

# Seattle Industrial

The Puget Sound region’s industrial market saw the vacancy rate inch up to 3.3% compared to the 3.0% at year end. The quarter saw delivery of 570,606 s.f., while absorption was a negative 457,147 s.f. This was surprising considering the high level of leasing activity that has occurred over the past seven-plus years. The consensus is that this was just an anomaly due to timing. During 1Q 2018 there were over 1.1M s.f. of leases signed, but most will not be moving into their new spaces until the second quarter, so we expect the vacancy to remain in the 3% and 4% range. Construction activity is still quite robust with 24 projects totaling 6.1M s.f. underway. Another 15.3M s.f. is in the pipeline, with the bulk of these in Pierce and Thurston Counties. Looking ahead, there isn’t much cause for concern as all economic indicators still point to a healthy local economy.

The Northwest Seaport Alliance reports strong volumes at the ports. Total container volumes grew 6% in February 2018 compared to February 2017. Total international container volume was also up 7.4%. Breakbulk cargo volume grew 29.7%. The only continuing declining trend is the auto volume, down 8%.

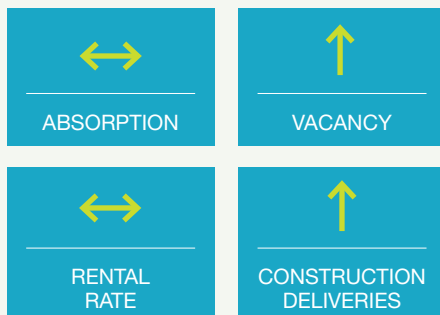
The region’s employment continues to perform well. Year-over-year growth (February 2017 to February 2018) grew by 3.1% (nearly 65,000 jobs). The key sectors that have an impact on the industrial market include Construction (+9,200 jobs), Transportation & Warehousing (+2,500 jobs), and Wholesale Trade (+1,300 jobs). These gains helped offset the continuing decline in Manufacturing (-5,700 jobs). The Puget Sound Economic Forecaster’s 1Q 2018 report projects employment growth of 2.3% in 2018 and 1.4% in 2019, compared to their prior projections of 2.0% and 1.2%. Wholesale & Retail trade is expected to grow by 7,100 jobs followed by Construction at 3,200 jobs, and Transportation at 1,600

jobs. Manufacturing is expected to lose another 3,300 jobs, primarily in Aerospace. Looking at key employers, Microsoft has been discussing plans to grow their campus in Redmond, while Amazon’s search for HQ2 has led to a potential local hiring slowdown. On the Boeing front, production continues, especially for the 737. There are concerns that President Trump’s steel and aluminum tariffs could hurt a manufacturer such as Boeing who relies on these for their plane production. However, much of Boeing’s metal is domestically sourced and the effect on plane cost is minimal. On the flip side, China has made up a huge amount of Boeing’s recent orders. They could decide to retaliate against the U.S. if tariffs are implemented and shift some of their orders to Airbus, which would not be good for our economy.

Sales activity in 2017 totaled 204 transactions totaling \$998.8M compared to 250 sales and \$1.46B in 2016. Sales activity in 1Q 2018 was active with 59 sales totaling \$362M. The average cap rate on sales in the quarter was

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### Market Forecast Trends



### Market Up Close

6.1M s.f. currently under construction

Another 15.3M s.f. in the pipeline

The majority of the buildings in the pipeline are in Pierce and Thurston Counties

Rental rates continue to increase in most markets and holding steady in others

The Northwest Seaport-Alliance reports February volumes are up over prior year results

# Area Review

## Seattle CBD / Surrounding Area Review

The Seattle close-in market vacancy remains below 2%, but did inch up from 1.5% to 1.6% due to negative net absorption of 59,018 s.f. Despite the small rise in vacancy, tenants are still challenged to find space and many have had to look elsewhere. One project, Prologis Georgetown Crossroads (589,615 s.f.), is under construction with an expected 3Q 2018 delivery. One of the largest sales to occur in the region was the former Sears Merchandise Building that sold for \$42M (\$179/s.f.). The buyer was Terreno Realty Corp. The Lam Building also sold for \$8.0M (\$310/s.f.) to KN Holding LLC.

The forecast for the Seattle close-in market for the next six months is for lease rates to see some increases, ranging from \$0.90 to \$1.60/s.f./month, NNN for medium- and high-grade buildings. Overall, average asking rent increased from \$1.06/s.f. to \$1.09/s.f., blended. Demand for sale properties continues to remain high with a very limited supply. Better quality buildings will sell between \$180 and \$300/s.f. When available, depending on size and whether it is paved, graveled, and fenced, yard rates will vary from \$0.18 to \$0.25/s.f. going south to north.

## Eastside Review

East King County, which has a high concentration of flex buildings, saw a steady level of activity on the leasing side, with the majority of new leases and renewals under 10,000 s.f. Similar to the Seattle close-in market, tenants have been extremely challenged to find suitable spaces. Overall, vacancy held steady at 3.2%. With no new projects under construction, the market will continue to see low vacancies. Not surprisingly, the average asking rent on a blended basis (warehouse/office combined), increased from \$1.31/s.f. to \$1.35/s.f. On the sales side, Interpoint Corp in Redmond sold just prior to the end of 2017 for \$20M (\$277/s.f.). Crane Electronics was the seller and Menlo Park the buyer. RD Totem Auto 2018 LLC purchased Building A at 13209 NE 126th Place in Kirkland for \$7M (\$245/s.f.).

The forecast is for NNN warehouse lease rates with high-bay warehouse manufacturing space to range between \$0.70 and \$1.00/s.f./month, with most in the \$0.75 to \$0.95/s.f. range. In some markets such as Bellevue, the rate is pushing closer to \$0.95/s.f. and above. Office rates are in the \$1.40 to \$1.65/s.f. range. Flex space rents to range between \$1.00 and \$1.40/s.f./month, NNN. Building sale prices are between \$170/s.f. to \$220/s.f. of building area for industrial (owner/users at the high end), and over \$200 to close to \$300/s.f. for flex properties. Land prices will run from \$15 to nearly \$40/s.f. for a premium site, although there is a limited amount of available land ready for development.

## South King County Review

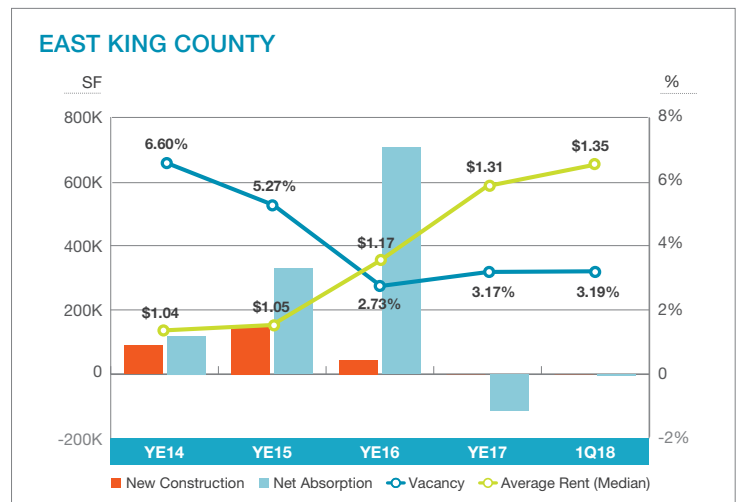
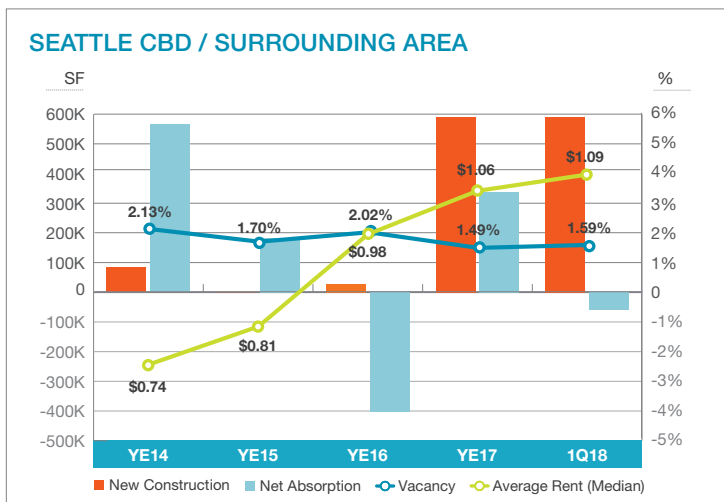
The South King submarket also saw their vacancy rate increase from 3.4% to 4.0% on negative net absorption of 393,863 s.f. We do note that nearly 573,000 s.f. of space has been leased, with tenants slated to move-in within the next few months. Notable leases in the quarter include Volvo Aero Services Corp (238,121 s.f. at Kent North Corporate Park), and Hydro USA (70,496 s.f. at Hill Investment-Space Center Building). Development continues to be active, with Seattle Gateway Center 1 & 2 (458,490 s.f. combined), DCT Hudson Distribution Center (287,832 s.f.), Des Moines Creek Business Park Phase IV Buildings A & B (514,121 s.f.), North Auburn Logistics (261,553 s.f.), and 234 Distribution Center (125,400 s.f.). There was one delivery this quarter, CenterPoint Kent 167 (220,800 s.f.), which is fully leased. Sales activity included KWDC 168 Holding purchasing the Electrical Distributors Building in Tukwila for \$7.9M (\$157/s.f.), and Terry LLC acquiring 1820 West Valley Highway for \$6,920,000 or \$105/s.f.

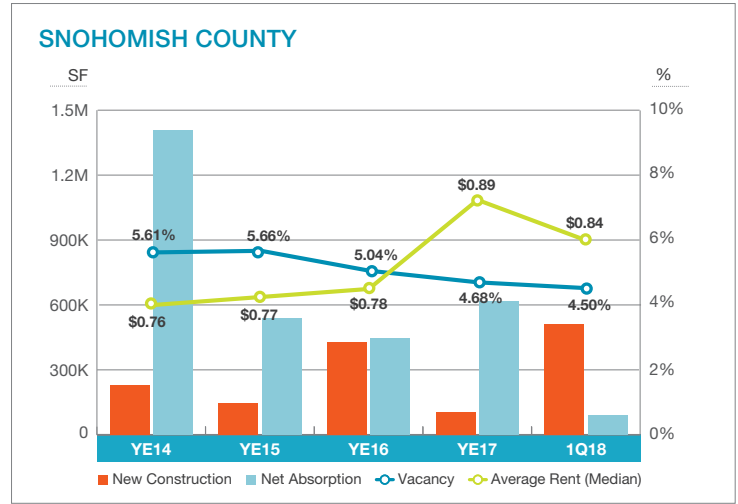
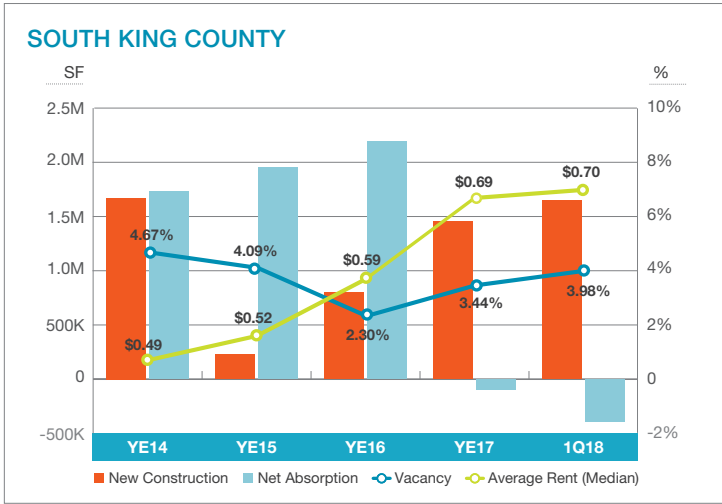
Average asking rents (blended) continue to climb, now at \$0.70/s.f., \$0.01/s.f. higher than last quarter. For smaller spaces (under 10K s.f.), shell rates range from \$0.45 to \$0.60/s.f.; \$0.42 to \$0.45 for spaces between 10K s.f. and 20K s.f.; and \$0.36 to \$0.45 for spaces larger than 20K s.f., depending on age and quality. Newer properties are at the upper end of this range. Office add-on rates vary from \$0.75 to \$0.95, depending on age and quality of the build-out. Building sale prices are expected to range from \$110 to \$160/s.f. Land values will range between \$14 to \$19/s.f. for fully improved sites, with higher prices further north.

## Snohomish County Review

Over the past year, Snohomish County has seen an increase in activity on leasing, sales, and development. On the development side, Dermody Development's LogistiCenter @ Woodinville Buildings A & B broke ground in Maltby. The two-building project will total 409,500 s.f. Seaway West Building A in south Everett (64,781 s.f.) is scheduled to be completed next quarter, as is Leifer Industrial Park 2 (37,363 s.f.). Also, GS Venture Partners just announced that their Gayteway Business Park, a 54-acre development of the former Northwest Hardwoods and Weyerhaeuser log mill site in Arlington, is pad ready for a 300K s.f. industrial building. Up to 1.0M s.f. is planned. The market's vacancy rate dropped from 4.7% to 4.5% due to positive net absorption of 92,166 s.f. One notable lease was Premier Fixtures (153,350 s.f.) taking space at Everett Technical Park II.

There were several larger sales. Merrimack Pharmaceuticals acquired the former Berlex Laboratories in Lynnwood for \$45.4M (\$480/s.f.). Sanofi-Aventis US LLC was the seller. Lake Tye Business Campus in Monroe sold for \$30.4M (\$161/s.f.). Sterling Realty Organization was the buyer. This





also included some vacant land. Red Hook Brewery also sold for \$24.5M (\$190/s.f.). The buyer was Cowen Partners LLC. The Wesmar Building in Woodinville sold for \$13.2M (\$160/s.f.). Northwest Building LLC was the buyer and Inco Properties, the seller.

Average asking rental rates dropped to \$0.84/s.f. from \$0.89/s.f. The forecast over the next six months is for warehouse lease rates to range between \$0.60 to \$0.70/s.f./month, NNN in the closer-in submarkets and lower (\$0.50 to \$0.55/s.f.) in the outlying markets. Office rents are \$1.25 to \$1.35/s.f. for second generation space and \$1.35 to \$1.40/s.f. for new space. Building sale prices are predicted to range from \$140 to \$170/s.f. for buildings in the 5K to 20K s.f. range; \$115 to \$150/s.f. for buildings in the 20K to 60K s.f. range. Flex space will be higher (over \$200/s.f.). There is a lack of larger buildings offered for sale in the market. Land values should range from \$5 to \$12/s.f. with an ample supply of industrial-zoned sites, particularly up north in Arlington and Marysville.

### Pierce County Review

Pierce County's vacancy rose from 2.2% to 2.7%, with negative net absorption of 79,714 s.f. in the quarter. The County remains very active on the construction front with 11 projects totaling 3,351,019 s.f. or about 55% of the total for the region. Development hot spots include Port of Tacoma/Fife, Puyallup, Lakewood, and DuPont. One project, Prologis Park Tacoma Building D, was completed (319,806 s.f.) and is 100% leased, including Tiger Logistics who leased 160,000 s.f.

Sales activity was modest. The largest was the \$60M purchase of DuPont Corporate Center by CRG Investments. The center includes an existing

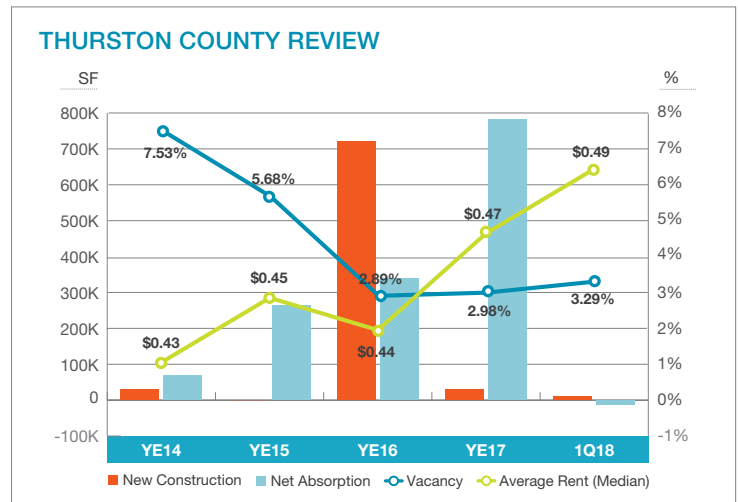
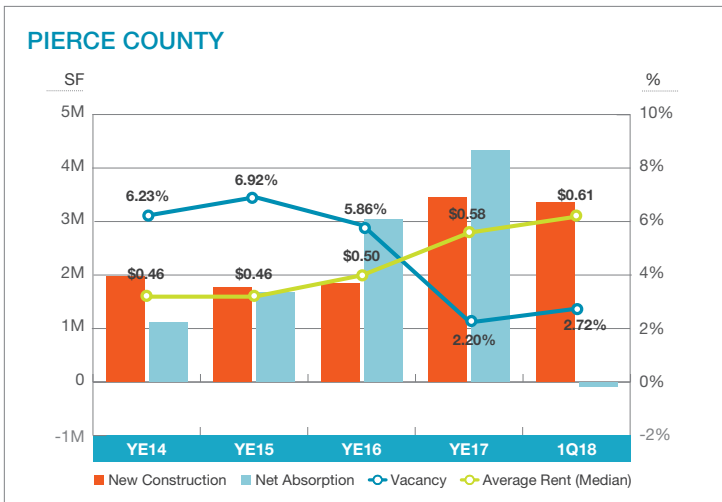
340K s.f. facility that will undergo extensive capital improvements plus adding 1.6M s.f. of new product. Bixby Land Company also acquired the recently built Cummins NW building in Sumner for \$18.75M (\$336/s.f.) from Panattoni.

Pierce County's forecast is for shell rates to range between \$0.35 to \$0.55/s.f./month, NNN, plus add-on office rates of \$0.70 to \$0.95/s.f./month. Industrial building sale prices will range from \$50/s.f. for older buildings to \$100 to \$140/s.f. for new or smaller buildings. Land values typically range between \$10/s.f. and \$16/s.f.

### Thurston County Review

Thurston County saw its vacancy rate increase from 3.0% to 3.3%. There was one delivery of 30K s.f. along with negative net absorption of 11,452 s.f. There is one project (10K s.f.) under construction. On the leasing side, Walmart leased 40K s.f. at Medline Distribution Center. With an abundance of land, the County has a substantial amount available for development. Currently, there is nearly 5.3M in the pipeline with a potential of about 2.4M s.f. that could start in 2018. Average asking rents increase from \$0.47 to \$0.49/s.f.

Shell rents are ranging between \$0.38 to \$0.40/s.f. on larger spaces and office add-on rates between \$0.75 to \$0.90/s.f. Smaller spaces are \$0.45 up to \$0.55/s.f. on the shell with office add on at \$0.85 to \$0.90/s.f. Building sales are expected to range from \$50 to \$100/s.f. Land values range between \$4.00 to \$7.00/s.f., with some smaller lots being offered at up to and over \$8.00/s.f.



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5.5% compared to 6.42% in 2017. There were several notable sales in the quarter, including the off-market sale of the former Sears Merchandise Building in South Seattle selling for \$42M (\$179/s.f.). DuPont Corporate Center sold for \$60M and represents an extensive renovation of a 340K s.f. facility and will add 1.6M s.f. of new product. Lake Tye Business Campus in Monroe sold for \$30.4M (\$161/s.f.). The Red Hook Brewery sold for \$24.5M (\$190/s.f.). Berlex Laboratories in Lynnwood sold for \$45.4M (\$480/s.f.). Interpoint Corp in Redmond sold just prior to the end of 2017 for \$20M (\$277/s.f.).

On the nationwide side, The Blackstone Group acquired a 22M s.f. portfolio from Cabot Properties totaling \$1.8B. Included in the portfolio were several properties in the region: Puyallup West Distribution Center, Cabot Commerce Center (Tacoma), Federal Way Corporate Center, Lakewood Corporate Center, Building B, and 31 Sound Tire in Auburn.

## Vacant Space / Vacancy Rate

A total of 507,606 s.f. was delivered in 1Q 2018. With negative net absorption of 457,147 s.f., the region's vacancy increased by 31 bps from 3.0% to 3.3%. With several signed leases that have not yet occupied space, absorption should be positive in the next quarter.

## New Construction Activity

There are 24 buildings totaling 6.1M s.f. now under construction, with only about 5% of this space pre-leased or owner-user facilities. Pierce County once again is the most active at 3,351,019 s.f. (11 projects), followed by South King with 1,647,396 s.f. (seven projects). Seattle Close-in has one project (589,615 s.f.), and Snohomish County is also active with 511,644 s.f. (four projects).

## Rent Forecast

Rental rates over the past three months saw an increase in five of the six markets. Overall, for the region, the average asking rental rate has held steady.

## Market Demand/Absorption

As noted above, absorption was negative at 457,147 s.f. for the quarter. Only Snohomish County saw positive results at 92,166 s.f. All of the markets did see a good level of leasing activity with many move-ins expected to occur in the next quarter.

## Development News/Significant Transactions

Notable projects under construction include:

- Panattoni's Lakewood Tacoma Gateway (467,526 s.f.); expected delivery 2Q 2018
- IPT Tacoma Logistics Buildings A & B (286,525 s.f. & 837,620 s.f.); expected delivery 2Q 2018
- DCT Blair Logistics Buildings A & B (542,750 s.f. & 428,228 s.f.); expected delivery

2Q 2018 (Building A) 4Q 2018 (Building B)

- Seattle Gateway Center 1 & 2 (325,290 s.f. & 133,200 s.f.); expected delivery 2Q 2018
- Prologis Georgetown Crossroads (589,615 s.f.); expected delivery by 3Q 2018
- Des Moines Creek Business Park Phase IV Buildings A & B (514,121 s.f.); expected delivery by 2Q 2018
- North Auburn Logistics (261,553 s.f.); expected delivery 2Q 2018
- LogstiCenter @ Woodinville Buildings A & B (275,500 s.f. & 134,000 s.f.); expected delivery 4Q 2018
- DCT Hudson in Auburn (287,832 s.f.); expected delivery 3Q 2018
- The Viking in Pierce County (438,065 s.f.); expected delivery by 2Q 2018
- Gayteway Business Park in Arlington is ready to move forward with 300,000 s.f.; a 12-month construction period is projected

Notable Sales over \$20M include:

- DuPont Corporate Center sold for \$60M; buyer is CRG Investments; seller is Fortress Investment Group LLC
- Former Berlex Laboratories sold for \$45.6M (\$480/s.f.); buyer is Merrimack Pharmaceuticals, Inc.; seller is Sanofi-aventis US, LLC
- Former Sears Merchandise Building sold for \$42M (\$179/s.f.); buyer is Terreno Realty Corporation; seller is Marx-Realty & Improvement Co., Inc
- Lake Tye Business Campus sold for \$30.4M (\$161/s.f.); buyer is Sterling Realty Organization; seller is Rudeen Development
- Red Hook Brewery sold for \$24.5M (\$190/s.f.); buyer is Cowen Partners, LLC; seller is Redhook Ale Brewery, Inc.
- Interpoint Corp in Redmond sold for \$20M (\$277/s.f.); buyer is Menlo Park; seller is Crane Electronics

Notable leases include:

- Volvo Aero Services (238,121 s.f.) at Kent North Corporate Park Building D
- Tiger Logistics (160,000 s.f.) at Prologis Park Tacoma Building D
- Premier Fixtures (153,360 s.f.) at Everett Technical Park II

Data Source: CoStar