INDUSTRIAL INDEX

PULLING THE LEVERS: REGIONAL AND MARKET SELECTION AS MEANS OF ACHIEVING OUTPERFORMANCE IN AN OUTPERFORMING SECTOR

There is no denying that industrial has been the asset class of choice over the past several years. Investor appetite for the asset class seems insatiable due to powerful secular, demographic, and technological tailwinds driving the sector's steady returns. Already experiencing powerful tailwinds prior to the COVID-19 pandemic, national shutdowns further fueled the asset class as consumers were compelled to adopt ecommerce methods to fulfill basic necessities. Given the widening divergence between property sector returns, which has only intensified with the pandemic, it comes as no surprise that investors are piling into the asset class.

With robust fundamental momentum has come steady sector outperformance. In the twelve months through Q1 2021, the industrial sector posted a robust 14.1% total return, far outpacing the next-best sector's returns of 2.6% observed in apartments, a delta that has only increased in recent quarters. And while sector selection remains a critical component in achieving broad benchmark outperformance –indeed, virtually every industrial market has outpaced the NPI-All average returns in recent periods – so too is regional and market selection, as a geographically-agnostic approach even within an outperforming sector can offer meaningfully different returns.

In the industrial sub-index, the clear and persistent regional outperformers are the generally more supply-constrained, infill East and West regions. In aggregate, the East outperformed the NPI-I by 326 basis points in the year through Q1; the West, by 55 basis points, while the South and Midwest regions underperformed over the same period by 200 and 424 basis points, respectively.

This has naturally led to greater competition for industrial assets in these regions as investors have sought outperformance. An elevated propensity to "get it right" in these parts of the country has also furthered their appeal – 78.9% of markets in the East outperformed the NPI-I in the annualized period through the first quarter, whereas just one Midwest market earned the same high marks. Yet even within an outperforming region, the spread of returns between markets can be considerable. For example, in the trailing twelve months through Q1, the Reno industrial market outperformed the NPI-I by 571 bps, while the lowest performer, Denver, lagged the industrial sub-index by 569 basis points, generating a wide regional total return performance delta of 11.4% in just one year. And while in aggregate the Midwest is a regional laggard, certain markets such as Columbus (15.1%) and Indianapolis (13.4%) have demonstrated an ability to outperform their East and West counterparts by a considerable margin. All that to say, thorough analysis at a more granular level remains a critical component in identifying metros with the highest propensity for capturing superior returns.

The outlook for the industrial property sector remains bright as reflected by the continued growth in asset prices, which expanded 25% year-over-year in April according to Green Street's sector-level CPPI. But with increasing amounts of capital rotating into the sector, investors would be wise to remember that sector selection is just one of many levers that, when pulled correctly, generate outperformance, though diligent market selection is also key.

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INDUSTRIAL TOTAL RETURNS

	Total NPI	Total Industrial	East	Midwest	South	West
1st Q 2021	1.72	4.72	5.17	3.38	3.82	5.24
4th Q 2020	1.15	4.68	6.10	2.94	4.04	4.77
One Year	2.61	14.11	17.37	9.87	12.11	14.66
Three Years	4.89	13.68	15.31	9.21	11.88	14.85
Five Years	5.81	13.34	14.24	9.50	11.32	14.81
Ten Years	8.82	13.22	13.02	10.41	11.95	14.57
Twenty Years	8.15	10.02	10.04	7.77	8.82	11.23

INDUSTRIAL INCOME RETURNS

	Total NPI	Total Industrial	East	Midwest	South	West
1st Q 2021	1.04	1.08	1.06	1.25	1.18	1.01
4th Q 2020	1.01	1.10	1.11	1.22	1.20	1.02
One Year	4.14	4.46	4.52	5.08	4.85	4.13
Three Years	4.40	4.65	4.74	5.29	5.03	4.29
Five Years	4.52	4.84	4.99	5.41	5.26	4.46
Ten Years	5.01	5.40	5.68	5.90	5.80	4.98
Twenty Years	5.93	6.37	6.65	6.79	6.66	6.01

INDUSTRIAL APPRECIATION RETURNS

	Total NPI	Total Industrial	East	Midwest	South	West
1st Q 2021	0.67	3.63	4.11	2.13	2.64	4.23
4th Q 2020	0.14	3.58	4.99	1.72	2.85	3.75
One Year	-1.48	9.34	12.44	4.61	7.00	10.22
Three Years	0.48	8.73	10.21	3.77	6.61	10.23
Five Years	1.25	8.21	8.92	3.93	5.83	10.02
Ten Years	3.68	7.52	7.03	4.32	5.90	9.24
Twenty Years	2.13	3.48	3.21	0.93	2.06	4.99

INDUSTRIAL INDEX—QUARTILE RANGE OF RETURNS