong despite broader softening. With only 4% of land zoned for industrial use, leasing activity for quality small bay continues to outperform other industrial segments due to its essential role in regional commerce. Meanwhile, in Toronto, small infill product continues to outperform as well, supported by owner-occupiers and local distributors, keeping industrial rents among North America's highest even amid moderating demand.

Industrial Vacancy by Building Size

Smaller buildings remain the tightest segment of the U.S. industrial market, with vacancy nearly 40% lower than large-scale logistics as of the third quarter.



A resurgence of manufacturing activity is also bringing renewed flex and small-tenant demand to Midwestern cities such as Grand Rapids, Minneapolis, Columbus, suburban Indianapolis, and Chicago.

In Cleveland, where vacancy hovers around 4%, nine out of ten leases are under 25,000 square feet, reflecting the strength of smaller manufacturers. These markets benefit from established infrastructure, skilled labor pools, and central logistics access.

In the Northeast, micro-industrial parks in Lehigh Valley, Southern New Hampshire, NYC's outer boroughs, and Central Connecticut offer specialized, flexible spaces tailored to local market needs and proximity to major consumer bases. In the Eastern Pennsylvania-Southern New Jersey market, where small-bay supply has grown only 1.7% since 2020 (compared to 21% for larger properties) vacancy remains near 4.5%.

The Southeast Corridor offers affordability, strong infrastructure, and business-friendly regulation. Jacksonville, Orlando, Tampa, and Charlotte continue to post tight conditions for strategically located assets. Atlanta is a leading example of successful small-bay growth, driven by urban density, population expansion, and a diverse economic base even without direct port access. Nashville tells a similar story: small-bay leases have accounted for more than half of all industrial transactions there since 2020 as per CoStar, and excluding buildings over 150,000 square feet, the city's effective vacancy falls to just 2.85%, underscoring the depth of demand for smaller footprints.

Notable submarkets such as Greenville–Spartanburg, Savannah, and Central Florida's I-4 Corridor offer strong logistics advantages and expanding consumer bases. Supply constraints and construction costs have driven small-bay rents in Central Florida up as much as 100%, versus 20–30% for larger properties.

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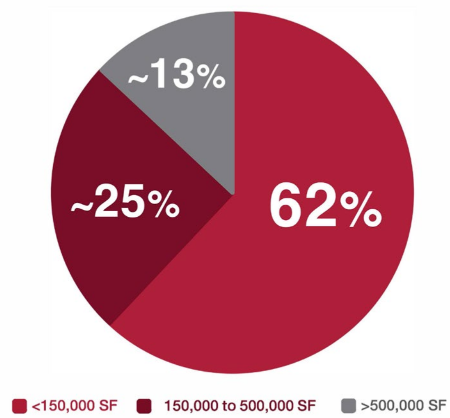
This heightened demand and small-bay segment's operational strengths are allowing landlords to capitalize on rent growth and resilient occupancy, but there are early signs of tenant pushback in some overheated markets. A few users are expressing affordability concerns and, in some cases, opting not to renew or expand due to steep rent increases. For landlords, evaluating tenant credit and financial stability is essential to mitigate potential risks. Strategic pricing and disciplined underwriting will help balance profitability with long-term retention.

Investor Activity by Property Size

Small-bay transactions now account for nearly two-thirds of all industrial sales.

Source: Green Street



SMART MONEY'S ON SMALLER FOOTPRINTS

Small bay asking rents continue to maintain a premium over larger industrial assets, helping sustain strong underwriting metrics despite broader cap rate expansions. Lee & Associates' data further supports this, with heightened investor activity and competition in strategic corridors in the U.S. and Canada. In fact, recent industrial investment volume has been significantly driven by small-bay transactions. Green Street Advisors reported that properties under 150,000 square feet accounted for 62% of all Q2 2025 industrial sales volume, with transactions in the $5-million to $25-million range reaching $5.89 billion that quarter alone.

This strong transaction volume underscores the growing confidence and strategic interest of investors in small-bay assets. A considerable part of that activity has been from institutions, which are wading deeper into the sector. Yet while the headlines might make it seem that institutional encroachment is rising, small bay is still very much a local landlord's game. In Central Florida, there is strong investor interest from local and regional investors seeking off-market opportunities. Buyers increasingly pursue off-market opportunities to avoid bidding wars, resulting in continually rising prices and rental rates, particularly for well-configured, shallow-bay buildings.

The same trends are observed in the Eastern PA-Southern NJ market, where private firms now control more than 60% of small-bay asset value, with users holding 28%. Even as deal volume normalizes post-2022 highs—coming in at $1.6 billion through Q3 2025—pricing momentum remains robust. Sale price per square foot has risen 55% since Q3 2020 to an average of $104.

Strategic opportunities include value-add roll-ups in Central PA, premium infill assets in Lehigh Valley and Metro Philadelphia, and select acquisitions in Southern NJ's strongest submarkets. Pittsburgh also offers attractive prospects in shallow-bay and flex properties near its airport corridor.

THE LEE LENS: SCALE, SCARCITY, AND THE STRENGTH OF THE MIDDLE MARKET

The industrial cycle has entered its segmentation era. The big-box narrative, once synonymous with e-commerce dominance, is giving way to a more balanced ecosystem where local production, service trades, and regional distribution shape demand. Small bay isn't the sideshow anymore; it's the connective tissue of industrial real estate.

For investors, the lesson is structural, not cyclical. Scarcity at the small end of the market isn't temporary, it's systemic. Land constraints, construction costs, and zoning restrictions are locking in long-term imbalance between supply and demand. At the same time, short leases and diversified tenant rosters provide a natural hedge against volatility, making this segment the stealth outperformer of the post-pandemic economy.

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In a cycle where discipline, flexibility, and local intelligence matter more than scale alone, small-bay industrial offers all three. The next decade of industrial performance won't just be about size. It will be about agility, adaptability, and execution.

SMALL-BAY HOTSPOTS

From Southern California to Southern New Hampshire, small-bay demand is surging in strategic infill locations.

NORTHEAST: Micro-industrial parks in Lehigh Valley, Southern NH, and NYC's outer boroughs are thriving thanks to local distribution and contractor needs.

MID-ATLANTIC: In Pennsylvania and South Jersey, small-bay supply has grown just 1.7% since 2020 (vs. 21% for larger formats), supporting rent durability. Value-add roll-ups in Central PA and infill plays in Metro Philly are key targets.

SOUTHEAST: The I-4 Corridor, Savannah, and Greenville-Spartanburg offer logistics infrastructure and friendly regulation. In Central Florida, strong tenant demand is tempered by rising rents, while Nashville and Atlanta continue to push outward into suburban markets.

WEST: Reno, Boise, and Salt Lake City are emerging as low-cost alternatives to coastal markets. Phoenix's East Valley continues to capture overflow from more expensive submarkets.

MIDWEST: Manufacturing momentum in Grand Rapids, Columbus, and the western Chicago suburbs is driving new leasing and repositioning plays.

CANADA: In Metro Vancouver, zoning constraints (only 4% of land is industrial) and healthy demand from owner-operators and trades have created one of North America's tightest small-bay markets.

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This article is part of Lee & Associates' ongoing thought leadership series, offering market intelligence and expert perspectives from across the platform. The insights shared here reflect contributions from the following Lee professionals:

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