



INVESTORS SHIFT FOCUS FROM RETAIL TO INDUSTRIAL SPACE

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Real estate investors are dealing with significant risks resulting from shifts in two of the major real estate sectors: a significant decline in the values of retail properties and an upsurge in demand for industrial spaces. The massive increase in e-commerce over the past five to seven years has contributed to large-scale vacant retail properties, including regional malls and shopping centers. On the upside, there have been rapid growth and higher demand for warehouses by potential tenants. Marcum LLP's Real Estate Group has observed significant decreases in fair values for entities owning regional malls and shopping center portfolios across the U.S. The vacant retail properties have created opportunities for developers to convert these spaces into industrial spaces to meet the growth in e-commerce and logistics businesses.

Both domestic and foreign investors have monitored the changes in the U.S. real estate market and proactively invested in the sector. The market has seen the demand for industrial properties outpacing the supply, and there is major construction of industrial properties under way, with the majority of space being speculative. Institutional investors are interested and eager to invest in large-scale industrial property transactions. Recent industry reports indicate that national warehouse inventory occupancy exceeds stabilized rates, and market rental rates have been at their

all-time high. Marcum's Real Estate Group expects that the high, rising demand for industrial properties will continue for the remainder of 2019 and beyond.

E-commerce

The rise in demand for warehouse spaces is being driven by the significant increase in e-commerce. Industrial properties built in the last 10 years and properties being built now are expected to be constructed with modern, sophisticated data management systems and more worker-friendly facilities. Employees will need to spend full days working in warehouses to accurately fulfill customer orders. The accuracy of an entity's inventory management system in ensuring that advertised items are on the shelves and being able to deliver them to customers as quickly and efficiently as possible is mission critical in the e-commerce economy.

As retailers increasingly close underperforming locations, consumers, particularly those in remote areas, are relying on e-commerce to fill the gap. Pinpoint fulfillment systems have largely been the key to Amazon's phenomenal success as an e-commerce leader, as its revenues skyrocketed to billions over its 25 years of operations.

Physical Condition

Industrial developers are challenged to ensure that warehouses meet the safety and

health requirements for a safe workplace environment that satisfies regulations and is comfortable and appropriately designed for workers to spend long hours working. Traditionally, warehouses are treated as housing locations for inventories that were later shipped to retail stores designed and built for consumers to browse. The traditional warehouses had low tenant and building improvement costs compared to office and retail properties, since sophisticated layouts and designs weren't a priority for warehouses.

As an increasing number of warehouse jobs are created in the e-commerce economy, we can expect tenant allowances and building improvement costs to rise for landlords, which will be reflected in higher rents and price per square foot for industrial properties.

Technology & Outlook

Over the next five to 10 years, industrial property construction volume will continue to expand and will become more technologically advanced, with greater use of artificial intelligence software and data management systems. With more sophisticated and high-tech warehouses, it's expected that the market share of industrial properties will increase while there will be continued contraction in the retail property sector. The industrial sector will become more appealing to real estate investors due to higher returns and increase in asset values.