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County filled with aging industrial inventory

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A rendering of Murphy Development's proposed 3.2 million-square-foot Brown Field Technology Park. It will feature at least 1 million square feet of Class A industrial buildings

While new industrial projects come out of the ground in San Diego County, aging industrial space continues to be an issue.

A new Cushman & Wakefield report found that more than 80 percent of the county's industrial inventory was built prior to 2000, and a mere 3 percent was erected after 2009.

Starting with the 1970s, industrial inventory grew at an average rate of 39 million square feet per decade. Since 2010, however, that inventory has grown by less than 4.5 million square feet.

"At this level, there is not enough new supply to satisfy demand for new and functional industrial space," Cushman & Wakefield stated.

"It's not a surprise," added Dan Broderick, a Cushman & Wakefield regional managing principal. "There hasn't been a lot of industrial development."

An opportunity for redevelopment lies in the 82 percent of industrial inventory built prior to 2000, according to the commercial real estate firm.

The report said with the countywide industrial vacancy rate at a 15-year low of 4.8 percent, "we are not only seeing asking rental rates increase but also an increasing trend of renovations of older product to make them more appealing to tenants."

The older product doesn't just date back 20 years, however. Approximately 12.3 million square feet, or 7 percent of the current inventory, dates back 50 years.

In San Diego County, 36.3 million square feet of industrial space was added during the 1970s; followed by 54.2 million square feet in the 1980s. From 1970 through the 1990s, an average of 43.5 million square feet was built each decade, compared to 15.2 million square feet thereafter.

Only 25 percent of existing buildings are 100,000 square or larger.

The average size of an existing industrial building is 22,000 square feet compared to 88,000 square feet for buildings built in 2010 and after. The average building size currently under construction is 172,000 square feet.

Tenants are not only looking for larger spaces, they are wanting significantly higher clear heights than they can find in older existing structures.

For example, Cushman & Wakefield noted that about 59 percent of inventory has a clear height of less than 23 feet -- making it significantly lower than the average of 33 feet for buildings currently under construction.

Broderick said it can be hard to justify building industrial when it is competing against such asset classes as medical office, apartments, and even a grocery-anchored center for the highest and best use of a given property.

Broderick did note that quite a number of new industrial projects are coming out ground in the North County in particular.

"And we're seeing some really good activity on it," he said.

There are speculative projects in various stages, extending from Otay Mesa to Carlsbad.

A CoStar Group report noted that most of these projects are less than 100,000 square feet, and fewer than five projects have more than 500,000 square feet planned.

One of the biggest projects is Murphy Development's proposed 3.2 million-square-foot Brown Field Technology Park that will have at least 1 million square feet of Class A industrial buildings alone.

"Industrial development may not return to the sustained level of development of the heady pre-recession days, when it was common for more than 2.5 million square feet to be under construction," CoStar stated. "However, developers are currently underway on 1.6 percent of inventory, or about 3.1 million square feet -- the most this cycle by a considerable margin."

Roughly half of the new space is speculative, according to CoStar. Some of the spec projects include Pacific Vista Commerce Center and distribute in Carlsbad -- a submarket that boasts 1 million square feet of space under construction, 80 percent of which is available.

Others speculative projects are in South County, generally in Otay Mesa, where more than 500,000 square feet is underway with 85 percent of the space still available. It doesn't include Otay Crossings Commerce Park, a project situated on more than 300 acres near a future border crossing called Otay Mesa East.

CoStar noted that build-to-suits continue to influence the landscape. General Atomics is increasing its Poway footprint by 300,000 square feet at Ridgeview Business Park.

In Escondido, Badiie Development is building the 212,000-square-foot Exeter Industrial Park for Atlanta-based Veritiv.

The Badiee project has been on an incredibly quick timetable given that the site was only purchased last August.

"Of the more than 3 million square feet of inventory that has [been] delivered since 2016, less than 25 percent is still available," CoStar reported. "For 2016 deliveries, 20 percent is still available; only 5 percent is available [of] the 1 million square feet that [was] delivered in 2017; and more than 70 percent is still available in deliveries so far in 2018."

With recently completions and space under construction, more than 2.5 million square feet of new inventory is still available for lease, providing tenants plenty of options across San Diego County. But only a couple of properties will accommodate a 200,000-square-foot tenant at this point, CoStar added.

With land, and therefore ground-up construction, still very limited, Broderick said the race is on to redevelop existing industrial buildings.

"Amenities are a hot button for these industrial tenants right now," he said. "They want places for downtime, and outdoor spaces where they can convene."

"Landscape design is important. You want to make these spaces interesting to the eye."

Broderick said he does have some concerns.

"I wonder about the mom and pop industrial tenants in the back office," he said. "What happens when demand is pushed so high? What are the options for them?"