VALUATION & ADVISORY

INDUSTRIAL INVESTOR SURVEY & OUTLOOK

SPRING 2023

CUSHMAN & WAKEFIELD

Cushman & Wakefield Valuation & Advisory's Logistics & Industrial Practice Group periodically surveys investors regarding their decision-making processes in selecting overall capitalization rates. In this report, we present our latest results, followed by recent industrial market highlights.

Annual Industrial Investor Survey Results

Following are the results from an investor survey conducted by Cushman & Wakefield Valuation & Advisory's Logistics & Industrial Practice Group that investigates investors' decision-making processes in selecting overall capitalization rates. The process involves a myriad of factors, but primarily includes analysis of the physical aspects by asset quality (Class A, B or C) and location in relation to current market conditions and tenancies, as well as a forecast of future trends driven by changing demand indicators. For our Spring 2023 edition, we interviewed representatives from some of the nation's most prominent institutional buyers and sellers of industrial assets, as well as experts from Cushman & Wakefield's Industrial Capital Markets group.

PHYSICAL CRITERIA/LOCATION

These participants, typical for the market, focus on the type (Class A, B and C) and location of an industrial asset prior to selecting an appropriate overall capitalization rate. While the criteria relative to defining the asset type may vary, most agree on the following, as defined by CoStar Group Inc.:

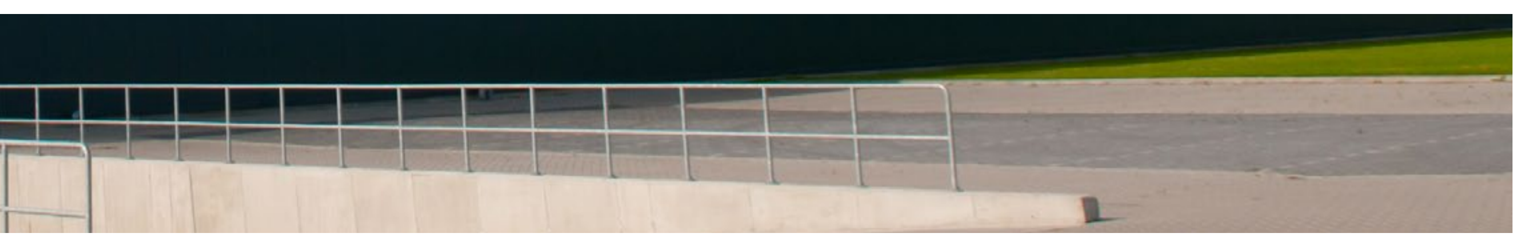
- **Class A Industrial:** Class A buildings generally qualify as desirable investment-grade properties that command the highest rents or sale prices compared to other buildings in the same market. Such buildings are well located and provide efficient tenant layouts as well as high-quality (and in some buildings, one-of-a-kind) floor plans. These buildings contain the best quality materials and workmanship in their trim and interior fittings.
- **Class B Industrial:** Buildings in this category command lower rents or sale prices than Class A properties, as Class B buildings tend to offer utilitarian space without special features. These buildings typically have average to good maintenance, management, and tenants. They are less appealing to tenants than Class A properties, and may be inferior in a number of respects, including floor plans, condition, and facilities.
- **Class C Industrial:** These structures generally can be classified as no-frills, older buildings that offer basic space, commanding lower rents or sale prices compared to other buildings in the market. Such buildings typically have below-average maintenance and management, with mixed or low tenant prestige, low clear ceiling heights, and/or inferior mechanical/electrical systems.

RISK FACTORS/MARKET CONDITIONS/TENANCIES

Although the above criteria are of primary focus, the participants also identified the following risk factors influencing their purchasing decisions:

- Overall vacancy and strengths/weaknesses of the local market, occupancy, and near-term rollover
- Readily available developable land for potential competition
- The functionality of the asset (clear ceiling height, layout, design, ratio of office to total warehouse space, lighting, power, adequacy of parking and truck storage, truck turning radius, etc.), as well as the age and condition of the asset, including the roof structure
- Access to major transportation linkages (interstate, rail, port access, etc.)
- Proximity to growing populated urban areas
- Creditworthiness of the tenant(s) and contractual rent in place in relationship to market rent levels (above/below market), and potential of rent increases
- Replacement cost considering rising construction costs

In addition to the above, investors are far more attuned to addressing the needs of the end-users/occupiers who want facilities that are more efficient to operate and offer the ability to ship product faster, while being located in close proximity to readily available labor markets.



Final Results

SPRING 2023

The results of our investor survey (overall capitalization rates), conducted in Spring 2023, were provided by representatives of some of the largest institutional/pension fund buyers and sellers of industrial assets nationally. They are presented as follows:

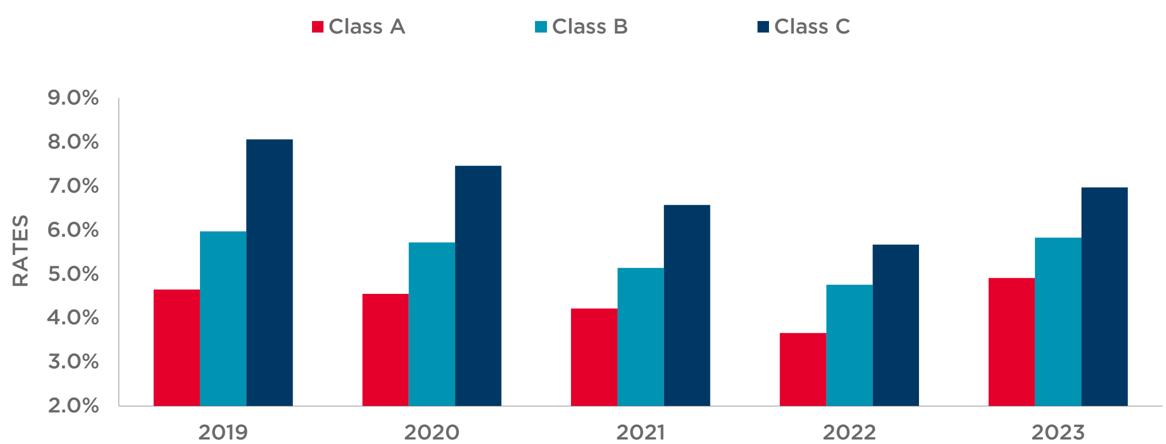
INDUSTRIAL OVERALL CAPITALIZATION RATES - COMPARISON ANALYSIS SPRING 2023									
	Spring 2023	Spring 2022	Spring 2021	Spring 2020	Spring 2019	12-Mth Change (BPS)*	24-Mth Change (BPS)*	36-Mth Change (BPS)*	48-Mth Change (BPS)*
Class A	4.00% - 6.00%	2.50% - 4.75%	3.25% - 5.50%	3.75% - 6.00%	3.75% - 6.50%				
Range Average	4.91%	3.66%	4.22%	4.55%	4.65%	1.25	0.69	0.36	0.26
Class B	4.50% - 7.00%	3.00% - 6.00%	4.00% - 7.00%	4.00% - 7.50%	4.25% - 8.00%				
Range Average	5.83%	4.76%	5.14%	5.72%	5.97%	1.07	0.69	0.11	-0.14
Class C	5.00% - 9.00%	4.25% - 7.50%	5.00% - 9.00%	6.00% - 9.00%	7.00% - 10.00%				
Range Average	6.97%	5.67%	6.57%	7.46%	8.06%	1.30	0.40	-0.49	-1.09
Overage Average	5.90%	4.70%	5.31%	5.91%	6.23%	1.21	0.59	-0.01	-0.32

Note - The lower-end of the range reflects Class A assets with long-term credit tenants at market rent levels or short-term tenants with below market leases in-place located in Southern CA (Inland Empire), New Jersey (Northern & Central), Southern Florida and Dallas markets. Predominately U.S. port cities.

**Ending Spring 2023*
Compiled by Cushman & Wakefield's Valuation & Advisory Logistics Practice Group (LPG).

The results of our survey over the previous five-year period are presented as follows:

INDUSTRIAL OVERALL CAPITALIZATION RATES COMPARISON ANALYSIS SPRING 2023



Source: Cushman & Wakefield's Valuation & Advisory Logistics Practice Group (IPG)

Based on the Spring 2023 results, overall capitalization rates range widely by asset class, indicating nearly a 100-bps differential between Class A and B industrial product, and just over a 200-bps difference between Class A and C industrial facilities. Overall rates for Class C properties are 114 bps higher than Class B industrial product. The lower end of the range reflects Class A assets with long-term credit tenants at market levels or assets with short remaining lease terms and below-market leases in place, located in Southern CA (Inland Empire), New Jersey (Northern & Central), Southern Florida and Dallas markets; predominately U.S. port cities. Atlanta and Phoenix markets were also noted as high demand and growth markets, but to a lesser extent.

Investors are also targeting Class B and, in some cases, Class C product, seeking higher rent growth and greater yield/return expectations—especially from those assets with below-market leases in place and located near populated urban areas with access to a readily available work force. Assets near urban areas have become the driver to reduce shipping and delivery times.

The current survey indicates that average capitalization rates for Class A assets increased 125 bps, Class B assets by 107 bps, and an even greater increase indicated for Class C assets of 130 bps since our Spring 2022 survey. The increases in the average capitalization rates for all asset classes can be attributed to the significant increases in interest rates over the last 12 months. However, most investors do not anticipate additional significant increases in overall rates since their current yield rates have considered and/or have priced in any additional near-term rate hikes. Nonetheless, investors are closely monitoring 10-year Treasury yield rates as a benchmark.

Observations and Key Takeaways

- Solid demand is expected to continue, and the Coastal (port cities), Southwestern and Southeastern regional markets are expected to continue growth at their current pace. The New Jersey markets are as well due to their strong medical and pharmaceutical presence and port access. In fact, record growth in 2022 placed New Jersey/New York ports as the second busiest in the U.S., surpassing Long Beach, CA. Los Angeles still ranks first at 9.911M TEUs for 2022.
- Class A properties in the top core U.S. markets will continue to command more aggressive overall capitalization rates—predominately in U.S. port cities, while the Midwest markets have experienced greater upward pressure on overall capitalization rates by comparison. Class B and, in some cases, Class C assets in close proximity (infill locations) to populated urban areas with readily available work force are in demand as investors/occupiers continue to solve the last-mile dilemma in urban locations.
- Acquisitions are moving forward, but the deal flows have been reduced, as investors rethink their pricing strategies. However, more recently, both buyers and sellers have become more realistic with their expectations, as the "bid/ask" differential continues to narrow.
- As the Federal Reserve increases interest rates to combat inflation, the thin yields that industrial properties command made acquisitions difficult to underwrite. Additionally, as vacancy remains historically low, and rents continue to rise, fewer owners are pressured to sell in a volatile market.
- Industrial fundamentals are expected to remain strong throughout 2023 and into 2024, with continued rent growth, albeit at a slower pace than 2022. Nonetheless, investors are closely monitoring the interest rate environment and fluctuations in 10-Year Treasuries regarding their pricing strategies.
- Minimal concern is seen with the anticipated interest rate hikes relative to pricing, as investors see greater rent growth potential, solid demand for space (leasing velocity) and rising construction costs as offsetting factors impacting any significant rise in cap rates.
- Logistics, food and beverage, cold storage and biotech/pharmaceutical assets are the preferred asset classes.
- With a strong infrastructure in place in most U.S. markets, vacancy rates still at historical lows, and the availability of natural resources, the long-term investment outlook for the national industrial market is positive. More specifically, seaport cities and major logistics hubs are expected to remain the strongest performers, especially as e-commerce continues to expand, in order to satisfy customer demand.

Industrial Market Highlights

Following several years of unprecedented growth, the national industrial market showed some signs of slowing in 2022. Growth in e-commerce slowed, with some entities giving back market share captured during the pandemic, and the nation's largest warehouse user delayed occupying several completed projects. Construction starts decreased in the fourth quarter as some developers delayed ground-breakings due to the current economic environment and the challenges of securing financing for projects.

Nevertheless, the industrial sector remained strong, with record-low vacancy and high demand for well-located, high quality logistics facilities. According to Cushman & Wakefield, the U.S. industrial market finished 2022 with the second highest total for leasing activity and absorption, behind 2021. Fundamentals are solid and are expected to remain so over the long-term; however, recessionary concerns, global inflationary pressures, high interest rates, as well as geopolitical issues are creating economic volatility and are anticipated to slow activity in the commercial real estate market.

Access Cushman & Wakefield's U.S. Industrial MarketBeat reports for current, comprehensive quarterly market information here. The following is value-add information from several key sources not generally included in Cushman & Wakefield's Industrial MarketBeat reports:

- The **U.S. Census Bureau** reported month-over-month in December 2022 that new orders for durable manufactured goods increased $15.3B, or 5.6%, to $286.9B. Excluding transportation, new orders decreased 0.1%. Excluding defense, new orders increased 6.3%. Transportation equipment, increasing four of the last five months, drove the increase, $15.5B or 16.7% to $108.1B.
- According to the **Federal Reserve**, overall industrial production expanded 1.6% in the 12-month period ending December 2022, while the consumer goods sector increased 1.7% over this same period. The motor vehicles and parts sector increased 5.1%, petroleum and coal products production decreased 2.3%, and oil and gas well drilling rebounded 36.3%.
- The Institute for **Supply Management Manufacturing**'s latest **Purchasing Manager's Index** (PMI) for the U.S. registered 47.4% in January 2023, 100 basis points (bps) lower than the seasonally adjusted 48.4% recorded in December 2022. Regardless of the overall economy, this figure indicates a second month of contraction after a 30-month period of expansion. The number is the lowest since May 2020, when it registered a seasonally adjusted figure of 43.5%. The chair of the ISM states, "The U.S. manufacturing sector again contracted, with Manufacturing PMI at its lowest level since the coronavirus pandemic recovery began. With Business Survey Committee panelist reporting softening new order rates over the previous nine months, the January composite index reading reflects companies slowing outputs to better match demand in the first half of 2023 and prepare for growth in the second half of the year." The New Order index contracted strongly, and New Export Orders remained below 50%, though improving. The Employment Index remained slightly above 50% and the Production Index logged a second month of contraction.
- The **U.S. Commerce Department** advanced statistics reported for the month of December 2022 that seasonally adjusted year-over-year retail and food service sales increased 6% compared to December 2021. Total sales for the 12 months of 2022 increased 9.2% compared to 2021. In 2022, retail and food services sales increased 9.2% compared to 2021. Auto sales and their components increased 3.3% over the year. Clothing and clothing accessories store sales increased 6.2%. Food and drink sales increased 16.7%, electronics and appliance store sales decreased 6.3%. E-commerce/non-store retail sales increased 11.4% over sales reported in 2021. Sales at general merchandise stores increased 3.2% in 2022 and sales at building materials and garden equipment and supplies dealers increased 6.6%.

ABOUT CUSHMAN & WAKEFIELD

Cushman & Wakefield (NYSE: CWK) is a leading global real estate services firm that delivers exceptional value for real estate occupiers and owners. Cushman & Wakefield is among the largest real estate services firms with approximately 52,000 employees in over 400 offices and approximately 60 countries. In 2022, the firm had revenue of $10.1 billion across core services of property, facilities and project management, leasing, capital markets, and valuation and other services. To learn more, visit www.cushmanwakefield.com or follow @CushWake on Twitter.

CUSHMAN & WAKEFIELD CAPABILITIES

Service Lines

Agency Leasing
Asset Services
Capital Markets
Facility Services
Global Occupier Services
Project & Development Services
Tenant Representation
Valuation & Advisory

Industries & Specialties

3PL
Airports & Aerospace
Automotive
Build-to-Suit
Data Centers
E-Commerce
Education
Energy (oil & gas)
Financial Services
Flexible Workplace
Food & Beverage
Global Supply Chain
Government
Healthcare
Hospitality
Industrial
Land
Legal Services
Life Sciences
Logistics & Industrial
Multifamily
Net Lease Investment
Not-for-Profit
Office
Ports & Intermodal
Public Sector
Rail
Retail
Sports & Entertainment
Technology

MICHAEL J. SCHAEFFER, MAI, FRICS
Executive Managing Director
U.S. Logistics and Industrial Practice Leader
Valuation & Advisory
+1 312 470 1870
mike.schaeffer@cushwake.com

Cushman & Wakefield's integrated approach to the logistics/industrial valuation process is unmatched, in a complex and always-changing asset class requiring our high level of knowledge, expertise and experience. Find out more.