

Special Report | 20 April 2020

Logistics Real Estate – Infrastructure of a Shifting Economy



Elion Logistics Park 55, Chicago, IL

With consumers forced to stay home, e-commerce has seen an acceleration in sales, placing a strain on inventory levels and supply chains. This catalytic shift in consumer behavior is driving logistics real estate to serve as the infrastructure to answer that demand.

Infrastructure of a Shifting Economy

The pandemic is sparking vast changes among the logistics real estate space, requiring companies to adjust to fluctuations in demand, supply and labor availability. The long-term effects are projected to boost demand for logistics real estate in three ways:

1. Acceleration of E-commerce

- As a result of the pandemic, quarantines are creating new online consumers and driving demand for goods bought online, fueling the need for distribution facilities at a rate much higher than the current cycle.¹
- E-commerce sales represented 15 percent of total retail sales in 2019, and is expected to jump to 39% by 2030.¹
- These changes drove record increases in online purchases over the course of a few days.²
 - Online grocery in the U.S. saw a +100% boost in daily online sales.²
 - Overall e-commerce in the U.S. increased by 25%, largely propelled by grocery.²
 - Grocery delivery app downloads hit record levels and worldwide online searches for “grocery delivery” increased by 450% versus last March.³

2. Supply Chain Diversification

- Demand for U.S. East Coast and inland port locations should increase as companies diversify their supply chains largely due to U.S.-imposed tariffs and the pandemic disrupting their reliance on China.¹
- The rapid shift in consumer behavior toward e-commerce has put pressure on supply chains to adapt – for every dollar of sales an e-commerce retailer realizes, it needs three times the level of supply chains compared to other forms of commerce.⁴

3. Inventory Controls

- Companies and suppliers may decide to increase their inventory levels in the long term to ensure they are adequately able to meet demand for business continuity purposes, thus increasing the demand for warehouse space.¹

U.S. E-commerce Penetration, % of Total Retail Sales Forecast



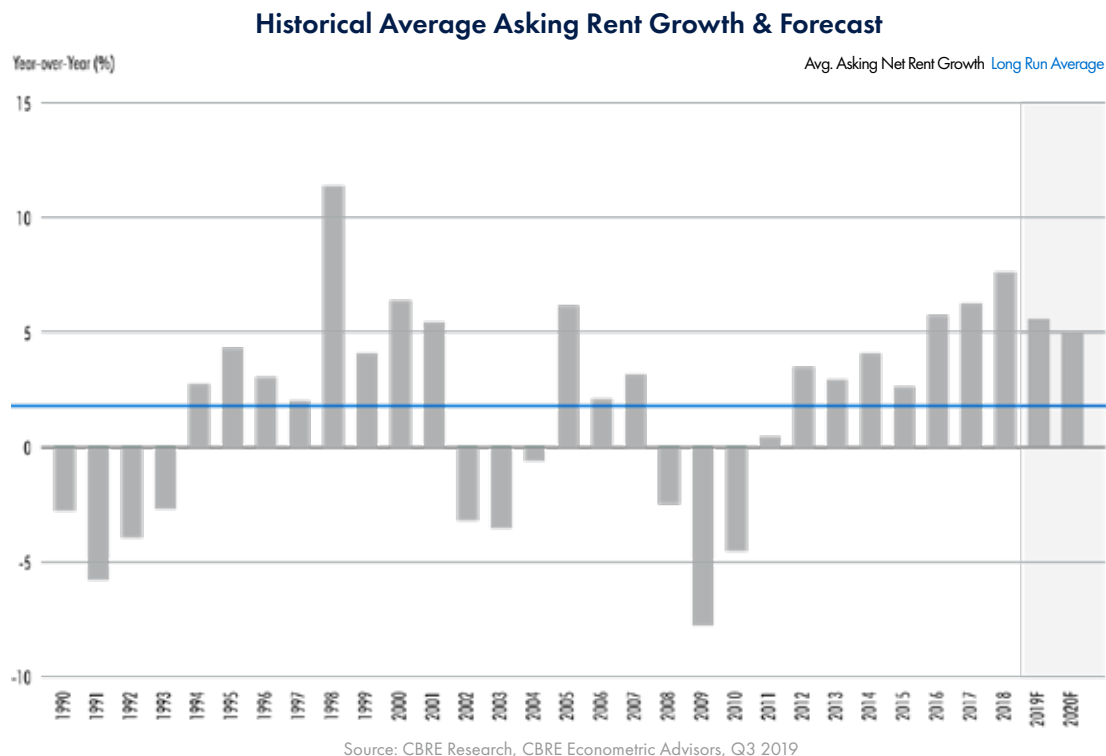
Source: CBRE U.S. MarketFlash, Post-Coronavirus Industrial Real Estate, March 23, 2020

Strong Real Estate Fundamentals Pre-Crisis

Fundamentals in the logistics real estate sector were strong heading into the crisis, with solid occupancy levels and consumer preferences driving demand for infill locations.

Persistent Rent Growth in Infill Locations

- Q4 2019 represented the 33rd consecutive quarter of rent growth in the U.S. with average net asking rent rising to \$7.63 per sq. ft., an increase of 5.1% year-over-year.⁵
- Rising rents were forecasted to be partly driven by infill industrial space in supply constrained markets as e-commerce companies race to offer same-day delivery to customers.⁶
- Warehouses of less than 120,000 sq. ft. have seen rents rise by 30% in the past five years.⁶



Historically Low Vacancy Rates

- The overall vacancy rate remained unchanged from Q3 to Q4 2019 at 4.4%, with a marginal 20-basis-point increase year-over-year.⁵
- With extremely low vacancy rates and limited space options in several markets, higher than normal renewal rates were projected for 2020.⁶

Population Growth

- Estimated U.S. population growth of 2.5 million per year equates to +100-125 million sq. ft. of new warehouse demand per year.⁷
- Over the next five years, the U.S. population is expected to increase by 12.5 million, further driving consumption and thus leading to additional demand for warehouse space.^{7,8}

Efficiency in Middle- & Last-Mile Distribution

- Distribution and fulfillment supply chains are being transformed to accommodate short delivery promises, forcing supply chain models to become more efficient nationwide.⁹
- Light-industrial properties, typically smaller than 200,000 sq. ft. and often located in or adjacent to infill urban markets, have been identified as the solution to the “last-mile” needs driven by e-commerce.⁹

For the reasons discussed here, we believe that logistics is better positioned than other real estate sectors due to the potential boost to long-term demand from e-commerce and supplier inventory needs.

Elion and its affiliates are well-positioned to respond to this demand with a healthy pipeline of identified logistics assets.

Long-Term Leases Counter Volatility

- Compared to other real estate asset classes, industrial leases are longer-term and are less likely to respond to short-term disruptions, decreasing the likelihood that warehousing lessees vacate industrial properties because of the spread of the virus.¹⁰

Investor Allocations Anticipate Resiliency

- Though near-term denominator effects could impact institutional allocations, more than 88% of investors who allocate to industrial would consider new investments over the next six months indicating the overall sentiment toward logistics real estate should remain positive.¹¹
- 64% of institutional investors are making no changes at this time to their private market allocations despite dislocations caused by the crisis, with some 15% even increasing allocations according to a recent LP survey conducted by placement firm Eaton Partners.

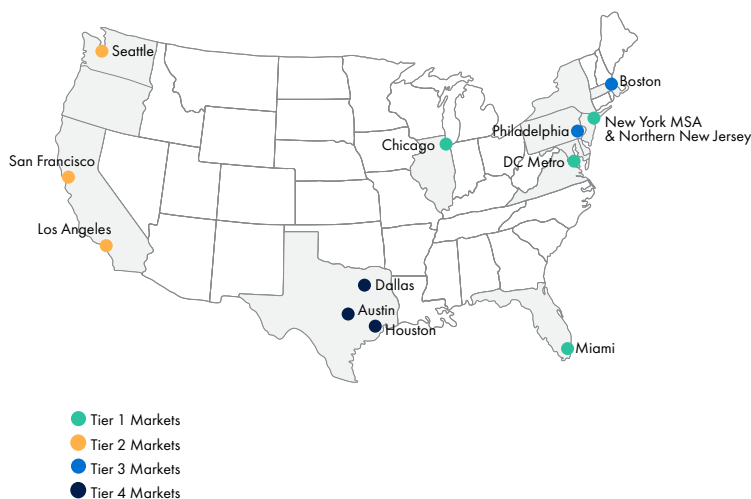
Downside Protection Independent of Market Cycles

- Elion and its affiliates seek to generate risk-adjusted returns by employing a rigorous bottom-up investment process focused on real estate fundamentals, providing downside protection independent of market cycles.
- Before an opportunity is presented to Investment Committee for approval, it must pass Elion's three fundamental pillars for investment: located in supply constrained core markets, priced at- or below replacement cost, and offer attractive risk-adjusted returns without excess leverage.

Identified Pipeline in High-Barrier, High-Growth Markets

- Some states are seeing a bigger overall e-commerce boost with online sales lifting 20% or more since the crisis.²
- Elion's last-mile investment strategy focuses on high-barrier to entry, high-growth urban markets and sees pipeline opportunity in following areas:
 - last-mile grocery distribution throughout New York and the Five Burroughs, northern New Jersey, San Francisco, Los Angeles, and Seattle;
 - continuation of middle- and last-mile value add strategy in supply constrained markets and sub-markets with specific focus on those that are exhibiting resiliency in tenant demand during the shutdown, most notably in northern New Jersey, Chicago, the D.C. metro area and South Florida;
 - responding to a "flight to quality" by acquiring existing buildings that exhibit Class A characteristics with a minimum square footage of 100,000;
 - speculative development of Class A logistics facilities geared toward e-commerce users in target supply constrained markets and sub-markets; and
 - expansion of first-mile build to suit opportunities in 2021 and beyond.

Focused on supply-constrained, densely populated urban markets with strong consumer ordering habits.



END NOTES

- 1 CBRE U.S. MarketFlash, Post-Coronavirus Industrial Real Estate, March 23, 2020
- 2 Growth from March 13 – 15 compared to baseline period of March 1 – 11, 2020. Adobe Analytics Digital Economy Index 2020
- 3 Apptopia, Google Trends as of March 17, 2020
- 4 eCommerce Drives Industrial Real Estate Boom, PYMNTS, April 2, 2020
- 5 CBRE U.S. Industrial & Logistics Figures Q4 2019
- 6 CBRE Industrial & Logistics 2020 U.S. Real Estate Market Outlook
- 7 CBRE Research
- 8 U.S. Census Bureau
- 9 CBRE Research: Same-Day Speed
- 10 Coronavirus and Supply Chain: Implications for the Industrial Market, CBRE, March 6, 2020
- 11 PREA Survey, Industry Conditions in the Wake COVID-19
- 12 Elion is registered as an investment adviser with the SEC under the Investment Advisers Act of 1940 (the “Advisers Act”).
Registration as an investment adviser with the SEC or with any state securities authority does not imply a certain level of skill or training.

IMPORTANT NOTICE

Neither Elion nor any of its affiliates makes any representation or warranty, express or implied, as to the accuracy or completeness of the information contained above and nothing contained herein may be relied upon as a promise or representation whether as to the past or future performance. No representations are made as to the accuracy of any targets, estimates, approximates or projections or that such targets, estimates, approximates or projections will be realized. Forward-looking statements are based upon certain assumptions and information available on the date hereof. Actual events are difficult to predict.

ABOUT ELION PARTNERS

Elion Partners is a logistics-focused real estate investment firm and registered investment adviser.¹² As a vertically integrated platform, Elion is both a fiduciary and operator, managing more than \$1.5 billion in real estate assets through closed-end funds and permanent capital investment vehicles. As long-term stewards of capital, principals of Elion invest personally in each of the firm’s funds to ensure alignment of interests and transparency with its capital partners.

Elion Partners

Miami Office

3323 NE 163rd Street
Suite 600
Miami, FL 33160
+1 305.933.3538

New York Office

445 Park Avenue
Suite 16E
New York, NY 10022
+1 (212) 894.4713

www.elionpartners.com