DTRE

Q2 2022
RESEARCH

Big Box Logistics

OCCUPIER & INVESTMENT
MARKET REVIEW

5 Things You Need to Know

ABOUT **BIG BOX LOGISTICS** IN Q2'22

1. **9.3 million sq ft** of take up in Q2'22

2. **20.1 million sq ft** of take up by the end of June - **3rd best H1 on record**

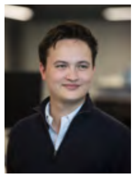
3. The DTRE Big Box vacancy rate now stands at **2.1%**

4. Q2'22 has seen **£1.72 billion traded** with a further **£1.1 billion under offer**

5. According to MSCI yields for distribution warehouses have fallen to 3.3% to end May, **despite sentiment indicating otherwise**

Occupational

Big Box take up in Q2 2022 has reached 9.3 million sq ft, bringing the half-year total take up to 20.1 million sq ft, exceeding the 10-year average of 18.3 million sq ft and by the end H1, 2022 has therefore experienced the third highest ever take up.



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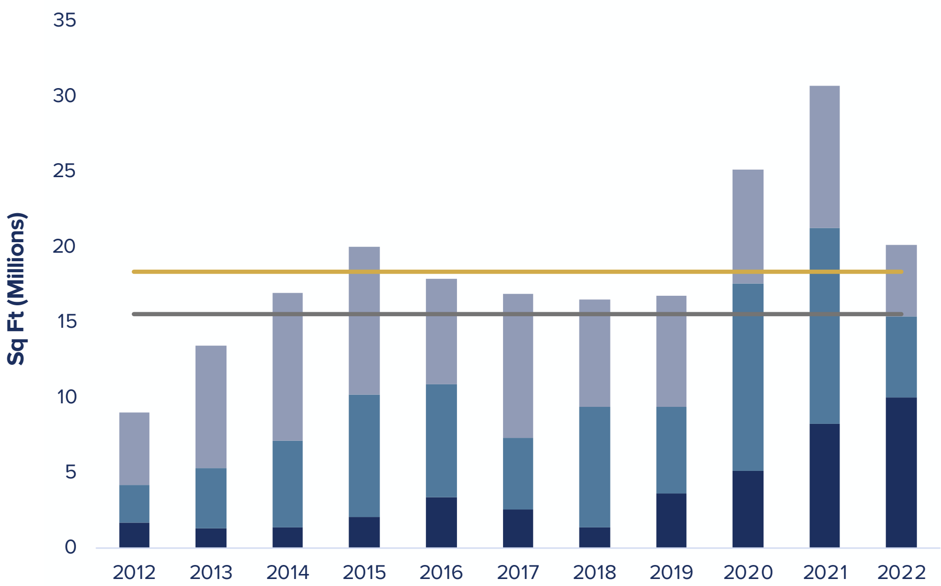

Fig 1
10-year H1 average take up

- New / Spec Built
- Design & Build / Pre-let
- 2nd Hand
- 10 Year Average (2010-2019)
- 10 Year Average

Source | DTRE Research

Take up in Q2 was heavily influenced by Iron Mountain's lettings at Symmetry Park Rugby, where they took c.1 million sq ft of space over four units. Two of the units are under construction, whilst the remaining two are currently in for planning. The letting of 484,000 sq ft at Coventry Logistics Park and the letting of Monarch 330 to Danish Crown in Rochdale were significant contributors to H1's take up figure.

> The first half of 2022 has seen 20.1m sq ft transact – third highest on record

The DTRE Big Box vacancy rate has continued to fall since the start of the year and now stands at an all-time low of 2.1% of existing stock available for immediate occupation. This is highlighted most starkly in the 300,000 sq ft+ market where only 2 Grade A buildings in the entirety of the UK are available for immediate occupation.

Despite the acute lack of supply, speculative development remains at low levels, with 16 million sq ft due to finish construction by the end of 2022. Of this, only 13.5 million square feet is over 100,000 sq ft, equating to less than 6 months of supply according to the 10-year average take up.

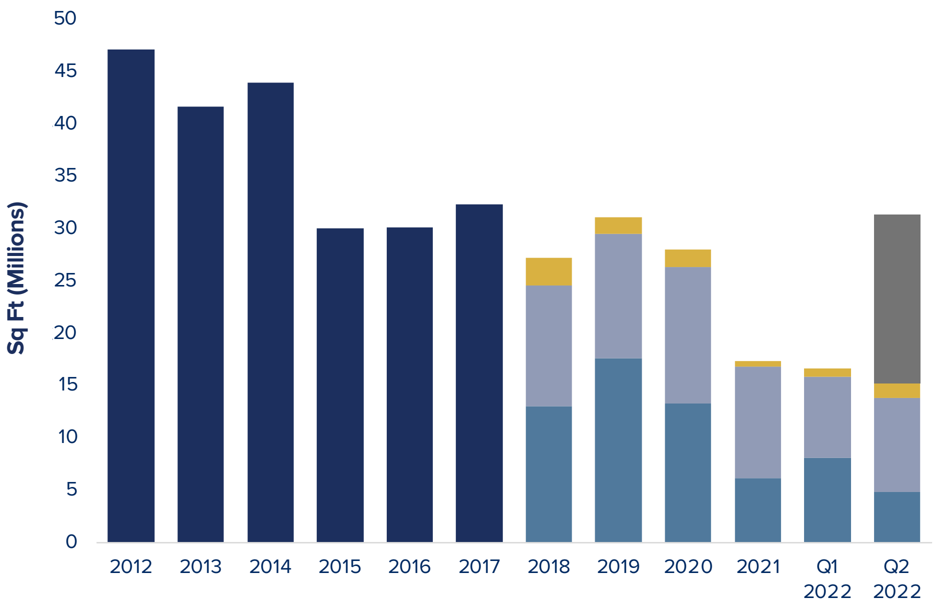

Fig 2
A Further drop in Supply

- Total
- Grade A
- Grade B
- Grade C
- Under Construction

Source | DTRE Research

As inflation soars and supply chain issues persist, the cost of construction has continued to rise. As a result, the desire to speculatively build new warehouses may come under pressure and could potentially result in less construction, further squeezing an already under supplied market.

Finally, despite macroeconomic difficulties we expect occupier demand to remain strong throughout the coming months, in support of the structural shift further towards online retailing. Ending well above the 10-year average of 28 million sq ft in the 10 years prior to 2019.

"Just two Grade A buildings are available for immediate occupation in the entirety of the UK"

Investment

The Big Box investment market has seen a slowdown albeit from historic highs, with £1.72billion of single let units being traded in Q2, bringing the half year total to £3.4 billion. This is c.5% down on the previous quarter of £1.8 billion and c.43% down on the previous half year. There is also a further £1.1 billion of single let investments under offer.

Volumes were heavily influenced by the biggest deal in Q2; Project Resolve, a cross-sector portfolio purchased by Oval Real Estate for £925 million of which £453.5 million was industrial; and the sale and leaseback of the Boots Distribution Centre, a 466,000 sq ft unit in Burton on Trent, for £73.75 million to ICG Longbow.

DTRE are tracking £1.1 billion worth of stock that is currently under offer however, a further £2.16 billion of stock is available to purchase.

> According to MSCI's Monthly Index yields fell to 3.3% to end May

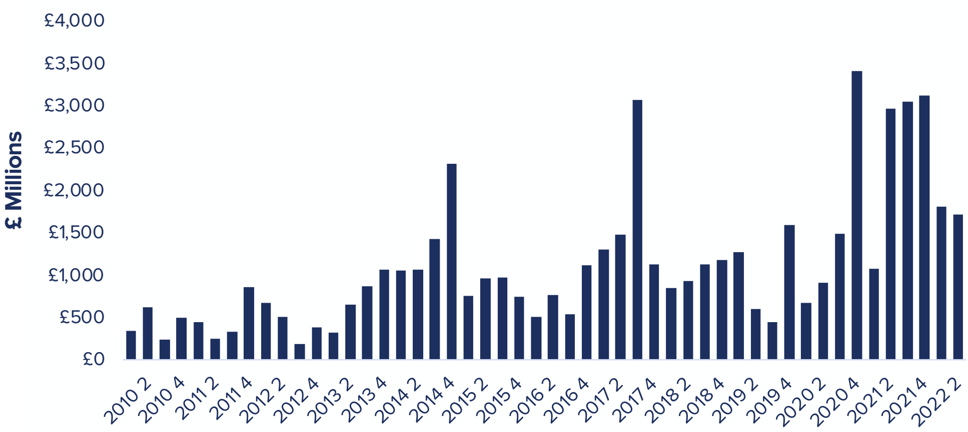

Fig 3
Quarterly Investment Volumes
Source | DTRE Research

Despite continuing concerns amidst rising inflation and interest rates, yields have continued to fall throughout Q2,from 3.6% at end of March to 3.3% at end May according to MSCI's Monthly Index. This stands in contrast to the wider market sentiment and we expect to see an adjustment in yields for end June. As of yet the shift in yields is sentiment driven, with a lack of hard evidence, albeit we understand Project George has exchanged with a 'sensible' adjustment.

Costs of debt and interest rate rises are causing prime, low yielding investments to struggle in the market. This issue is less problematic in under-rented properties and on multi-let estates as quicker access to the reversion mitigates the problem by raising the running yield and covering the increased debt cost.

In order to stay ahead of inflation and the increasing cost of debt, investors are continuing to back rental growth to remain strong. Indeed, according to MSCI's Monthly Index, average annual rental growth for 'Standard Industrial' was 12.1% for the year to May 2022, whilst London industrials continue to outperform the wider market significantly at 17.1%.

> **MSCI's Monthly Index saw rental growth for 'Standard Industrial' reach 12.1% for the 12 months to May 2022**

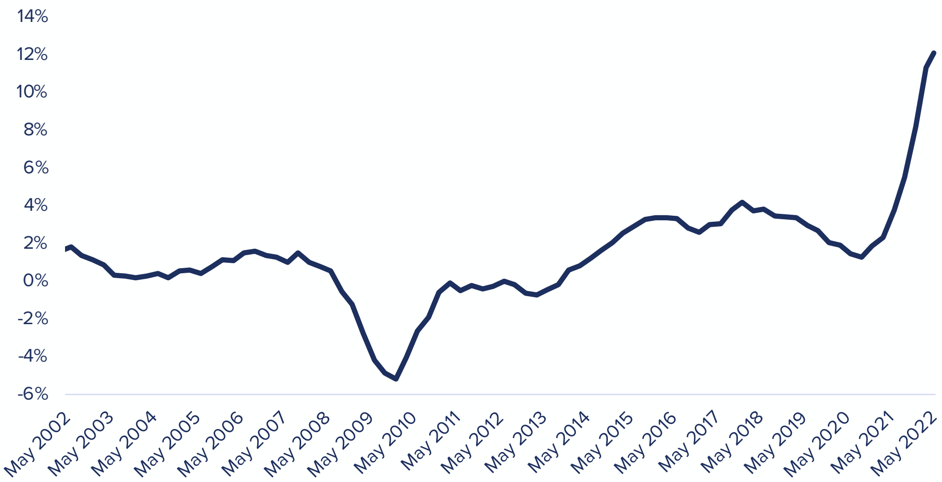

Fig 4
Standard Industrial Market Rental Growth

Source | MSCI

In the last two months, we have witnessed pricing soften in reaction to the rising cost of debt and investor attitudes are now more conservative with regards to their underwriting assumptions. However, the industrial sector is still underpinned by healthy occupier demand and a lack of supply - a key driver to the rental growth we have seen in previous years.

Whilst the wider UK economy stumbles, the industrial market is expected to weather the storm better than others. However it will not be immune to turbulence over the coming months, but whilst vacancy rates remain so low, we continue to predict further strong rental growth, with DTRE forecasting average annual rental growth of 4.6% across the UK to end 2024.

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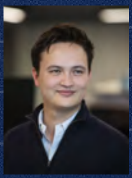

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