MONTGOMERY COUNTY INDUSTRIAL MARKET REPORT

Scheer Partners
A Reputation for Results

2ND QUARTER 2017

Robust demand, restricted land supply and municipal interference have conspired to push Montgomery County's 14 million square foot (msf) industrial market to near-record low vacancy for the region at 7.8%. This market crunch is driving rental rates, land prices and building values higher while crimping expansion or relocation plans of businesses left with few options to grow or set up shop in the region. The pressure resulting from this collision of factors (predicted by Scheer Partners since at least 2014) has been building during the past 18 months. Despite attempts by the industry to meet the demand for additional industrial space, vacancy is forecast to tighten through 2017 and will likely approach the record low vacancy rates. Montgomery County's industrial market has barely expanded in the last 10 years due in part to the expansion of regional infrastructure (residential and retail). The rise of activity has also placed further pressure on the already limited supply of existing industrial buildings available for lease.

TOTAL MARKET SIZE (SF)

14,415,374 SF

CURRENT AVERAGE RENTAL RATE

$11.77 PSF

VACANCY RATE

7.8%

The strong demand for industrial space, whether for lease or sale, by investors and developers (as well as tenants and owner-occupiers) has resulted in landlords' asking rental rates expectations being met. This has resulted in even more competition for industrial assets and, more importantly, development sites, leading to higher prices and greater cap rate compression throughout the market. Historically, owner-occupiers were generally willing to pay more to acquire industrial assets as they were less likely to seek the returns necessary for an investor to justify an acquisition. Due to rising rental rates and the increases in strata pricing now being achieved, investors are justifying the high costs of acquiring industrial property for redevelopment. This has led to developers, particularly in core industrial markets, to acquire sites to develop multi-story mixed-use buildings, such as the Greencourt Innovation Center on Parklawn Drive.

Projects in Rockville currently command the highest pricing for non-typical industrial developments (which often include extra density with flex office and showroom space) as developers seek to capture the higher rents and the pricing these units can command. Boosting the efficiency of industrial space and the industrial land remaining will be a key focus of industrial users and developers moving forward. The expense and difficulty of securing new or expanded premises will also force owner/occupiers and tenants to make the most of the space they have, and perhaps curtail growth in order to remain in their current space. While a strong industrial market is a characteristic of a strong economy, near-record-low vacancy and rising prices for buildings and land can start to slow business expansion, force companies to relocate outside our core markets or limit new companies from entering the market in the first place. With vacancy continuing to tighten and rental rates rising in 2017, the county's industrial market is facing its first test at the start of a new era where the constrained supply of costly industrial land is beginning to impact market fundamentals, and where new supply cannot be delivered in a timely enough fashion to boost availability or meet demand. The next steps will require some political risk and a nuanced approach to industrial development that the market has yet to embrace.

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