4 reasons logistics real estate will dominate in 2018

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As we look to 2018, four themes have emerged in the logistics real estate market:

Greater pace and breadth of rent growth. Rent growth accelerated in 2017 with rents up 9% in the U.S. and nearly 3% in Europe. Clear differentiation emerged by market, by sub-market and by size category. Infill locations and dynamic economies with multiple demand drivers have performed best. At the same time, customers continue to outbid one another as rents remain low on an inflation adjusted basis and rents are a very low share of supply chain costs (5%) and total costs (<1%).

Historic low vacancies are making it hard for U.S. customers to expand. Close observers of the U.S. market know that demand growth (net absorption) slipped slightly in 2017 vs. 2016. At the same time, customers are on their front foot. Among many indicators of demand, the Prologis Industrial Business Indicator TM, has risen to near-record levels. Looking forward, capacity constraints should continue to limit demand as customers wait for new supply to come online.

Europe looking better and better. Demand and industry growth is strong; net absorption for modern facilities was 9M square meters in the top-50 markets during 2017, the highest on record. At work, despite its size, is that Europe remains an underserved market. Stock per capita is a third that of the U.S. Looking ahead, customer sentiment is still recovering, suggesting the long-term growth rate might be higher than previously thought. The European cycle is looking a lot like the U.S. back in 2014/2015.

Rising replacement costs changing the development landscape. This is one of the hardest trends to track in our industry; there's high variety by project requirements and locations. Looking through this noise, costs are rising by 5-10% annually and, in some cases, more as pricing for labor, land, materials and municipal fees all grow simultaneously. Looking forward, the accelerating global economic expansion should produce further growth in replacement costs. With more buildings more expensive than ever, new development will only be warranted by compensating increases in rental rates.

(By Chris Caton, Senior Vice President, Global Head of Research at Prologis)