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OAHU INDUSTRIAL REAL ESTATE FORECAST

C. Mark Ambard, CCIM
Creating this presentation starts as an elusive process. Initially, the premise may be unclear.
Economy is gaining traction but it has been slow. Dropped off in 4th quarter. ACA? Every reason to have expected a solid recovery by now. Not yet. I think this one will be built on actual business recovery, growth and optimism rather than fiscal chicanery and money manipulation offering easy cheap money to borrow.
Uncertainty- holding back recovery though
Federal, state, private capital still not flowing freely to private market. Environmental responsibilities vs. Near term social needs to be considered
Rents moving up and down in a 10% tunnel for the past 4 years. Initial drop in 2008/2009 was fast. Trend is still flat for 2-3 quarters with respect to NOI.
Rents are going up, but prices still not moving because NOI is constrained by NNN increases. i.e. RPT, trash, management, electricity, WATER/SEWER!
But rent has upward bias on most any good news so prices will strengthen late in the year.
Fee sales are fueled by scarce inventory of land and fee properties as well as low interest rate environment. This will continue as development is constricted or corralled to TOD areas for political, not practical or profitable, reasons.
Private, market driven development will succeed.
Solar has supported the small contractor industry. Needs this support at least 2 more years. In the case of Hawaii, tax credits and subsidizing an emerging industry has been beneficial.
Unfortunately, saturation problems with HECO stripped the industry of work in 4th Q 2013. This should ease by summer as industry matures further.
Roofers have been innovative to get business. i.e. hail repairs in Kailua.
Construction recovery will come in waves First Kiewit size, then Nordic size, then the little guys who make up the vast market.
We will see them effect warehouse NOI late in 2014 into 2015.
If we avoid Black Swans locally and nationally.
The effect of ACA on small industrial businesses in 1& 2Q 2014 remains to be seen. GDP low growth expectations for 2014 will effect velocity of recovery not inevitability of recovery.

"The economy is better but not strong enough." The shoots are poking through the ground. How fast will they grow?
EASILY HALF AN HOUR WORTH

Renters
Lock in longest term at lowest rate you can right now.
Review and challenge NNN every year.

Investors/Owners
If your investment window is under 2 years- sell now.
- Low rates, low inventory and buyer interest offer best near term prices.
- Interest rates will inflate pushing down valuation from 2016 to 2018
- Values not offset by price inflation until 2017-19.

If your investment window is 6 years or longer- buy now.
- 2008 closed deal prices were about 10% higher than current asking prices.
- Interest rates are still at historical low
- Interest rate inflation in 2016-18 will batter paper values. Hold on!
- Growth and return on investment will take until 2020 to mature.
- Low rental inventory could support rents and investment through the value soft patch of 2016 to 2019.

If you have land and can build. Do it now. Rents will only go up. Costs are low and builders want work.

Land prices are strengthening on future income projections. Actual rents are lagging and will take at least 2 years to catch up with fee values. Once again, appreciation over income. The Hawaii way.

From Jay Elicker.
Here are the 4 deals closed in town:
- Wasa Electric purchased 3 acres at the Hawaiian Telcom Site for $13,900,000 ($106/SF)
- Royal Star purchased the 4 acres Foremost Dairy Site at 2277 Kam Hwy for $20,000,000 ($115/SF)
- REIT Management purchased 49,000 square feet at 889 Ahua St for $6,300,000 ($127/SF)
- Pacific Commercial Services purchase 1.46 acre site at 2200 Kam Hwy for $5,900,000 ($92/SF)
Upshot- Town Fee Industrial @ $100/psf

Here are 4 deals in Kapolei:
- Rengo Packaging purchased 8.5 acres at Malakole Industrial Park for $6,290,717 ($16.99/SF) (this was my deal)
- Road Builders purchased 4.49 acres at Malakole Industrial Park for $4,000,000 ($25/SF)
- American Pipe & Boiler purchased 3 acres on Kalaela Blvd for $3,497,000 ($26.50/SF)
- BCP Construction purchased 2 acres at Malakole Industrial Park for $2,178,000 ($25/SF) (this was my deal)
Upshot- Kapolei fee Industrial @ $25/psf

The tenants in Mapunapuna are in a bad situation. There are market deals that would suggest an 8% return and that pushes annual leasehold rents as high as $9 to $10/SF. Kapolei is still working itself out and trying to find where the market will be in the next year. Likely to strengthen.
Now get 10 minutes out of all this.
THEN EDITED TO 10 MINUTES

ALL THE WHILE LOOKING FOR THE CORE THESIS OR COMMENT
AFTER ALL THAT...
SOMETIMES THE PRESENTATION IS HANDED TO YOU

PACIFIC BUSINESS NEWS,
JANUARY 17, 2014

COMMERICAL REAL ESTATE

Prices will rise as industrial market strengthens

Honolulu's industrial market continues to strengthen with more space being leased out in 2013 and vacancy rates heading south to their lowest level in seven years, according to a new report.

Although there was negative net absorption (occupied space becoming vacant) in the fourth quarter of 2013, the year-to-date figure stood strong at 375,098 square feet, with a vacancy rate of 2.71 percent, according to the Cohn Year-end 2013 Industrial Market Report by Colliers International Hawaii.

“Strength in nearly every industrial sector and government initiatives leaves industrial real estate pricing with only one way to go — upward,” Colliers International Hawaii Vice President of Industrial Services Bill Frielich said in a statement.

The main reason for the sudden decline in vacancy rates is the reallocation of land by the state for the expansion of Honolulu Harbor facilities and Honolulu International Airport. It involves the relocation of tenants to private-sector industrial properties, boosting demand throughout the island for warehouse space, the report said.

Tightened market conditions are fueling competition for limited warehouse space and rents have begun to climb as a result with the number of available listings declining by 41 percent during the past three years, Colliers said.

In terms of rental rates, the average asking base rents for Oahu's industrial market rose for the second straight year and eclipsed the levels established in 2005.

During the past two years, rents have increased 7.9 percent to the current level of $9 per square foot per month and are projected to climb further as tenants face a shortage of available warehouse space.

Colliers International Hawaii predicts that Oahu's industrial vacancy rate will fall below 2.3 percent by the end of 2014.

The report noted that landlord concessions, which have been fairly limited to a few months of free rent, are disappearing.

Looking ahead, Colliers projects that Honolulu's island-wide industrial vacancy rate will continue to fall to below 2.3 percent by the end of this year.

Another strong year of occupancy growth and more than 300,000 square feet of new tenant growth will lead to tenants scrambling to find suitable relocation and expansion spaces. Colliers predicted rents are likely to grow by double digits as many urban industrial parks post vacancy rates below 2 percent.
PRICES WILL RISE AS INDUSTRIAL MARKET STRENGTHENS
I AGREE WITH THE HEADLINE WHICH CITES 3 REASONS FOR RISING PRICES (RENTS)

- Removal of State Owned Industrial Space From Industrial Market.
- Low Inventory Due To Reduced Development Activity.
- Anticipated Growth In Construction Industry.
BUT NONE OF THIS FORECASTS LONG TERM GROWTH

- Few new houses.
- Tourism is not booming.
- Solar and hail damage will not sustain recovery of construction industry.
STATE USE OF SHAFTER FLATS WAS LONG ANTICIPATED

- Major users found space replacements long ago.
- A number of businesses closed rather than move.
- They could not continue under a market rent business model.
SPACE IS AVAILABLE, JUST NOT ABUNDANT

- Business growth still relatively slow.
- Current spaces often not matching current users.
- Develop now if you can find land.
IF IT SERVES A PURPOSE FOR THE USER
EVERYTHING WILL LEASE
CONSTRUCTION
GROWTH TIERED
OVER THREE YEARS

1. Biggest players now creating infrastructure. Train, Kaka'ako & West Oahu Shopping Centers. 4-18 months.

2. Then we pour slabs, raise walls and frame roofs. 8-24 months.

3. Industry all in. Painters, flooring, plumbing etc. are fully engaged. 12-36 months.
AND...THERE IS MORE TO THE RENT STORY

- Rising rent does not always mean higher prices for property.

- Net Operating Income (NOI) and Capitalization Rate (CAP) derive value.

- Fees and Taxes affect the NOI. They are going up.
Rents are going up and so are NNN expenses.

Taxes, fees and services are all more costly.

Must control these to improve profitability.
THE 2014 INDUSTRIAL FORECAST

- Rents will go up. Tenants should lock in now.
- Land is gold. Get it now. Develop it now.
- Asset prices will rise when base rents strengthen to overcome NNN cost increases.
- Patience. The recovery will not feel like one.
- Net base rent will rise 5% later this year. Asset prices will follow.
- Industrial sector recovery must be built on actual business growth and sound public policy rather than fiscal chicanery, tax credits and policy manipulation.
- Then there is the inflation thing...... 2016?
THANK YOU

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