

Record Customer Activity Intensifies Competition for Space



Prologis Northpark, Houston, Texas.

The Broad View

- Customer activity is setting records, with Prologis' IBI™ activity index rising from 59 in Q1 to 71 in Q2. These results indicate sustained robust activity as supply chains race to restock amid rapid consumer purchasing, in turn creating strong future demand. Logistics demand reached a record quarterly high of 110 million square feet (MSF) in the second quarter, bringing absorption for the first half of the year to an unprecedented 194 MSF, more than double from the same period last year.¹ Demand was broad-based across a range of customers, with urgency to secure space a major factor.
- Space utilization, which remained in the 84-85% range in the second quarter, reveals the challenges supply chains face keeping items in stock during a period of record retail sales growth.
- Record-level rent growth is also underway, as surging demand runs up against high barriers to new supply. Vacancies fell to 4.1% in the second quarter and rents rose by 4%, each a record.
- Prologis Research has revised our 2021 forecast upward for both demand and supply, to 360 MSF and 325 MSF respectively. Supply continues to rise but cannot keep pace with demand. Robust demand, increasing replacement costs and limited availabilities should push rent growth above 10% in 2021.

Exhibit 1

IBI ACTIVITY INDEX

Index, 50 = neutral, seasonally adjusted

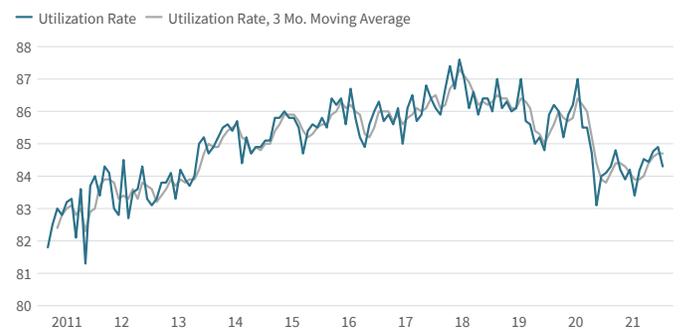


Source: Prologis Research.

Exhibit 2

UTILIZATION RATE

%



Source: Prologis Research.

The Details

- Record customer demand levels.** The IBI activity index has risen from the high 50s in the first quarter of 2021 to the low 70s in the second quarter—the highest on record. With the index above 66 in all meaningful customer sizes and regions, we see another key aspect: breadth. Further to that, consumer confidence and retail sales are strong. At the same time, the savings rate is higher than pre-pandemic levels, which could translate to sustained strong consumption for the foreseeable future and support ongoing high supply chain activity. The modality shift from in-store to online, where now more than 20% of all goods transactions occur, is driving demand, given the [3x higher intensity of use](#). U.S. net absorption was a record 110 MSF in 2Q'21.
- Average utilization levels point to more inventory growth ahead.** The IBI utilization rate was 84.7% in the second quarter, below pre-pandemic levels. TEUs are up 50% year-over-year and are up 25% from pre-pandemic levels as retailers replenish their supply chains.² While inventories have increased 3% from their low, they have struggled to catch up as retail sales are 19% above pre-pandemic levels.³ As a result, retailer inventory-to-sales ratios are at historic low levels (1.09 in June), limiting space utilization.⁴ Looking forward, target inventory-to-sales ratios will likely be higher in a bid for resilience, pushing up utilization rates and supporting logistics demand as supply chains boost inventories.
- Rents are rising at a record pace.** E-commerce demand remains strong with a notable pickup in apparel, yet demand is spread across many industries. Although demand for bulk space (more than 100,000 SF) is leading the pack, smaller spaces are becoming more attractive to logistics customers as the economy recovers. In fact, customers are moving faster than ever, competing for space and placing a premium on quickly securing prime logistics space. The vacancy rate fell by 40 bps from the prior quarter to 4.1%. Rents increased across the board, with growth highly concentrated in bulk markets with shrinking opportunities for development and coastal higher-barrier markets. Rent growth accelerated to 4% quarter-over-quarter and is up 10% in the past year. Top rent growth markets include Southern California, New York/ New Jersey and Pennsylvania.
- Supply is struggling to keep pace with rapid demand.** Given record demand, developers are working hard to monetize entitled land. Starts continued to grow, fueled by record rental rates and asset value growth, yet they do not appear significant enough to weigh on rental rate levels and growth. As a sign of the strength of demand, pre-leasing of the pipeline reached a record high of more than 60%.⁵ In addition, supply growth has largely been fueled by regional, small and lower-barriers-to-supply markets, with starts in larger inland markets focused in outlying submarkets. More

Exhibit 3

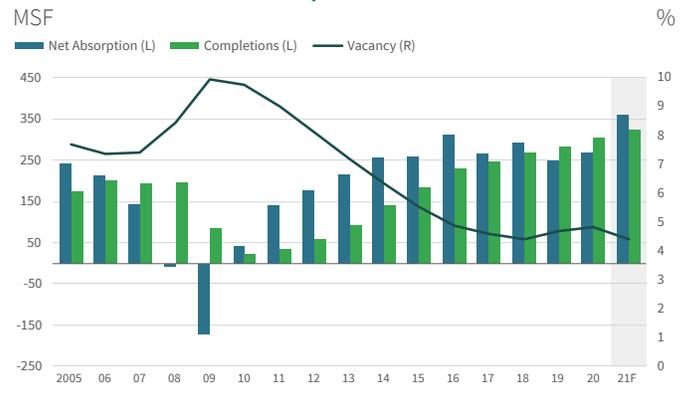
SUMMARY OF NET ABSORPTION INDICATORS

	LATEST READING	AS OF	EST. NET ABSORPTION, MSF		REGRESSION FIT (R-SQR)
			Quarterly	Annualized	
IBI-Activity	69.3	Jun 2021	109	434	0.80
Weighted Average of Econ Variables			106	422	
PMI (non-mfg)	62.3	Jun 2021	114	458	0.69
Jobs (private)	468	Jun 2021	96	384	0.55
Core Retail Sales	20.0%	Jun 2021	138	554	0.58
Inventories	-92.0	1Q 2021	70	280	0.56

Note: Values are a 3-month trailing average, except inventories. Source: Institute for Supply Management, Bureau of Economic Analysis, U.S. Census, Bureau of Labor Statistics, Prologis Research.

Exhibit 4

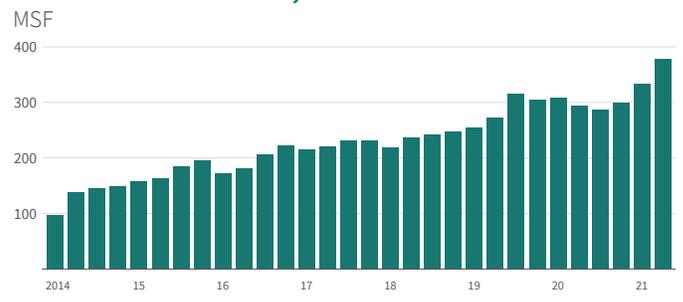
MARKET FUNDAMENTALS, U.S.



Source: CBRE, JLL, Cushman & Wakefield, Colliers, CBRE-EA, Prologis Research.

Exhibit 5

UNDER CONSTRUCTION, U.S. INDUSTRIAL



Source: CBRE, JLL, Cushman & Wakefield, Colliers, CBRE-EA, Prologis Research.

significantly, construction cost growth has also been a record alongside disruptions in the availability of materials and extended delivery times.⁶ For the first time in more than five years in the U.S., we see no markets where supply appears to be a threat to local vacancies or rents.

- **We expect tight market conditions to persist through 2022 and likely beyond.** Prologis Research forecasts 325 MSF of completions in 2021. Broad-based demand will drive robust absorption in both newer, larger spaces upstream of supply chains and smaller infill units near the consumption end of supply chains. Therefore, we expect 360 MSF of net absorption in 2021. With demand outpacing supply, the vacancy rate will end the year at 4.4%. Limited availabilities, rising replacement costs, and extreme competition should drive up rents broadly through the remainder of the year. Prologis Research forecasts that full-year net effective market rent growth will set a record, exceeding 10%. For customers looking to expand, the need for advance planning and speedy execution is paramount.

Endnotes

1. CBRE, JLL, Cushman & Wakefield, Colliers, CBRE-EA, Prologis Research
2. Port of Long Beach, Port of Los Angeles, Port of Oakland, Georgia Ports (Savannah), Port Authority NY/NJ, Maryland Open Data Portal (Baltimore), South Carolina Ports (Charleston), Port of Houston, Port of Virginia, U.S. Department of Transportation (Laredo), Port of Vancouver, The Northwest Seaport Alliance (Seattle/Tacoma)
3. U.S. Bureau of Economic Analysis, Census
4. Census
5. JLL
6. Prologis Research

Forward-Looking Statements

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Prologis' Research department studies fundamental and investment trends and Prologis' customers' needs to assist in identifying opportunities and avoiding risk across four continents. The team contributes to investment decisions and long-term strategic initiatives, in addition to publishing white papers and other research reports. Prologis publishes research on the market dynamics impacting Prologis' customers' businesses, including global supply chain issues and developments in the logistics and real estate industries. Prologis' dedicated research team works collaboratively with all company departments to help guide Prologis' market entry, expansion, acquisition and development strategies.

About Prologis

Prologis, Inc. is the global leader in logistics real estate with a focus on high-barrier, high-growth markets. As of June 30, 2021, the company owned or had investments in, on a wholly owned basis or through co-investment ventures, properties and development projects expected to total approximately 995 million square feet (92 million square meters) in 19 countries.

Prologis leases modern logistics facilities to a diverse base of approximately 5,500 customers principally across two major categories: business-to-business and retail/online fulfillment.

Prologis
Pier 1, Bay 1
San Francisco, CA 94111
United States
+1 415 394 9000
www.prologis.com

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