

Metro Philadelphia Industrial, Q3 2017

# Economic growth driving tighter market conditions

Net Absorption  
1.8 Million sq. ft.

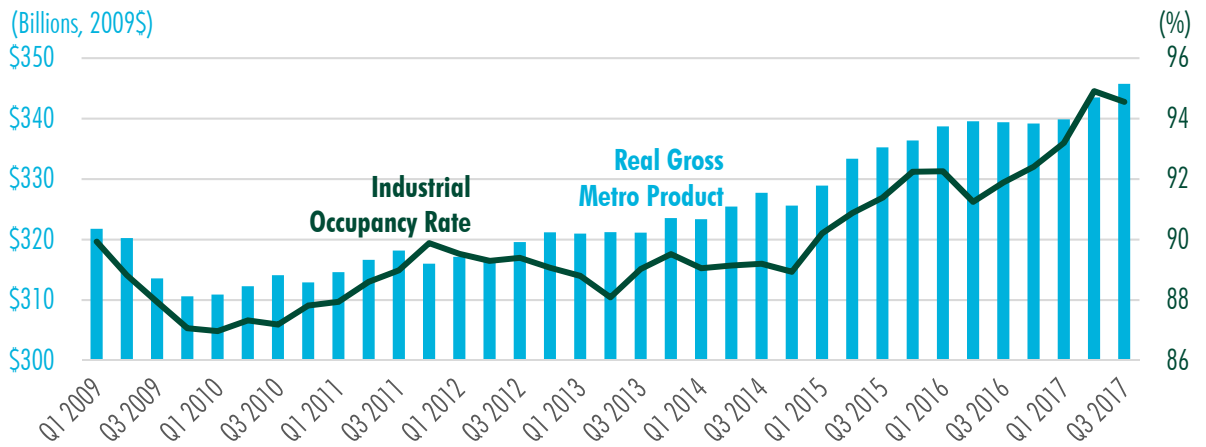
Vacancy Rate  
5.4%

Asking Lease Rate (NNN)  
\$4.35

Development  
2.2 Million sq. ft.

Figure 1: Philadelphia MSA Real GMP (lagged 4 quarters) and Industrial Occupancy

\*Arrows indicate change from previous quarter



Source: CBRE Research, Moody's Analytics, Q3 2017

- Vacancy moved sideways from the previous quarter's historic low level. A lack of new supply against the backdrop of sustained demand, especially in Southern NJ, points toward sustained high occupancy levels in the short term.
- Asking rents persisted higher as landlords clearly retained leverage during negotiations. Warehouse/distribution product in Southern NJ and flex product in the PA portion of the market enjoyed some of the largest year-over-year gains in rents as a result of limited supply.
- The first speculative project in New Castle County during recent history broke ground. Measuring 100,000 sq. ft., the building will add supply to an immediate area where available space is nearly non-existent. In Southern NJ, a 650,000-sq.-ft., built-to-suit project broke ground and is slated for e-commerce use.
- Investment sales activity settle toward recent historic averages as investors remained interested in the metro's tight, active market.

Although the region's burgeoning I-78/I-81 logistics corridor, stretching from Scranton past Harrisburg, draws most of the attention, the Philadelphia metropolitan industrial market is experiencing a boom of its own.

Occupancy in industrial properties in the Philadelphia area are at their highest levels ever, according to our records, and rents are surging higher. Continued favorable economic conditions and rapidly changing supply chain logistics are driving market conditions much tighter.

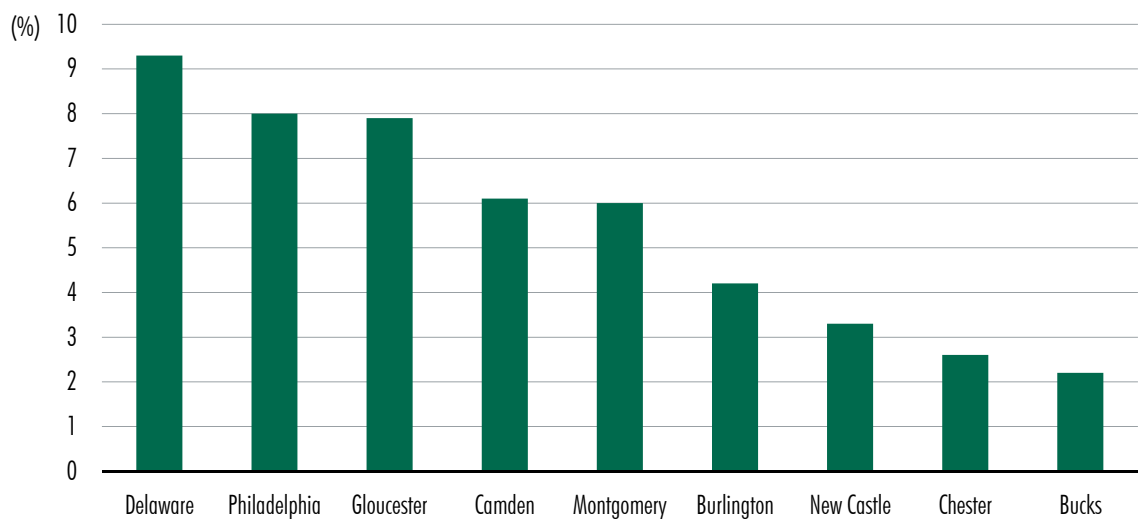
The vacancy rate in Southeastern PA dropped 200 basis points (bps) over the last year to a near-cyclical low of 5.5%. In Northern Delaware, the vacancy rate plummeted 860 bps since one year ago to a very tight 3.3%. Rents are surging higher across submarkets. The average asking rent in Metro Philadelphia rose 4.1% over the last year.

Figure 2: Industrial Market Statistics for All Properties Greater than 100,000 sq. ft.

Submarket	Inventory (SF)	Total Vacancy Rate (%)	Total Availability Rate (%)	Completions (SF)	Under Construction (SF)	2017 YTD Total Net Absorption (SF)	Avg. Asking Lease Rate (\$/NNN/PSF/YR)
Bucks County, PA	27,433,847	2.2	2.2	0	0	1,030,554	4.78
Chester County, PA	12,269,153	2.6	5.6	0	0	-20,823	---
Delaware County	10,605,300	9.3	10.9	0	0	-73,245	4.23
Montgomery County, PA	30,624,046	6.0	9.2	0	0	262,471	4.98
Philadelphia County, PA	29,621,499	8.0	9.3	0	175,000	342,822	4.00
<b>Southeastern PA Subtotal</b>	<b>110,553,845</b>	<b>5.5</b>	<b>7.3</b>	<b>0</b>	<b>175,000</b>	<b>1,541,779</b>	<b>4.39</b>
Burlington County, NJ	27,514,657	4.2	6.8	1,060,148	192,402	2,832,712	4.81
Camden County, NJ	14,753,405	6.1	8.9	0	600,000	93,167	3.59
Gloucester County, NJ	17,886,666	7.9	8.7	1,318,520	1,130,480	1,663,766	4.16
<b>Southern NJ Subtotal</b>	<b>60,154,728</b>	<b>5.8</b>	<b>7.9</b>	<b>2,378,668</b>	<b>1,922,882</b>	<b>4,589,645</b>	<b>4.16</b>
New Castle County, DE	13,912,828	3.3	4.6	0	100,000	388,808	5.66
<b>TOTAL</b>	<b>184,621,401</b>	<b>5.4</b>	<b>7.3</b>	<b>2,378,668</b>	<b>2,197,882</b>	<b>6,520,232</b>	<b>4.35</b>

Source: CBRE Research, Q3 2017.

Figure 3: Vacancy Rates by County.



**ABSORPTION**

Recent geographic and business-sector demand trends continued across the Philadelphia metro area during the third quarter. Southern NJ outperformed the other submarket while e-commerce or third-party logistics companies accounted for the business types driving positive absorption. Supply constraints in the PA portion of the market tempered activity as most of the desirable, modern space was occupied. In DE, companies such as DowDuPont and M Cubed helped take down larger blocks of space, helping drive the most active quarter, year-to-date, in New Castle County.

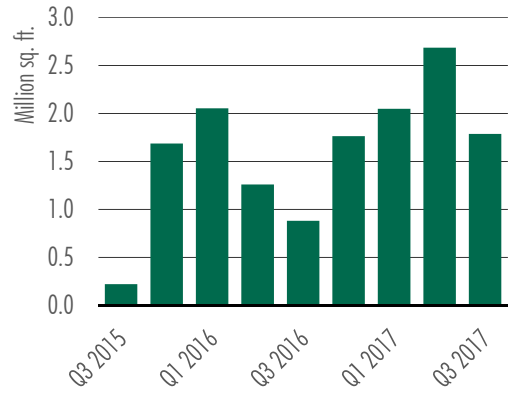
**VACANCY**

Vacancy moved sideways this quarter as construction deliveries kept pace with demand. At 5.4%, there is little room for vacancy to move lower. Segments of the market, such as flex product in-and-around the King of Prussia area, have no supply available and face development constraints that will offer little-to-no new options in the near future. Where few barriers to development exist in areas of low vacancy and rising rents, construction pipelines remained active. Expect vacancy to persist at low levels with no significant supply slated to deliver to the market in the near term.

**DEVELOPMENT PIPELINE**

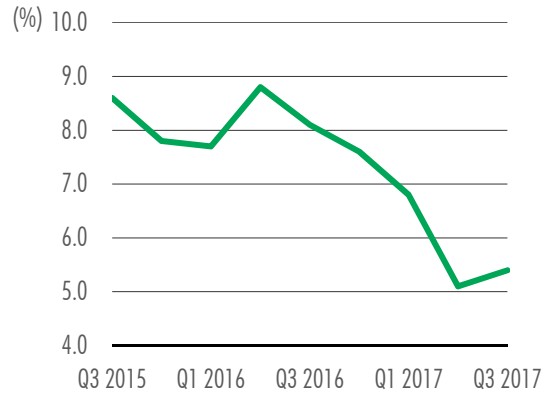
While the bulk of construction activity remained focused on the Southern NJ portion of the market, one speculative project kicked-off this quarter in New Castle County – its first in several years. It measures 100,000 sq. ft. and is expected to deliver by mid-2018. Construction levels in Southern NJ dipped following the completion of 2.4 million sq. ft. of new supply, most of which delivered leased. Another 650,000-sq.-ft. building broke ground in Gloucester County, but as a built-to-suit project slated for e-commerce use.

**Figure 4: Net Absorption**



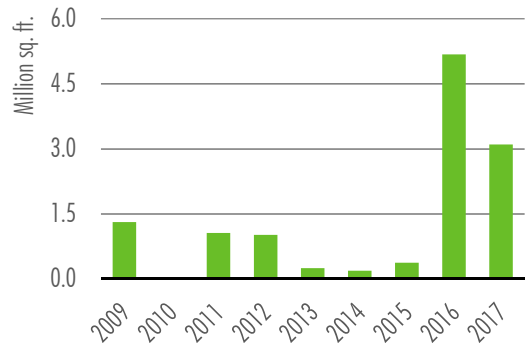
Source: CBRE Research, Q3 2017.

**Figure 5: Vacancy Rate**



Source: CBRE Research, Q3 2017.

**Figure 6: Completions**



Source: CBRE Research, Q3 2017.

**LEASE RATES**

A dearth of speculative development against a backdrop of persistent demand pushed rents higher, on average, throughout the region. This trend is most notable in Southern NJ and Northern DE. In the Philadelphia market, a lack of available space dampened rent growth, somewhat, as the most desirable space was already leased. But, in certain markets, comparable lease data continues to show strong rent growth and will most likely give developers reason to risk speculative development in the Montgomery and Chester Counties within the PA portion of the market.

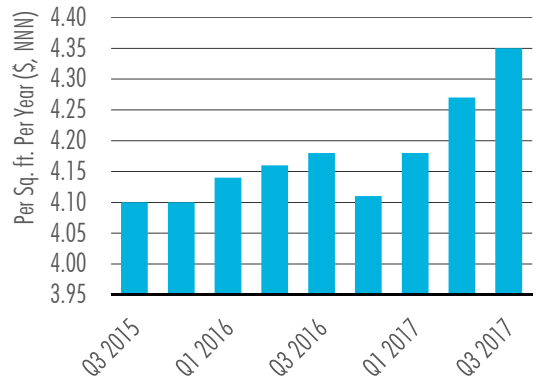
**CAPITAL MARKETS**

Industrial investment sales volume trended lower from its recent peak tallied in 2015 and 2016. Buyer composition, year-to-date, trended toward private capital and institutional capital as REITs comprised a smaller portion of buyer activity. To note, the largest acquisition during the third quarter was SSH's purchase of a five-building portfolio from a joint venture between Endurance Real Estate and Thackray Crane. The portfolio consisted mainly of fully occupied flex product in Marcus Hook, PA. As last-mile requirements grow in number, expect investors to eye stabilized warehouse and flex product proximate to condense urban populations.

**MANUFACTURING OUTLOOK**

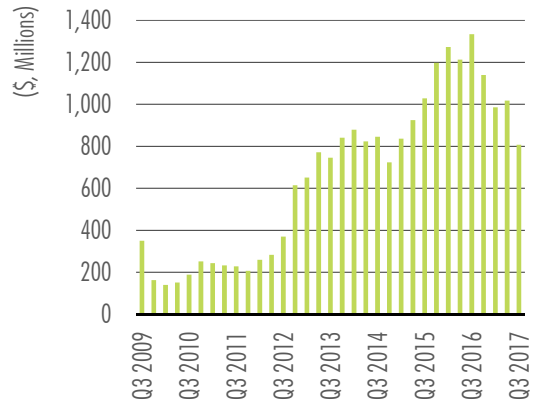
Manufacturing activity persisted to grow after showing slight signs of stalling during late 2015 to early 2016. But, while manufacturing activity grew relatively consistently since 2012, manufacturing employment only decelerated its decline as a result. Since then, overall manufacturing employment flattened out, showing no consistent signs of gains, hinting toward increased productivity as the driver of manufacturing growth. But, in the most recent Philadelphia Federal Reserve manufacturing survey, 30.6% of respondents expected increases in production to be accomplished through hiring compared to 25% who would accomplish through increased productivity, pointing toward potential jobs gains.

**Figure 7: Industrial Lease Rates**



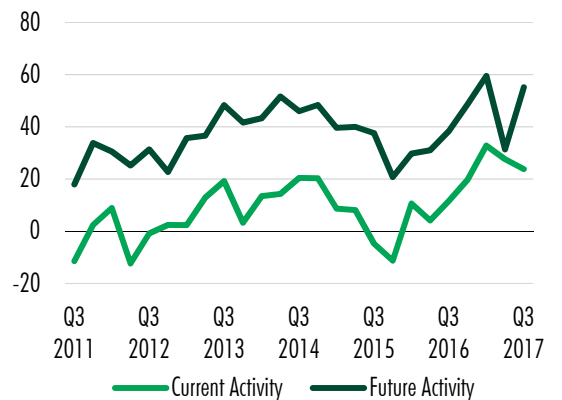
Source: CBRE Research, Q3 2017.

**Figure 8: Industrial Sales Transactions**

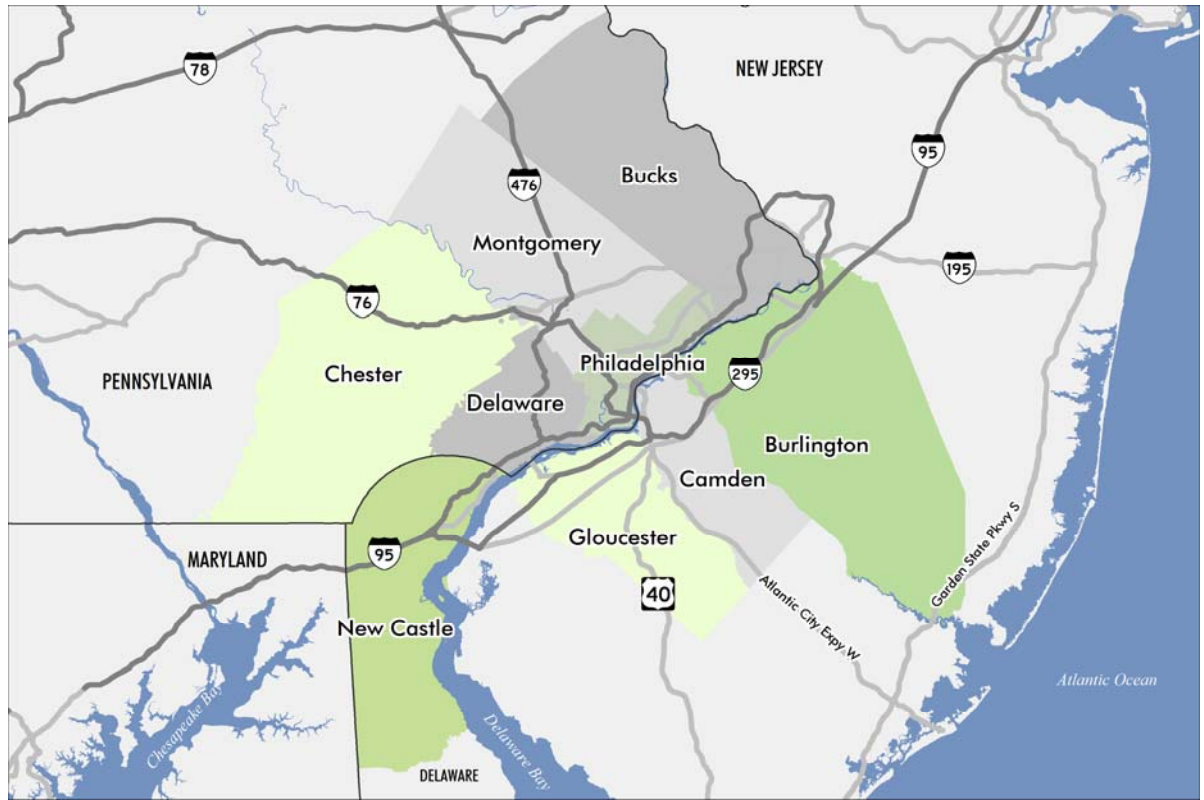


Source: Real Capital Analytics (4-Qtr. Aggregate).

**Figure 9: Philadelphia Metropolitan Business Outlook Survey (index > 0 implies manufacturing growth)**



Source: Federal Reserve Bank of Philadelphia



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