

# I-81/78 CORRIDOR - PA INDUSTRIAL MARKET

## NATIONAL RETAIL TROUBLES HAVE RAMIFICATIONS IN THE REGIONAL MARKET

It was inevitable: the decade-long streak of positive absorption in the I-81/78 industrial market was finally interrupted in the second quarter of 2019. 1.1 MSF of negative absorption was tallied, and 2.1 MSF of new speculative inventory delivered without a tenant lined up, causing vacancy to pop from 6.3% to 7.1% quarter over quarter, its highest measure in three years. Although this quarter's performance stands in sharp contrast to years of occupancy growth, the fundamental strength of the market remains intact. The negative absorption is clearly a consequence of the primary driver behind the market's growth, the evolving dynamic between logistics and retail, led by structural shifts in consumer e-commerce adoption. National retailers Sears and Kmart, struggling in the aftermath of bankruptcy, closed multiple warehousing operations this quarter in Central and Northeastern PA, returning more than 1.6 MSF to the market. The typical net-absorption needle-movers, major big-box warehouse move-ins, were muted this quarter and new occupancy came predominantly from third-party logistics and e-commerce firms in smaller size segments - not enough to eclipse the significant downsizing by Kmart and Sears.

Record-breaking development totals were reported this quarter, with 18.6 MSF of industrial product currently under construction, the highest quarterly level ever recorded. Next quarter is tracking to see significant net absorption with major big-box occupancies slated to occur (Lowe's and QVC among them). The second half of the year will certainly end on a positive note - but this quarter proved that supply and demand dynamics have reached a parity, and we predict more frequent quarterly fluctuations in demand performance.

### CENTRAL PENNSYLVANIA

The I-81/78 Corridor's largest submarket was responsible for the lion's share of negative absorption this quarter; two of the aforementioned three large Sears and Kmart warehousing facilities were located within the region. While that downsizing eclipsed overall occupancy growth, there were still numerous significant move-ins this quarter, demonstrating healthy demand, especially in the under-500,000-square-foot segment. Among the quarter's new occupancies, Boxzooka Fulfillment took the 133,800-square-foot warehouse at 300 Capital Lane, and Dayton Parts occupied 320,000 square feet at 485 Saint John's

## CURRENT CONDITIONS

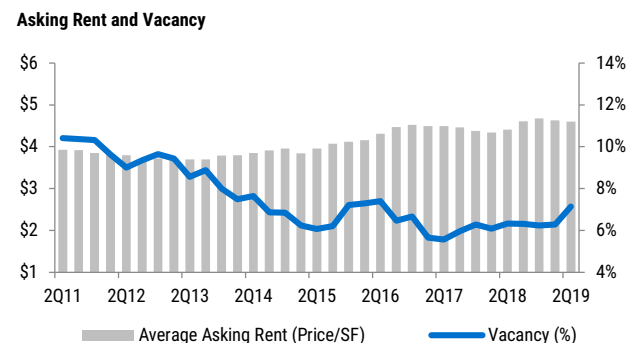
Closures by struggling national retailers Kmart and Sears contributed to the first quarter of negative absorption the market has seen since 2009.

The development pipeline continues to expand to record-breaking levels: 18.6 MSF was under construction in 2Q19.

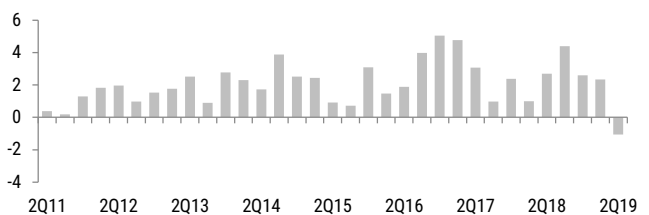
Vacancy rose from 6.3% to 7.1% quarter over quarter, but is expected to taper in the second half of the year due to large scheduled occupancies.

## MARKET ANALYSIS

### Asking Rent and Vacancy



### Net Absorption (SF, Millions)



## MARKET SUMMARY

	Current Quarter	Prior Quarter	Year Ago Period	12 Month Forecast
Total Inventory	349 MSF	347 MSF	337 MSF	↑
Vacancy Rate	7.1%	6.3%	6.3%	↓
Quarterly Net Absorption	-1.1 MSF	2.3 MSF	2.7 MSF	↑
Average Asking Rent	\$4.60	\$4.63	\$4.41	↑
Under Construction	18.6 MSF	15.2 MSF	8.5 MSF	↓
Deliveries	2.1 MSF	1.0 MSF	3.7 MSF	↑

Church Road. This size segment has been somewhat overlooked in the development boom. Approximately 15.0 MSF delivered in the submarket since 2017 and over 85% of the space has been in warehouses with less than 500,000 square feet. New groundbreakings this quarter indicated developers are turning more towards the underserved size segments: construction began on a 148,500-square-foot warehouse at 165 Shady Lane and a 374,125-square-foot warehouse at 350 North Lingle Avenue, the latter of which is a build-to-suit for General Mills in an expansion of the company's existing footprint in the East Point Trade Center. Overall, 5.6 MSF of new development was in the pipeline by quarter-end.

### Lehigh Valley

The Lehigh Valley was the only submarket this quarter to tally positive absorption, accumulating 337,211 square feet of new tenancy. Among the largest move-ins this quarter were Geodis (224,000 square feet at 651 Boulder Drive) and ShipBob (123,140 square feet at 4779 Hanoverville Road). Vacancy in the submarket nonetheless rose 50 basis points from the previous quarter to 6.2% on the heels of two warehouses delivering vacant. Despite this increase, the Valley remained the tightest submarket of the Corridor, a full 1.3 percentage points lower than the other two. The submarket also maintained its standing as the development epicenter for the Corridor with more than 6.5 MSF underway. Ground broke on six new warehouses in the past three months, all under 500,000 square feet, and there will be further groundbreakings next quarter. In addition to 20+ proposed warehouse developments already in the works, Black Creek Group announced plans this quarter to construct three buildings totaling nearly 1.0 MSF in

South Whitehall Township. Although this may seem like a lot in the proposed pipeline, the supply of viable industrial development sites has been depleted by the years-long warehouse expansion, and there is increasing strain on the labor supply. Lehigh Valley's development pipeline will remain elevated through 2019, but these two factors will likely reduce new groundbreakings in 2020.

### Northeastern Pennsylvania

Developers finding less opportunities for viable new construction sites in the Lehigh Valley have begun a real push into Northeastern Pennsylvania where land – and labor- is still plentiful. The significant jump in development in the second quarter made this trend apparent as the pipeline nearly doubled, from 3.5 to 6.5 MSF, the highest quarterly construction total on record for the submarket. Construction began on three new warehouses, one of which, the 510,510-square-foot 198 Commercial Boulevard, has already been leased by a medical equipment supplier.

The submarket lost 302,166 square feet in tenancy in the second quarter due almost entirely to the Sears warehouse closure at 1070 Hanover Road, pushing vacancy up 50 basis points from the first quarter to 7.5%. Looking forward, large planned occupancies such as NFI's move into a 1.1 MSF warehouse in Tobyhanna currently under construction will ensure the submarket ends the latter half of the year on a positive note.

## LEASE/USER TRANSACTIONS

Tenant	Building	Submarket	Type	Square Feet
Ferrero USA	112 Bordnersville Road	Central Pennsylvania	Direct	738,720
Confidential Medical Equipment Supplier	198 Commercial Boulevard	Northeastern PA	Direct	510,510
Distribution Management	1495 Dennison Circle	Central Pennsylvania	Direct	419,344
Overstock.com	100 Louis Parkway	Central Pennsylvania	Renewal	400,596
General Mills	350 North Lingle Avenue	Central Pennsylvania	Direct	374,125

## SELECT SALES TRANSACTIONS

Building	Submarket	Sale Price	Price/SF	Square Feet
555 Nestle Way	Lehigh Valley	\$111,600,000 (allocated)	\$107/SF	1,045,153
3262 Schoeneck Road	Lehigh Valley	\$4,400,000	\$339/SF	12,970
90 E Market Street	Northeastern PA	\$2,900,000	\$48/SF	61,081
8 Barnhart Drive	Central PA	\$2,275,000	\$39/SF	70,000

**SUBMARKET STATISTICS**

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Absorption (SF)	YTD Absorption (SF)	W/D Asking Rent (Price/SF)	R&D/Flex Asking Rent (Price/SF)	Total Asking Rent (Price/SF)
Central PA	178,485,061	5,606,903	7.5 %	-1,085,803	1,145,008	\$4.58	\$8.23	\$4.63
Lehigh Valley	100,775,542	6,537,074	6.2 %	337,211	556,844	\$5.45	\$7.47	\$5.50
Northeastern PA	69,561,833	6,489,934	7.5 %	-302,166	-408,661	\$4.05	\$8.50	\$3.86
<b>Market Total</b>	<b>348,822,436</b>	<b>18,633,911</b>	<b>7.1 %</b>	<b>-1,050,758</b>	<b>1,293,191</b>	<b>\$4.55</b>	<b>\$7.95</b>	<b>\$4.60</b>

**SUBMARKET STATISTICS BY SUBTYPE**

	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	Qtr Absorption (SF)	YTD Absorption (SF)	Total Asking Rent (Price/SF)
Warehouse/Distribution	234,599,770	17,656,911	8.5 %	-1,154,873	977,361	\$4.55
R&D/Flex	11,651,021	-	7.4 %	-20,387	11,288	\$7.95
General Industrial	102,571,645	977,000	3.9 %	124,502	304,542	\$4.14
<b>Total</b>	<b>348,822,436</b>	<b>18,633,911</b>	<b>7.1 %</b>	<b>-1,050,758</b>	<b>1,293,191</b>	<b>\$4.55</b>

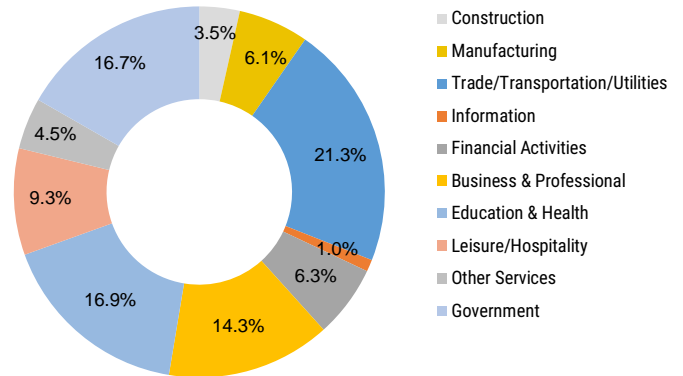
## ECONOMY

The unemployment rate for the Harrisburg-Carlisle area tightened to 2.7% (not seasonally adjusted) in the second quarter of 2019, the lowest measure recorded in at least a decade and indicative of the challenging landscape for employers seeking quality talent across industries. Yet, the trade, transportation and utilities super-sector continued to expand in a healthy fashion, growing by approximately 1,700 jobs year-over-year with no signs of significant deceleration. This poses good news to warehouse occupiers considering labor issues, particularly in the Central Pennsylvania submarket, which is anchored by the Harrisburg-Carlisle metro area.

On the national level, much ink has been spilled on the topic of tariffs but there's yet to be significant impact seen in consumer spending habits. According to the National Retail Federation, national retail sales were up 3.2% year over year in May, and e-commerce growth was up 11.3%. As e-commerce continues to gain market share, more warehouse space will be necessary to house and distribute material purchased online.

## METRO EMPLOYMENT BY INDUSTRY

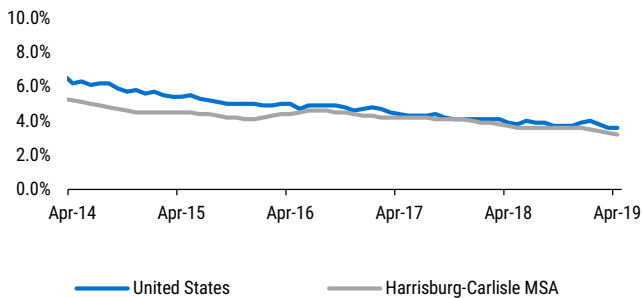
Harrisburg-Carlisle MSA, Annual Average 2018



Source: U.S. Bureau of Labor Statistics

## UNEMPLOYMENT RATE

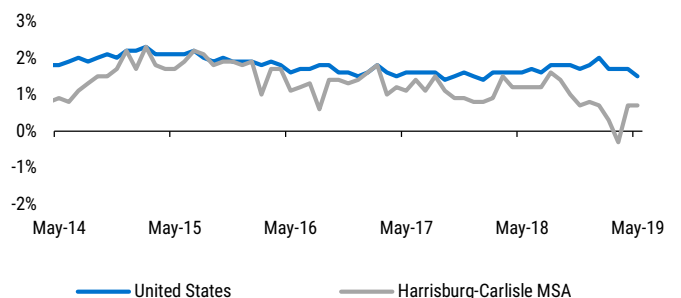
Seasonally Adjusted



Source: U.S. Dept. of Labor, Philadelphia Federal Reserve

## PAYROLL EMPLOYMENT

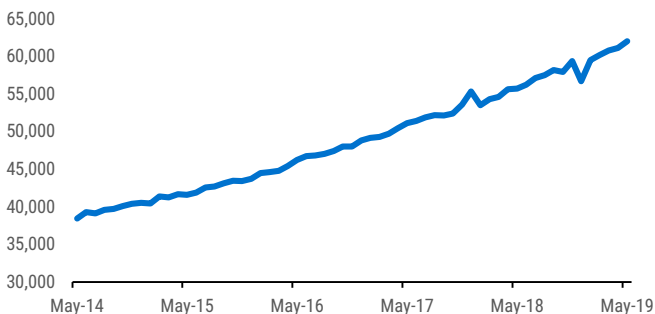
Total Nonfarm, Not Seasonally Adjusted, 12-Month % Change



Source: U.S. Bureau of Labor Statistics

## National E-Commerce Sales

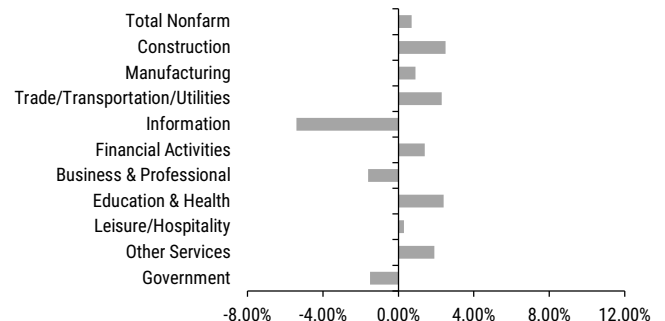
\$ Millions, Seasonally Adjusted



Source: U.S. Census Bureau, National Retail Federation

## EMPLOYMENT GROWTH BY INDUSTRY

Harrisburg-Carlisle MSA, May 2019, 12-Month % Change



Source: U.S. Bureau of Labor Statistics

