

MARKET CHECKUP: Industrial



IBJ's INDUSTRIAL PANEL: Jamie Browning, vice president of real estate development for locally based Browning Investments; Jake Sturman, senior vice president for industrial in the local office of Jones Lang LaSalle; and **Tony Hupp, a co-leader of the industrial group at locally based Summit Realty Group.**

IBJ: *What do you see as the biggest story in the industrial market for 2009?*

BROWNING: Liquidity problems in the credit markets are forcing those who were overleveraged to do transactions at below 2008 pricing levels. The result is depressed valuations on existing buildings. Once existing space gets absorbed, new space in the future could become more expensive to compensate for greater financing costs.

STURMAN: The biggest story for 2009 is the effect of capital markets on all factors of commercial real estate. Given the Indianapolis industrial market is primarily a speculative market, most developers depend on ample supply of capital for the development of projects. Buyers of these developments depend of debt structures to purchase assets at reasonable market capitalization rates supported by reasonable rental rates. As the capital markets have all but deteriorated on a national/ international basis, the local market has had to re-establish underwriting parameters for all industrial real estate.

HUPP: If I had to call it now, I would say the headline would read "Could have been a lot worse!" Year-to-date occupancy has remained level. We started the first quarter at 9.2 percent vacancy and it's rising slightly now to 10 percent. This slight bump is primarily due to Axxess 70 and AllPoints Midwest coming on line with over 780,000 square feet of speculative space already in progress before the economy dipped.

IBJ: *Some key players in the local market have taken big hits in this recession, and in many cases have trimmed their staffs. How will the shakeout affect the market, and who do you see as the winners?*

BROWNING: The unfortunate result is there are no real winners. With some exception, increased uncertainty

with lenders has caused them to change their underwriting standards, causing larger spreads on yield, increased credits to stabilized income, and greater equity requirements. The net result is that the cost of money is more expensive for deals that do exist.

HUPP: We will continue to see the larger developers downsize, change the way they do business and perhaps some may close shop. The winners will be the reinvented investors or new cash players that consist of smaller groups of owners and break-off developers, mainly local, that will take advantage of these available assets.

STURMAN: In economic downturns, most industries, with the exception of government and health care, typically trim their head counts. Our firm believes this same correction in real estate is needed and tracks with other professional/financial/ consulting industries.

Winners in this market for any real estate firm can be categorized into three areas: Bronze medal winners are firms that are or have become lean enough that their monthly liabilities meet or beat monthly cash flows. Silver medal winners are firms with a plan to deal with existing/future debt maturities to remain sustainable for a minimum of 12 to 24 months. Gold medal winners are firms that have or will return to the true fundamentals of real estate and have stable sources of flexible capital to compete and win in very complex transactions.

IBJ: *The city put together prepackaged tax abatements to entice AmeriPlex tenants. Will moves like this help Marion County give Hendricks County a run for its money, or is it still an uphill battle?*

BROWNING: This change in policy may be helpful from a marketing perspective, but the reality is that tax abatement was always available for build-to-suit projects at AmeriPlex. Since no speculative projects are plausible at this juncture, nothing has changed for the time being.

STURMAN: The fact that Marion County has not considered blanket tax abatement for speculative development and has only considered tax abatement on specific deals has hindered their ability to compete. Our firm believes that the city's move to consider pre-package abatements to entice development in AmeriPlex will help Marion County to compete with all of the doughnut counties. A lack of capital will push our market, at least for 12 to 24 months,

into a build to suit market. AmeriPlex and the city of Indianapolis will be just as competitive as Hendricks County in these pursuits.

HUPP: This absolutely was the right move. It will give every county with tax abatement in place a run for its money and will allow deals to come to Ameri-Plex that never would have had a chance before. Currently it is a 90- to 120-day, several-committee process for abatement approval. However, it will handicap those counties with no inventory. Pre-existing buildings will be cheaper and easier transactions to complete rather than the cost and timing for new construction, even with tax abatements in place.

IBJ: *Are we seeing many new tenants to the market or is leasing being driven more by existing tenants?*

HUPP: In 2008, I estimate the percentages were 60 percent new and 40 percent renewals. For 2009, I'm seeing a total reverse at about 20 percent new and 80 percent renewals.

STURMAN: With some rare exceptions, the current market is an existing tenant market.

BROWNING: The mix of new versus existing customers is about equal. Our view is that as new third-party logistics providers become accustomed to doing business in Indianapolis, they will bring in more outside business to take advantage of our lower occupancy costs and our geographical location.

IBJ: *Any more blockbuster deals lurking on the market?*

STURMAN: We are aware of a handful of mega-deals between 400,000 and 1.2 million square feet considering central Indiana as a location. The ample supply of great product will hopefully allow us to win our fair share of these deals.

HUPP: Within the past few weeks, activity has increased significantly. We're seeing decent-size modern bulk distribution center requirements coming in. Many of these deals will or have stimulus money or have federal government funding.

BROWNING: In 2009, Browning has been fortunate to have the opportunity to develop the Elanco headquarters in Greenfield, the Dow AgroSciences research-and-development building at Northwest Technology Center and a land assembly project as an extension of our Meridian & Main development in Carmel. We continue to work on other op-

portunities and see deals that are as customer-specific in nature as possible.

IBJ: *Is Anson losing its momentum after the blockbuster Medco and Amazon deals last year?*

BROWNING: The past nine months are more indicative of the market rather than a reflection of Anson. All-Points at Anson, and for that matter AllPoints Midwest, are two premier locations that are well positioned to take advantage of a market rebound as users and customers will want to take advantage of locations that retain their value.

STURMAN: Our firm believes in well-located, well-funded parks. All-Points at Anson possesses excellent fundamentals of a vibrant industrial/ mixed-use development.

HUPP: Since its inception, this project has been successful. Like several other new developments, Anson is in emerging markets with no real tenant base yet. They did

pull back on the construction of a new, 250,000-square-foot speculative building due to the economy. Anson is in the same boat as any undeveloped or partially developed park—the current credit and underwriting climate does not allow ongoing development unless it's under the most ideal of conditions and even then, it's tough.

IBJ: *What's your outlook for 2010?*

HUPP: I see vacant land harder to move and new construction being limited to build-to-suit, high-end users and little to no speculative projects. Existing space should have reasonably healthy lease activity and a noticeable reduction in vacancy, which is a good sign the economy is changing for the better. As a whole, Indianapolis is performing reasonably well compared to similar secondary markets we compete against.

BROWNING: I expect more fallout from the difficulties in the credit markets as lenders and owners continue to de-lever their assets. Tenant-specific deals will get done and a slower pace for speculative space to get absorbed. However, the outlook is better than 2008.

STURMAN: Our outlook for the first half of 2010 will feel much the same as 2009. There will still be a lack of liquidity which may limit the number of construction starts to a slow trickle, especially on the speculative-development side. Some optimism exists in the marketplace given the possibility of a great deal of pent-up demand that may break loose in the second half of 2010.

“We are aware of a handful of mega-deals between 400,000 and 1.2 million square feet considering central Indiana as a location.”

*Jake Sturman, senior vice president
for industrial at Jones Lang LaSalle*
