Brookfield

Logistics: Resilient Demand Creates Room for Sustainable Growth

Logistics: A Vital Real Estate Sector

The logistics sector is composed of real estate that enables one of the most fundamental elements of our economy—the transportation of goods and services. Logistics real estate allows companies to store and move goods across the globe and is directly tied to changes in supply and demand fundamentals of consumers. It includes warehouses, distribution centers, fulfillment and micro-fulfillment centers, cross-docking facilities, cold storage facilities, as well as flexible spaces and other industrial buildings with storage facilities (**Figure 1**). The positioning of logistics properties is vitally important. They need to be close to key transportation hubs including airports, seaports and highways, and most importantly, they must consider the distance to the end consumer.

Figure 1: Types of Logistics Real Estate

Warehouses
Large buildings used for storing goods typically located near transportation centers

Distribution centers
Warehouses used for sorting, packaging and shipping goods in order to distribute goods to retailers and consumers

Fulfillment centers
Smaller warehouses used for picking, packing and shipping goods to consumers located near major metro centers and are favored by e-commerce

Micro-fulfillment centers
Compact and strategically placed warehouses in urban areas, situated near large populations, optimized to provide fast delivery often within 24 hours (same-day delivery)

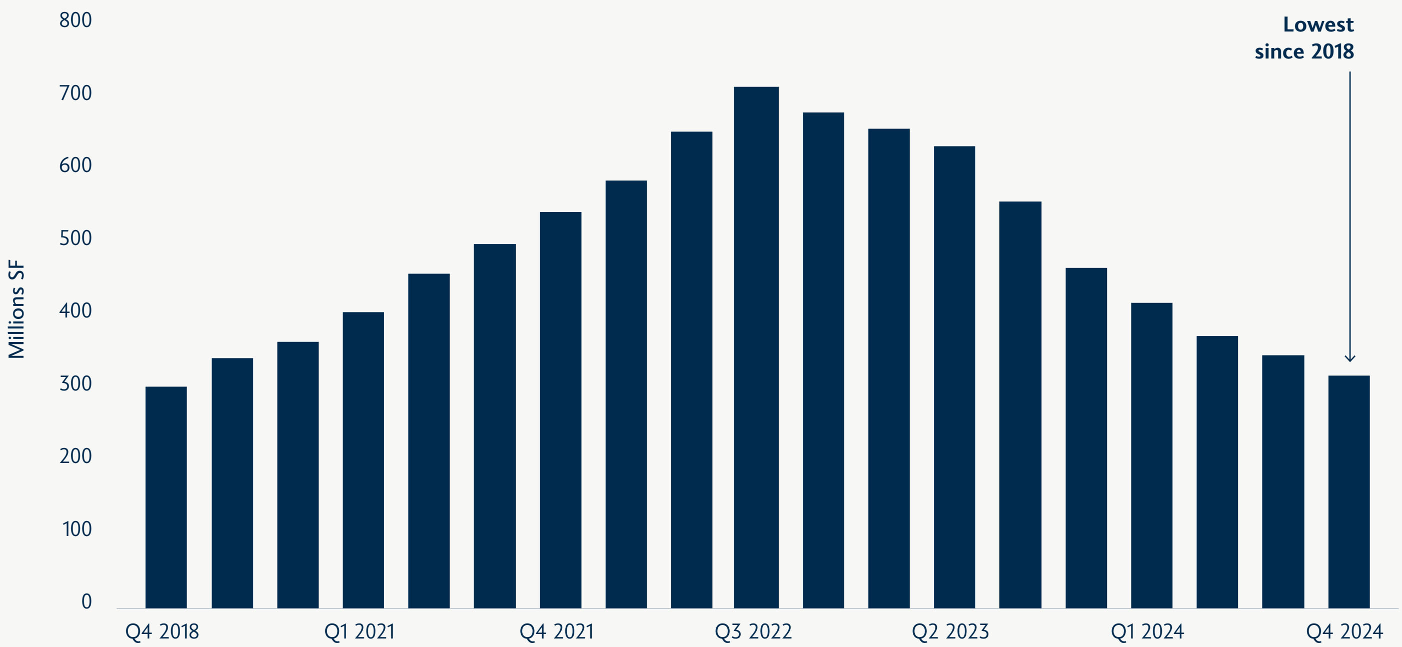
High-Flow-Through facilities
Critical nodes to facilitate the rapid movement of goods through the supply chain, includes truck terminals, transload, IOS, and cross-docking assets

Cold storage facilities
Warehouses used for refrigeration of temperature-sensitive products including food and pharmaceuticals

Current State of the Logistics Market

Global economic conditions and changing consumer preferences have a direct influence on the logistics sector. In recent years, the industry was forced to meet a rising demand in e-commerce, which accelerated due to shifting consumer preferences as a result of the COVID-19 Pandemic. As demand outstripped supply in the U.S., new construction in the sector more than doubled from 2018 to 2022 (**Figure 2**).

Figure 2: Logistics Construction Starts (Square Feet in Millions)



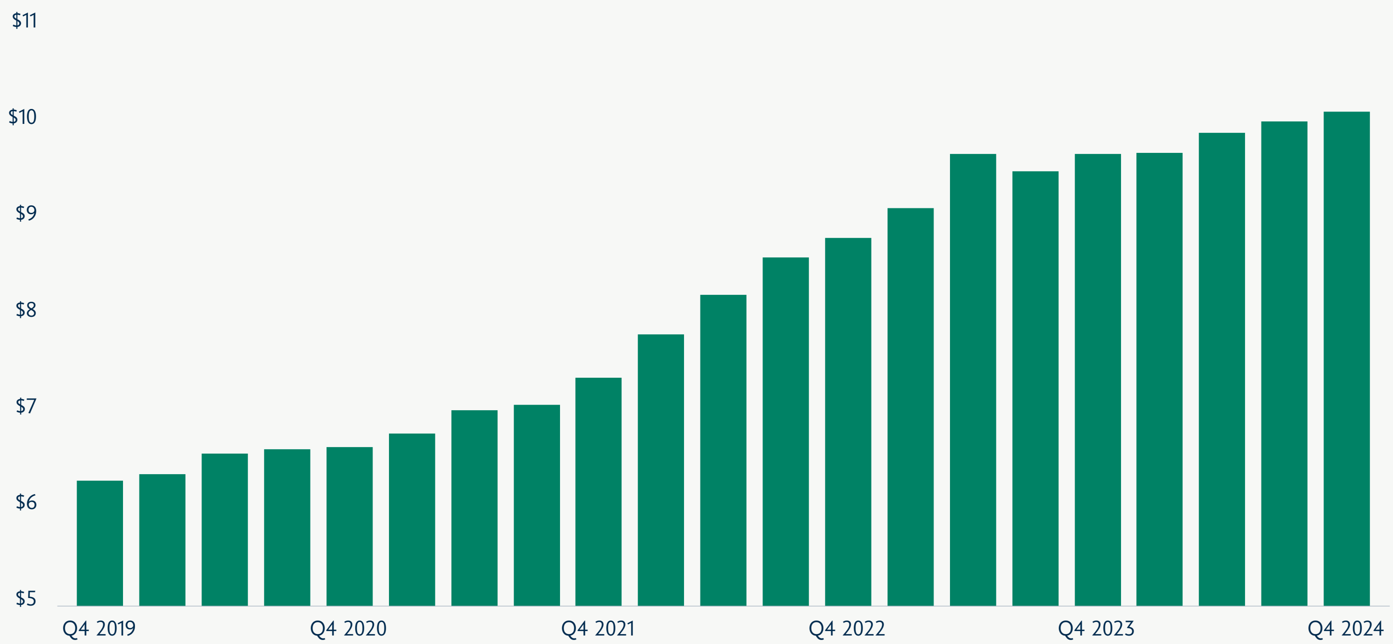
Source: CoStar, as of Q4 2024.

Competition for space slowed from 2022 through 2024, as supply chains and consumer demand normalized and tenants worked through the space they absorbed during the Pandemic. The average warehouse vacancy rate in the U.S. increased to 6.0% at the end of 2024, which is double the level at the end of 2022.[1] In the face of slowing demand coupled with higher interest rates and lower financing liquidity, new construction starts declined dramatically in late 2023 and throughout 2024. As a result, new construction levels at year-end 2024 returned to their lowest point since 2018 (**Figure 2**). Given the approximately 18-24 months development cycle for industrial product, the implication of this construction hiatus is a scarcity of new supply delivering in the next two years.

With typical lease terms of a minimum three to five years, many leases that were signed during the frenzied pace of the Pandemic era are set to expire during the next two years. And because availability was so low during the Pandemic, many tenants were forced to take space that was not ideal for their operations. As these leases expire, tenants are expressing a more measured approach, evaluating their space needs and exhibiting a preference for new construction, which offers more modern building specifications such as higher clear heights for more cubic storage, wider column spacing and better truck circulation, all which enhance their operational efficiencies and provide the opportunity to utilize automation or robotics.

Currently, a fundamental factor is proving advantageous for rental growth and expected to continue over the next few years—the broader market for warehouse space remains extremely tight by historical standards, with availability still far below pre-pandemic levels. The lack of new supply has created a floor for rents in the space, with pricing for new rentals remaining at or near the premiums that lessors were able to demand during the height of the pandemic. Across the U.S., warehouse rents rose to $10.13 per square foot at the end of 2024, up 4.5% from a year earlier and 61% from the fourth quarter of 2019 (**Figure 3**). As leases continue to come up for renewal, owners are benefiting from increased pricing power as they bring rents in line with current market rates.

Figure 3: Average U.S. Warehouse Asking Rent Per Square Foot



Source: Wall Street Journal, Cushman & Wakefield, January 2025.

Preferences for Functional Spaces

In addition to the lack of new construction driving demand, companies are exhibiting a strong preference for newer supply. Last year, companies exhibited a noticeable flight to quality, as older buildings constructed before 2000 accounted for more than 100 million square feet of negative absorption in 2024, while new buildings completed after 2022 demonstrated 200 million square feet of positive absorption. Demand for new facilities with modern specifications are becoming more prevalent as they create efficiencies and allow for automations and robotics to complete tasks such as picking, packing and sorting goods.

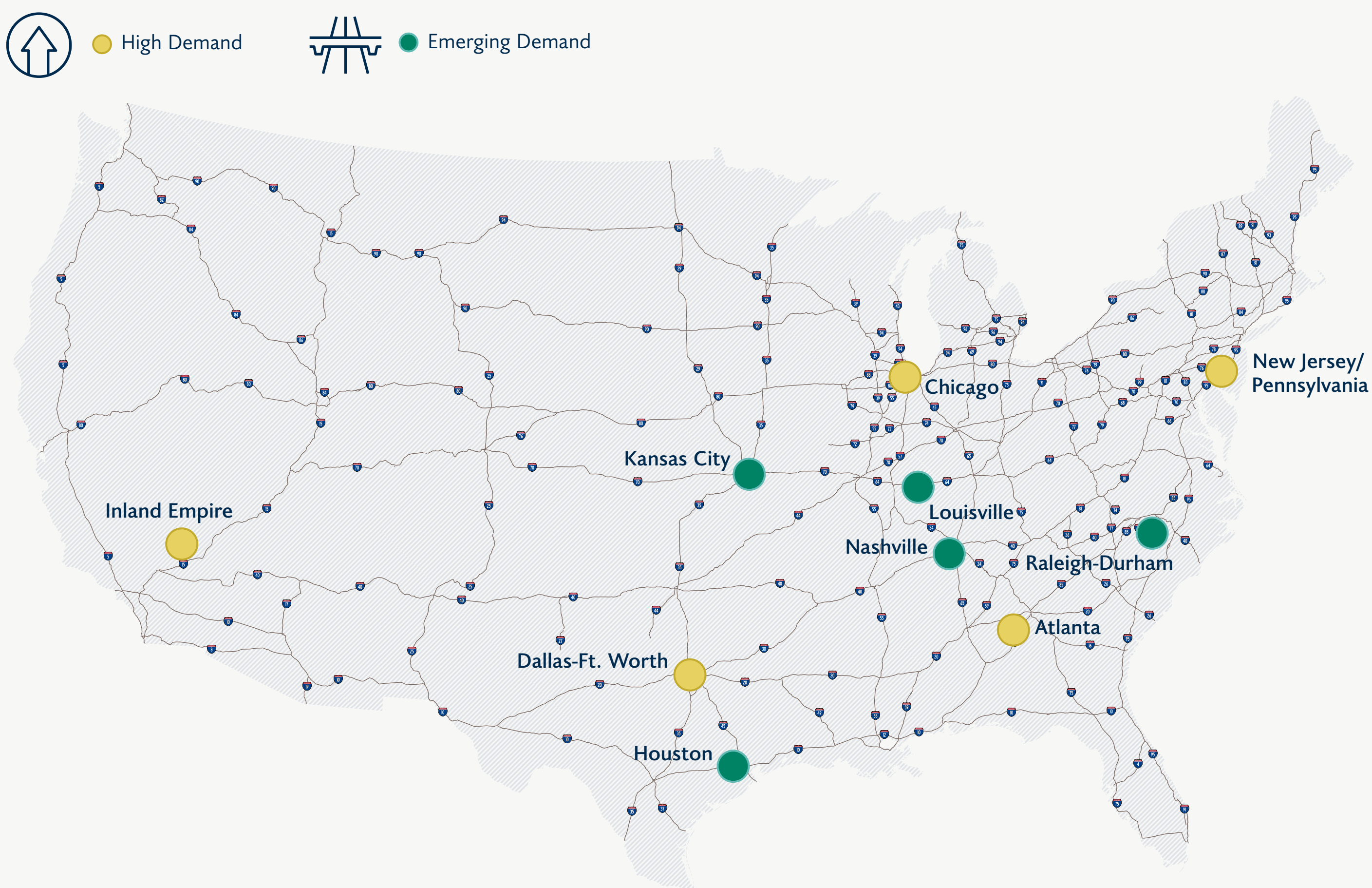
On a global scale, the quality of logistics infrastructure in many large, industrialized countries has not caught up with modern standards, creating compelling investment opportunities to renovate and increase rental revenue or build new institutional quality facilities. One example is Japan, where 54% of the logistics stock was constructed over 30 years ago and only 16% was developed within the last 10 years.[2]

The demand for newer, modern warehouses is also providing investment prospects for opportunistic real estate investors, as older buildings remain vacant and owners become motivated sellers. In addition, many owners of older buildings have challenged capital structures due to the recent capital markets stress resulting from a higher interest rate environment. These owners may not be willing or able to put up the needed capital to renovate. Refitting older buildings to bring them up to current standards, particularly in high-demand infill locations, presents an attractive real estate investment opportunity.

Location and Size: Key Drivers of Asset Performance

A prime location is often an important factor in the functionality of a logistics property, as it may contribute to the long-term success of the underlying business it supports. Markets like Dallas-Ft. Worth, Atlanta, Chicago, the Inland Empire, and the New Jersey/Pennsylvania region typically enjoy a steady stream of demand driven by healthy consumer populations and nearby transportation hubs (**Figure 4**). Emerging industrial markets that service manufacturing in both the U.S. and Mexico, such as Houston, Kansas City, Louisville, Nashville and Raleigh-Durham, are likely to provide opportunities to expand logistics development as onshoring of manufacturing to North America continues to gain traction. Potential U.S. tariffs may come into play on the sector as the new administration shapes their policies on products coming from Asia and Europe, and new location hubs may emerge. For example, a warehouse along main interstate highways may become as critical to a company's infrastructure as those at a seaport location.

Figure 4: U.S. Logistics Markets in Demand



When it comes to logistics real estate, location is a primary driver of performance, but size can also dictate the profitability of an asset. Smaller warehouses, which can often demand higher rents per square foot due to their tendency to be in central, urban and suburban infill locations, are currently in high demand from tenants. These properties are favored by companies looking to spread inventory across multiple warehouses closer to customers, speed up delivery and cut shipping costs rather than using one big, central building. The vacancy rate for U.S. warehouses under 100,000 square feet was 3.9% in the fourth quarter, well below the 6.7% overall vacancy rate for the sector (**Figure 5**). The lack of new supply in this category has been exacerbated by the higher cost per square foot and longer stabilization timing for light industrial multi-tenant buildings. Developers have been focused on constructing larger big box buildings to meet the demand from e-commerce and large distribution centers (**Figure 6**). Because the older vintage assets are often in the best locations within urban markets with limited space and costly land, many of these assets offer the potential for renovation to modernize and bring to an institutional standard and attract a higher quality tenant base.

Figure 5: Vacancy Rate by Size/Square Feet

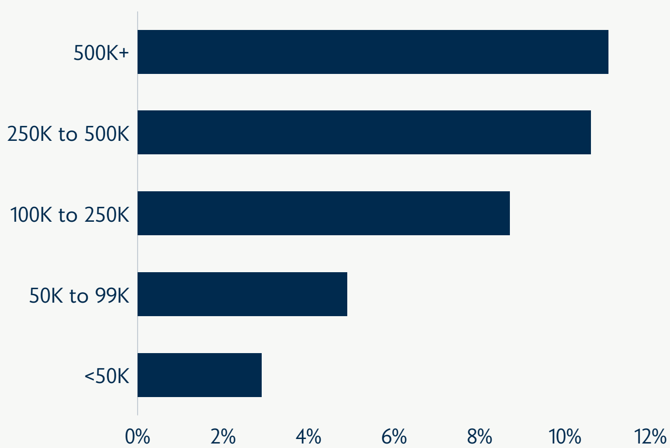
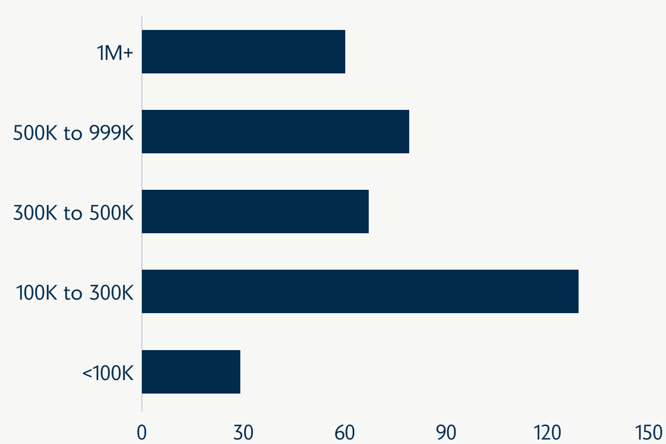


Figure 6: Newly Built Warehouses by Size (Square Feet)



Source: Cushman & Wakefield, February 2025.

Outlook: Tailwinds Driving Opportunities for Investors

The logistics sector is a vital part of the global economy, with no shortage of investment opportunities for skilled real estate managers to meet emerging and evolving demand for the foreseeable future. Logistics tenants are constantly seeking to improve warehouse efficiency, ensure supply chain resiliency and meet the needs of an evolving consumer base. All of these elements may drive continued demand in the sector, with infill markets likely to continue to be favored for their proximal location to end consumers. E-commerce, which continues to dominate total retail sales, reached a record-high 23.2% of all retail in the third quarter of 2024, and is expected to reach 25.0% by year-end 2025.[3] In our view, the future of logistics real estate looks promising with the support of steady tailwinds from the growth of e-commerce and increased trade on a global scale. As demand continues to evolve in the logistics sector, the importance of working with a skilled real estate manager is paramount to success, as they have the operating experience and resources to anticipate and adapt to emerging trends in markets, demographics and consumer preferences.

ENDNOTES

[1] Source: CoStar as of Q4 2024.

[2] Source: CBRE, May 2024.

[3] Source: CBRE, January 2025.

DISCLOSURES

All real estate investments, ranging from equity investments to debt investments, are subject to some degree of risk.

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