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## **The focus on functionality in industrial real estate**

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If you have ever taken the time to think about how any single item you use in your daily life got into your house or in your hands you'd come to one conclusion; logistics is fascinating. Industrial real estate comes in all sizes and forms for a seemingly endless variety of users. There are light and heavy manufacturers, warehouses, distribution centers, cold storage, truck terminals, flex, assembly, fulfillment, and on and on. At an increased pace, older, less functional facilities are falling to the wayside as they no longer meet the demands of modern users. This holds true for both manufacturing and distribution space.

When analyzing industrial properties it is important to distinguish functionality as well as quality and location. When appraising an industrial building, what site, building and location characteristics do you use to quantitatively compare a set of buildings? Some basics you might look at are the ceiling heights; number of dock height and drive in doors; percentage of finished office space. However, a building with 100,000 s/f with 50 dock height doors does not necessarily justify an upward adjustment over the same building with 25 dock doors.

The end user of the space ultimately determines whether an existing building is functional or not. For example, the depth of a distribution center can be more impactful to an end user than the exact number of loading doors. Buildings with shallower depths are much more functional for businesses that are continuously moving inventory and do not expect product or materials to be sitting on the racks for more than a day or two. Conversely, deeper buildings can be more functional for users with products and materials with prolonged storage lives. It would seem reasonable that air conditioned warehouses would command a rent premium because they provide a level of comfort to employees and cooling for equipment. However, you need to dig a little deeper to find the fine print. Who is responsible for maintaining/replacing the air conditioning units the landlord or the tenant? The roof will surely have more penetrations from roof mounted units. If there is no demand in the market for users requiring air conditioned space your long term vacancy rate becomes uncertain and the rent/price premium for air conditioning may evaporate.

Thickness of the concrete slab can be another hot button issue for users. A building with a 5" slab may be functional in all other areas but not to a user whose equipment and storage weights require a 7" slab. Other important user-based issues include building power, trailer parking, truck court depth, car parking, the presence of a modern ESFR (Early Suppression Fast Response) sprinkler system and the capability for expansion should the need ever arise. When looking at ceiling heights, most modern distribution users require 30'+ clear heights.

Strategic location selection is becoming increasingly more important. E-Commerce is projected to grow by multiples of its current volume over the next few decades. Many E-Commerce suppliers rely heavily on ground transportation companies to get products to consumers at the fastest pace possible and in the most cost effective way. Consumers have become accustomed to two-day

shipping and in several major cities Amazon has successfully implemented game changing same day delivery processes. You can expect other players to follow suit as the demand for instant gratification from online consumers' increases with time. Therefore proximity to a major FedEx ground or UPS distribution center may be a critical deciding factor in selecting a site to develop or an existing building to lease. When dealing in larger distribution markets intermodal transportation has become a key issue. Drayage is the cost associated with transporting containerized cargo from a manufacturer, port, rail yard, or airport to a company's distribution center. The closer a distributor can locate to the ground transportation, the lower the cost of transporting goods. These drayage savings can be substantial enough to justify what would be considered an "above market" rent or sale price for a well located property.

It can be challenging to quantify the differences from building to building in terms of adjustments to lease rates and sale prices for location and physical characteristics. However, the more you understand the intricacies of the demands of the most likely end users in the market, the better equipped you will be in distinguishing between functionality in the market. Ultimately this leads to increased competency and confidence in defending your work and conclusions.

Scott Burns has been actively involved in the research, valuation and underwriting of commercial and industrial properties throughout the northeast for over 10 years.

New England Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540