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Site Selection Focuses on Second-Tier Markets

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As import activity surges ahead with rising transportation costs close behind, shippers big and small are reevaluating their warehousing and distribution strategies to maintain a competitive edge. While the prime markets such as Los Angeles, Chicago, and New York continue to pack them in (at a premium price), a host of second-tier markets are becoming more attractive thanks to new intermodal hubs and less-congested roadways, which offer reliable access to major populations centers.

The new kids on the block

When it comes to industrial real estate development, several trends are continuing to drive expansion. Containerized imports from Asia—which are pouring in at major gateways along the U.S. West Coast (primarily LA-Long Beach) and increasingly through major East Coast seaports—show no signs of letting up. But space is tight near the ports, and expensive, which means cities like Louisville, Kentucky and Nashville, Tennessee, along with eastern Pennsylvania, for instance, are seeing tremendous growth. In fact, logistics has now replaced manufacturing as the bread and butter for the warehousing and distribution and it's helping to

revive cities, particularly in the Northeast, that not so long ago were 'victims' of globalization, while giving new opportunities to areas in the Southwest that were once heavily dependent on agriculture, such as California's central valley.

According to global real estate developer ProLogis (www.prologis.com), eastern Pennsylvania has become one of the top four East Coast distribution centers. Along with a relatively short drive time to major seaports, the region has affordable housing, labor, and real estate, along with a highly educated work force, which has helped it attract a number of high-tech companies in recent years.

Sara Lee Corporation announced it June that it would construct a $24 million distribution center and regional customer service center on a 40-acre site in Pottsville, Pennsylvania. The company will also construct a 15,000 square foot, two-story office building at the site. The facility is expected to be up and running by October.

On the opposite side of the state, Seattle-based Recreational Equipment Inc. (REI) is building a 400,000 square foot distribution center in Bedford, about 250 miles west of Philadelphia. When it's completed next year, it will handle 40 percent of the company's total sales.

And earlier this year, Sears announced that it would lease a 1 million square foot, build-to-suit distribution facility in Lackawanna County to support its stores in Pennsylvania, New York, and New Jersey.

In the Midwest, Louisville, Kentucky, which boasts a major hub for UPS (www.ups.com) as well as a new 64,000 square foot service center for DHL (www.dhl.com) is another city that is attracting attention from shippers who want affordable, first-class distribution facilities with exceptional infrastructure and proximity to key markets. The Louisville International Airport is the tenth-largest air cargo airport in the world and the city sits within 600 miles of two-thirds of the U.S. population. Rail carriers CSX (www.csx.com) and Norfolk Southern (www.nscorp.com) serve Louisville and the city is located near interstates 64, 65, and 71. Aside from UPS, automakers Toyota and Ford and GE

Consumer Products are some of the major employers.

Kansas City's SmartPort (www.kcsmartport.com) is another example of how import trade is supporting warehousing and distribution growth in the nation's interior. The development is designed to serve multiple corridors—inbound from the West Coast, East Coast, or NAFTA corridors—and does so by rail, truck, air, and inland waterway. It's also got the most space devoted to foreign trade zones than anywhere else in the U.S.

In May, The Allen Group (www.allengroup.com) announced that it had finalized land purchase rights with BNSF (www.bnsf.com) for the development of the Logistics Park-Kansas City intermodal rail hub, which is slated to open in 2009. Meanwhile, KC Southern rail (www.kcsouthern.com) has 1,300 acres, which is being developed by CenterPoint (www.centerpoint-prop.com) for a logistics park that will target freight from Mexico. In addition, the Kansas City International Airport (www.flykci.com) is one of the largest available land airports in the country and has selected CB Richard Ellis (www.cbre.com) to develop about 700 acres of that for distribution. Some of the well-known retailers who have facilities there include American Eagle Outfitters, Target, Wal-Mart, and Lowe's.

Although manufacturing jobs are dwindling in many states, in Indiana nearly one-third of the state's economic output is tied to manufacturing and logistics combined. The Indianapolis International Airport is also home to the second-largest FedEx (www.fedex.com) hub in the world. Europe's largest air cargo carrier, Cargolux, has a gateway there too and has added non-stops flights from Europe. However, you don't earn the title "Crossroads of America" without having a highway system worth boasting about, and Indianapolis certainly does. Seventy-five percent of all businesses in the U.S. are within a one-day's drive from the city and more interstate highways intersect in the Indianapolis region than anywhere else, including interstates 65, 70, 74, and 465.

The other benefit of second-tier markets is sheer cost, which in the current environment is all the more important given that rising fuel prices have put transportation, logistics, and distribution under the microscope. Simply put, industrial real estate is considerable cheaper in most of these markets, which means rents are lower. For example, last fall, property costs in eastern Pennsylvania averaged about $3.50 to $4.50 per square foot, compared to $5 to $6 per square foot in southern New Jersey and $7 to $8 in northern New Jersey.

Another state that has seen a turnaround in its economy, thanks to increased logistics and distribution activity, is Ohio. Near the state capital, Columbus, the Rickenbacker International Airport has positioned itself as a center for air cargo and multimodal transportation. One major project underway is a partnership with rail carrier Norfolk Southern (www.nscorp.com) to create an intermodal facility on and adjacent to the airport. The new Rickenbacker Intermodal Terminal is expected to be operational in early 2008. According to Grubb & Ellis (www.grubb-ellis.com), "The plans include bridge construction in several counties in Ohio and increasing tunnel size in Virginia and West Virginia, which will allow the double stacking of cargo containers on trains. This project will create new distribution routes between the East Coast and Chicago and is expected to create considerable job growth. It is estimated that this project will contribute 10,000 jobs to the central Ohio area in the next 30 years. Central Ohio is already recognized as a distribution center and this project will place an emphasis on the area as a top choice for prospective tenants looking to relocate/expand this operations."

The intermodal facility will also link to the Heartland Corridor rail system, which will connect Columbus via double-stack train to the port complex in Norfolk, Virginia.

Columbus is within a one-day truck drive to 58 percent of the U.S. population and 61 percent of its manufacturing capacity, and 50 percent of the Canadian population. Columbus is the third-largest port of entry for textiles in the U.S. (Limited Brands is headquartered there), with more than 40 freight forwarding companies and 140 trucking firms operating in the region.

As part of its plan to restructure U.S. distribution operations, Avon Products announced recently that it had selected Zanesville, Ohio, located 50 miles east of Columbus, as the site for its new distribution center. The new facility will employ approximately 500 people and will have the capacity to ship 50 percent of Avon's U.S. beauty products volume when fully operational.

Payless ShoeSource, the largest footwear specialty retailer in the Western hemisphere, also chose Ohio for a new facility that will serve as the company's distribution center for roughly 2,900 retail stores.

As further proof of the growing activity in and around Columbus, DHL recently announced the opening of a new service center to help support increased demand for package pickup and delivery operations in the area. The company also maintains an air and ground hub in Wilmington, Ohio, about one hour's drive from Columbus.

Second-tier cities and regions also have more (and typically less expensive) land on which to build huge warehouses, which is another emerging trend. According to Cushman & Wakefield (www.cushwake.com), "The proliferation of very large, million-square-foot distribution centers is a direct result of the increased importance of imports and container traffic on the supply chain." In addition, "Strategically located distribution centers near ports or highways can lead to substantial savings by reducing two critical linkages—port to distribution center and distribution center to highway. This is especially true for larger retailers that have large volumes of goods from multiple vendors. In many cases, the efficiencies realized from super-sized centers result in a net cost savings even if an additional step is being added to the supply chain."

Warehouse technology, including electronic stock management systems and RFID, are also making operations and inventory management more efficient at these huge warehouses, explains the real estate firm. At the same time, "Very large facilities also allow for the deployment of multiple shipping strategies within one facility based on the needs of the retailer or end-user. Some goods are quickly being cross-docked and shipped out immediately to regional distribution centers and stores; other goods are being transloaded, providing a mix of goods in single containers; while still other products are being stockpiled in order to ensure that seasonal demand can be met at critical times of the year. All of this can be accomplished if the facility is large enough and designed for these purposes with the proper clear-heights, door configurations, rail spurs and yard space." wt

Sidebar: The ABCs of FTZs

What is a foreign trade zone (FTZ)? A foreign trade zone is a defined physical area within the United States that, for customs purposes, is treated as if it is outside U.S. borders. FTZs are often at ports, airports, or industrial parks. Companies may use FTZs for both storage/distribution activities or, after specific approval by the U.S. FTZ board, for manufacturing.

Why would I want to consider manufacturing in a FTZ? When you manufacture in a FTZ, your company is treated (for purposes of customs duties) like it's located outside the United States. That can mean that U.S. import duties don't have to be paid on imported components coming to your factory. If your finished product is ultimately shipped to the U.S. market, you may have the option of paying the finished product duty rate rather than the component duty rate. (Many finished products have lower duty rates—or are duty-free—than their components.) And, if you re-export the finished product, you don't ever pay any duties on the component materials. There are other potential savings, too, like avoiding duties on imported materials that become scrap, and possible administrative savings and efficiencies.

What is involved in getting authority to manufacture in a FTZ? To manufacture in a FTZ, you work with your local foreign trade zone to put together an application. The U.S. FTZ Board has created simplified procedures to make the benefits of the FTZ program accessible to a broad range of companies. The FTZ Board can then use the information from those forms to make decisions on whether to approve individual applications.

What does the FTZ Board base its decisions about applications on? The Board reviews applications to make sure they are not inconsistent with U.S. trade policy and that the proposed activity would have a positive impact on the U.S. economy.

Do I already have to be located in a FTZ to apply? No. If it's practical, you may choose to relocate to an existing FTZ site—there are more than 200 FTZs all across the United States, many of which encompass multiple sites. However, if it's not practical for you to relocate to an existing site, the FTZ Board has a procedure for you to work with your local FTZ to create a "subzone" at your facility.

Is there a fee to apply? There is no fee for manufacturing authority within an existing zone. For subzone applications, there is a one-time fee (either $4,000 or $6,500, depending on the number of products.)

For more information, visit the Import Administration at the Department of Commerce online at http://ia.ita.doc.gov/ftzpage/, or call the FTZ staff at 202.482.2862.