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MARKETS | PROPERTY REPORT

Blackstone Bets Big on Logistics

Deal to pay $1.5 billion for portfolio of logistics centers shows strength of e-commerce-driven business

The logistics sector's strength is being fueled by rising demand for space from Amazon.com and other Internet retailers. One of the company's distribution centers in Czech Republic *PHOTO: MICHAL KRUMPHANZL/ZUMA PRESS*

By **PETER GRANT**

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Private-equity giant Blackstone Group LP has cut a deal to pay $1.5 billion for a portfolio of logistics centers, in the latest sign that this e-commerce-driven business is one of the hottest areas in the commercial-property industry.

Blackstone, the world's largest private real-estate owner, has signed a contract to buy the 12 million-square-foot portfolio of mostly West Coast property from LBA Realty LLC, an Irvine, Calif.-based investment company with properties in the western U.S., according to people familiar with the matter.

Once closed, the deal will mark Blackstone's biggest purchase of U.S. distribution centers since it exited from the U.S. logistics business in 2015 by selling IndCor Properties for $8.1 billion.

Logistics properties typically include warehousing and distribution facilities for moving goods from manufacturers to stores and customers.

Investor demand for such real estate has shown unusual resilience during what many analysts and investors consider to be a late stage of a bull market for commercial property. Prices keep rising even as those in other commercial-real-estate sectors, such as office buildings and malls, have shown signs of cooling.

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>
> —Charles Sullivan

Executives at logistics companies say their businesses are benefiting from the growing importance of distribution in retail and other industries. Increasingly, business profitability is being determined by the efficiency, speed and costs of moving goods, they say.

Some businesses, like retailing, are being completely transformed by distribution as consumers migrate online, cutting out the need for bricks-and-mortar stores. Many mall owners have suffered while owners of logistics properties have been the big winner from this trend.

"Distribution used to be just another part of the supply chain," said Charles Sullivan, president of U.S. operations for Global Logistic Properties Ltd., the second-largest owner in the U.S. sector. "Now logistics has moved up in its importance in corporate strategy."

Big private-equity firms like Blackstone and foreign investors such as Singapore's GIC Pte. Ltd. and the Abu Dhabi Investment Authority have been among the most recent

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investors. Meanwhile, other investors such as private-equity giant TPG, LBA and Ross Perot Jr.'s Hillwood Development Co. have been responding by putting logistics portfolios on the block. Hillwood sold a $1.1 billion portfolio earlier this month to Singapore-based Global Logistic, whose major shareholders include GIC.

Stock investors also have been bullish. Big public logistics companies such as Prologis Inc. are trading at a premium of about 7% to the value of their properties, according to analysts. Companies that own other properties like malls, office buildings and hotels are trading below asset values.

The logistics sector's strength is being fueled by rising demand for space from Amazon.com Inc. and other Internet retailers. Rents and occupancy rates are rising beyond the expectations of many analysts and industry participants.

Net income of real-estate investment trusts that focus on logistics, warehouses and other industrial property is expected to rise 4.8% this year, more than any other property type except apartment buildings and self-storage, according to Green Street Advisors LLC. Last year, income in the industrial sector increased 4.5% versus the industry average of 4.2%.

Investing now could be particularly risky. An expected surge in new supply in several parts of the country—including the Atlanta and Dallas regions—could weigh on returns, analysts said, while the torrid growth of e-commerce could slow. Because of razor-thin margins and high delivery costs, online retail remains unprofitable or barely profitable for many companies despite its surging popularity.

But so far, demand growth from tenants is outpacing new supply, according to analyst Eric Frankel of Green Street. "In some markets there's meaningful new supply, but it's being absorbed very quickly," he said.

Investor appetite for logistics property began growing in the early years of the economic recovery and expansion partly because they expected online retail to grow. Also prices were low thanks to the pounding the sector took during the downturn.

As the economy strengthened, the sector was helped by improvements in the home-building and automotive industries, both heavy users of warehousing and distribution space. In some regions, other factors fueled demand, including marijuana legalization.

"In the Denver market, all the functionally obsolete space got absorbed by the marijuana industry," said Andrew Van Tuyle, chief acquisitions officer of BH Management Inc., which owns about 500,000 square feet in that market. "All of a sudden the vacancy for the overall industrial market became very low."

Changes in the online retail business also have fueled demand for logistics space. As Amazon and others began offering faster delivery, they began looking for so-called in-fill properties closer to population centers that were partly designed to process individual packages rather than pallets of goods bound for stores.

TPG spent about $300 million of equity capital to build a portfolio of about 16 million square feet of in-fill properties starting in 2014, which it named Evergreen Industrial Properties. Earlier this summer, the firm hired Eastdil Secured LLC and CBRE Group Inc. to sell Evergreen.

Blackstone was one of the early movers of the recovery in the logistics market. It built its IndCor portfolio through about 18 acquisitions, often buying buildings from distressed sellers like the Lehman Brothers estate. Blackstone cut a deal to sell IndCor to Global Logistic in late 2014.

Blackstone made its IndCor investment through one of its "opportunity" funds, which tend to make shorter-term, more highly leveraged bets in pursuit of higher returns. Its purchase of the LBA portfolio is through one of Blackstone's "core-plus" funds that typically uses less leverage and hold investments for longer periods of time, say people familiar with the matter.

Blackstone also owns 150 million square feet of logistics real estate in Europe that it accumulated during the recovery. The firm has been expected to try to sell it soon in an initial public offering but so far hasn't announced its plans.

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