



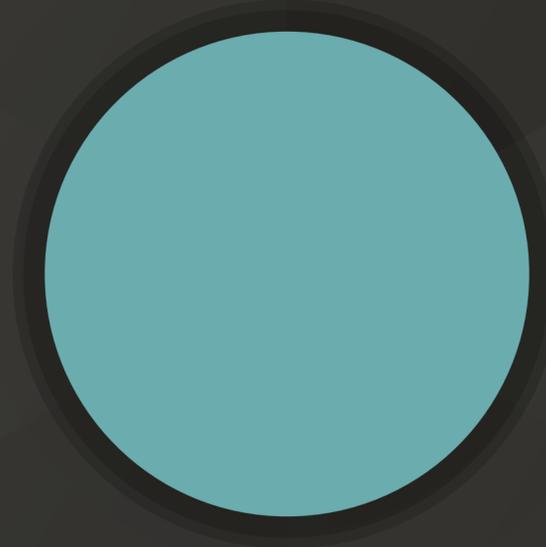
INDUSTRIAL & LOGISTICS

FUTURE GAZING

Gazing into the future is never an exact science. The magnitude, frequency and pace of change is often misinterpreted. Issues that grab the headlines often fail to materialise in the way envisaged, whilst other less sensational themes can often usher in a more profound and rapid transformation than anyone could rightfully have anticipated.

This is the inspiration behind Knight Frank's Future Gazing research.

Our intention is not to focus on a narrow set of established issues and simply add to the noise emerging from the crowd. Instead, we seek to map out the full landscape shaping real estate futures. For us, the depth and breadth of issues that could drive property market change are more important than the few themes currently winning the headlines. Good advice stems from the identification of, and mitigation against, those issues that reside in the blind-spot as well as the spotlight.



The following mind-map illustrates an extensive range of factors that will shape industrial property over the medium term. We have assessed each of these factors through two lenses – the potential speed at which they will become a market reality and the potential transformative impact of those issues in relation to current market orthodoxy.

This industrial and logistics mind-map shows that the complex interaction of technology, changing consumer and supplier behaviours together with an evermore challenging operating environment is recasting occupier demand. In response, the supply side of industrial property must equally be recast in terms of specification, location and the capacity to effectively accommodate a mix of human and technological resources on a flexible basis.

TECHNOLOGY

The emergence of new technologies will both disrupt and enhance the operations of industrial occupiers and the efficiency of supply chains. It is, however, easy to get swept away with the visions of a tech-led industrial utopia that is in such marked contrast to the current reality. Whilst the potential of automation, robotics, augmented reality and the internet of things are alluring, the reality is that the adoption of such technologies will not be as universal, seamless or rapid as many visions of the future often maintain.

This is not to suggest that technology will have no direct impact on industrial property. Rather, our view is that new technologies will be applied unevenly across the market – serving to bring competitive advantage to those who are able to make the necessary investments and have the required level of digital fitness.

We believe in a future where automation and robotics are an integral part of the industrial landscape and the operations of industrial occupiers. We witness at first hand the power of such technology in driving the operations of some of the titans occupying and utilising industrial space. We understand that technology is bringing dramatic change to the effectiveness of supply chains. But we stop short of seeing a future where rapid utilisation is universal.

Just like in the office sector, competitive advantage will come to those able to apply leading-edge technology. For the remainder, the application of technology will be a little more prosaic but no less significant. For example, the greater use of data and analytics to drive efficiency or enhance customer experience will be less capital intensive but arguably as powerful as the adoption of robotics and automation for many industrial occupiers.

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OPERATING ENVIRONMENT

Many industrial occupiers are seeing the economics of their operations fundamentally altered. For example, in responding to consumer demands retailers are faced with a supply chain challenge as the volume (and cost) of returns has expanded hugely. This is driving an increased focus on greater efficiency in an attempt to off-set heightened costs.

This difficult balancing act between responding to consumers and creating a cost-effective supply chain is occurring within a macro-economic environment which, whilst showing growth, is somewhat anaemic by historical standards. In such conditions all are playing closer attention to margins.

This poses a further problem. Cost sensitivity does not square well with a need to respond to greater technological input into industrial and logistics operations. A dilemma is at work within the sector. Should the focus be on careful cost management or on investing in the technology that can bring efficiency and effectiveness to operations? The answer to this fundamental question will be unique to each occupier. It is the key reason why we believe that the adoption of technology by industrial occupiers will be slower and less widespread than many suggest.

Technology will usher in a range of new challengers. Companies with access to data and digital platforms will change supply chain dynamics, for example, by selling spare capacity through e-brokerage platforms.

Although naturally longer-term in impact, the emergence of a broad confluence of policy agendas will also shape the operating environment for industrial occupiers. Industrial policy, planning policy, clean air legislation and regulation relating to drones are just some of the items that will shape the sector, although in ways that are as yet far from obvious.

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CLIENT/CONSUMER NEEDS

Emboldened by digital technology, consumers are making greater demands on the supply chain. Omni-channel retailing ensures that consumers seek almost instant gratification, increasing reputational risks to the retailer unable to meet these heightened expectations.

In response, the supply chain is required to work harder and faster to support the promises made by the retailer to the consumer for a positive, quick and trouble-free retail experience. As delivery options become more frequent and ever more rapid, the focus for retailers and their 3PLs is to excel at 'last mile' delivery.

Advances in manufacturing technology, coupled with increased consumer demand for differentiation, is supporting the increased customisation of products to suit individual requirements. This brings additional stress to supply chains as the 'batch of one' becomes reality.

It is not just consumers that are changing their focus and *modus operandi*. Significant changes are occurring within the supply chain itself. Traditional clients within the supply chain – specifically retailers – are themselves investing in their supply chain expertise; both for their own competitive advantage but perhaps longer term to provide a wider service to the market. The transition from client to competitor is a key dynamic of change within the industrial markets.

We will also see greater collaboration across the supply chain over the next five years, as traditional players realise and accept that the only way to achieve greater efficiency and maximise their capacity is to collaborate and share with those historically regarded as direct competitors.

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LABOUR SUPPLY

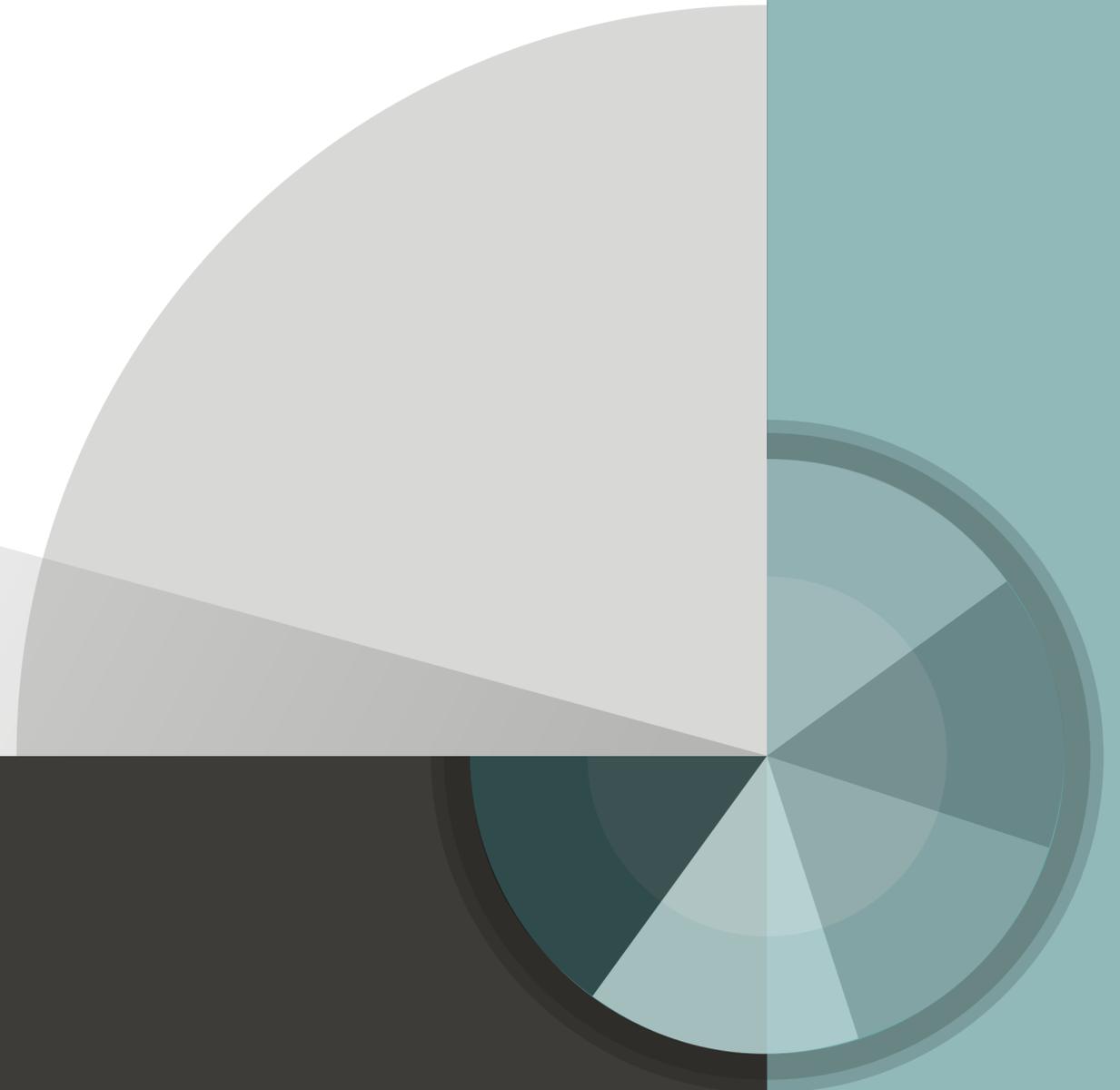
The key challenge facing industrial occupiers and determining the location of industrial assets over the last decade has been the availability of suitably skilled and priced staff. This dynamic will intensify over the next five years but labour needs will undergo change in both quality and quantum terms.

The short-term intensification of labour market challenges are a function of demographics and politics. The UK labour market is highly constrained at all skill levels with marked shortages of HGV drivers, for example. As Britain moves towards Brexit firms will no longer be able to rely on labour from the EU, but the tap is being switched off at a time when unemployment is at its lowest level in 42 years. As a result some firms will invest more in automation, robotics and AI to fill the gap.

In this sense two significant, but different, labour dynamics will begin to have greater influence within the sector. First, there will be demand for more technical and computer based skill sets as technology becomes a source of competitive advantage. This will place the industrial occupiers firmly in the war for tech talent raging across the entire economy. Second, the balance between human and technology based labour will be reset. There will be a steadily lessening reliance upon human labour and an associated reduction in the importance of labour in the industrial location decision-making process and hence the hot-spots for asset selection. Essentially, industrial location dynamics will change away from a strong focus on labour availability and towards more physical attributes such as power, resilience and connectivity.

In keeping with the wider economy, labour markets will also become more flexible and temporary, with the gig economy being heavily drawn upon to support last mile delivery strategies.

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LOCATION

The location of industrial property has historically been conditioned by the geography of infrastructure as well as land-use allocations by local authorities. Thus we have seen the heavy concentration of industrial property along key motorway routes and on the outskirts of urban centres.

This geographical fixity will be challenged over the medium term. The lessening requirement for human resources will be one contributory factor, but so too will be the importance of last mile delivery. We anticipate the continued rise of urban logistics facilities close to urban centres and, increasingly, within the context of mixed-use development schemes.

Longer-term, and subject to changes in land values, we may see retail warehousing becoming a preferred option for many industrial occupiers seeking to boost their ability to service urban markets through delivery services, but also as a means of extending their click and collect capabilities.

One thing is clear; land capacity will not increase. This will lead to greater innovation in the siting of industrial property. Although prone to sensationalism and easily dismissed as overly futuristic, there will be growing interest in both underground and underwater industrial facilities as a means of building much needed capacity.

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SPECIFICATION

Real estate product ultimately needs to reflect the requirements of the end-user. Whilst difficult to draw generalisations in the nature of industrial real estate product given the extent of change, there are some broad characteristics that will become more dominant.

The next phase of the industrial property cycle will be one where bespoke product will come increasingly to the fore. As technology takes hold in a variety of ways, there will be a divergence of occupier requirements that will be difficult to satisfy speculatively. As industrial real estate becomes more of a source of strategic and competitive advantage, occupiers will be prepared to work in partnership with the supply side and make long-term commitments to product that suits their operational requirements and has the required levels of future proofing.

The next phase of the cycle will also be one where industrial product shows a greater degree of design variance. It will be an age in which multi-user, multi-level and mixed-use product will become more commonplace as technology, land constraints and collaborative operational models are reflected in physical product. Industrial product will also be characterised by greater levels of security – physical security has always been a key requirement but with operations becoming underpinned by data and analytics, cyber security will be a concern with occupiers keen to mitigate reputational risk through disruption.

Finally, specification will continue to bring greater consideration to environmental issues and will become more self-sufficient via the greater use of solar panels and waste processing facilities – particularly as these environmental technologies become less cost prohibitive.

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