Warehouse Construction Hot Spots for 2020

The e-commerce boom continues, with logistics providers struggling to keep up with tremendous demand, particularly for last-mile delivery. That will lead to more warehouse construction across the United States, but the growth will be concentrated in a few areas throughout 2020, most of them in urban centers.

This is a continuing trend. Warehouse vacancy kept declining in 2019, dipping to 4.4 percent in the first quarter of that year alone. That's remarkable, given that warehouse construction is rising at rates few in the industry have experienced before. Upwards of 250 million square feet of warehouse space were under construction in the first quarter of 2019, up 32 percent compared to Q1 2018.

It seems that the industry can't get enough new warehouses and distribution centers to meet the market's explosive demand. The big question, of course, is where the boom will land next.

What Do Warehouse Construction Hot Spots Have in Common for 2020?

The best predictor of a future construction boom is similarity to currently booming areas. We scanned through the top 10 markets for U.S. warehouse construction — all new constructions, all built on spec — tenant-driven construction is another set of statistics entirely — to see what they all had in common.

The similarities boil down to three things. These are the best indicators we've uncovered that a given market is likely to see a significant uptick in new warehouse construction over the opening months of 2020:

1. **Population density.** Much of the current growth in the warehousing space is driven by e-commerce, and last-mile delivery is the next hurdle for many online retailers. In order to compete on delivery times, retailers are looking for space in the closest possible proximity to the largest possible market.

   This is why 9 out of the 10 leading markets for warehouse construction in 2019 are significant urban centers. (The outlier — Pennsylvania's I-78/I-81 corridor — remains a major logistics artery for the East Coast.)

   Of course, population density alone doesn't paint a picture of the existing warehousing infrastructure in a given area. And the demand for urban last-mile distribution centers argues in favor of building smaller, mini-logistics outposts rather than the big box warehouses that power much of the industry's investment.

   These considerations lead to the other two major factors that currently booming markets have in common.

2. **The warehouse vacancy rate.** Major real estate providers like CBRE frequently publish warehouse vacancy rates for a variety of markets. This is a key statistic, because it tells builders where the unmet demand lies.

As of this writing, the latest reporting shows a national average warehouse vacancy rate of 4.4 percent. Using this figure as a baseline, if a given market's vacancy rate is *below* 4.4 percent, there is likely a higher-than-average demand for new warehouse space in that market. If the rate is *higher* than 4.4 percent, there may still be considerable unmet demand — but it's also likely to be lower than the national average.

3. **Growth trends in warehouse rental costs.** Typically, lower vacancy rates equate to higher annual rent growth for a given market. That stands to reason. Given the number of factors that influence an area's construction capacity, though, some markets see significantly higher rates of rent growth than others, regardless of vacancy rate.

   The rental price is another crucial indicator of unmet demand. Where rent is growing fastest, there may be an opportunity to compete on pricing. That could lead to more construction for warehouses.

   The national average annual rent growth for on-spec warehouse construction in the top 10 Q1 2019 markets was about 6.2 percent. Where rent growth is significantly higher than this, builders could take close interest.

We look to the present to predict future changes to the warehouse construction market. Note that many of the latest figures we could access as of this writing date from Q1 2019, creating a bit of a data gap.

For that reason, we intend this document to be more of a model than up-to-date analysis; however, given the lead time on construction in general, these figures are likely to remain relevant going into the opening of 2020. Where later figures were available, we have used them.

Leading Markets for Warehouse Construction In 2019

Through the third quarter of 2019, the latest period for which numbers are available at the time of this writing, the average rent price on industrial and logistics buildings (including warehouses) reached the highest it's been since real-estate company CBRE began tracking the statistic in 1989.

That figure — $7.57 per square foot in Q3 2019 — reflects the disparity between supply and demand for warehousing space. Analysts at Collier's International were already predicting a big year for urban warehousing through 2019 at the end of the previous year.

They weren't wrong. According to CBRE, these were the top 10 U.S. locations for warehouse construction on spec — these builders are confident they'll find renters upon completion — during the first quarter of 2019:

1. **Inland Empire, California.** In Q1 2019, 23.4 million square feet of new warehouse space was under construction, making Inland Empire the largest market for speculative warehouse building at the time. The overall vacancy rate for existing warehouses was just 3.2 percent in this market, and rent was growing at an annual rate of 9.4 percent.

2. **Atlanta, Georgia.** The greater Atlanta region saw 16.1 million square feet of warehouse construction in Q1 2018, with a 6.4 percent vacancy rate and annual rent growth of 7.9 percent.

3. **Dallas/Ft. Worth, Texas.** This North Texas hot spot was the third-largest market in the nation for speculative warehouse construction, with 15.2 million square feet added in Q1 2019, a vacancy rate of 5.9 percent, and an annual rent growth of 3.1 percent.

4. **Pennsylvania I-78/I-81 Corridor.** Interstates 78 and 81 in northeast Pennsylvania carve out a logistics corridor with quick, easy access to major New England cities and ports. Cities and towns like Hazleton, Wilkes-Barre, Pittston, and Scranton, PA, are home to millions of square feet of warehouse space. In 2018, the region netted 11 of the largest industrial leasing deals in the country, with 11,821,966 million square feet leased, largely to e-commerce companies.

   The PA I-78/I-81 corridor witnessed the fourth-largest growth in warehouse construction in Q1 2019. A total of 12.1 million square feet of space were under construction in the region; the vacancy rate was 6.7 percent and the annual rent growth was 4.9 percent.

5. **Houston, Texas**. The southeast Texas metropolis boasts an extraordinary population density (the fourth-highest in the nation). It's also home to the Port of Houston, a major international logistics hub.

   During CBRE's latest study period, the Houston area was home to 10 million square feet worth of warehouse construction, with a vacancy rate of 5.8 percent and annual rent growth of 4.1 percent.

6. **Chicago, Illinois.** The third-largest city in the U.S. in terms of population density, Chicago makes an ideal location for last-mile distribution centers. That demand places the city sixth on the CBRE list of largest warehouse-construction markets for 2019. In Q1, builders constructed 7.7 million square feet of new warehouse space. The vacancy rate was 6 percent, and the annual rent growth was a relatively low 2.9 percent.

7. **New York and New Jersey.** A market this large, with such population density, is a clear attraction for last-mile distribution centers. CBRE recorded 7 million square feet of warehouse space under construction during the study period. The vacancy rate for warehouse rental in New York and New Jersey was well below average, at 3.4 percent, but the annual growth in rental rates were just 4.8 percent.

8. **Seattle, Washington.** This northeast logistics hub was home to an impressive 6.1 million square feet of new warehouse construction during the study period. The vacancy rate was near average at 4.2 percent, as was the annual rent growth rate of 6.1 percent.

9. **Los Angeles, California.** This port city is the second largest market in the nation, in terms of population density. An extremely low vacancy rate of 1.4 percent during the study period will also make warehouse builders take another look at this region. Add to that the annual growth rate for rent on warehousing space — a whopping 8.5 percent — and this market seems poised for growth for a good while yet. In Q1 2019, 5.6 million square feet of warehouse space was under construction.

10. **Las Vegas, Nevada.** Rounding out the list we have the Las Vegas area, which had 5.5 million square feet of warehousing capacity under construction in Q1 2019. Interestingly, a very low vacancy rate of 2.4 percent and a very high annual rent growth of 10.2 percent make Las Vegas seem primed for even more warehouse construction in the coming months.

Note that the top 5 markets for industrial construction in Q4 2018 are all represented on this list, suggesting steady growth. (Those were, from top to bottom, Inland Empire, Dallas-Ft. Worth, Chicago, Atlanta, and Central New Jersey.)

Given some of the statistics, growth is likely to continue in these areas. And of the 10 top markets listed above, three stand out as meeting all three of our criteria for likely future growth: They have high population density, lower-than-average vacancy rates, and higher-than-average rates of annual rent growth. The top markets we'll be watching in 2020, then, are **Las Vegas**, **Los Angeles**, and **Inland Empire**.

Inland Empire saw more warehouse construction than any other market in Q1 2019; it is possible that current construction will fill the gap. Los Angeles and Las Vegas, on the other hand, were numbers 9 and 10 on the list, respectively, in terms of existing construction projects. That looks like an opportunity for warehouse builders.

One thing is for sure: Builders have not yet begun to worry about oversaturating the market. For now, and into 2020, warehouse construction is likely to continue its current boom.

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