Savills Research – Q3 2021

MARKET IN MINUTES

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Dublin Industrial and Logistics Market

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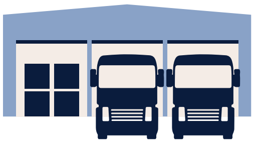
Macro view • Market activity • Outlook

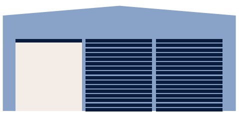


712,000 sq ft

of take-up transacted in Dublin in Q3

39%

increase in average deal size y/y



70%

of stock under construction is committed

3PLs

accounted for 40% of enquiries in Q3

Macro view

Occupier demand is being supported by the expansion in key macroeconomic indicators.

Table 1: Key macroeconomic indicators of logistics demand

Indicator	Correlation to logistics demand*	Annual change Q2 2021
GDP	Strong	21.6%
Manufacturing output	Strong	27.1%
Trade volume	Strong	27.4%
Retail sales (total)	Moderate	35.9%
Retail sales (online)	Strong	36.7%

Sources: CSO, Central Bank of Ireland, Savills Investment Management

Note* Demand = total aggregated take-up volume 2007-2020 in major European markets; correlations. As r^2 > 0.70 (strong); > 0.5 (moderate)

As restrictions have eased throughout the year, we have seen a strong recovery in the majority of the macroeconomic indicators affecting occupational demand in the market. Table 1 sets out five key indicators and their correlation to industrial and logistics take-up. We have then taken measures from the CSO and the Central Bank of Ireland to demonstrate the strong recovery that has begun in each of these measurements.

The Irish economy proved to be resilient to the worst of the pandemic's effects

From Table 1, we can see that there has been a strong recovery in all of these indicators, crucially Ireland has experienced strong growth across all of these indicators, including GDP, trade, manufacturing and retail sales. Ireland's specialisation in ICT and Pharma (which forms part of the industry-based component of GDP), combined with a surge in retail sales, helped to buoy demand for space though the pandemic.

€2.8bn

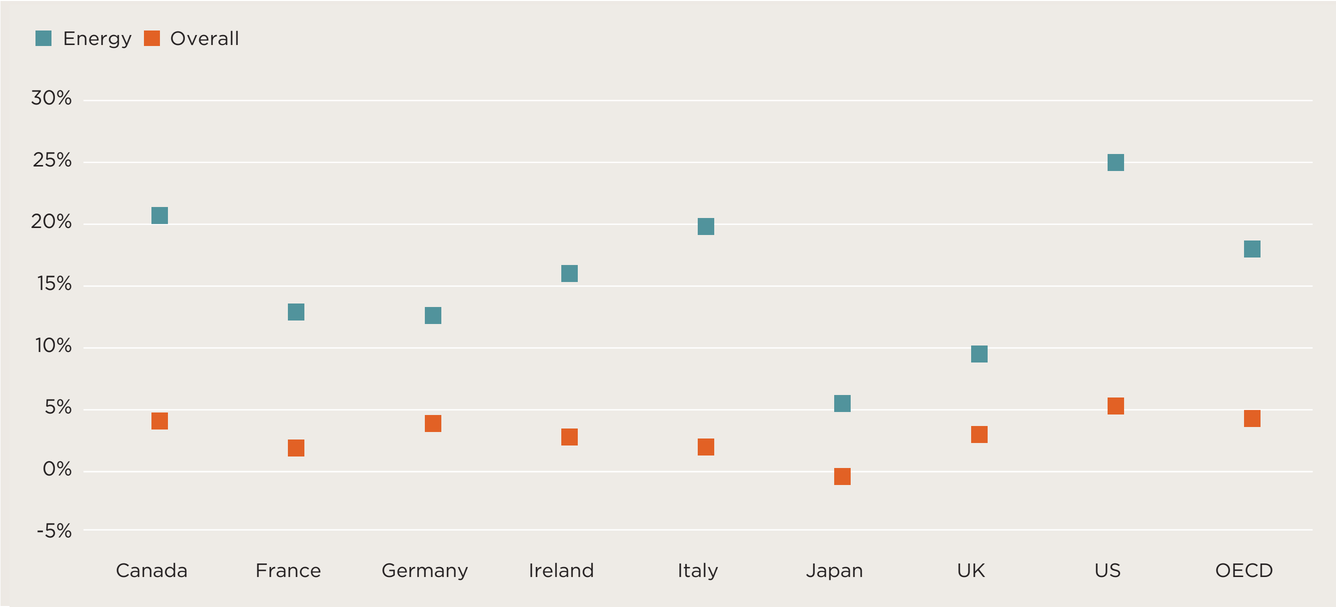
of e-commerce expenditure in August

High-frequency indicators show a continued strong performance

While much of this data is released with a delay, we have seen continued growth in several more frequently released indicators. The Manufacturing Purchasing Managers Index has now indicated 16 months of consecutive expansion and shows that the manufacturing sector is expanding at the fastest rate since the Index began in 1998. The Retail Sales Index shows that retail is continuing to perform well despite the pandemic, growing by 6.0% y/y, reaching another all-time high. In August, the Central Bank's measure of e-commerce expenditure showed that total spend on cards reached €2.8bn, its second-highest point, while Ireland's goods exports grew by 1% y/y in August on a seasonally adjusted basis.

> **Ireland's specialisation in ICT and Pharma, combined with a surge in retail sales, helped to buoy demand for space though the pandemic.**

Figure 1: Energy v overall inflation – August 2021



Source: OECD

Macroeconomic headwinds are rising

The aforementioned indicators have held up remarkably well in the context of a global pandemic demonstrating the resilience of this segment of the Irish economy. As 2021 has progressed however, industrial and logistics firms have experienced a series of headwinds. While demand for goods and services in Western economies has recovered at pace in 2021, the global supply chain has shown signs of weakness. A chain is typically only a strong as its weakest link, but in this case, the entire chain is coming under pressure. Covid-19 has had a significant knock-on impact on the container market, shipping routes, air cargo, trucking lines, warehouses and railways. This has led to shortages of key manufacturing components and dramatically lengthened trading timelines. In a service-based economy like Ireland, the effect has become increasingly pronounced leading to spikes in transportation costs and consumer prices.

After a decade in which the average inflation rate was 0.6% y/y, 2021 has seen inflation surge with prices increasing by 3.7% y/y in September 2021. Indeed, Europe has been gripped by an energy crisis that has seen fuel prices surge in recent months. Data from the OECD released in August shows that increases in fuel costs have dramatically outpaced general inflation over the last year. For many industrial and logistics firms, this will lead to rising operating costs which will cut into profit margins. This may cause firms to prioritise the efficiency of their operations if this price inflation persists into the long-term.

Building 1, Greenogue Logistics Park

Market activity

712,000 sq ft of industrial and logistics space transacted in Dublin during Q3, representing an increase of 66% compared to both Q1 and Q2 and an increase of 33% on the same quarter in 2020. This is particularly impressive in the context of a market that has been severely constrained by supply as indicated by a vacancy rate of just 1.2% at the start of the quarter.

The top deals of the quarter were leases on several large units, all greater than 50,000 sq ft. Nearly all of these were signed under confidentiality agreements limiting the ability to discuss individual deals. Notably, the signing of the Former Lufthansa building in Baldonnell Business Park for 200,000 sq ft represented the largest deal of the year so far and accounted for 29% of total take-up this quarter. Three of the top five deals this quarter were pre-lets, with the lease of Building One in Greenogue Logistics Park, Site B in Northwest Logistics Park and Unit 634 Northwest Logistics Park accounting for almost a third of the quarter's take-up. While the vacancy rate remains at a markedly low level, it is worth noting that the industrial and logistics market does not typically see a large amount of speculatively built stock coming to the market. That said given that the majority of stock is being let before reaching practical completion it shows that there is a depth of demand present in the market that is keeping the pipeline well contained.

With five deals in excess of 50,000 sq ft in the quarter the average deal size was 31,000 sq ft. While this is just above the quarterly average over the last five years it represents an increase of 39% compared to Q3 2020. One factor driving this was the fulfilment of several large requirements that came to the market between Q4 2020 and Q1 2021.

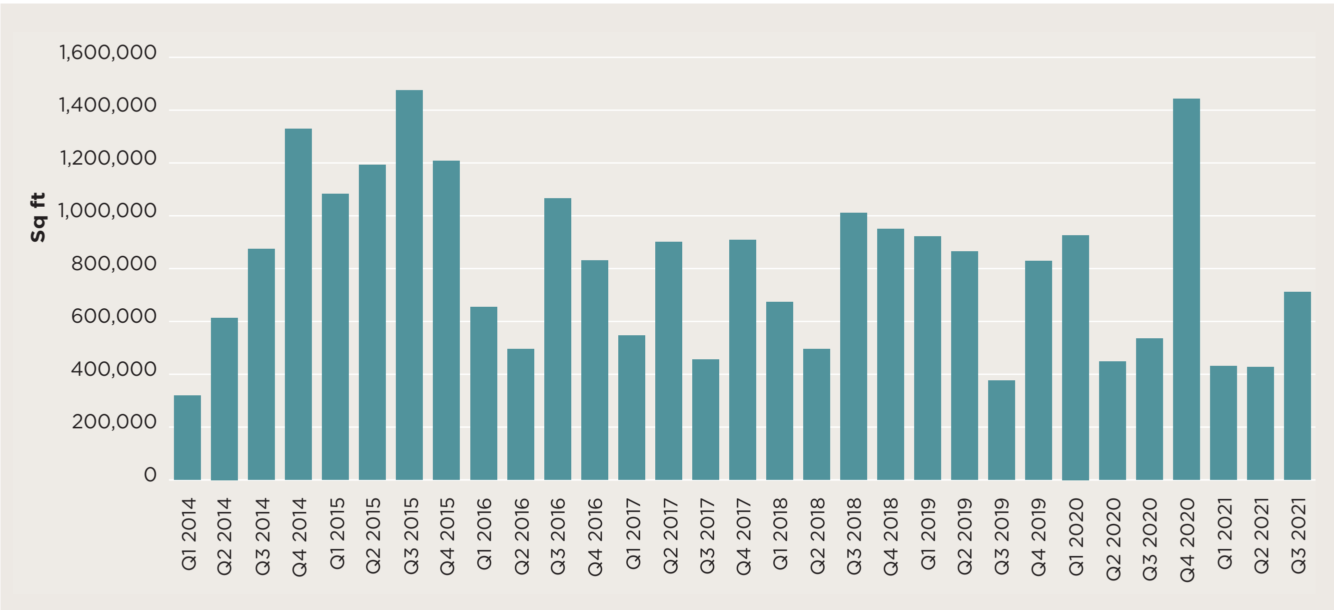
Table 2: Top deals

Property	Sub-market	Sq ft	Lease/Sale	Pre-let/Standing stock
Former Lufthansa Building, Baldonnel Business Park	South-west suburbs	200,000	Lease	Standing stock
Building One, Greenogue Logistics Park	South-west suburbs	83,700	Lease	Pre-let
Site B, Northwest Logistics Park	North-west suburbs	83,500	Lease	Pre-let
Font House, Unit 19 Fonthill Business Park	South-west suburbs	52,900	Lease	Standing stock
Unit 634 Northwest Logistics Park	North-west suburbs	51,900	Lease	Pre-let

Source: Savills Research

> **712,000 sq ft of industrial and logistics space transacted during Q3 2021, an increase of 66% compared to the previous two quarters.**

Figure 2: Take-up by quarter

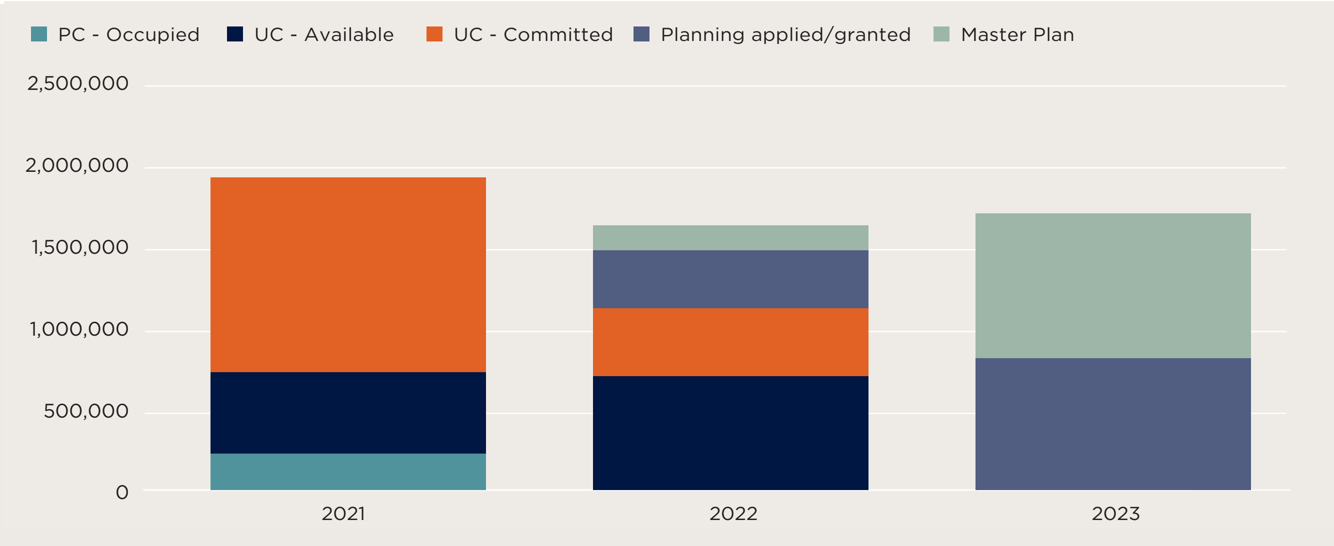


Source: Savills Research

Sales activity

The dearth of suitable stock is particularly apparent in the sales market with only seven sales out of a total of 23 transactions during the quarter. Despite accounting for almost a third of transactions, sales to owner-occupiers only accounted for 12% of the volume of space that transacted. This reflects a lack of opportunities for owner-occupiers with large requirements.

Figure 3: Construction pipeline



Source: Savills Research

Supply

Just one unit was completed in Q3 with Crane House in Dublin Airport Logistics Park adding 50,000 sq ft to stock. This unit was pre-let before coming to market which put downwards pressure on the vacancy rate. With the start of the year characterised by interruption to the pipeline, there have only been three units completed so far this year, totalling 221,000 sq ft. All of these were let before reaching practical completion indicating robust demand for modern stock.

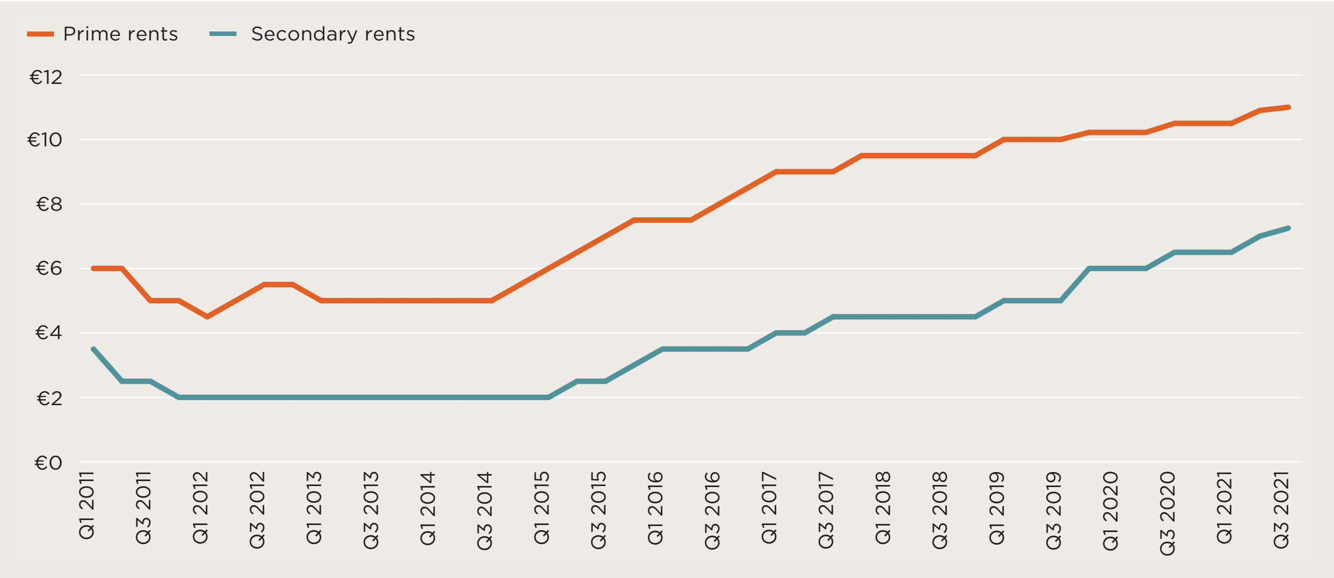
Looking ahead to year-end, there are currently 11 units totaling 1.7m sq ft under construction and due for completion in Q4. Eight of these units are already committed accounting for 70% of total stock coming to the market. The remaining three available units account for 30% of the space currently under construction and are likely to be leased in the final quarter of the year. Looking further ahead to 2022, an additional 1.6m sq ft of space is expected to complete during the year. Of this, 1.1m sq ft of space is currently on site of which 38% is already committed. The majority of space that comes to Dublin tends to be leased before completion. As such, this remaining space will provide a unique opportunity for prospective occupiers to secure quality modern space and this availability may boost take-up as they complete over the coming year. Looking out to 2023, we have identified 1.7m sq ft of space to come on-line but this delivery is much more uncertain given it has yet to commence.

Contrail House & Peregrine House, Dublin Airport Logistics Park

Rents

With pipeline supply constrained and limited availability of standing stock, we have seen upward pressure on rents: rents for prime stock have increased from €10.50 to €11.00 over the last year, representing an increase of 4.8%. This pressure has fed through to the secondary market which has seen rents increase from €6.50 to €7.25 over the period, an increase of 11.5% y/y.

Figure 4: Headline rents psf



Source: Savills Research

> **Rents for prime stock have increased from €10.50 to €11.00 over the last year, representing an increase of 4.8%.**

C1 North City Business Park, Dublin 11

Logistics hubs – a natural progression of the market

Modern development

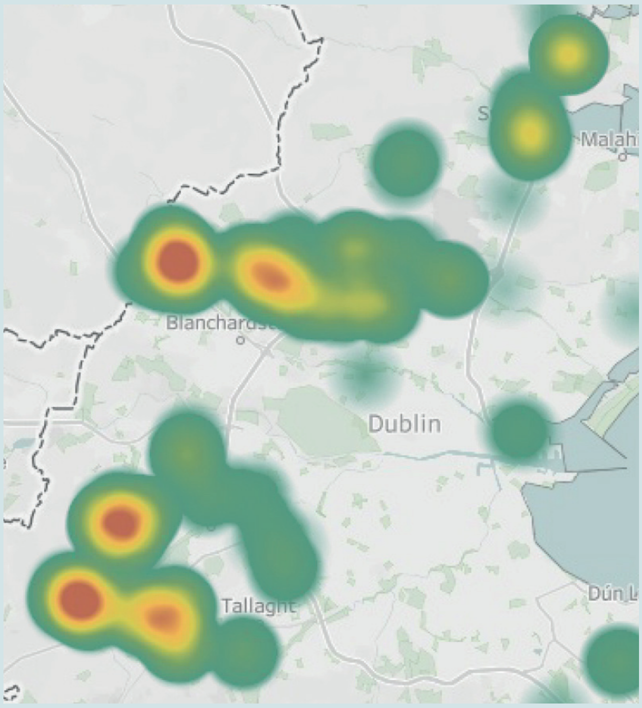
Development of modern stock in Dublin (post-2000) has been focused on two key locations. These are the South-west suburbs business parks clustered around the N7 corridor which have strong links to Ireland's other major population centers of Cork and Limerick. The other key location is an amalgamation of schemes in the North-east and North-west suburbs, which benefits from close proximity to Dublin Airport, the M1 and the Port Tunnel.

After accounting for 45% of stock built in the 2000's the South-west's share of stock completed shrank in the 2010's to just 30%. The increase in the share of development in the North-east and North-west from 21% and 31% to 36% and 32% respectively accounts for the decline seen in the South-west. That said, only 2.3 million sq ft or 3% of space was added to stock in the last decade and thus the South-west continues to account for a large share of overall stock.

68%

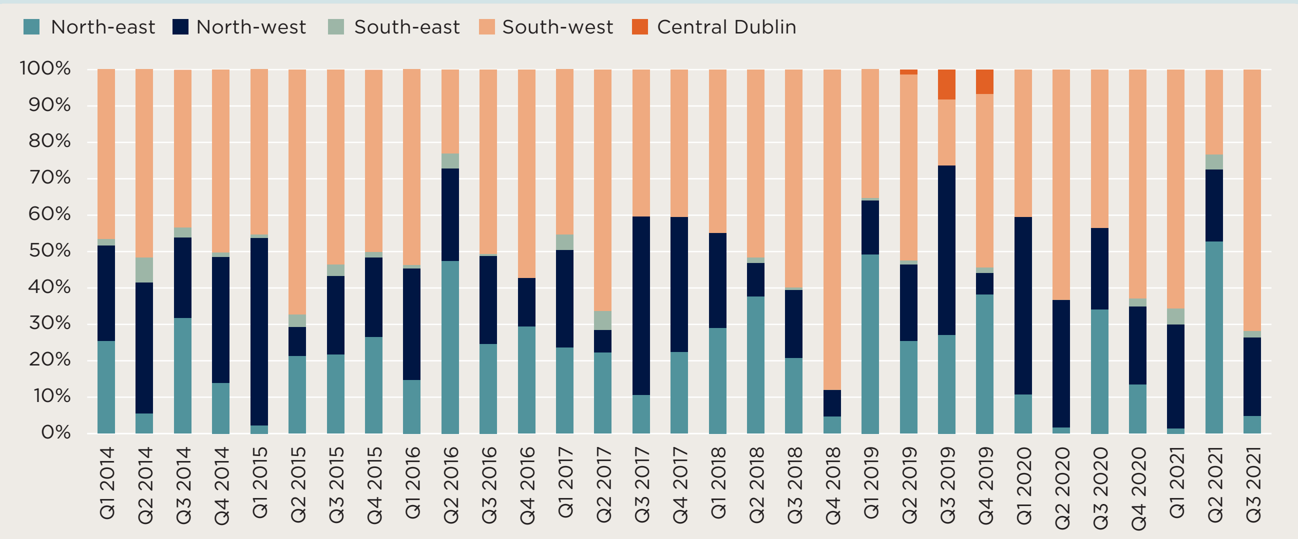
of development in the 2010's was in the North-east and North-west suburbs

Figure 5: Dublin industrial and logistics development 2010-2021



Source: Savills Research

Figure 6: Take-up by location



Source: Savills Research

Pipeline

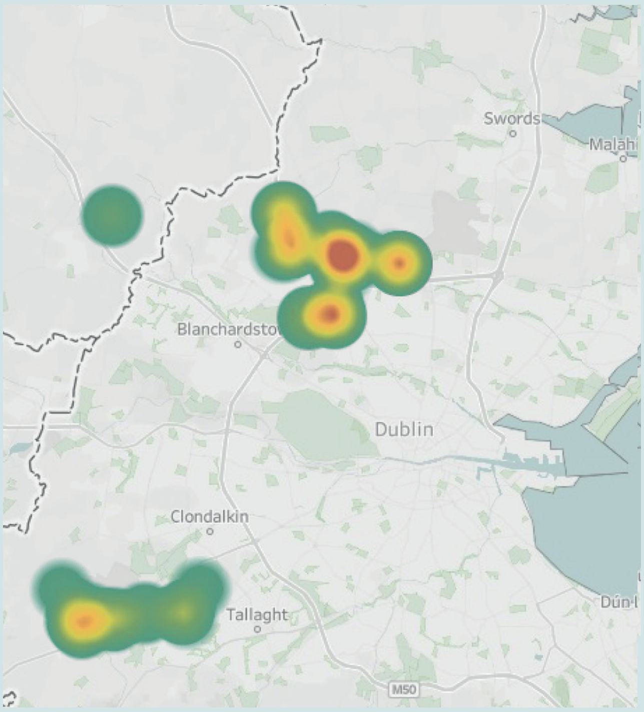
Returning to pipeline supply, the trend of development in the North-east and North-west outweighing development in the South-west appears to be reversing. Of the 1.9m sq ft that will have been delivered during 2021, 74% of this space will be located in the South-west. Not only are there more overall units being developed in the South-west, but the average unit size in the area is also almost three times larger than in the North-east and North-west. This should lead to a boost in take-up in the South-west over the next year or so.

Looking further ahead, the amount of space currently in the planning process is relatively evenly split between the North and South-west. Between 2022 and 2024, 715,000 sq ft is expected to complete in the North-east and 481,000 sq ft is forecast in the North-west totaling 1.2m sq ft overall. In the South-west, a further 1.1m sq ft is expected to complete.

We are also aware of an additional 2.4m sq ft of space in various stages of the planning set to be complete by 2028 in the North-west and 0.6m sq ft in the North-east. Over this time horizon, it is difficult to accurately predict what will likely be added to the South-west pipeline where only 300,000 sq ft of additional space is currently expected. Further to this, IPUT recently acquired 64 acres of development land at the Cherryhound interchange off the M2 motorway. The site, which has strong road network links and is adjacent to Dublin Airport, would add over one million sq ft of space to stock in the North-west.

74%
of the 1.7m sq ft of space currently on-site in Dublin is located in the South-west

Figure 7: Dublin industrial and logistics pipeline 2021+



Source: Savills Research

Take-up trends

This concentrated development has inevitably channelled take-up into these locations. The South-west has accounted for just over half of all take-up over the last five years while the North-west and North-east have accounted for 24% and 23% respectively. The dominance of these locations in terms of take-up will inevitably continue, driven by the modern supply coming to market over the next few years. This forms a positive feedback loop where proven demand for stock in a location leads to further supply which is then absorbed by the market as it grows.

Advantages of clustering

A wide range of literature points to advantages for logistics firms that locate close to each other. The hierarchy of logistics hubs starts with individual warehouses, depots and sorting centres and is followed by specialised facilities in logistics zones. At the third level are logistics hubs that encompass several zones in a given location. Fourth and finally are large-scale agglomerations in a metropolitan/regional area. Certainly, the Irish examples above of Dublin's suburbs exhibit the characteristics of a nascent third level hub with scope for these locations to act as an metropolitan/regional logistics area as the market develops.

Another defining trait of logistics hubs and regions is the complexity of the logistics activities and the number of logistics providers in the area. Dublin has seen an explosion of growth in the last decade, with new entrants to the market adding even greater complexity in recent years. In particular, third-party logistics firms (3PLs) have become increasingly active and quick to adapt to changing needs. As the market achieves further scale this will allow additional service providers (truck servicing providers, specialised law firms, international financial service providers) to enter the market with a service economy based around facilitating 3PLs. We are currently seeing an expansion in this area highlighted by the growing share of inquiries from 3PL firms. Our agents estimate that, an average 40% of enquiries from July to the end of September were from 3PLs. These units will be used to accommodate stockpiling by customers in terms of materials and finished products. Two key drivers of this are the aforementioned supply chain issues facing importers and Brexit.

Crucially, logistics hubs have unique advantages beyond the simple agglomeration economies present in most dense urban areas. For example, firms can take advantage of economies of transportation. Freight flows are typically asymmetric with more goods moving in one direction than the other resulting in lorries making return journeys with no cargo. A carrier will only be able to collect revenue from loaded moves and thus movements into areas where less freight originates will be more expensive. As more companies move into a given logistics hub, the ability of carriers to find follow-on loads to take on the return leg of a journey rises, lowering transportation costs. As the size of a cluster grows the ability of firms to take advantage of these features grows in tandem, creating a positive feedback loop.

Domestically, several factors will drive demand for logistics activity over the next decade. As we noted in our macro-view online retail industrial and logistical requirements are more intensive than traditional retail. Ireland is set to see steady growth in online retail sales of 13.0% over the next five years, which will drive further demand for logistics space. Finally, Ireland benefits from favourable demographics: Ireland's natural population growth of 0.5% y/y is the highest in the EU and its total population is forecasted to grow by 27% by 2050. As Ireland's population scales up, it will provide demand for logistics services, with positive feedback loops stemming from this overall expansion in the logistics market resulting in even greater clustering.

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