

Shipper Roundtable: Forecasting Supply and Demand | Republicans Take the Hill | Lean Inventory in Pacific Trade  
Trans-Atlantic Is Tested | Truckload Carves Out Capacity | Rails Go Off-Road | Logistics in the Cloud

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ANNUAL REVIEW & OUTLOOK

2011

SPACE FOR RECOVERY

# 2011

## SPACE TO RECOVER

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in the 3rd annual Shipper Roundtable, Jonathan Gold of the National Retail Federation, Donna Lemm of Mallory Alexander and Gordon Macko look at carrier relations, logistics strategies and regulatory issues in 2011.?

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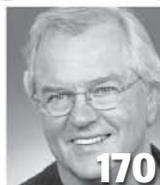
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# Out-of-the-Box Thinking



By Jon DeCesare

World Class Logistics Consulting

**AS THE INDUSTRIAL** real estate industry enters a new decade, the light of optimism is shining a little brighter than in recent years. According to Real Capital Analytics, sales of significant U.S. industrial facilities totaled \$4 billion in the third quarter of 2010, the highest quarterly sales volume in two years.

Another bright spot is the relatively low share of distressed properties compared to other property types. According to CBRE Richard Ellis's Industrial Leading Indicator Report — Fourth Quarter 2010, demand for industrial real estate space across the sum of the markets tracked by CBRE Econometric Advisors totaled 10.5 million square feet in last year's third quarter. This represents the first quarter of positive absorption after 10 consecutive quarters of decline.

But a number of elements make the light flicker, and sometimes fade. New industrial construction hit a record low in the third quarter of just 2.7 million square feet of new space completed, a mere 6 percent of the quarterly historical average of 42.8 million square feet. Construction volume will undoubtedly be weak until high availability rates — and the corresponding pricing pressure — subside. The U.S. industrial property vacancy rate climbed from 9.8 percent in 2006 to 13.9 percent in 2009 and was on pace to finish 2010 at 14.4 percent, according to RREEF Research.

With consumer spending fragile and unemployment running at historically high levels, manufacturers and distributors are keeping imports and inventory levels in check, weakening demand for warehouse space.

Federal Reserve Chairman Ben Bernanke summed up the depth of the problem when he told "60 Minutes" in December it could take another four or five years for the U.S. to return to "a more normal unemployment rate" of 5 to 6 percent. Unemployment stood at 9.8 percent in November, the 19th consecutive month above 9 percent and matching the worst stretch since World War II.

So what can industrial real estate companies do to better compete in the next couple of years? To address that question, let's turn to the world of the supply chain.

## SUPPLY CHAIN DYNAMICS

Supply chain dynamics — market-focused distribution centers, transloading and ports of entry, for example — have had a major influence on demand for industrial real estate facilities' locations and designs. In the post-recession environment, those dynamics will likely have an even more dramatic impact on industrial real estate companies' successes and failures.

For insight into how supply chain elements shifted during the recession, let's look at some of the conclusions in the Council of Supply Chain Management Professionals' 12th Annual State of Logistics Report.

- Retail sales are up, but inventory restocking isn't, and this lean inventory strategy is expected to continue.
- Out of necessity, shippers and service providers took all the fat — and more — out of their operations to reduce costs.

They are now exposed to re-emerging risks, including tight transportation capacity.

- Many shippers responded to their own internal cost pressures by moving from long-term carrier relationships to the spot market or third-party logistics partnerships.
- Length of haul decreased further as shippers shifted more long-haul moves to rail intermodal and utilized regional distribution strategies where possible.
- Even with a steady recovery of demand, volatility on the supply side of transportation capacity means 2010's challenges won't end this year for logistics professionals.

Helpful insight also can be found in Saddle Creek's 2010 Distribution Network Trends report. Based on a survey of 235 logistics professionals representing diverse market segments, including manufacturers, retailers and distributors, the report highlights supply chain executives' goals on operating highly efficient and effective supply chain strategies.

Asked about their optimal characteristics for DC location, respondents cited the following: Closer to market/customers, 57.2 percent; low operational costs, 50.3 percent; and inbound/outbound transportation, 47.6 percent. This indicates an ongoing shift to market-oriented DC locations and strong focus on reducing costs.

Two-thirds of respondents confirmed they had made changes to their supply chain distribution network design as a result of the

economic downturn, illustrating the severity of the recession. The top three areas of change for respondents overall were transportation-related changes, 44.1 percent; warehouse size and/or configuration, 33.8 percent; and consolidation of shipments from suppliers, 24.8 percent. These activities confirm the importance supply chain executives put on warehouse site locations that provide the best possible location logistics elements support.

The third source of supply chain insight comes from the Retail Industry Leaders Association and Auburn University and their State of the Retail Supply Chain Study. Consisting of interviews with senior executives and a national survey of major retailers, the report is full of insight. Among the highlights:

- Nearly 94 percent of survey respondents agreed or strongly agreed that their CEO recognizes the key role of supply chain management operations in achieving corporate success.
- Supply chain management, which has long played a critical role in the success of retailers, was elevated in importance because of how it can help corporations closely manage the total cost of global procurement, streamline inventories and keep transportation expenses in check without hurting product availability or customer service.
- Cost control and the drive for greater efficiency across supply chain management activities, including warehouse operations, remains a point of emphasis.

So what's the takeaway from these three studies in terms of the impact on the industrial real estate industry?

- **LOCATION:** Supply chain executives are committed

to continuous improvement programs with their supply chain networks. Warehouse locations with strong logistics profiles will be in high demand. Locations offering goods movement flexibility such as numerous transportation providers, quality interstate highways, quality and quantity labor sheds, availability of 3PL services, and proximity to transportation nodes will be in higher demand.

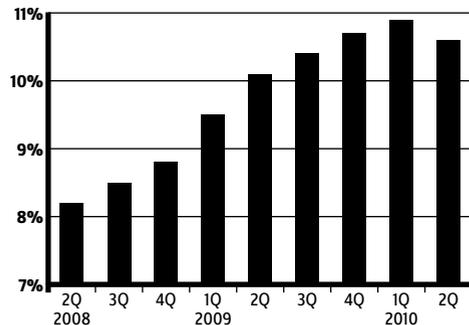
- **FACILITIES:** Companies dramatically reduced their inventories during the recession, and the high pre-recession inventory levels won't return. This has created excess storage capacity. Facility designs offering efficient throughput capabilities — cross-docking and transloading, for example — and the flexibility yard spots, dock doors and other user-friendly features offer will be in demand.
- **STRATEGIES:** Corporations will operate with lean management teams, creating challenges for those workers when conducting warehouse site selection studies. The industrial real estate developers and brokers who can assist tenants by providing site location logistics information will have a competitive edge.

## A MATTER OF TIMING

Prior to the recession, industrial real estate development and brokerage companies developed their internal industrial real estate logistics resources. Some companies were able to use complex warehouse site location information to make better investment, portfolio, development and marketing decisions. The recession forced many companies to slash their industrial real estate logistics resources. The timing was ironic in that

## SPACE TO FILL

■ U.S. industrial vacancy rate by quarter.



Source: Grubb & Ellis, [www.grubb-ellis.com](http://www.grubb-ellis.com)

these reductions occurred as supply chain executives were increasing their need for help with warehouse location logistics information.

When industrial real estate developers and brokers better understand the logistics strengths and challenges of facility location compared to the competitors, they are able to make better investment and marketing decisions and provide critical information to potential tenants.

We recommend industrial real estate professionals conduct their own warehouse site location logistics profiles. A partial list of those components could include:

- Major operating costs.
- Proximity to transportation nodes.
- Availability of labor.
- Access to markets.
- Quality of life.
- Utilities.
- Highway infrastructure.
- Business costs/taxes.
- Availability of trucking.
- Availability of 3PL services.
- Cost of living.
- Business incentives.

The next 12 to 18 months will be challenging. Industrial real estate companies that can implement new, tenant-focused, out-of-the-box strategies will gain a competitive edge. **joc**

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