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2024: THE OPPORTUNITIES & CHALLENGES IN UK WAREHOUSING

“Need pallet space?”, “Ready now”, “Best pallet storage quote”, “Find warehouse space fast”. It feels like only yesterday that warehouse take up was at an all-time high. Yet now, cheap and rapidly available warehouse space seems to be everywhere.

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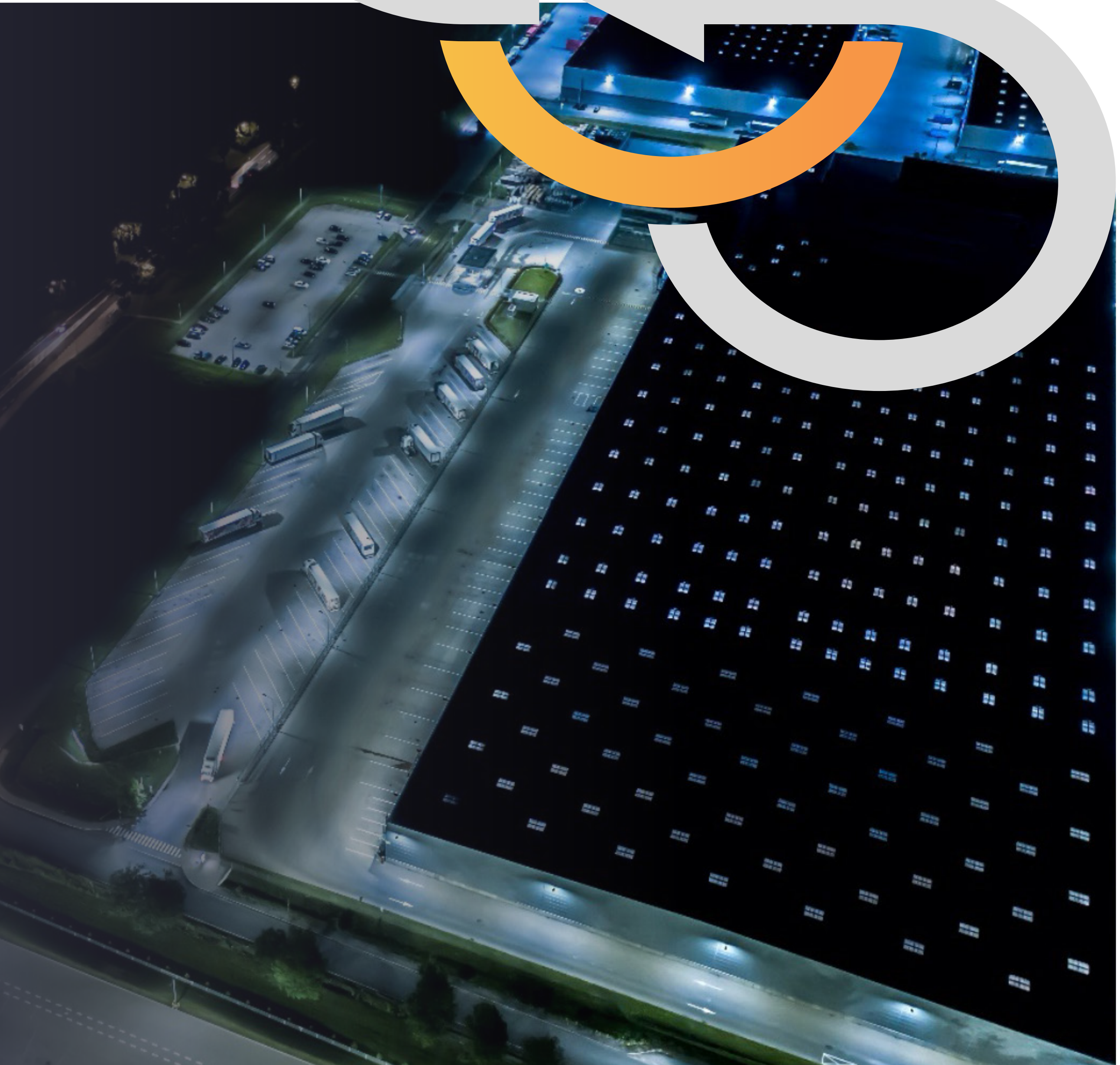

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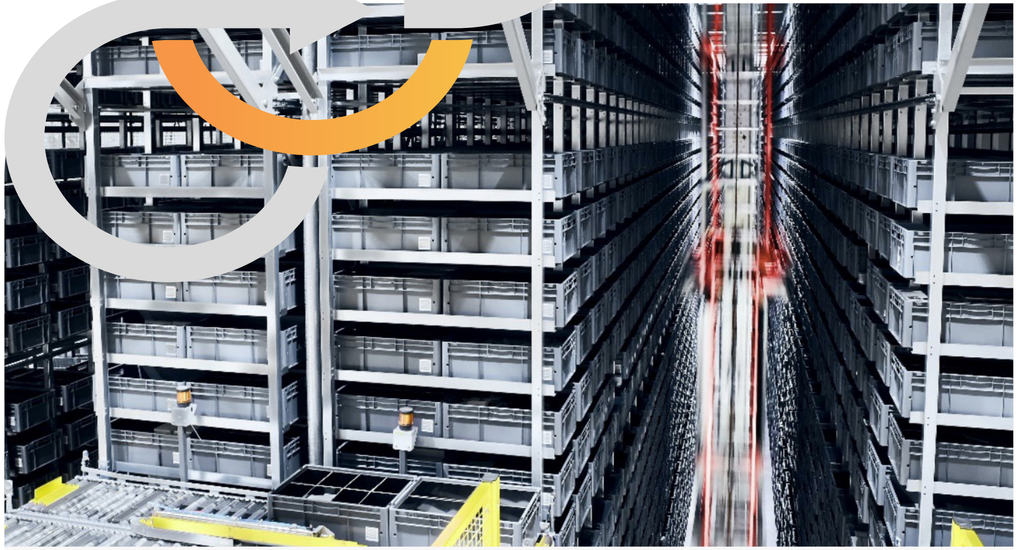
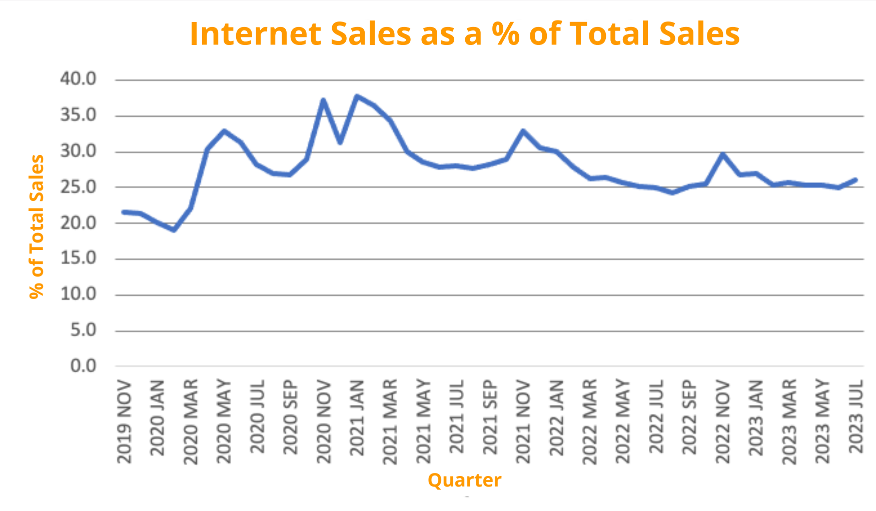
WHAT'S HAPPENED?

Before and during the Covid-19 pandemic, several factors were driving the demand, and, with it, warehouse rental rates.

- Firstly, we experienced the impact of Brexit on UK stockholding and increases in Hard Brexit contingency inventory.
- Next, the huge effect the pandemic and lockdown had on online sales added to the surge in demand for warehouse space. Developers were building warehouses throughout the country and almost all speculative builds seemed to be snapped up before completion, sometimes even before building started. Demand was clearly outstripping supply.
- But, with economic headwinds gathering pace, we're now experiencing lower take up rates, similar to pre-pandemic levels. Commercial real estate firm #Colliers has reported that Q2 2023 was the weakest quarter for logistics property take-up since 2017.
- We're also seeing a reduction in speculative development. The heady days of online sales growth driven by the pandemic have gone. Combined with the increases in the costs of building materials and the cost of finance, it's not surprising to see developers' confidence reduce.
- As we can see from the graph, below, (ONS Internet sales as a % of Total Sales) the proportion of online sales has dropped significantly from the pandemic peak of 37%, settling at 25% of the total sales.





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WHAT'S CHANGED?

- Following the planning for a "hard" Brexit, from 2016-2019, where many organisations increased contingency stocks, much of the early stock builds have been reduced as businesses adapt to the new trading conditions. Post-Brexit trading has seen many UK businesses acquiring facilities on mainland Europe with a commensurate, although lower level of incoming investment.
- As lockdown ended and the effects of the pandemic eased, shoppers began returning to the High Street, reducing the demand for further online fulfilment capacity. The additional impact of a likely economic downturn has also affected confidence; in February this year Ocado decided to pause the building of new warehouses and subsequently announced the closure of their long serving Hatfield facility. In January this year, even Amazon, traditionally a bellwether for the health of online sales, announced the closure of three of their fulfilment centres.
- As warehouse rents increased through the pandemic, many businesses sought to optimise their inventories and supply chain networks, eliminating surplus space where feasible. Sainsbury/Argos announced the closure of two of their facilities earlier this year, for example.
- Another pandemic-related impact is still being worked through. The massive stockbuild of Personal Protective Equipment (PPE), required through the pandemic is being managed down. At the moment, circa 750,000 pallets of PPE have been removed from the NHS's network, donated, recycled or otherwise processed. This volume alone equates to 10-15 reasonably sized distribution centres and it's likely that there is a similar amount being considered for disposal during 2023-2024. Those facilities that have held significant volumes of PPE since mid-2020 will now need to secure different customers.

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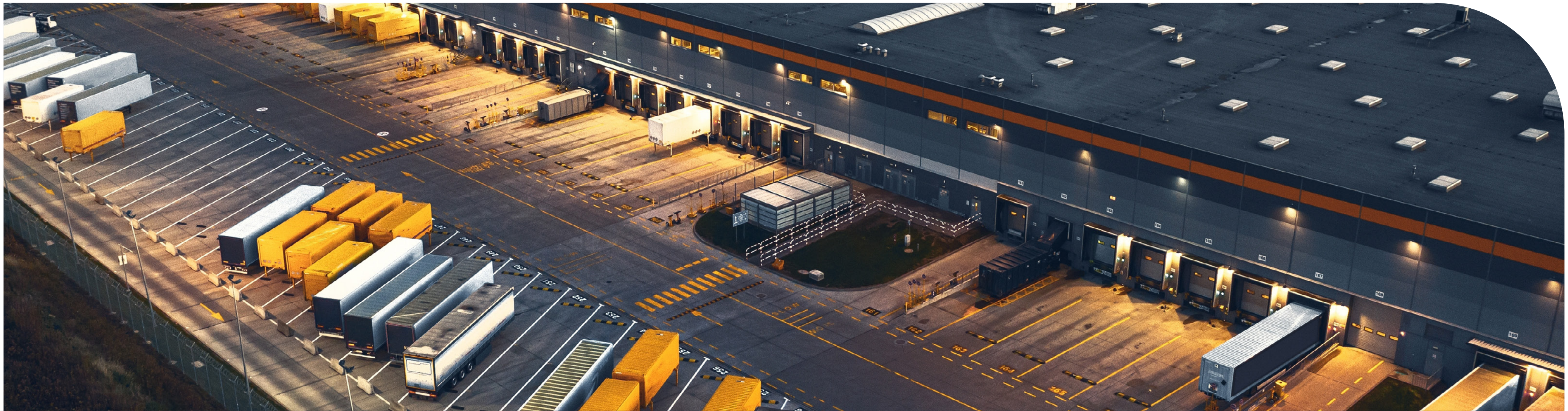
WHAT DOES THIS MEAN?

We're now experiencing a slowdown in rents.

- #Colliers says that, according to data from MSCI, warehouse rents increased by 1.8% in Q2 2023, contributing to a total increase of 3.7% in the first half of the year. Given that inflation has been hitting double digits for some months now, this suggests that the demand vs supply equation has shifted. In favour of the user. The ONS reports that the CPIH rose 6.4% in the year to July, 2023, putting a first half increase in rates of 3.7% into perspective.
- Additionally, leaseholders, including third party logistics providers, are understandably keen on securing users for their available space; in an extremely competitive market. As #Gerald Eve reports, sub-lets or assignments are now estimated to account for 10% of all availability, up from around 4% in Q4 last year. Clearly a significant shift that is predicted to continue this year.
- However, there is a further issue. Where possible occupiers are terminating leases when it is feasible, or, in some cases, becoming landlords themselves by offering their fully fitted warehouses on the "grey" market. Hence the plethora of "Need pallet space?" offers.
- One of the results of greater availability of warehouse space is the move toward premium warehouse space, particularly where ESG credentials are important. As Kevin Mofid at leading property agents Savills, reports, **"Much like the rest of commercial real estate, we are seeing occupiers place a greater emphasis on quality, with a particular focus on ESG. Environmental factors are becoming increasingly important, especially as businesses look to measure their Scope 3 emissions."**
- Simon Dixon, CEO at Hatmill also suggests there's another factor at play. **"Some of the older stock of warehouses with lower eaves heights are no longer good value for businesses seeking to minimise space costs. For automated operations, height is often a key factor when selecting a warehouse. Therefore we could see rents being based on cubic metres rather than footprint in years to come."**



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NEXT STEPS

Given the current market conditions vis a vis warehousing availability and rental costs, it is important for all involved to carefully consider their next steps

- For developers, it's clear that a focus on premium developments, particularly encompassing strong ESG elements, is the appropriate course to maintain a premium rent.
- As a user of warehouse space, whether you hold the lease yourself or are contracted with a 3PL, a pause and a serious review of options is required. If a lease or contract is coming to an end or a break clause is imminent, current market conditions impel you to consider your priorities and review your supply chain and network options.
- For peak storage or occasional overflow, it is worth exploring the grey market.
- Further consolidation of inventory and operations may well result in a significant saving in warehouse lease costs and could also improve the efficiency of the network. Simon Dixon comments that **"many organisations deferred any network reviews during the Brexit and COVID periods. We're now seeing businesses wanting to optimise their warehouses and transport networks which could see more sites changing occupiers."**
- It may be tempting to transfer your existing operation to a site offering lower rent. However, as Ian McRae, independent industrial and warehousing property expert advises, **"There are so many angles to consider with relocations and/or acquisition of additional premises, most of which could have substantial cost implications. Not all warehouse occupiers advertise the fact that they may want to offload a lease and therefore picking up the phone and asking if they might wish to exit has worked very well for some of my clients. With the increase in availability of accommodation, there are many warehouses that have been refurbished and are fully fitted, sometimes even with racking, thereby saving capex. Above all market knowledge is key to securing the best deal, in the best suited warehouse for your business."**

In summary, there are opportunities for occupiers and operators to review their options comfortable in the knowledge that there are now options available. Whatever position you are in, or about to experience, the message is the same. Before making any decisions, seek independent, impartial advice.

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