

INDUSTRIAL INDEX

INDUSTRIAL RETURNS TURN NEGATIVE FOR THE FIRST QUARTER SINCE THE GLOBAL FINANCIAL CRISIS

Despite strong operating fundamentals and overall demand, the U.S. industrial sector total quarterly return experienced its first decline since the 4th quarter of 2009 primarily due to an increase in cap rates. While industrial NOI growth steadily increased as occupancy continued to climb higher over the quarter, a decrease in transaction volume and widespread dislocation in financing markets were the primary contributors to the sizable cap rate expansion.

The U.S. economy grew increasingly more uncertain amid dislocation of debt markets and higher inflation which experienced a 40 year high in 2022. To combat the high inflation, the Federal Reserve increased the Federal Funds Rate by 425 bps in 2022 with 125 bps of increases in the fourth quarter. Today, the Federal Funds Rate target range is 4.50% to 4.75% following an additional 25 bps increase in early February 2023. The high interest rate environment along with the 10-year treasury rate yielding its highest returns since 2008 have led to increases in cap rates resulting in decreases in real estate valuations.

Fourth quarter industrial returns totaled -3.56% with a significant -4.32% in appreciation return. All regions of the U.S. experienced a negative total return during the quarter with the steepest declines being realized in the Midwest and East regions which had a total return of -4.21% and -3.96% respectively. Industrial was the second worst performing sector of the NCREIF Property Index during the fourth quarter, trailing apartments (-3.21%), retail (-1.61%) and hotels (3.37%) and only outperforming the office sector (-4.80%).

Although the sector ended the year with a negative fourth quarter return, industrial performed well throughout 2022. The one-year return for industrial in the NCREIF Property Index was 14.55% with income returns of 3.18%. In comparison, the annualized total return for industrial properties since the inception of the NCREIF Property Index is 10.75% with income returns of 7.35%. Industrial was the strongest performing sector of the NCREIF Property Index in 2022. Industrial has also been the best performing sector in the NCREIF Property Index over the three-year, five-year, ten-year and since inception periods ending December 31, 2022.

The overall outlook for industrial real estate in 2023 is mixed. The possibility of a recession may cause a pullback in e-commerce demand, however continued demand from easing supply chains and onshoring are still bright spots for the sector. Well-located industrial assets with the ability to serve a large population of end users will be better positioned as the lack of entitled land and increases in development costs will cause a barrier to entry. We believe that last-mile logistics and other infill industrial assets will continue to see strong NOI growth and have higher returns in comparison to the broader industrial sector. Overall, we believe that industrial fundamentals will continue to remain steady and the sector will outperform the total NCREIF Property Index over the medium and long term.

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INDUSTRIAL TOTAL RETURNS

	Total NPI	Total Industrial	East	Midwest	South	West
4th Q 2022	-3.50	-3.56	-3.96	-4.21	-3.28	-3.38
3rd Q 2022	0.57	1.11	0.84	0.85	0.98	1.34
One Year	5.53	14.55	11.61	7.48	12.38	18.18
Three Years	8.06	22.43	22.64	13.78	18.74	25.91
Five Years	7.46	18.92	19.37	12.03	16.11	21.53
Ten Years	8.82	16.02	15.77	11.67	14.12	17.94
Twenty Years	8.63	11.80	11.50	8.59	10.41	13.40

INDUSTRIAL INCOME RETURNS

	Total NPI	Total Industrial	East	Midwest	South	West
4th Q 2022	0.95	0.76	0.76	1.05	0.87	0.67
3rd Q 2022	0.93	0.76	0.75	1.01	0.87	0.67
One Year	3.90	3.18	3.14	4.18	3.66	2.81
Three Years	4.11	3.93	3.96	4.69	4.34	3.59
Five Years	4.28	4.27	4.33	4.98	4.68	3.92
Ten Years	4.68	4.90	5.12	5.50	5.34	4.49
Twenty Years	5.54	5.91	6.16	6.39	6.22	5.54

INDUSTRIAL APPRECIATION RETURNS

	Total NPI	Total Industrial	East	Midwest	South	West
4th Q 2022	-4.45	-4.32	-4.72	-5.27	-4.15	-4.05
3rd Q 2022	-0.37	0.35	0.09	-0.17	0.11	0.67
One Year	1.58	11.12	8.28	3.20	8.49	15.07
Three Years	3.83	17.98	18.15	8.79	13.96	21.75
Five Years	3.08	14.19	14.58	6.79	11.04	17.11
Ten Years	3.99	10.72	10.25	5.93	8.44	13.01
Twenty Years	2.97	5.63	5.09	2.10	4.00	7.53

INDUSTRIAL INDEX—QUARTILE RANGE OF RETURNS

