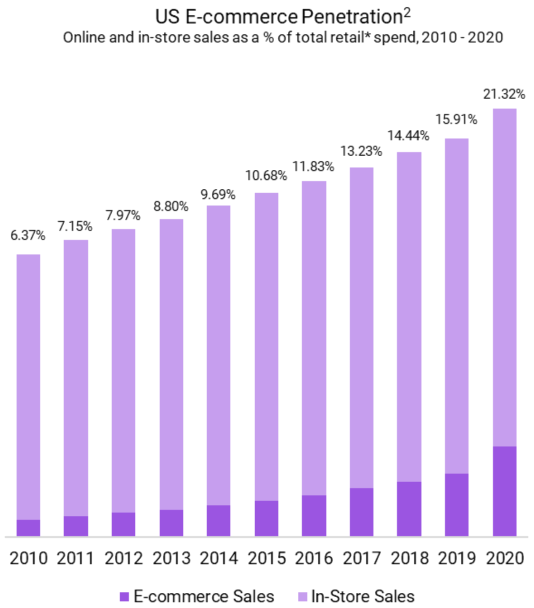
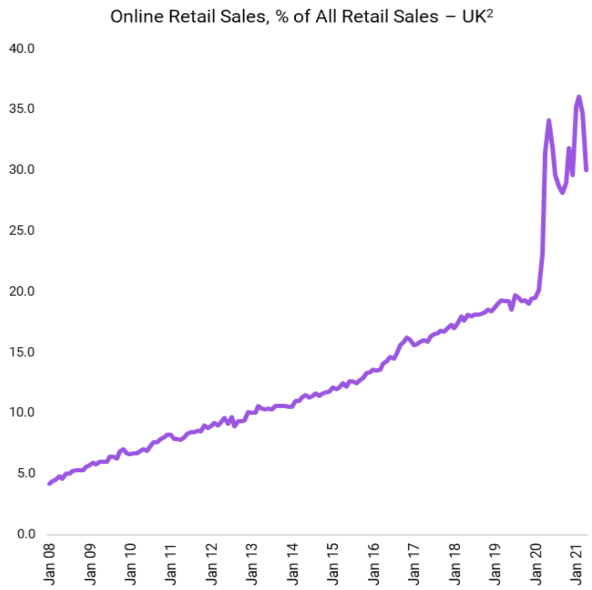
Logistics: ‘Fulfilling fulfilment’

Modern logistics buildings are among the key beneficiaries of the digital revolution, with the acceleration of technology and the internet transforming the way we live, work, and play.

Almost every aspect of our lives has been fundamentally changed, and these developments have prompted the decline of our dependency on many traditional sectors, such as shop front retailers. Online shopping, whether doing the weekly food shop, or finding the next gadget on AO.com, offers a level of convenience demanded by modern lifestyles. One barely needs mention that the outbreak of Covid-19 and subsequent public lockdowns acted as a propellant to growth for many online retailers. Between January 2020 and April 2021, online retail sales in the UK, as a percentage of total retail sales, grew from 19.5% to 30.0%, the equivalent of 3 years growth in just 15 months[1].





Amazon is by far the most obvious example of a business that has fully taken advantage of, and furthered, the shift to online shopping, putting its focus on ever-faster delivery times and expanding its product offering. To meet customer demand for next-day and same-day deliveries of anything from baby formula to Apple MacBooks, Amazon and other e-commerce retailers have focused their efforts on developing high-tech and well-located fulfilment solutions. However, instead of owning the property, they and many other e-commerce businesses are often the tenant, leasing space from a Real Estate Investment Trust (REIT) landlord.

In advanced warehouses acting as the storage and supply function for the biggest online e-tailers, ‘collaborative robot solutions’, known as ‘cobots’, now navigate a vast warren of shelving, picking stock and supplying the boxes to their human counterparts ready for packing.

These ‘cobots’ are just one part of the increasingly sophisticated generation of logistics real estate that has developed in recent years. No longer are logistics spaces used simply for storage, they are part of a complex supply chain solution, marked by increasing rates of automation. One of the most well-known REITs in this sector, Tritax Big Box, cites 54% of its assets as ‘automated’, an example being

[1] Office for National Statistics
[2] Digital Commerce 360 analysis of U.S. Department of Commerce data. *Total retail figures exclude sales of items not normally purchased online such as spending at restaurants, bars, automobile dealers, petrol stations and fuel dealers.
[3] https://datareportal.com/global-digital-overview

their c.£100m asset in Erith. Ocado, who are the sole tenant, have spent c.£200m on the 'cobot' and fulfilment technology inside the building.

Bolstered by the growth of the digital world and the grip of internet shopping, logistics centres are in increasing demand, with this coming in various forms. Modern logistics buildings are not uniform in size or purpose, the span of logistics real estate stretches from large 'big box' warehouses to much smaller urban warehouses.

A typical 'big box' could be more than 10,000 sq. m in size, roughly the size of a rugby pitch, with some, such as those located on the M1 near Milton Keynes, over 10 times larger. These vast spaces are generally located centrally and near motorway junctions, often filled with sophisticated fulfilment technology and serve as the storage and supply function for e-commerce.

Additionally, there is growing demand for smaller logistics warehouses, located within or near towns and cities, that offer a more immediate fulfilment option for retailers and customers than larger warehouses. The smaller urban warehouses face rising demand as the centres for 'last mile' distribution as the nation's appetite for next day – or even same-day – delivery proliferates. These smaller hubs enable e-tailers to be nimbler and provide products quickly to nearby homes.

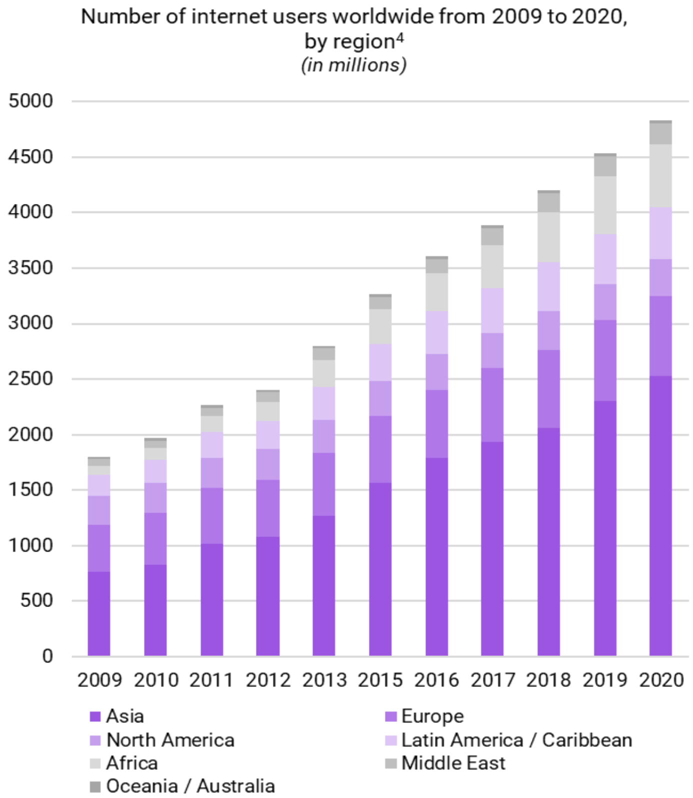
This increasing demand is matched by limited supply due to fierce competition for land for new urban hubs as the populations of cities continue to grow. Already, in areas of high urban density, it is possible to witness the odd spectacle of articulated lorries driving up ramps to the third or fourth floor of a distribution centre, as landlords develop solutions to increase the available space in constrained locations.

Digitalisation is creating a boom in demand for modern logistics space, with automation increasingly sought after, and competition for land increasing, there is likely to be consistent upward pressure on rental values. Specialist REITs which own these sheds, such as Goodman Group, Prologis, and SEGRO – likely investments for the VT Gravis Digital Infrastructure Income Fund –are therefore well-placed to benefit.

Gravis estimates that that average unexpired lease lengths of REITs in this sector is 5.9 years, with these long-term leases incorporating contractual escalators. Tenants tend to be relatively 'sticky', with occupier turnover low. In the event of a tenant moving out, the meaningful amount of money involved in moving from one location to another makes staying in place a far more appealing option for businesses; industry experts estimate the cost of relocation at £4 million per 100 sq. ft of warehouse space, not to mention the disruption. Equally, the level of investment required to automate systems to improve efficiency – such as the introduction of the 'cobot' – means many tenants are less likely to move and abandon the improvements they have put in place.

The REITs that own logistics real estate have delivered steady long-term income for investors and the last, difficult year has only served to entrench their value. These assets have become critical to society, thereby underpinning their income. That is however not just a recent phenomenon, rental sustainability has been a feature of this asset class for years. For example, Prologis, the largest global logistics REIT, has increased its dividend per share every year since 2013 and thanks to the growth of e-commerce, the rental income from their tenants has been steady and growing worldwide. The likes of Prologis offer big space at relatively affordable starting rents, particularly when compared to the high street and retail parks. As an added boost, many contracts incorporate contractual rental uplift or index-linkage.

We have previously explored the growth of digitalisation and shown that, powered by our insatiable habit for connectivity, mankind is driving a new industrial revolution. The last stop on the journey for each e-commerce interaction lies with the less glamorous, but ever necessary, function of fulfilment. The landlords of big warehouses are already in place and are expanding their estates to meet the growth we expect. Whether that is acquiring or developing big sheds in central locations, or smaller sites in more urban locations, the trend is heading in one direction. This is coupled with the increasing investment required by tenants to automate their fulfilment process and boost efficiency.



Exposure to specialist logistics REITs via the **VT Gravis Digital Infrastructure Income Fund** offers investors an opportunity for reliable income coupled with the potential for capital growth. With the global REIT market offering daily liquidity, these assets provide access to diversified returns from what is a growing, long-term trend shaping the future of life around the world.

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[4] https://www.statista.com/statistics/265147/number-of-worldwide-internet-users-by-region/