Savills Research – Q3 2022

MARKET IN MINUTES

Savills Research

Dublin Industrial and Logistics Market

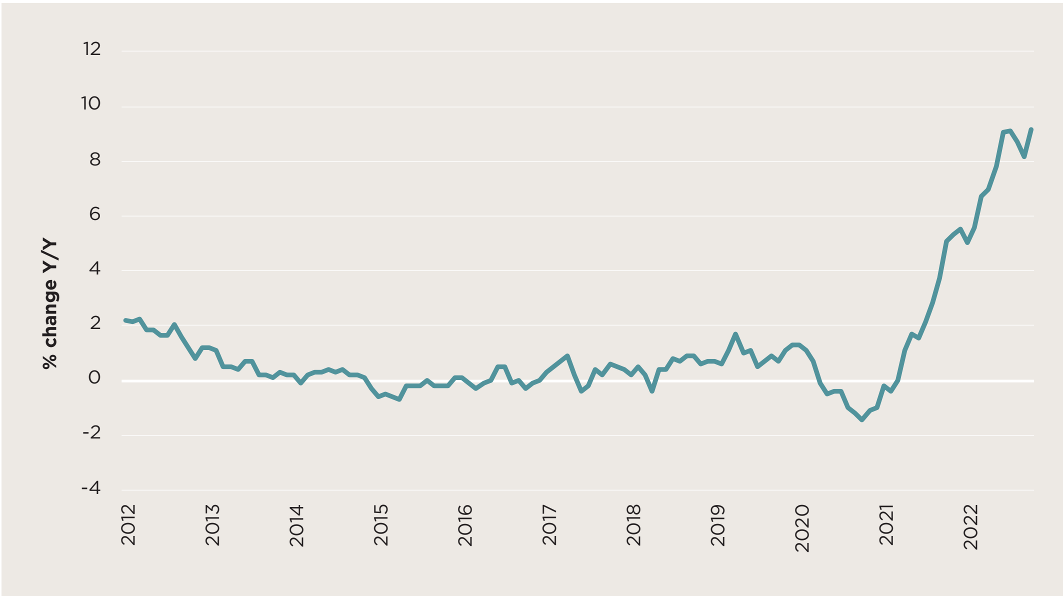
Macro view • Market activity • Supply

Macro view

Global economic headwinds are testing firms

Industrial and logistics firms are navigating a complex economic landscape: high levels of inflation, an energy crisis, supply-chain disruption, and a period of weakened consumer sentiment. While the global savings glut from 2020 through 2021 set the foundation for an inflationary period, the conflict in Ukraine exacerbated the situation through the reduction in the supply of commodities. This has been reflected in The Consumer Price Index (CPI), which rose from 5.6% in February to stand at 9.2% in October.

Figure 1: Consumer Price Index



Source: CSO

Energy demand-supply dynamics an ongoing concern

According to the International Energy Agency, Europe's demand for Liquefied Natural Gas (LNG) will outpace supply for the remainder of 2022, raising concerns over energy costs for the Irish industrial and logistics market heading into 2023. With a substantial cut in the supply of Russian oil and LNG to the European continent exacerbated by further recent supply reductions by other OPEC+ members, European nations will continue to be exposed to higher prices amidst unstable supply. While Ireland does have access to alternative energy sources such as domestic and UK gas production, it will nevertheless be adversely affected by energy shortages in Europe. Energy prices here have already risen significantly, with home heating oil up 65% year-on-year to October, while gas and electricity are up 93% and 71% respectively. These increases have pushed up the costs of transport and manufacturing for industrial and logistics firms, creating cost competitiveness challenges in a weakening macroeconomic environment. Firms are responding by optimising their energy consumption strategies in order to mitigate against rising costs, such as working to non-peak energy pricing hours.

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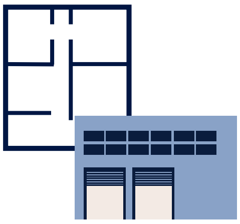


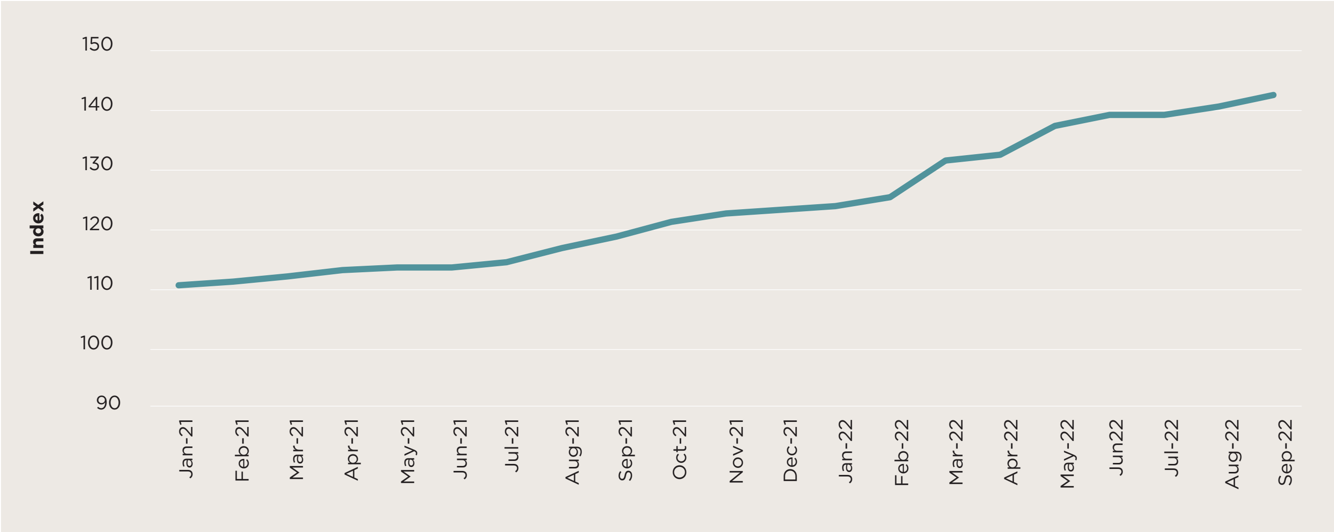
1.3m sq ft
of take-up in Q3

81%
of take-up was for logistics use

The vacancy rate increased from 1.0% to
1.4%

Shipping container prices have fallen by
-66%

Figure 2: Energy Products CPI



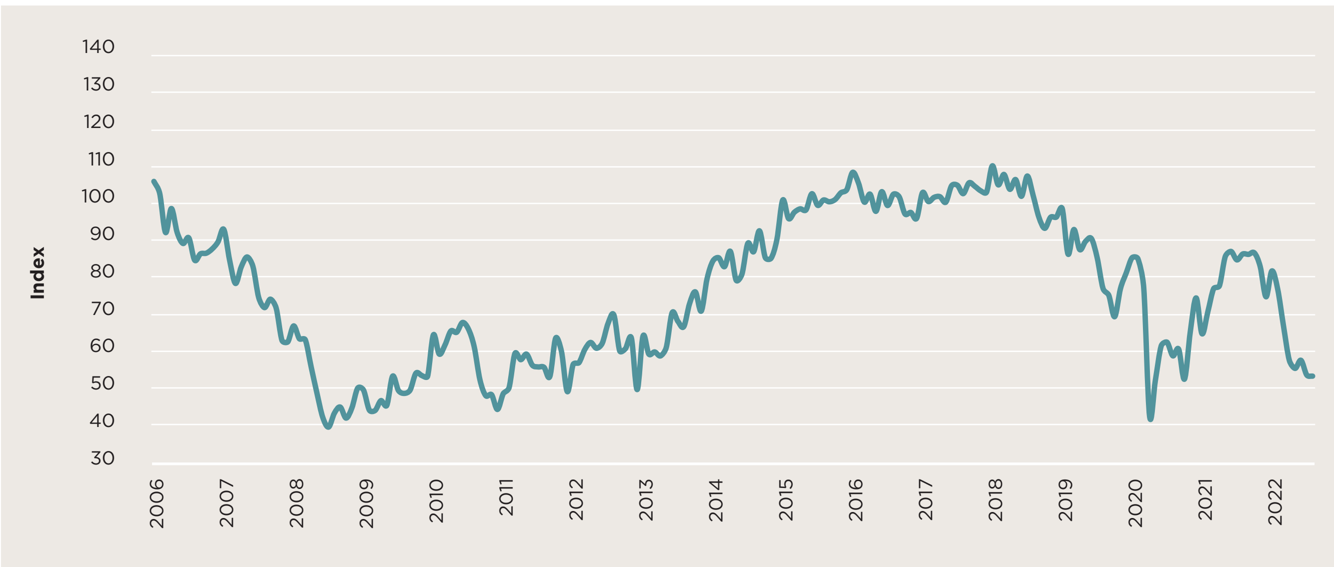
Source: CSO

Consumer sentiment places focus on prices

The Consumer Sentiment Index (CSI), as measured by KBC, is down 38% year-on-year in the latest reading. Elsewhere, new research by Deloitte has found that 52% of Irish consumers are delaying purchases as a direct result of inflation. With a fall in consumer sentiment, product volumes of goods sold is set to reduce, as indicated by AIB's Ireland Manufacturing PMI. The Stocks of Finished Goods Index rose for a fourth consecutive month in October, while at the same time, the New Orders Index fell for a fifth consecutive month.

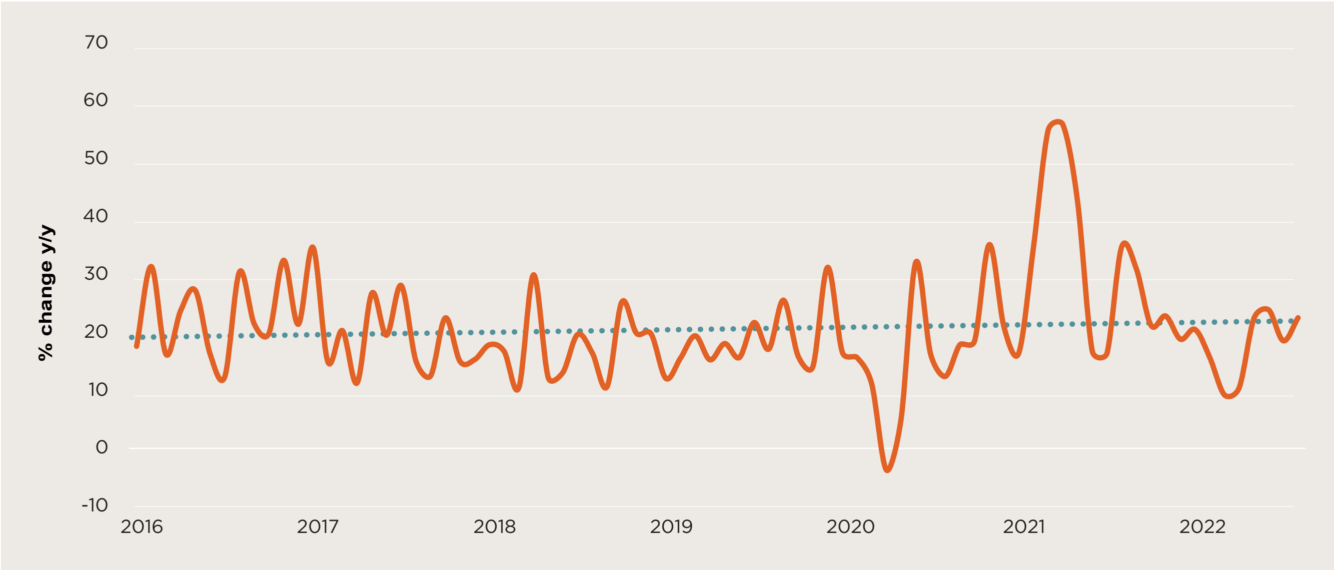
One subsector that is positioned to capture more cost-focused consumers is e-commerce. The overall growth in the sector, while less in magnitude compared to growth during the pandemic, is still positive, with e-commerce expenditure up 23% y/y for September, according to the Central Bank of Ireland. As illustrated in Figure 4, the e-commerce market in Ireland - despite large seasonal and pandemic led swings - has consistently delivered 20% annual growth since 2016. Low-cost digital retailers are better suited to handle periods of weaker consumer sentiment compared to their higher-cost physical counterparts. Morgan Stanley stated in June that the global e-commerce market will continue to expand from $3.3 trillion to upwards of $5.4 trillion by 2026. They note that countries with young populations stand to see faster e-commerce adoption, which means Ireland – as the youngest county in Europe – should see faster growth in this regard. While the bricks and mortar retail sector has benefited from a post-lockdown boom this year as shoppers returned to the shops, e-commerce platforms will be seeking out ways of encouraging cost-conscious consumers to revisit their online pandemic spending habits.

Figure 3: Consumer Sentiment Index



Source: ESRI / KBC Bank Ireland

Figure 4: E-commerce expenditure



Source: Central Bank of Ireland

Global shipping container prices are falling

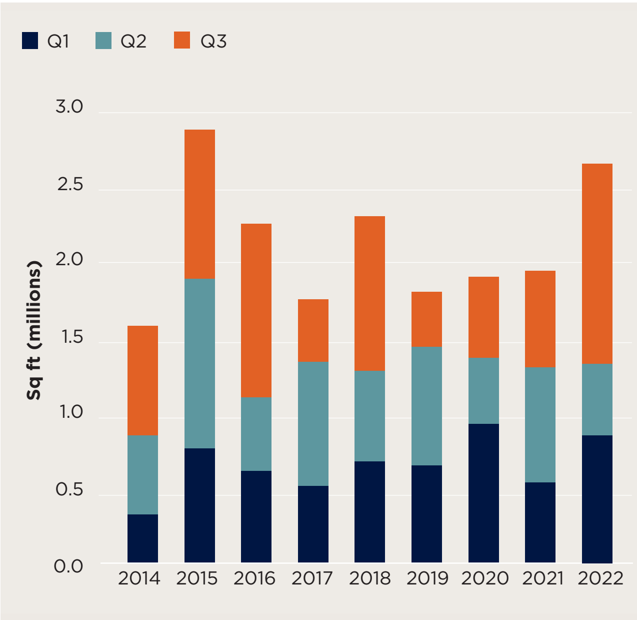
While weakened sentiment and high inflation place pressure on the industrial and logistics sector, an interesting development may help offset rising costs. As the Chinese economy struggles on a number of fronts, significantly more shipping containers are becoming available. According to the World Container Index, 40 ft container prices decreased by 66% since September 2021, and are signalled to fall further, according to maritime research firm Drewry. The tasks of acquiring and transporting shipping containers are a large cost component in both the industrial and logistics business domains. With shipping costs decreasing and container supply increasing, firms can address supply bottlenecks and entice demand through passed-on savings. This relief was demonstrated in the latest Global Supply Chain Pressure Index by the Federal Reserve Bank of New York, which found that supply chain pressures are returning to historical norms.

Peregrine House, Dublin Airport Logistics Park

Market activity

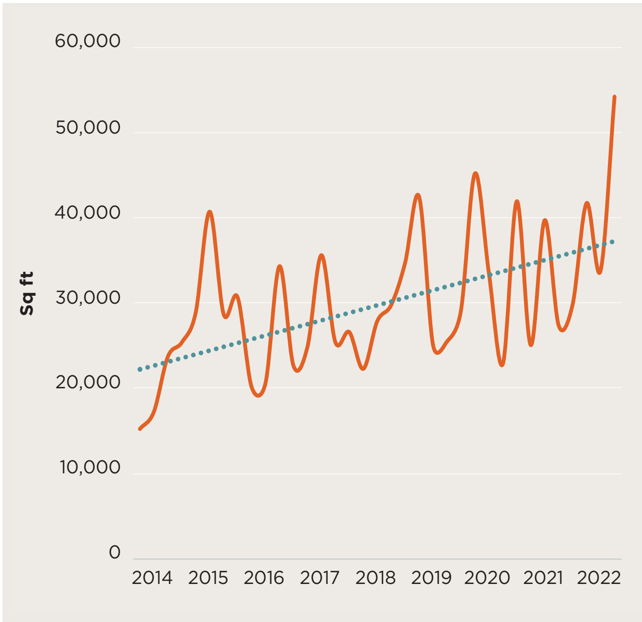
Take-up totalled 1.3m sq ft in Q3, more than double the level witnessed in Q3 last year and 45% above the five-year average for a third quarter. Furthermore, the year-to-date take-up (Q1-Q3) of 2.6 million sq ft is 27% higher than the five-year average. In fact, 2022 has already surpassed the average annual take-up witnessed over the last five years. The average deal size in Q3 was 54,000 sq ft, more than double the Q3 five-year average of 26,000 sq ft, emphasising that it was an increase in deal size that drove take-up rather than the number of deals completed. Ten deals greater than 50,000 sq ft traded this quarter, well above the average number of deals of this magnitude. The number of deals greater than 100,000 sq ft were also substantial, with three signed this quarter, one of which was over 200,000 sq ft. Deals for big-box units, units which are 50,000 sq ft and greater, are the explanation behind the massive take-up gains in Q3, accounting for 79% of total take-up this quarter.

Figure 5: Take-up



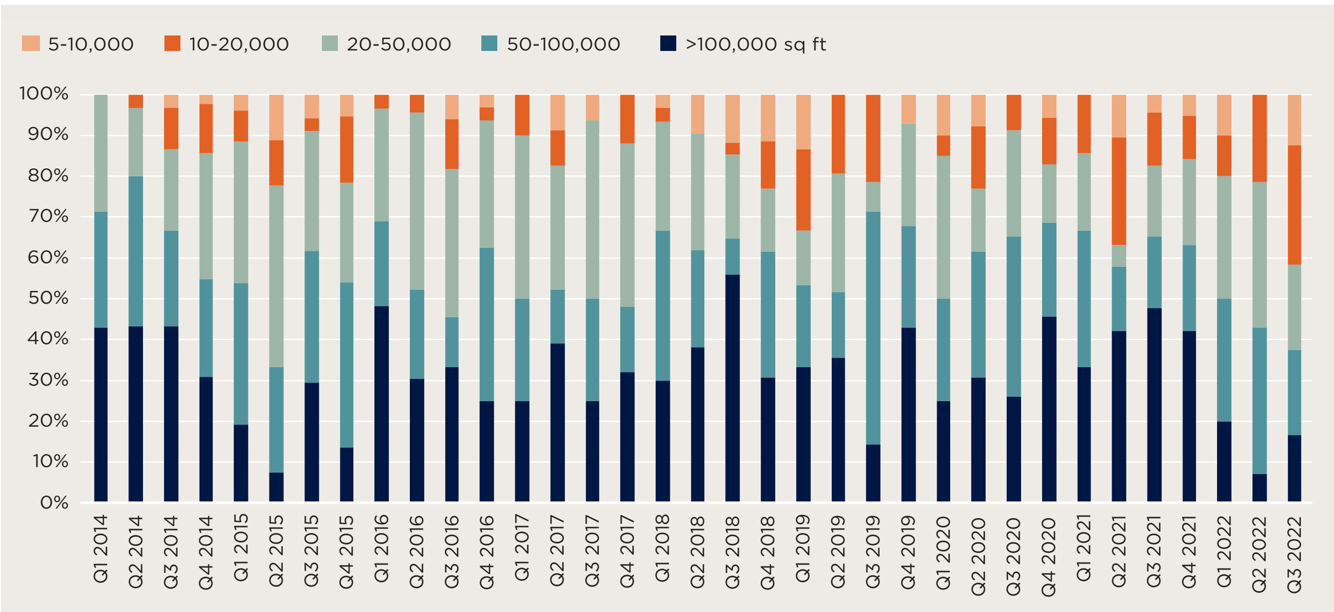
Source: Savills Research

Figure 6: Average deal size



Source: Savills Research

Figure 7: Share of deals by deal size



Source: Savills Research

Strong demand for larger units

Located near Dublin Airport, Quantum Logistics Park saw pre-lets from two global logistics firms this quarter. In the largest deal of the quarter, and indeed the year so far, was the pre-letting of 206,000 sq ft at Unit 1 to DHL. Meanwhile, integrated logistics firm Maersk pre-let 178,100 sq ft at Unit 3 in what was the quarter's second largest deal. In addition, the firm pre-let the 73,800 sq ft Unit 4, bringing their total footprint in Quantum Logistics Park to 251,900 sq ft.

In the third-largest deal, US-headquartered Iron Mountain signed for 161,700 sq ft at the newly completed Unit Q, Aerodrome Business Park. The organisation provides storage and management solutions for information and records. Another pre-let accounted for the fourth-largest deal and was also taken by a global logistics firm. UPS signed for 91,500 sq ft at Unit 8, Horizon Logistics Park, which is due to be completed by the end of the year

Table 1: Top five deals

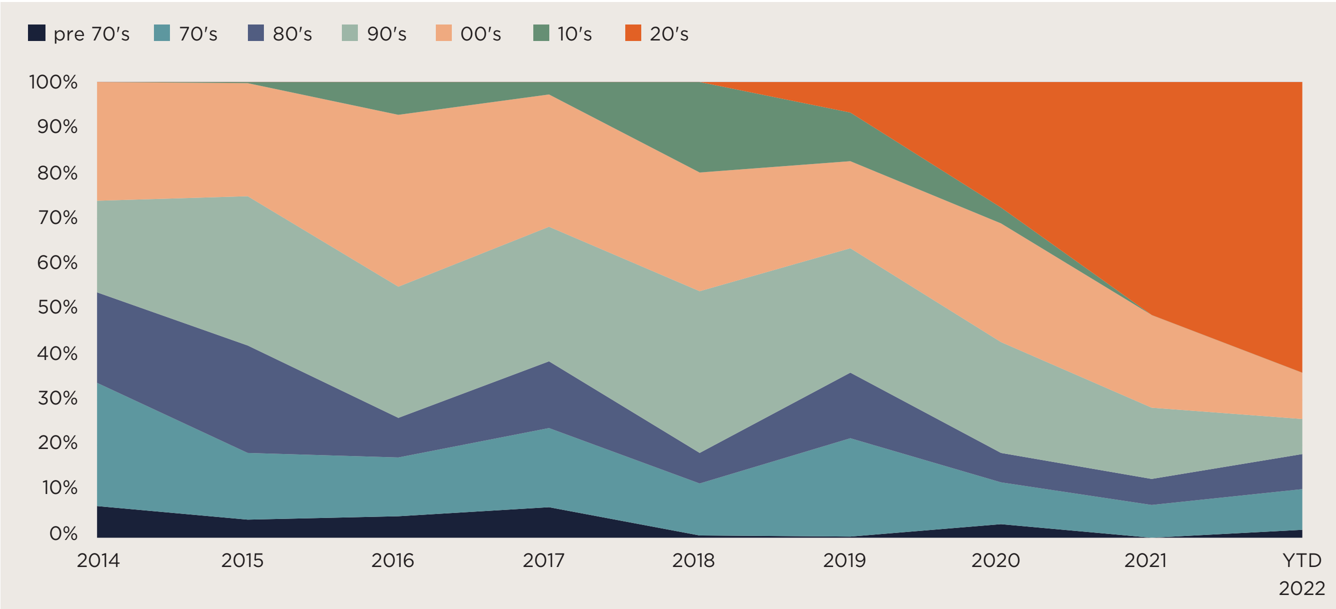
Property	District	Sq ft	Tenant	Type
Unit 1, Quantum Distribution Park	NE	206,000	DHL	New Build
Unit 3, Quantum Distribution Park	NE	178,100	Maersk	New Build
Unit Q, Aerodrome Business Park	SW	161,700	Iron Mountain	New Build
Unit 8, Horizon Logistics Park	NE	91,500	UPS	New Build
Unit at Huntstown Business Park	NW	91,400	Confidential	New Build

Source: Savills Research

New builds drive take-up

Take-up of stock built this decade accounted for 74% of take-up in Q3, a significant increase compared to the prior four-quarter average of 45%. Six of these deals were pre-lets, which accounted for 51% of quarterly take-up. While this represents an increase relative to previous quarters, the overall volume of deals for new builds reflects the strong demand for modern, large, high-quality buildings. Legacy stock, on the other hand, continues to account for only a small portion of take-up, with firms citing corporate ESG requirements, size specifications, as well as refitting and energy costs as the main causes behind the weak demand for legacy units.

Figure 8: Take-up by age

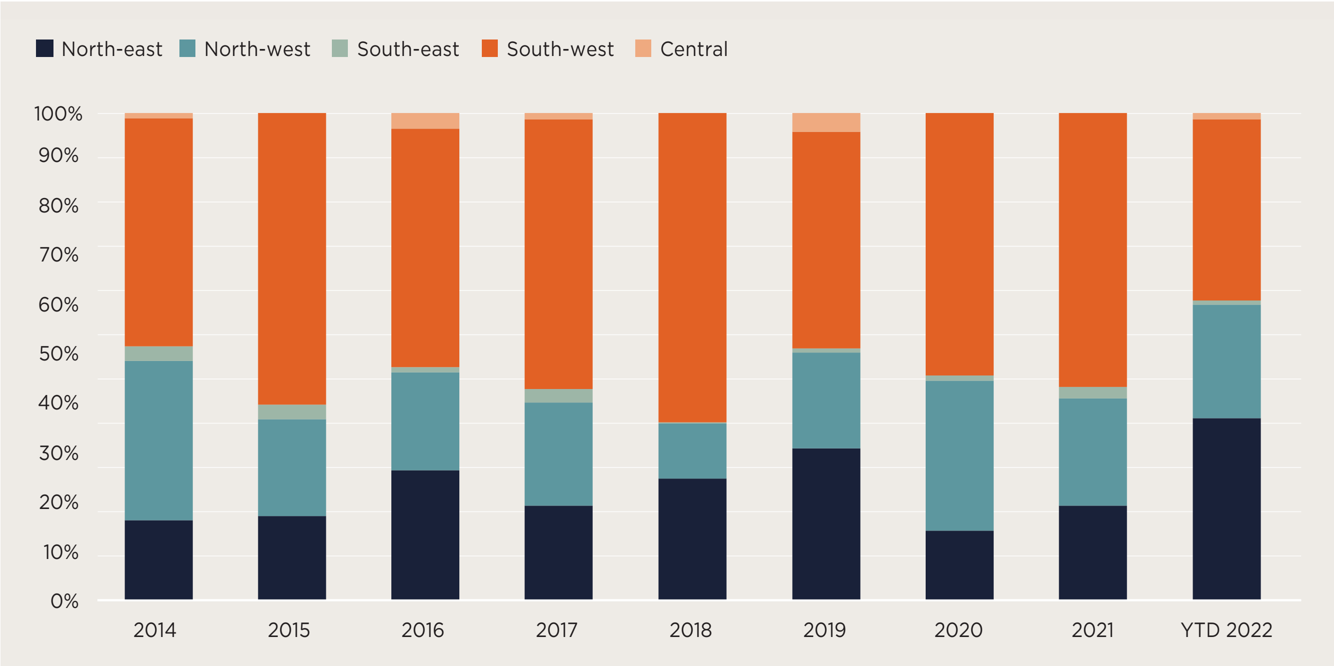


Source: Savills Research

North-east sets record take-up

The North-east accounted for 63% of take-up in Q3, well above the long-run average of 21%. Notably, this was the largest share of take-up ever for a quarter by the North-east suburbs, with eight out of the top 10 big box deals located in the district. With a large portion of new stock being built in developments in the North-east - such as Dublin Airport Logistics Park, Quantum Distribution Park and Horizon Logistics Park - combined with the prevailing lack of modern stock city-wide, the explanation for the record take-up for the area is evident. Meanwhile, the South-west accounted for 27% of take-up, the North-west for 9% with 2% in the South-east. Interestingly, while the share of take-up of the South suburbs fell to 29% from 46% quarter-on quarter, the number of deals increased to 11 from 7, highlighting a smaller average deal size.

Figure 9: Take-up by location



Source: Savills Research

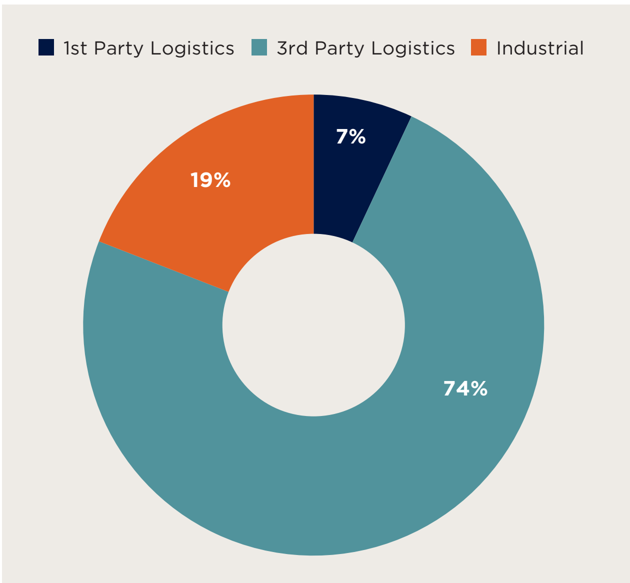
Third-party logistics continues to thrive

Logistics firms contributed 81% of take-up in Q3. Third-party logistics (3PLs) accounted for the majority of this with 825,500 sq ft taken, or 74% of take-up. Three of the top five deals this quarter involved global, large-scale logistics firms including UPS, DHL and Maersk. This suggests that the importance of establishing facilities within Ireland is of significant strategic importance to the global logistics sector. First-party logistics accounted for 7% of take-up in the quarter. The UK kitchen supplier firm, Howdens, accounted for four out of five deals completed in the subsector, following their announcement of expanding operations within Ireland in May of this year. The industrial sector made-up 19% of take-up in Q3. Take-up by 3PLs was 57%, whereas first party logistics and industrial accounted for 26% and 17% respectively.

81%

of take-up was accounted for by logistics firms.

Figure 10: Take-up by sector, Q3



Source: Savills Research

Supply

Pipeline remains strong despite fewer units completed

Q3 saw two units, totalling a combined 221,700 sq ft, reach practical completion. The largest was IPUT's Site Q in Aerodrome Business Park, which extends to 161,700 sq ft and was pre-let to Iron Mountain. The other was Unit D in Greenogue Logistics Park, totalling 60,000 sq ft.

Pipeline remains strong with 534,800 sq ft of new delivery remaining this year, which would bring new supply in 2022 to 2.1m sq ft. This would be 119% higher than the 982,000 sq ft that was delivered in 2021. Of the remaining space due to be completed this year, 55% is already committed, alongside 8% currently reserved, leaving a remaining 37% or 197,400 sq ft of space available to let.

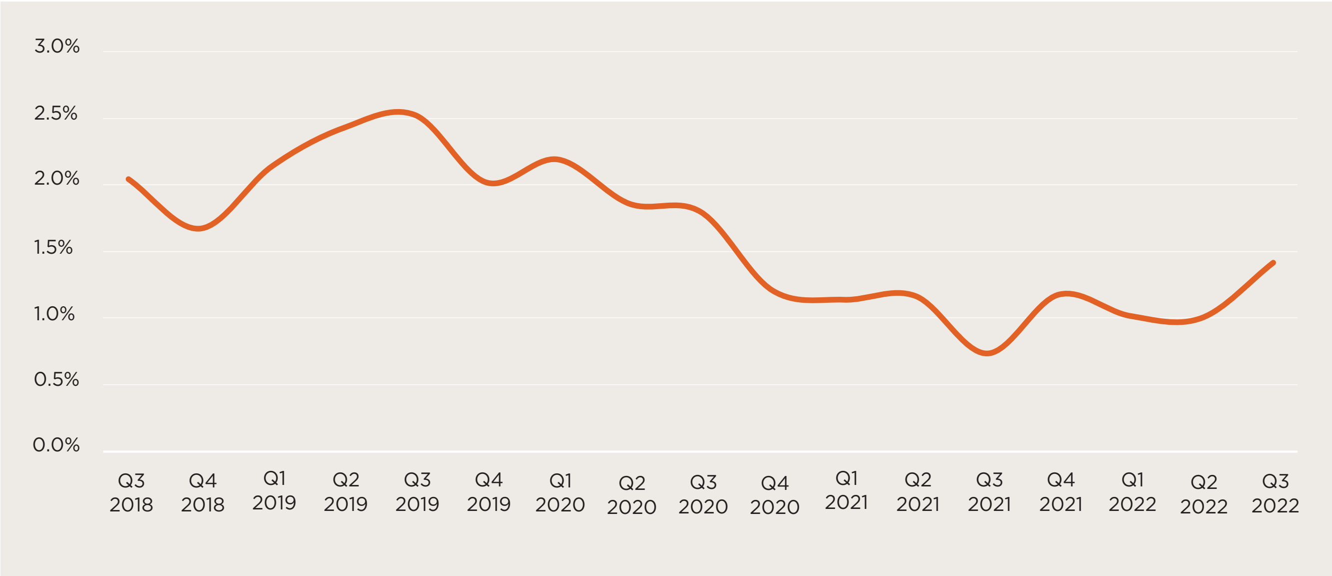
Looking forward to 2023, we forecast completions of three million sq ft next year, of which 1.8m has already started construction. As discussed in our macro view, rising material costs will have challenging implications for construction, with developers needing to balance their construction ambitions with building cost uncertainty.

Figure 11: Pipeline commitment

Source: Savills Research

Building 2, Greenogue Business Park

Figure 12: Vacancy rate



Source: Savills Research

The vacancy rate increased to

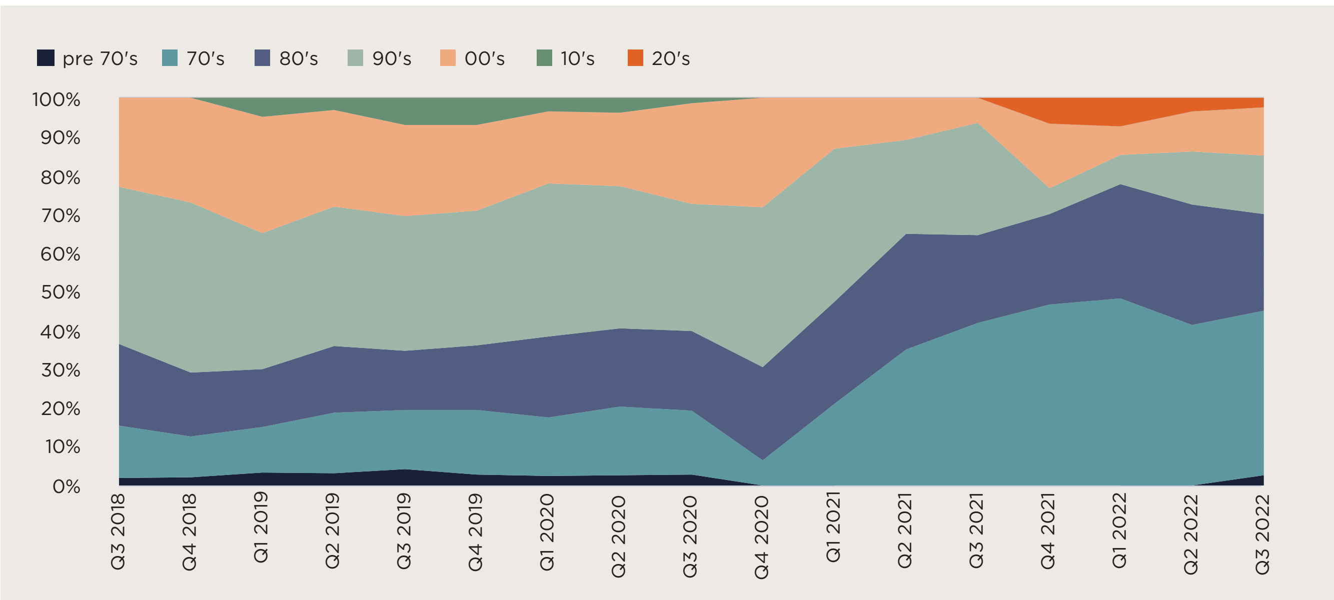
1.4% in Q3 from 1.0% in Q2

The number of vacant units remains low, despite the increase in availability

Q3 witnessed a rise in the vacancy rate to 1.4% in Q3 from 1.0% in Q2, largely attributed to the big box unit in Belgard Square North of 105,050 sq ft and the addition of 11 smaller, legacy units of less than 50,000 sq ft. The increase in the number of vacant legacy units attests to the industry's demand for modern stock. In total, there are currently 37 vacant units, of which only six were built after 2000.

The market is currently summarised by a discrepancy between the demand for large, high-quality units required by modern occupiers and the existing stock of smaller, legacy stock. Currently, there are only five units greater than 50,000 sq ft available, only one of which was built this decade. There is limited availability in the 20,000 to 50,000 sq ft category, with the vast majority of units being less than 30,000 sq ft in size and built before the 2000s. The addition of newer units is likely to slow the absorption of these vacant legacy units, in the context of the high quality expected by tenants and the issues that legacy units present in terms of refitting and various other costs.

Figure 13: Vacant space by age

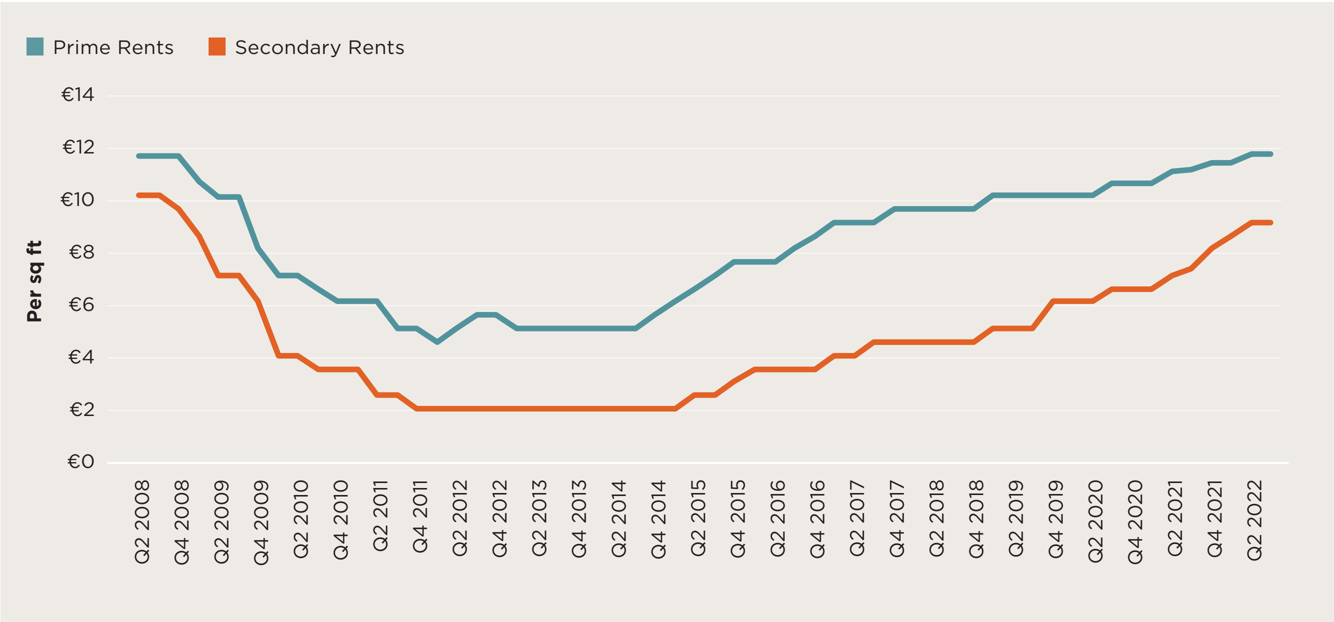


Source: Savills Research

Prime Rents

Rents for industrial and logistics units remain on an upward trajectory in Dublin, as construction cost inflation – combined with structural undersupply – continue to maintain the growth that occurred throughout the pandemic. Rents for prime stock remained at €11.75 psf in Q3, while secondary rents held at €9.00 psf. The market continues to be favourable for landlords, as tenants generally will have to commit to longer lease lengths to obtain stock. Minimum ten-year terms are achievable for prime stock and will likely be the trend continuing forward.

Figure 15: Prime and secondary rents



Source: Savills Research

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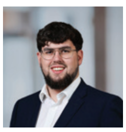

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