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The Big Impact of the Shrinking Industrial Supply

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With limited supply and dynamic demand, industrial rents are expected to increase as much as 10% in the next 12 months.

Barry Saywitz

The San Diego industrial market—like many markets across the country—is seeing record-low industrial vacancy rates and rapidly increasing rents. However, in San Diego, the culprit isn't ecommerce users. Instead, the market is a dynamic network of distribution facilities near the border, R&D and flex-industrial facilities in Central County and owner-user manufacturing companies in North County. As the industrial market continues to tighten, **Barry Saywitz**, president of **the Saywitz Co.** says that rents could rise as much as 10% in the next 12 months. We sat down with Saywitz for an exclusive interview to talk about the industrial demand and how it is impacting rents.

GlobeSt.com: We are seeing a shrinking industrial vacancy rate throughout Southern California. What is driving the market in San Diego?

Barry Saywitz: The San Diego market is different from Orange County and L.A. in that you have multiple submarkets for industrial. You have the product that is South of Downtown San Diego going down to the Mexican border, and then you have the stuff that is in Kearny Mesa that is older, smaller industrial buildings, and then you have North County industrial. You really have to take them one at a time, but generally, there is a supply and demand issue and there is a limited number of warehouse space. That is because, other than near the Mexican border, warehouse space in not your highest and best use or the real estate. You are better served in Central San Diego County flex, lab or creative office space than you are to build true warehouse space. In North County, a lot of the users have a larger office component or a light-manufacturing component because they are truly distribution companies. San Diego is not a market that is a hub for distribution. The major distribution isn't coming out of San Diego, except at the border.

GlobeSt.com: Ecommerce has been a major driver of industrial leasing activity in other markets. Do you not see ecommerce users as active in the San Diego market?

Saywitz: You are to some degree, but you are not seeing Amazon look at San Diego as a distribution hub. They are really looking at the Inland Empire, and they will push further north and east of San Diego for geographical reasons for shipping and trucking, plus it is cheaper with a cheaper labor force. You do have some regional warehouses, but they need 30,000 or 40,000 square feet, not 300,000 square feet. In the Inland Empire on the other hand, 500,000 to 1 million square foot buildings, and those owners will not split the building for a user that wants 100,000 square feet. They will hold out for a user that can use the full building.

GlobeSt.com: How has the limited supply impacted rents?

Saywitz: San Diego dragged a little behind Orange County and L.A., it has now caught up. You have industrial rates in North County, for example, that are $1 per square foot, just like you have in Orange County. In Otay Mesa, rates used to be $0.35 or $0.40 per square foot. Now, we are doing deals for $0.60 per square foot. So, percentage wise, rates have go up 50% to 100% over the last four to five years. The reason for that is really supply and demand, but the other reason is that when you have a company that is doing well, ownership typically wants to buy a building rather than pay rent. The dilemma then becomes that there are even less buildings to buy than there are to lease. So, those prices are up significantly.

GlobeSt.com: Where you think that rents are headed this year?

Saywitz: I think that there is limited supply, and I see rents increasing 5% to 10% in the next 12 months. You do have some new product coming online, but the new product is priced at a higher point. The people that want a new building are willing to pay for it and if it lease quickly at that number, the next person that comes along will lease for a little bit more.