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by Franklin Templeton

Building into the future: The case for U.S. industrial development

The industrial replacement cycle has begun

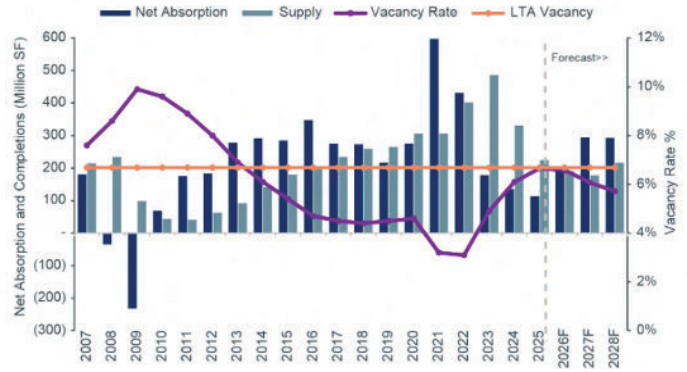
After an extraordinary expansion during the pandemic, the U.S. industrial market entered a period of recalibration. Leasing slowed, development activity retreated, and uncertainty surrounding capital markets and trade policy weighed on tenant demand. Yet the sector's long-term fundamentals remain intact. Demand is recovering, much of the existing warehouse inventory is functionally obsolete, and structural constraints are limiting new supply. These trends suggest the sector may be approaching the next phase of the development cycle, increasingly favoring experienced developers with entitled land, strong balance sheets and the ability to deliver modern logistics facilities.

Demand recovery signals the next phase of the cycle

Following the unprecedented expansion of the pandemic years, the U.S. industrial market entered a period of normalization beginning in 2023. As tenant demand moderated from exceptionally elevated levels and as capital markets tightened, leasing activity slowed and net absorption fell below historical norms. Increased policy volatility and geopolitical uncertainty, including the "Liberation Day" announcement in April 2025, added further caution to occupier decision-making. Even so, the current cycle has differed markedly from previous downturns. Unlike the global financial crisis, the industrial sector has avoided sustained negative net absorption, while vacancy has remained at or below long-term averages.

Signs of recovery are evident. After bottoming in 2025, net absorption is expected to return to equilibrium in 2026 before strengthening further through 2028 (Figure 1). National vacancy appears to be stabilizing and is projected to decline gradually as demand normalizes and the development pipeline contracts. Rather than signaling structural weakness, the recent slowdown represents a period of recalibration following an extraordinary expansion, leaving the market with comparatively little excess capacity as the next cycle unfolds.

Figure 1. U.S. industrial fundamentals



Source: CBRE-EA, Clarion Partners Global Research, 2025 Q4. Net absorption is based on quarterly change in occupied stock using vacancy rate. Orange line is LTA vacancy rate from 2002 to 2025. Forecasts have certain inherent limitations and are based on complex calculations and formulas that contain substantial subjectivity and should not be relied upon as being indicative of future performance.

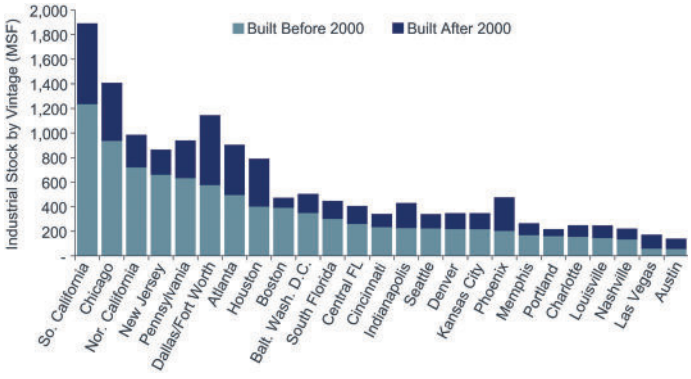
Early leasing activity among large-format distribution facilities provides further evidence that fundamentals are improving. Because big-box occupiers – including national retailers, ecommerce companies and third-party logistics providers – make expansion decisions based on long-term supply chain planning, they have historically served as leading indicators for broader market trends. These tenants were among the first to pause expansion during the slowdown and are now returning, which suggests that broader industrial demand is strengthening.

Improving net absorption, stable vacancy, and renewed activity among the industry's largest occupiers indicate that the industrial sector is entering the next phase of the cycle. As demand recovers against a backdrop of constrained new supply, market conditions are increasingly supportive of modern industrial development.

From expansion to replacement

While cyclical demand is beginning to recover, the need for new industrial development is increasingly being driven by a more durable structural trend: much of the nation's warehouse inventory was built for supply chains that no longer exist. Today's logistics networks require facilities capable of supporting greater throughput, automation, ecommerce fulfillment and sophisticated distribution operations, exposing the functional limitations of older industrial buildings and sustaining demand for modern logistics facilities.

Figure 2. Majority of U.S. industrial stock is functionally outdated

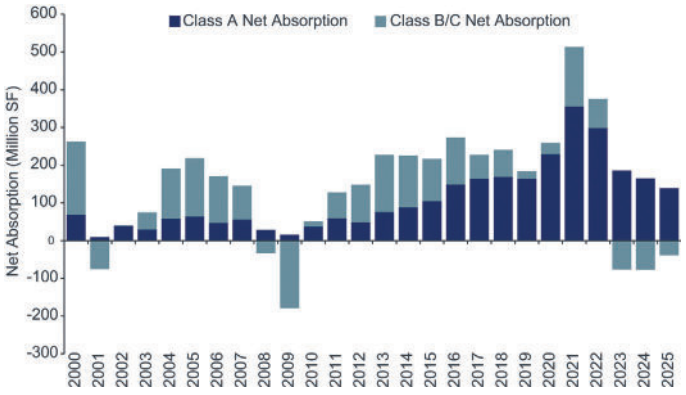


Source: CBRE-EA, Clarion Partners Global Research, 2026 Q1

Approximately 65 percent of U.S. industrial space was constructed before 2000, while nearly 88 percent predates 2010. Nearly 10 percent is approaching or exceeds 50 years in age (Figure 2). Following robust development cycles in the 1980s and 1990s, new construction slowed, leaving much of the existing stock misaligned with current occupier needs. Although many older facilities remain operational, they often lack the physical characteristics required to support today's supply chains, including higher clear heights, more efficient layouts, greater trailer capacity, enhanced power availability, and infrastructure designed for automation.

Tenant leasing decisions reflect this shift. Over the past three years, class B and class C warehouse space has experienced persistent negative net absorption, while demand for modern class A logistics facilities has remained positive, even during broader market slowdowns. Since 2010, class A properties have accounted for approximately 71 percent of warehouse net absorption, demonstrating the market's preference for newer, more functional space (Figure 3). Modern facilities have also delivered stronger operating performance, generating faster rent growth over the past decade and commanding an average rent premium of roughly 20 percent compared with older properties.

Figure 3. Tenants prioritize modern functionality, location and efficiency



Source: CBRE-EA, Clarion Partners Global Research, 2025 Q4. Based on Warehouse Product Type.

This growing divergence between modern and legacy inventory represents more than a cyclical leasing preference. It reflects a structural replacement cycle expected to support industrial development for years to come. Even if demand moderates, occupiers will continue upgrading into facilities that improve efficiency and support automation. As a result, future industrial demand is expected to come not only from economic growth, but also from the ongoing replacement of functionally obsolete warehouse stock.

COMPANY OVERVIEW

Clarion Partners has been a leading U.S. real estate investment manager for more than 40 years. Headquartered in New York City, the firm has offices in major markets throughout the United States and Europe. With more than $73 billion in total assets under management as of June. 30, 2026, Clarion Partners offers a broad range of both debt and equity real estate strategies across the risk-return spectrum to its approximately 500 domestic and international institutional investors. For more information, please visit **www.clarionpartners.com.**

CORPORATE CONTACT

Evans Anderson
Head of Americas Institutional Distribution
212-883-2500 | clarionpartners@clarionpartners.com

Supply will remain constrained

Although industrial construction can begin quickly, identifying sites, securing entitlements, arranging financing and delivering facilities is complex. Thus, today's development pipeline is likely to expand more slowly than in previous cycles, allowing market fundamentals to tighten even as demand improves.

Higher financing costs and tighter lending standards have increased development hurdles, while regulatory requirements, longer entitlement timelines and growing community opposition have made new projects more difficult. In many major logistics markets, industrial development now competes directly with residential projects, data centers and other higher-value land uses for a limited supply of well-located sites. Meanwhile, infrastructure limitations, including power availability, traffic mitigation requirements, and utility capacity, have further extended development timelines and increased project complexity.

These challenges are no longer isolated to a handful of markets. Municipalities across the country have adopted stricter development standards, imposed moratoriums, or become more selective in approving new industrial projects. Even historically pro-development markets such as Dallas–Fort Worth, Nashville and Atlanta have experienced growing resistance to industrial rezonings, while California's AB 98 legislation has introduced additional siting and design requirements for logistics facilities. Together, these trends suggest regulatory and political friction is now a structural feature of industrial development.

Economic considerations further reinforce these supply constraints. Although demand is improving, developers must underwrite projects based on expected rents at delivery rather than current market conditions. In many markets, replacement rents continue to exceed achievable in-place rents, limiting development feasibility despite strengthening fundamentals. As rents adjust and vacancy tightens, additional projects are likely to become economically viable, but this process typically unfolds over several years rather than quarters. Consequently, new supply is unlikely to respond immediately to recovering demand.

The next industrial expansion is likely to be characterized by measured, selective development rather than excessive new construction. Developers with entitled sites, strong balance sheets, and deep local expertise should be best positioned to capitalize on that environment.

Conclusion

As we look ahead, four key takeaways continue to support our outlook:

- Demand is recovering, led by big-box leasing.
- An aging warehouse stock is creating durable replacement demand.
- Supply remains structurally constrained by land, infrastructure, capital, and entitlements.
- Today's quieter market offers an attractive window to initiate well-located projects.

Industrial real estate is entering a new phase as demand recovers, aging warehouse stock drives replacement demand, and structural barriers limit new supply. For experienced, well-capitalized developers, today's quieter market offers an opportunity to deliver modern logistics facilities into the next tightening cycle.

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