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# **CENTER FOR REAL ESTATE**

## Quarterly Report

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Volume 9, Number 2

Spring 2015

# CENTER FOR REAL ESTATE Quarterly Report

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*Publisher*

Gerard C.S. Mildner, Ph.D.

*Editor*

Eric Fruits, Ph.D.

*Staff*

Carly Harrison  
Synkai Harrison  
Clancy Terry

*Editorial Advisers*

Childs, Mark  
DuPont, Beth  
Lefeber, Robert  
Lehner, Josh  
Potiowsky, Tom  
Pozdena, Randall  
Raicht, Patricia  
Wood, Justin  
Zell, Craig

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## SUMMARY AND EDITORIAL

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ERIC FRUITS

Editor and Oregon Association of Realtors Faculty Fellow  
Portland State University

When imagining the future legalization of marijuana in Oregon, it may be difficult to have a clear picture. Promises of an economic bounty and a new stream of tax revenues class with objections, concerns, and near apocalyptic projections. **Synkai Harrison** and **Carly Harrison** look at Colorado and Washington's recent experience of recreational marijuana legalization. They provide a comprehensive review of the new state law, federal law, and how it may impact Oregon's real estate markets.

**Clancy Terry**, reports that while **residential markets** saw some pick up in the number of transactions since a year ago, but with little movement in pricing and days on market. As with much of the country, Oregon's **multifamily market** continues to see low vacancies and rising rents.

**Synkai Harrison** reports strength in the **office market** and **retail market** with each market experiencing shrinking vacancies, increasing rents, positive absorption. The **industrial market** remains strong, as asking rents continue to rise, vacancy rates continue their downward trend and absorption remains robust. Construction activity has increased with over a million square feet delivered to market

■ **Eric Fruits, Ph.D.** is editor of the Center for Real Estate *Quarterly Report* and the Oregon Association of Realtors Faculty Fellow at Portland State University. He is president and chief economist at Economics International Corp., a Portland-based consulting firm. Any errors or omissions are the author's responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.

during the past two quarters. Even though Portland is seeing more speculative construction, new construction is still low compared to historic levels.

I hope you enjoy this latest issue of the Center for Real Estate *Quarterly Report* and find it useful. The *Report* is grateful to the Oregon Association of Realtors and RMLS for their continued support. ■

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# OREGON'S MARIJUANA FUTURE

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A. SYNKAI HARRISON & CARLY HARRISON

Portland State University

When imagining the future legalization of marijuana in Oregon, it may be difficult to have a clear picture. Objections circulate, apocalyptic images abound, and Oregon is left with many questions marks. However, with Colorado and Washington going before us to legalize and regulate the recreational use of the Schedule 1 drug in 2014, Oregon can look to recent history and the current reality of these other pioneering states as we discover how to implement Measure 91.

■ **A. Synkai Harrison** is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. **Carly Harrison** is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions are those of the authors solely and do not represent the opinions of any other person or entity.





The measure does not amend or affect the Oregon Medical Marijuana Act, which maintains its jurisdiction over the medical market, but outlines the structure of the recreational market, directing the Oregon Liquor and Control Commission (OLCC) to establish, regulate, and license marijuana businesses. This means that effective July 1, 2015, a person is able to possess up to eight ounces and households can grow no more than four plants—provided the plants are not visible. The measure also imposes limits on liquid and other forms of marijuana.<sup>3</sup> While possession up to these limits will be legal, marijuana may only be legally consumed in private residence, meaning that public consumption will still be illegal and enforced.

## FEDERALLY ILLEGAL

However, despite the citizens of Oregon choosing to make recreational marijuana legal, it is still considered a Schedule 1 controlled substance by the federal government. The Controlled Substance Act (CSA), signed into law by President Nixon, places drugs into classifications or schedules which are based on their potential for abuse, medical benefits and their statuses in international treaties. Over 160 different drugs have been added, removed or reclassified since the act was signed into law, but marijuana remains a Schedule 1 drug, which is considered to have no accepted medical use.<sup>4</sup>

To provide guidance to federal prosecutors, the federal government issued what is referred to as the “Cole Memo.” Since then, states have used the memo for guidance. In 2013, Deputy Attorney General James Cole released a memorandum providing guidance to US Attorneys on marijuana enforcement under the Controlled Substance Act. The memo affirms that according to the Federal government, marijuana is a dangerous drug and that its sale and distribution provide a source of revenue to large-scale criminal enterprises. However, the memo lists the eight enforcement priorities of the Department of Justice such as distribution to minors, revenue to cartels, violence, and drugs and driving. The crucial part about the memo: provided a state’s system of control and enforcement adheres to these eight priorities, the federally-illegal nature of this market will not be a priority for federal prosecutors and their rightful enforcement under the CSA.

States that have set robust controls and procedures on paper and in practice and implement “strong and effective regulatory and enforcement systems” with regards to the “cultivation, distribution, sale and possession of marijuana” are less likely to threaten federal government’s priorities with CSA enforcement. While the Cole Memo is only a federal guideline, not a law, and can technically be revoked at any time, it has afforded some level of comfort for both direct and indirect participants in the industry. For states, it means that their created infrastructure of regulations and their enforcement must be incredibly robust. For the growers, producers, retail-

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<sup>3</sup> Measure 91 Summary. *Marijuana Policy Project*, November 5, 2014. Retrieved March 6, 2015 from <http://www.mpp.org/states/oregon/measure-91-summary.html>

<sup>4</sup> Controlled Substances Schedules. *Office of Diversion Control, U.S. Department of Justice*. Retrieved May 22, 2015 from <http://www.deadiversion.usdoj.gov/schedules/>

ers and property owners in the industry, complete compliance with this infrastructure becomes a necessity. Without both the public and private sectors cooperating together, there is risk of prosecution for aiding or abetting illegal activity under federal law, and involved property can be seized.

## OLCC—RULES, TAXES, AND MORE RULES

The Oregon Liquor Control Commission is charged with developing a recreational marijuana infrastructure. The OLCC began rulemaking in December 2014 to prepare for the January 4, 2016<sup>5</sup> deadline to accept business applications for licenses. These licenses will roll out thereafter, with retail sales expected to begin in the fall of 2016. There is a wide gap between recreational marijuana’s legalization (July 2015), and when it can be sold in stores (most likely 2016, when businesses have licenses), during which time it will still be illegal to purchase it, but not illegal to possess it.

Under Measure 91, four types of businesses are allowed: producers, processors, wholesalers, and retailers. For those unfamiliar with the production of marijuana, *producers*, also known as cultivators, grow the product, *wholesalers* sell to retailers or other non-consumers, and *retailers* sell to the consumer. *Processors* work within the distribution channel to create extracts and other byproducts to sell to retailers.

Measure 91 also establishes how recreational marijuana is to be taxed, which given the many forms of marijuana such as cigarettes, edibles, liquids, or vapor, require excise taxes specific to each form of the original plant. Every immature plant is taxed \$5, leaves are taxed at \$10 per ounce and a \$35 per ounce tax is imposed on marijuana flowers, the most potent and productive part of the plant and are paid by the producer. The legislation also designates the distribution of the revenue collected from the recreational market, with the distribution as follows:<sup>6</sup>

Common School Fund	40%
Medical Health Alcoholism and Drug Services	20%
State Police	15%
Cities for Measure 91 enforcement	10%
Counties for Measure 91 enforcement	10%
Oregon Health Authority for Alcohol and Drug Abuse Prevention	5%

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<sup>5</sup> Recreational Marijuana Frequently Asked Questions. *State of Oregon website*. Retrieved May 6, 2015 from <http://www.oregon.gov/olcc/marijuana/Pages/Frequently-Asked-Questions.aspx>

<sup>6</sup> Recreational Marijuana Frequently Asked Questions. *State of Oregon website*. Retrieved May 6, 2015 from <http://www.oregon.gov/olcc/marijuana/Pages/Frequently-Asked-Questions.aspx#Taxes>

The OLCC has estimated an expected revenue of \$16 million in marijuana tax receipts for 2015-2017, with other estimates ranging from \$12 to \$38 million<sup>7</sup>. With the additional revenue from application and licensing fees, and the estimated budget, the expected amount for distribution for the above uses is \$7.7 million. This estimated revenue of \$16 million is perhaps conservative given the range, as ECONorthwest's analysis projected gross revenue of \$78 million in excise tax during the first full biennium of tax receipts.<sup>8</sup>

In comparing Oregon's tax structure to Colorado and Washington's, Oregon is imposing much less tax burden on recreational marijuana. While this results in higher revenue for WA and CO per ounce of cannabis, the high taxes are passed on to the consumer, requiring higher prices. This makes the legal market less attractive than the medical market or illegal (i.e., "black") market.

Washington imposes a 25 percent tax at each point of sale, creating an effective tax rate of 44 percent, and Colorado collects an excise tax of 15 percent in addition to a 10 percent marijuana sales tax, a state sales tax of 2.9 percent and various local taxes, as high as 3.5 percent in Denver.<sup>9</sup> Combined, the effective tax rate is over 30 percent.

In Oregon, applying the excise tax of \$35 per ounce of flowers to the average price per ounce of marijuana of \$208,<sup>10</sup> the lowest in the nation, Oregon's effective tax rate is 17 percent. This relatively low tax rate is hoped to allow Oregon's legal and regulated market to compete with its flourishing black market.

Another positive attribute of Oregon's low tax rate is its competition for tourism. While currently, sales across state lines are illegal, competition for tourism and the business from neighboring states is not. While Colorado's tourism industry has grown significantly since legalization, it is difficult to speculate how tourism will affect Oregon, since unlike Oregon, Colorado does not have any neighboring states with legalization. But all these being equal, Oregon's tax rate is significantly less than Washington's, which could encourage patronage from our neighbor to the north.

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<sup>7</sup> 2015-17 Budget Request to Implement Recreational Marijuana. *Oregon Liquor Control Commission*. April 23, 2015. Retrieved May 15, 2015 from [http://www.oregon.gov/olcc/marijuana/Documents/OLCC2015\\_17\\_Budget\\_Request\\_Implement\\_Recreational.pdf](http://www.oregon.gov/olcc/marijuana/Documents/OLCC2015_17_Budget_Request_Implement_Recreational.pdf)

<sup>8</sup> Oregon Cannabis Tax Revenue Estimate. *ECONorthwest*. July 22, 2014. Retrieved April 15, 2015 from [http://www.econw.com/media/ap\\_files/7-31-2014\\_CannabisFinalReport.pdf](http://www.econw.com/media/ap_files/7-31-2014_CannabisFinalReport.pdf)

<sup>9</sup> Henchman, J. (2014, August 25). Taxing Marijuana: The Washington and Colorado Experience. *Tax Foundation*. Retrieved April 15, 2015 from <http://taxfoundation.org/article/taxing-marijuana-washington-and-colorado-experience>

<sup>10</sup> Average marijuana price by state. *Chicago Tribune*. September 1, 2014. Retrieved April 22, 2015 from <http://www.chicagotribune.com/medical-marijuana-costs-by-state-20140901.htmlstory.html>

For the municipalities that do not want to participate in the new recreational industry, Section 59 of Measure 91 allows municipalities to adopt “reasonable time, place and manner regulations” of nuisance aspects. Municipalities may also petition to prohibit the operation of licensed premises by holding local elections. On the medical side, and up until recently, state law allowed for a moratorium on medical marijuana dispensaries. However, that moratorium expired on May 1, 2015, with specific requirements of regulation still being considered at the state level.

Oregon recently announced the formation of a Recreational Marijuana Rules Advisory Committee, comprised of 15 members, including representatives from the marijuana industry, law enforcement and local government, and the public.<sup>11</sup> The group will act as the taskforce to provide recommendation on administrative rules needed to properly implement Measure 91, and will begin meeting in June of 2015.

As Oregon proceeds to address the many nuances of legalized and regulated marijuana, we can learn a lot from the states that have gone before us. Colorado’s Director of Marijuana Coordination Andrew Freedman stated that the most difficult task was to create a legitimate closed loop system of marijuana.<sup>12</sup> Under the priorities of the Cole Memo, state’s need to prevent distribution to minors, prevent revenues from going to support illegal activity, among other enforcement priorities. Therefore, the state needs to regulate and track the marijuana product that is grown and distributed, in order to ensure compliance. To close the loop in such a market, Oregon will follow Colorado and Washington’s suit, and implement a seed-to-sale tracking system. This will enable the OLCC to track the amount of marijuana and where and to whom it is distributed. It assigns a bar code to each individual plant, from its infancy, through its grow cycle, through potency labs, all the way to the label on its retail packaging.

Requirements for locations of facilities will not be fully understood until the OLCC’s Recreational Marijuana Rules Advisory Committee releases its recommendations but it is likely that recreational marijuana business will not be able to locate within 1,000 feet of anywhere minors can gather such as schools, parks, and recreational



Seed-to-sale bar codes. Denver, CO.

<sup>11</sup>OLCC announces Recreational Marijuana Rules Advisory Committee. *Oregon Liquor Control Commission News Release*. May 1, 2015. Retrieved May 5, 2015 from [http://www.oregon.gov/olcc/docs/news/news\\_releases/2015/nr\\_05\\_01\\_15\\_Marijuana\\_RAC\\_Committee\\_Announced.pdf](http://www.oregon.gov/olcc/docs/news/news_releases/2015/nr_05_01_15_Marijuana_RAC_Committee_Announced.pdf)

facilities. This is probably of greater concern to owners of retail properties and will be difficult to determine any impact until the rules are released. For industrial property owners and tenants, many industrial properties are in areas zoned for general (EX) and heavy industrial (HI), and are by nature typically located away from residential areas, schools, public parks, etc., and therefore, location restrictions may not have a significant impact.

While the OLCC is in the process of creating the guidelines for recreational marijuana, we can look to Colorado to understand how they implemented their Amendment 64 to legalize cannabis. As Hudak points out,<sup>13</sup> in the context of marijuana policy, “implementation involves the design, construction and execution of institutions, rules, and processes related to a system of legalized marijuana.” In his opinion, some key elements that contributed to Colorado’s success were as follows: they had rapid response in their implementation of their task force, and they had clear signals and support from the governor, who had formally opposed the amendment, but had a “job to do” since it was passed. Additionally, Colorado had internal coordination between all departments, much like OLCC staff has, agency reorganization and staffing to meet the new demands, and well-chosen policy changes, such as the seed-to-sale tracking system, and video surveillance requirements. Ultimately, the requirements for success may be similar for Oregon. This will unfold in the coming months as the OLCC continues to update the public with their Measure 91 implementation via their website.<sup>14</sup>

## **BANKING**

Banking is one of the biggest challenges faced by the marijuana industry and those involved in an ancillary capacity. Since banks have to follow both state and federal laws, many financial institutions have resisted doing business with the marijuana industry, creating an environment where cash is often used. This large amount of cash creates problems: it needs to be stored and transported safely, requiring the use of incredibly large and costly safes, and sometimes transportation by armored-cars to the banks who will take it. Some businesses in the industry are able to obtain bank accounts, provided they do not disclose their line of business. However, if the bank determines that the funds came from illicit activity as defined by the Substance Control Act, any accounts associated with that business are shut down. In addition to safety and transportation, this poses a real problem to businesses ability to pay bills.

Oregon community bank, MBank recently made national news with its acceptance and subsequent refusal to do business with marijuana businesses. This refusal re-

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<sup>13</sup> Hudak, J. Colorado’s Rollout of Legal Marijuana is Succeeding: A Report on the State’s Implementation of Legalization. *Center for Effective Public Management at Brookings*. July 2014. Retrieved April 15, 2015 from <http://www.brookings.edu/~media/research/files/papers/2014/07/colorado-marijuana-legalization-succeeding/cepmmjcov2.pdf>

<sup>14</sup> Recreational Marijuana. *State of Oregon website*: <http://www.oregon.gov/olcc/marijuana/Pages/default.aspx>

sulted in MBank not only closing the accounts of marijuana businesses but of those offering support services as well. The reason given was that the bank did not have the resources to comply with federal regulations.<sup>15</sup>

In February of 2014, the Department of the Treasury Financial Crimes Enforcement Network (FinCEN) provided guidance on Bank Secrecy Act (BSA), the Controlled Substances Act and the marijuana industry. The memo referenced the Cole Memo's priorities and reiterated the goals of the Justice Department. Financial institutions are required to submit a suspicious activity report (SAR) if that institution believes that a transaction involves funds derived from illegal activity. For a marijuana business, whose cash can often retain the distinct scent of its merchandise, the scent alone raises the red flag for banks. If a bank has determined, after it has done its due diligence, that a marijuana business does not conflict with the priorities of the Cole Memo and does not violate state law, that bank is required to file a "Marijuana Limited" SAR. The information in the SAR should be limited to basically identifying information of those involved in the transaction and confirm that no other suspicious activity was identified. Note that the memo does not specifically state that banks are prohibited in doing business with the marijuana industry or those who provide services to the industry, such as landlords. However it does require an added level of compliance and paperwork, and banks must report any activity or transaction that occurs. For some banks this additional administrative requirement would be cost prohibitive. What this memo does is leave the door open for banks to do business with those involved in the industry if they choose to comply with the additional regulatory requirements. So far, there have been no banks nationwide who remain open to the challenge.

## INVESTMENT

Marijuana operations tend to have two types of investors: investors in operations and those who are in it as an ancillary investors. These latter investors, being "once removed from the plant" can play any number of roles. From a real estate perspective, these investors are often landlords and equity investors. As such, this level of investment is less risky and provides a greater level of comfort.

Because every marijuana business operator requires real estate, property is in high demand. However, if there is a loan on the property, it likely will be excluded from being a potential site for any facet of the marijuana industry, as loan covenants typically restrict any use inconsistent with federal law. If these covenants are violated, the loans could be recalled, limiting available properties to those without any debt on them, which is a minority of properties. As an example, real estate investor Chad Brue, founder of Brue Capital Partners indicates that 85 percent of commercial properties in Denver have some form of existing debt, whether CMBS, life insurance companies, or a bank loan, thus limiting the properties that CAN be leased to ten-

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<sup>15</sup> Mesh, A. MBank is Closing Its Marijuana Bank Accounts. *Willamette Week*. April 10, 2015. Retrieved May 5, 2015 from [http://www.wweek.com/portland/blog-33062-mbank\\_is\\_closing\\_its\\_marijuana\\_bank\\_accounts.html](http://www.wweek.com/portland/blog-33062-mbank_is_closing_its_marijuana_bank_accounts.html)

ants. Brue notes that an additional 10 percent of property owners are morally or ethically opposed to marijuana cultivation and sale or simply refuse to take on the risk. That leaves approximately 5 percent of total inventory that can and will lease to the industry, whose properties have a capital stack of willing private equity and non-traditional debt, or “hard money” lenders.

Residency requirements have been proposed in Oregon, and investors and property owners should be aware of it. In-state producers have an interest in keeping out-of-state investors and operators out of the Oregon market for the obvious reason of limiting competition. If applied, this would limit investment in the industry to only those residing in Oregon. However, there are two challenges with a residency requirement. First, it is possible that such a law would violate the commerce clause and privileges and immunities clause of the constitution, and would withstand a legal challenge if marijuana is reclassified as a Schedule 2 controlled substance<sup>16</sup>. Second, depending on how they are enforced, residency requirements could be circumvented making the requirement ineffective. Anthony Johnson, who is often referred to as a chief petitioner of Measure 91, in an interview in the Willamette Week, stated he believes that those with capital will find ways around any residency restrictions.<sup>17</sup> The main risk in approving a residency requirement is that it could have a dampening effect on the investment in the industry. Oregon will be able to benefit from the expertise of operators from states like Colorado, and capitalizing on that could be wise. Experienced growers and retailers that have successfully operated businesses in a robust enforcement environment like Colorado will benefit the Oregon marijuana industry as a whole and decrease risk to property owners. Oregon would also benefit from those with experience running large scale cultivation and extraction operations. Lastly, sophisticated operators would be a benefit to property owners, as they have experience operating in large industrial facilities and make good tenants.

In a recent memorandum, local law firm Zupancic Rathbone articulates many of the legal concerns landlords must be aware of. Marijuana leases require several additions than a standard lease, and given the changing legal landscape, should take care to build in some flexibility. Leases should allow the landlord to terminate if certain situations arise, , such as changes in marijuana legislation or enforcement, loss of licensing, or any governmental or bank action against the landlord or property. The permitted uses section should require the tenant to maintain appropriate licensure and operate in compliance with specific state marijuana laws and non-drug related federal laws. Additionally, the leases should be tailored to the industry and address the operational impacts such as pesticide use, odor issues, security require-

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<sup>16</sup> Borrud, H. Residency requirement considered for Oregon pot business investors. *East Oregonian*. May 3, 2015. Retrieved May 15, 2015 from <http://www.eastoregonian.com/eo/capital-bureau/20150503/residency-requirement-considered-for-oregon-pot-business-investors>

<sup>17</sup> Jaquiss, N. and A. Mesh. Smoke Signals. *Willamette Weekly*. November 12, 2014. Retrieved April 15, 2015 from [http://www.wweek.com/portland/article-23503-smoke\\_signals.html](http://www.wweek.com/portland/article-23503-smoke_signals.html)

ments including safes, security systems and surveillances. As the memorandum continues, for brokers trying to lease space, a broker must disclose the fact that a prospective tenant is in the marijuana industry, and should also tell a client that there are financial and legal risks involved in leasing to a marijuana business.

## CASE STUDY: COLORADO

Like with most new industries, the cannabis industry is full of opportunity for those directly involved as business operators and those more indirectly involved, such as those involved in the real estate of the industry. In trying to assess marijuana's impact on Oregon, Colorado is a good example where recreational marijuana has not only had a huge impact on the State of Colorado's revenue, but also on commercial real estate. For one, the industrial real estate market in Denver has benefited tremendously from legalization. Since marijuana became legal in Colorado in 2012 with the first retail sales taking place in 2014, the industrial market has seen incredible growth.

According to CoStar<sup>18</sup>, Denver saw 231 industrial sales transactions in 2014 at an average sales price of \$66.29 per square foot. Compare that to 2013 where there were 177 transactions averaging \$58.23 per square foot. That is an increase of over \$8 per square foot in just twelve months. In fact, in the



Indoor Growing Facility, Sweat Leaf Cultivation Center, Denver, CO

Denver market industrial sales less than 25,000 square feet averaged \$95.79 per square foot in 2014. At the end of the first quarter of 2015, there was over 1.3 million square feet of industrial space under construction, a million of which is expected to deliver second quarter of 2015, out of a total inventory of 288.8 million square feet.

Average asking rental rate for industrial space in Denver was \$7.60 per square foot at the end of the first quarter of 2015 compared to year ago at \$6.81. Asking rental rates for warehouse space averaged \$6.47 NNN compared to \$5.56 NNN per square foot a year ago. The warehouse market has also experience incredibly low vacancy rates, ending the first quarter at 3.1 percent, compared to 2012 and 2011 where the average vacancy rate for the warehouse market was 6.2 percent and 7.6 percent respectively.

While these sales prices and rents are averaged across all industrial spaces, regardless of marijuana affiliation, Colorado-based investor Chad Brue describes the per-

<sup>18</sup> CoStar Denver Industrial report Q1 2015



formance of real estate used for cannabis cultivation as highly lucrative. Mr. Brue currently owns 450,000 square feet of marijuana-related real estate, making the firm the largest holder in Colorado, and most likely in the United States. He describes his coincidental entrance into the market, where he was asked if he would lease his building to a marijuana grower. He had purchased a building for \$45 per square foot without any prohibitive debt. After agreeing to lease his property for marijuana cultivation, Mr. Brue received offers from 10 potential tenants which had outbid each other, to a final rent of \$12 per square triple net, which was triple the typical rent at that time. After this first transaction, he saw an opportunity. Two months later, he purchased another property at \$50 per square, and leased it at \$16 triple net. By October 2014, prices for these types of properties had climbed to \$90 per square foot.

According to Jones Lang LaSalle's Denver market Industrial report, tenants demanding spaces between 10,000 and 40,000 square feet “dominate market activity”.<sup>19</sup> It is interesting that this amount of space is within the sweet spot for marijuana cultivation in Denver currently. This is not to say that demand is being entirely driven by cultivation in this space, but marijuana is having a significant impact on demand. JLL also notes that this is creating demand for smaller speculative spaces of around 200,000 square feet that have the flexibility of being subdivided.

Deals for marijuana cultivation specifically provide a much more interesting story. Demand for marijuana cultivation space has skyrocketed since becoming legal and supply is not keeping up with demand. As one Denver area broker was recently quoted, “Supply is deficient, demand is excessive, and capital is abundant”.<sup>20</sup> Cultivation has expanded in the Denver market and as such traditional warehouse users and growers are actively competing for space. Some estimate that cultivation and manufacturing facilities in the Denver area occupy approximately 4.5 million square feet of space. Before medical marijuana sales took off in 2009, average rental rates were 25 percent of what they are now.

Rental rates for marijuana grow operations in Denver CO are typically two to four times that of traditional industrial user spaces. There are a number of reasons for this premium. Since so few properties are owned outright, that leaves very little space applicable for use by the industry, forcing marijuana businesses to actively outbid one another, raising market rents drastically. There is also the risk associated with breaking federal law, and landlords require a higher return for that risk. Anyone who is participating in the industry is technically aiding and abetting a federal crime personally. This places all related real estate at risk of immediate forfeiture by the federal government, should they decide to intervene. However, given the adherence to the Cole Memo's priorities, as investor Chad Brue mentions, no one has

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<sup>19</sup> Jones Lang LaSalle Denver Industrial Snapshot Q4 2014

<sup>20</sup> Raabe, S. Pot-growing warehouses in short supply as demand for legal weed surges. *The Denver Post*. March 11, 2014. Retrieved March 15, 2015 from [http://www.denverpost.com/marijuana/ci\\_25316132/pot-growing-warehouses-short-supply-demand-legal-weed](http://www.denverpost.com/marijuana/ci_25316132/pot-growing-warehouses-short-supply-demand-legal-weed)

been charged with aiding or abetting a federal crime and there are 1,600 pot-related properties in Colorado.

Surprisingly, there is also the risk premium for money laundering. Due to the lack of proper banking in the industry, landlords are limited in their means of receiving rent payments. As Brue mentions, operators must move from one bank to another, as their accounts are shut down, and their means of paying rent is limited. Therefore, rent payments come in the form of money orders, checks, wires and sometimes cash of \$40,000 to \$80,000 each month, so Brue is by default, also part of a money laundering chain. In his opinion, if the federal government's stance changes and they decide to recall the Cole Memo, they would "slowly dismantle the industry" and not simply shut everyone down, again provided the Cole Memo guidelines had been followed.

This risk premium costs money, and enables property owners who may own older sometimes obsolete warehouses and lease them to marijuana tenants for prices up to \$20 or more per square foot triple net.<sup>21</sup> The owner of Walking Raven dispensary in Denver was quoted saying that he felt fortunate to be paying \$18 per square foot for one of the two warehouses he was leasing.<sup>22</sup> As Brue states, tenants are able to pay these astronomical rents because they are able to bring in \$1,200 to \$1,500 per square foot in revenue. Operators often come with large amounts of cash able to pay deposits equaling several months' rent. A Denver Post article reported one story where an owner was negotiating a lease with a cultivation operator when he asked what assurances he could provide to ensure he was credit worthy. The grower walked to the parking lot, opened up the trunk of his car and produced a suitcase containing a million dollars in cash.<sup>23</sup> This highlights the safety issue when cash is concerned.

In the Portland area, industry professionals at a recent CCIM gathering are quoting at least 200 percent increases in rents for marijuana businesses. If Colorado is any example, cultivators may soon begin to outbid typical warehouse users, increasing competition and driving up rental rates.

Currently, rental rates for the Portland warehouse sector averaged \$5.78 per square foot annually at the end of the first quarter of this year, up from \$5.52 per square foot at the same time last year. There are some smaller warehouse submarkets

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<sup>21</sup> Perlberg, H. Ganja Gets Warehouse owners Buzzing as Pot Farms Thrive. *Bloomberg Business*. May 5, 2015. Retrieved May 15, 2015 from <http://www.bloomberg.com/news/articles/2014-05-05/ganja-gets-warehouse-owners-buzzing-as-pot-farms-thrive>

<sup>22</sup> Raabe, S. Pot-growing warehouses in short supply as demand for legal weed surges. *The Denver Post*. March 11, 2014. Retrieved March 15, 2015 from [http://www.denverpost.com/marijuana/ci\\_25316132/pot-growing-warehouses-short-supply-demand-legal-weed](http://www.denverpost.com/marijuana/ci_25316132/pot-growing-warehouses-short-supply-demand-legal-weed)

<sup>23</sup> [http://www.denverpost.com/marijuana/ci\\_25316132/pot-growing-warehouses-short-supply-demand-legal-weed](http://www.denverpost.com/marijuana/ci_25316132/pot-growing-warehouses-short-supply-demand-legal-weed)

where rental rates are much higher.<sup>24</sup> However, the challenge in Portland is that competition for industrial space is already very tight. According to CoStar, overall vacancy rates for the industrial market in Portland was 5.1 percent at the end of the first quarter of 2015. The warehouse sector ended the fourth quarter at 4.4 percent and was at 5.6 percent a year ago. As marijuana cultivators compete for space with typical warehouse users, this will only push vacancy rates lower and rents higher.

## SPACE NEEDS

In addition to the right property in the right location, there are particular needs that growers have above and beyond typical industrial users. Power requirements for cultivation facilities are much higher than for those who would typically use warehouse



Grow Facility, Sweet Leaf Cultivation Center, Denver, CO

space. A traditional heavy industrial user, power requirement could range from \$0.10 to \$0.80 per square foot. One property owner in Denver pays as much as \$15 per square foot for power in one grow facility as lighting is an essential component of grow operations. With older facilities in Denver, to compensate for the heat produced by grow lights, HVAC needs can reach 10 tons per square foot. With new technology, those needs can be reduced to 5 tons per square foot. In addition, facilities need security cameras and key card access but these are nominal when compared to lighting and cooling loads. Regardless, power is significant. Sweet Leaf Cultivation Center in Denver invested in approximately \$75 per square foot in improvements when they recently purchased a warehouse for their new grow operation. Other tenants have spent as much as \$100 or even \$135 per square foot in tenant improvements, which belong to the property owner and can be passed on to another marijuana tenant.

As mentioned earlier, state statute specifically identifies four license types: producers, wholesalers, processors and retailers. Facilities used by each of these license holders will have some similarities specific to the marijuana industry, with security being the most common. For example, Colorado law requires that each plant have at least two cameras on them at all times. Many industrial users have key card access to all spaces so that employee's movement can be tracked at all times.

Obviously, space needs will vary depending on the use. Retail establishments/dispensaries can require as little as 300 to 500 square feet. Facilities used for extraction and producing edibles can average around 3,000 to 5,000 square feet. And

<sup>24</sup> CoStar Q1 2015 Industrial Report

according to Brue, the “sweet spot” for an industrial cultivation facility in Colorado today runs between 20,000 and 25,000 square feet.

## **FUTURE CHANGES**

In addition to the changing winds as states move forward to legalize cannabis, Congress will have to deal with marijuana at some point in the near future. If marijuana is declassified to a Schedule 2 substance, this could increase investment in all states where it is legal for medical and recreational use. National financial institutions could begin to openly do business with the marijuana industry, providing opportunities for long term financing and investment. If marijuana is reclassified, this could even open up the possibility of interstate commerce for marijuana products and the expansion of medical research.

Consider this, the population of Oregon is just under 4 million people. The population of Los Angeles California County is over 10.1 million. It is not difficult to imagine the potential impact on the Oregon economy if interstate commerce were ever allowed. For investors, a reclassification would decrease the real and perceived risk, which would also decrease the risk premium. This would lead to a significant drop in rental rates, with property valuations dropping as well. However as Brue mentions, with the \$100 plus per square foot that tenants are paying for tenant improvements, their likelihood of signing a new lease with another property is majorly diminished. While the same high rents might not be achieved, a property already outfitted with the necessary systems is competitively valuable.

## **OREGON**

Much of Colorado’s marijuana is grown indoors, due to weather constraints, where cultivation can be controlled, down to the minute details of humidity and temperature. While this method of growing produces more growing cycles per year, this adds significant costs to produce cannabis. Currently in Colorado, supply is catching up with demand, and production costs become increasingly important to operating margins. However, unlike Colorado and several other regions, Oregon happens to have an ideal climate for growing marijuana.

Oregon representative Ann Lininger, a member of the Joint Committee of implementing Measure 91, states that “nationally, we are well-positioned to be good at this. We have prime outdoor growing space, especially in the southern part of the state, and if we want to attract the [flourishing] grey market to the regulated market, we need to make sure the barriers to entry are not too high.” As our industrial markets are tight already, and we have a lack of suitable industrial land to add, there may not be great capacity for indoor growing after all. Perhaps, this is where Oregon’s competitive advantage as an outdoor grower can take an even deeper root.

As the OLCC implements their plan, it will be interesting to see how Oregon’s business operators, growers, investors, landlords, banks, law enforcement and citizens respond to this new industry. With many issues to consider and many question marks still unanswered, Oregon is left with the biggest question of all: who is in? ■

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## THE STATE OF THE ECONOMY

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CARLY HARRISON

Portland State University

The global economy and the United States economy continue to grow moderately. In the United States, GDP increased very little, with increased but moderate growth projections, unemployment has dropped further, interest rates and the price of oil remain low, although the latter has increased since fall 2014. Job growth continues, although wage growth lags, and inflation is almost non-existent. There seems to be a slight improvement of the fundamentals nationally, while regionally and locally, Oregon and Portland MSA are showing strong signs of market health.

### THE WORLD ECONOMY

The International Monetary Fund projects global growth at a moderate 3.5 percent in 2015. This April World Economic Outlook echoes its January forecast, and follows a 2014 global growth of 3.4 percent.

In advanced economies, potential growth of output is expected to increase slightly from the average of 1.3 percent during 2008-2014, to 1.6 percent during 2015-2020. This can be contrasted with emerging economies, which is expected to have a slower projected growth of potential output, moving from 6.5 percent to 5.2 percent over the same time period. The decrease is largely due to lower productivity growth as technological gaps between advanced and emerging economies get narrower. Prior to the crisis, the output growth of emerging markets was over-stated

■ Carly Harrison is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.

as much of it was due to structural transformation and the expansion of global and regional value chains. As commercial infrastructure becomes more commonplace in these emerging markets, their growth rate slows to a more sustainable and fundamentally sound rate. In contrast, much of the advanced economies had already experienced exceptional growth due to innovation in information technology. Prior to the crisis, the output growth rate of these advanced economies had already started declining. In analyzing potential output growth, it is largely affected by the growth of the working-age population, changes in the labor force participation rate, and the productivity and investment of capital.

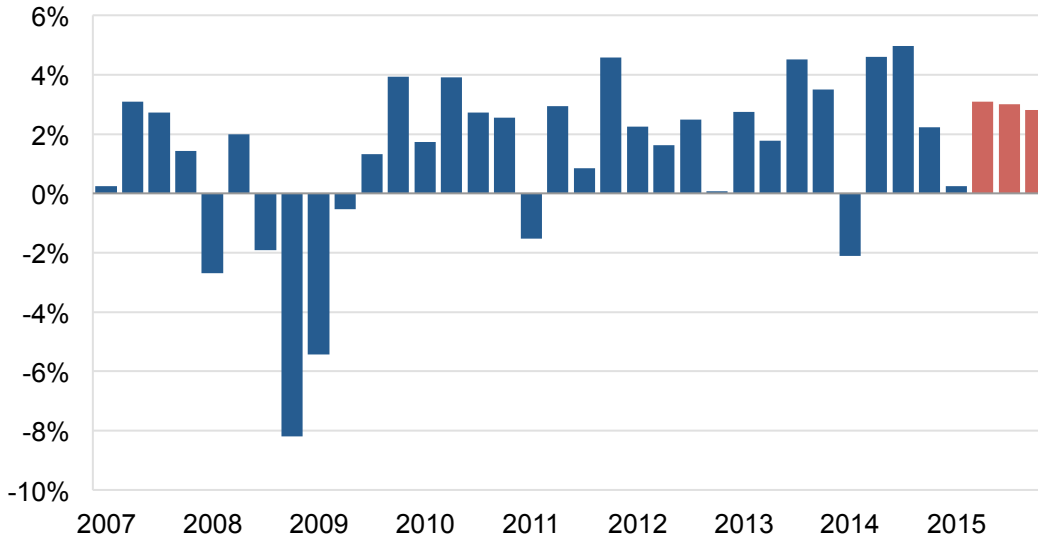
Oil prices continue to be low. While the price has increased by almost 30 percent since its recent low, which saw the largest drop since 2009, the price is still only at 60 percent of its 2014 high. This will provide an economic boost for oil importers, but will obviously dampen growth for exporters. As the Economist points out, the number of rigs drilling for oil in the U.S. has fallen by half since October 2014. While that reflects a loss of about 800 rigs, hydraulic fracturing (fracking) has surprisingly not slowed. As a costlier extraction method relative to conventional drilling, it was expected that the unconventional method of fracking would be unable to compete in the face of lower oil prices. However, frackers have been able to cut costs, due to the falling price in labor, steel and other inputs. With the cost improvements and productivity improvements in fracking, coupled with its gaining share of the capital investment in the United States, American oil production is still growing and is likely to continue. As the IMF mentions, Saudi Arabia has stated openly that it will not cut production, leaving some to argue that this strategy is aimed at pushing such higher cost extraction activities out of the market. In addition to the environmental concerns that accompany fracking, this minor shift in the source of our oil has other consequences. As local economist Bill Conerly suggests, “the collapse of actual oil drilling will have repercussions in a broader swath of the economy,” a good example being the steel industry. As rig counts decrease, so do steel shipments, reflecting the importance of oil drilling in steel demand, albeit not the only one. He notes that we should be on the lookout for other regions and sectors to understand more of the effects of cheap oil.

## **THE UNITED STATES ECONOMY**

Growth in the United States has been “energetic”, the IMF suggests, especially when compared with the diverging trajectories of the other major economies, which are showing weaker recovery. Despite a low 0.2 percent annualized first quarter GDP growth rate, as evidenced in Figure 1, GDP has shown strong growth over the last year, with consumption being the main engine of growth. As has been previously stated, this low growth rate in the beginning of 2015 is likely due to the cold weather, which kept Americans at home instead of in the shops. But another likely culprit is the stronger U.S. dollar, which affects the revenues that companies receive from abroad. According to the Economist, of third of revenues from companies in the S&P 500 index come from abroad, corporate profits fell by 1.6 percent in the fourth quarter of 2014, and were 6.4 percent lower than in the same quarter of 2013.

Nevertheless, Washington Street Journal’s survey of economists continues to forecast a GDP growth rate of approximately 3 percent in coming 2015 quarters.

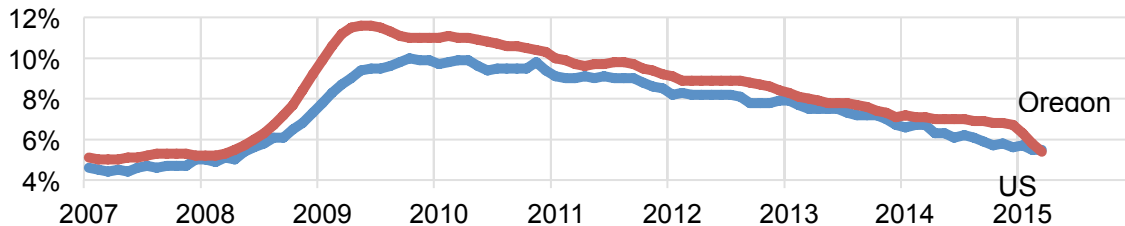
**Figure 1: Gross Domestic Product, United States, Annualized Percent Change, 2007–2015**



Source: Bureau of Economic Analysis and Wall Street Journal Economic Forecasting Survey

As the Bureau of Labor Statistics (BLS) states, unemployment in the U.S. continues to stay low at 5.5 percent (Figure 2), with an average trailing twelve month rate of 5.9 percent, and the number of unemployed persons was 8.6 million. In the first quarter of 2015, total nonfarm payroll employment increased by approximately 560,000 as of March, with a relative increase in professional and business services, health care, and retail trade, and mining losing jobs. Twelve-month job growth is 2.2 percent, however, as the Economist points out, many of these new jobs are low-wage professions such as retail, and many of the current jobs are not full-time.

**Figure 2: Unemployment Rate, Oregon and United States, 2007-2015**

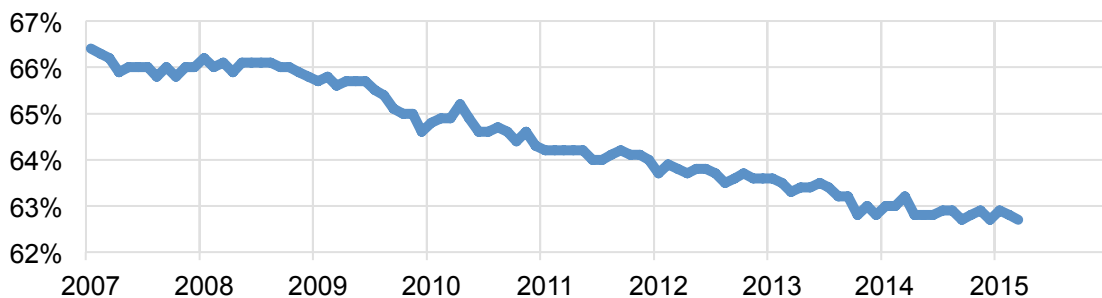


Source: Bureau of Labor Statistics

While the unemployment rate has continued to drop, the labor force participation rate has also continued to decrease to 62.7 percent, the lowest level since 1977, when there was a smaller share of women in the workforce (Figure 3). Over the last several years, many have been asking: Why is the participation rate decreasing? What are the drivers? The most common answers are: the increasing number of baby boomers who retired early upon losing employment, young people staying in higher education longer, delaying their entrance into the labor force, and people who were experiencing longer term unemployment and had dropped out of the labor force.

Perhaps the most important reason to look behind the 62.7 percent, is to know what could happen with wage growth in the future. When the economy improves further, who will come back into the labor force? BLS data shows that wage growth has increased slightly, but as the Economist points out, that may entice those out of the labor force to compete for jobs, having a negative effect on wage growth. Add this to the fact that the number of full-time jobs is lower and the number of part-time jobs is higher than before the recession hit. Conclusion: there is still slack in the market and we may not see substantial wage growth in the near future.

**Figure 3: Labor Force Participation Rate, United States**



Source: Bureau of Labor Statistics

Inflation continues to be mildly positive, but consistently low. The seasonally adjusted month-over-month Consumer Price Index continues to hover just above zero, at 0.2 percent in both February and March, following slight deflation from November to January. The BLS also reports the unadjusted CPI has decreased since March 2014.

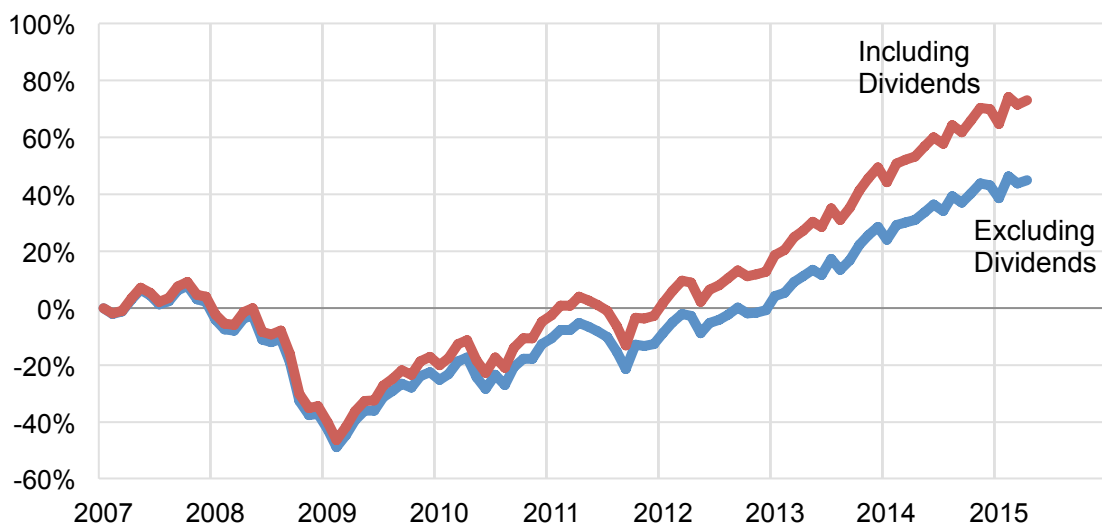
Dialing into the CPI, there were increases in the energy and shelter sectors, the former with major contributors being gasoline and fuel oil, and the latter evidenced by our booming national multifamily markets. There was also a noteworthy 1.2 percent increase in used cars and trucks, which has a twelve-month change of negative 1.3 percent. This is contrasted with a decline in food, and very low growth in all other sectors.

Since the end of Quantitative Easing in October 2014, the Federal Reserve no longer flushed the economy with money from their asset purchases, which had likely



contributed to a higher rate of inflation during their QE days. Now, with inflation barely above zero, there is still a long way to go to reach the Federal Reserve's objectives: 2.0 percent inflation and maximum employment. Reaching these goals will influence the timing of Federal Reserve's liftoff of policy interest rates, which is expected to occur in the third quarter of this year, according to the IMF. Because the market has been showing resistance to growth in both GDP and inflation, many think it is unlikely that they will raise interest rates this June, as had previously been thought. However, as the Federal Reserve anticipates its next monetary policy moves, former chairman Paul Volcker has announced a plan to reshape the Federal Reserve itself. As the Economist reports, Volcker has assembled a group of people to reshape the financial institution with a focus on improving effectiveness and accountability of regulators, by merging agencies and separating powers. As the article states, it is likely that many in D.C. will be unhappy with limiting governmental power in the financial world.

**Figure 4: Standard & Poor's 500 Index, 2007–2015**



Source: S&P Dow Jones Indices, McGraw Hill Financial

The U.S. Stock Market has continued to grow in the first quarter, with the S&P 500 (Figure 4) and NASDAQ Composite indices hitting record highs in February and April of this year. While this is impressive growth, surpassing the pre-recession peaks, many investors think the value of shares are being “propped up by lack of decent alternatives”, as the Economist points out. Bonds are overvalued and cash yields zero, or less in period of deflation. Concerns surrounding the global market's inflated value are illustrated in the earnings per share. While the global market has grown 10 percent since it 2007 high, earnings per share are essentially flat. In the

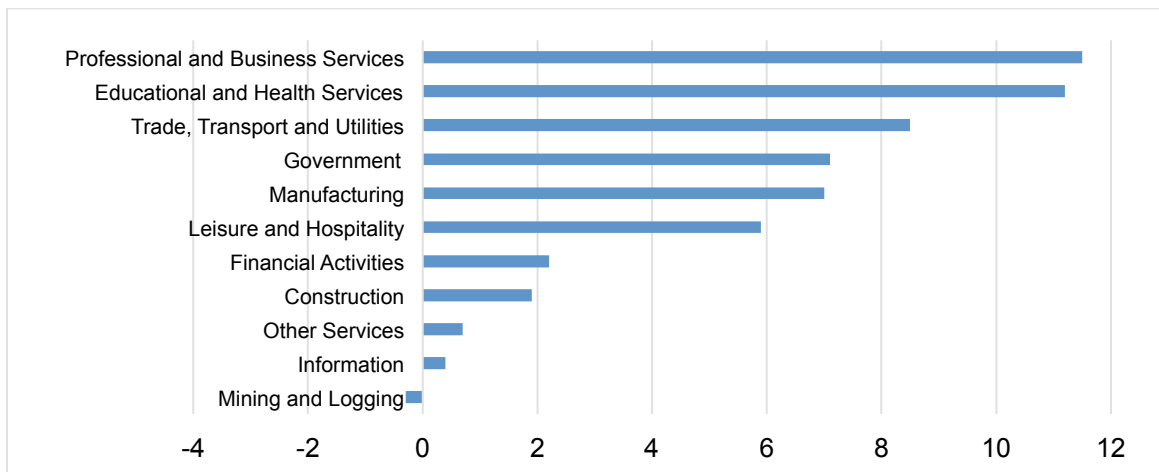
U.S. Stock Market, the market is 35 percent above its 2007 high, but earnings per share are up only 20 percent. As the article articulates, companies have squeezed higher margins out of these revenues, and investors are paying more for the value of these future cash flows, or the market is trading at a higher PE.

## OREGON AND THE PORTLAND AREA

The state of Oregon has continued to show a strong pace of growth throughout 2014 in jobs, wages, and labor force participation and is expected to continue in 2015. The Oregon Office of Economic Analysis economic report further states that the labor market is not back to full employment, but outlines that there is still slack in the job market attributed to a participation gap, a lower underemployment gap and an even lower unemployment gap. The report concludes that Oregon is approximately halfway back to full employment.

Oregon's unemployment rate has dropped from 6.7 percent in December to 5.4 percent in March, a decrease in 1.3 percent in one quarter. While this is an impressive decrease, the number of jobs has also increased by 3.3 percent in the last 12 months, with sectors in Figure 5 showing the most number of jobs added.

**Figure 5: Oregon Job Growth over last 12 months, Nonfarm Payroll Employment, Seasonally Adjusted (1,000's)**



Source: Oregon Employment Department

In addition to an increase in the number of jobs, wages in Oregon are increasing at nearly 7 percent per year, on par with the mid-2000s expansion, with an average wages growth per worker of 3 percent, slightly above the rates of inflation. This has

not had much of an impact on real wage growth, but expectations are that real wages will pick up further in the future.

The Portland Metropolitan Region unemployment rate has continued to decrease over the first quarter, with a March rate of 5.2 percent. Employment growth was up by 2.9 percent from the previous March, with the highest growth rates in the Professional Services, Manufacturing, Trade and Transport, and Education, and a decline in Construction (a 2.0 percent decline). 1,091 jobs were added in March. Portland's unemployment rate continues to decrease at the same rate as Oregon's, relative to the national unemployment rate.

## **CONCLUSION**

Overall, there is modest growth in the global economy, and the national economy is growing only slightly with incredibly low inflation and interest rates. Neither is expected to increase much soon. There is slight job growth coupled with a lower unemployment rate, but only a minor wage growth, a potentially over-valued stock market, fueled by a lack of comparable alternatives. Despite the uncertainty with the national economy, Oregon and Portland's local economies are showing healthy fundamentals and a continued positive trajectory. ■

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## RESIDENTIAL MARKET ANALYSIS

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CLANCY TERRY

RMLS Student Fellow  
Master of Real Estate Development Candidate

Oregon and national housing markets both demonstrated shifting trends in the first quarter of 2015 as they recovered from seasonal winter slowdowns, which were impacted in some areas by constrained supply and rising prices. Stabilizing employment provided a measure of support to housing markets as the quarter unfolded.

National existing home sales declined in January but experienced gains through February and March. The National Association of Realtors (NAR) reports total existing home sales fell almost five percent in January to a seasonally adjusted annual rate (SAAR) of 4.82 million units, although this total was three percent higher than a year prior. January's median existing home price for all housing types was \$199,600, reflecting 35 continuous months of year-over-year price increases.

This price appreciation continued unabated in February, when the median existing home price for all housing types reached \$202,600, an eight percent year-over-year increase. The volume of existing home sales also continued to increase, rising to a SAAR of 4.88 million homes. NAR chief economist Lawrence Yun tempered the interpretation of these increases, however. He points to "insufficient supply" driving up housing prices and thus raising a barrier to potential buyers. He

■ Clancy Terry is a current Master of Real Estate Development candidate through a joint program of Portland State University's School of Business Administration and School of Urban Studies and Planning. He is the 2015 RMLS Student Fellow at PSU's Center for Real Estate. Any errors or omissions are the author's responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.

cautions this trend could interact with an impending Federal Reserve rate hike to further restrict affordability.

Sales of existing homes grew most strongly in March, yet the number of unsold units for sale also increased, which Lawrence Yun identifies as a benefit to the market since he has been warning about the potential downsides of insufficient supply. At the close of March, two million existing homes were available for sale, a five percent increase from February and two percent greater than a year prior. This represented a 4.6 month supply. In terms of closed sales, a SAAR of 5.19 million transactions were completed in March, a six percent increase over February. For all existing housing types, March's median sale price was \$212,100, up eight percent year-over-year.

NAR also reports gradual increases in the share of first time buyers in the market, another welcome sign. The share of first time buyers rose in February for the first time since November 2014, to 29 percent from January's 28 percent. The share increased again in March to 30 percent, the same proportion seen in March 2014.

Freddie Mac reported a gradual increase in mortgage interest rates in March 2015. The average commitment rate for a 30 year conventional fixed rate mortgage reached 3.77 percent, up from 3.71 percent in February.

All cash sales registered declines throughout the first quarter, accounting for 27 percent of transactions in January, 26 percent in February, and 24 percent in March.

NAR released a new study in March analyzing the impact of rents rising faster than renters' incomes on home buying trends. Data surrounding income growth, housing costs, and changes in share of renter and owner-occupied housing units were compiled from 70 U.S. metropolitan statistical areas over a five year period. The study finds the gap between stronger rent growth and weaker income growth increasing barriers to homeownership among renter populations, with elusive new home construction key to fundamentally addressing this growing challenge. Explaining the findings, Lawrence Yun indicated the typical rent rose by 15 percent, yet renters' income experienced an overall 11 percent growth rate. He also explained that "an unequal distribution of wealth" has resulted as homeowners' net worth increases as home values appreciate and mortgage balances are paid down, while renters are simply faced with rising rents that hamper their ability to save. Also those rising home values impact renters similarly to rising rents as they seek to achieve ownership. One of the report's primary conclusions is that new home construction would have to increase significantly in order to temper price growth, and that a meaningful share of that envisioned new construction should be targeted at new and young first time buyers.

Indeed, Axiometrics reports total construction starts for privately owned housing units fell from January's revised SAAR of 1,081,000 units to a pace of 897,000 units

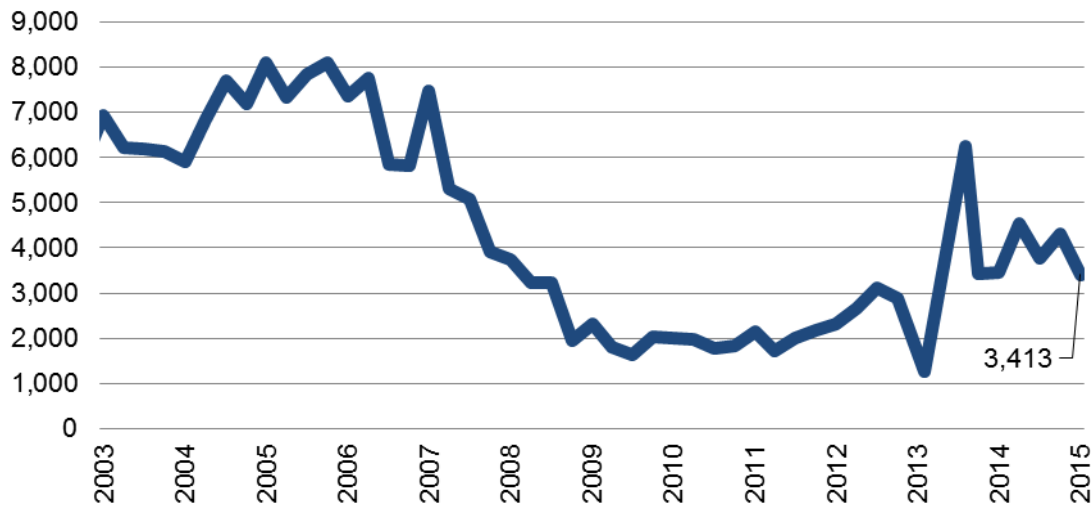
in February. The single family share of these totals fell in tandem, dropping around 15 percent from January to February and totaling 593,000 units. This should be tempered, though, by February's three percent increase in residential building permits over January. The 1,092,000 permits for privately owned housing units issued in February also represents a nearly eight percent year-over-year improvement. The single family share of these permits fell from January to February by six percent, however, with 620,000 single family units permitted in February. Nevertheless, Axiometrics cites several statistics in arguing national single family "continues to gain momentum." Actual single family units completed in February totaled 595,000 (SAAR), 12 percent less than January and four percent lower than a year prior.

## LOCAL PERMITTING

Statewide in Oregon, most measurements of permit issuances for new private housing registered declines in the first quarter of 2015 (as accounted on a seasonally adjusted basis). The Oregon total for this type of permit in the first quarter was 3,413, a 21 percent decrease of 902 permits from the prior quarter and a year-over-year decrease of approximately one percent or 50 permits. The Portland-Vancouver-Hillsboro Metropolitan Statistical Area (MSA) declined from the fourth quarter of 2014 by 16 percent or 506 to 2,609 permits, but did register a nine percent year-over-year increase of 225 permits.

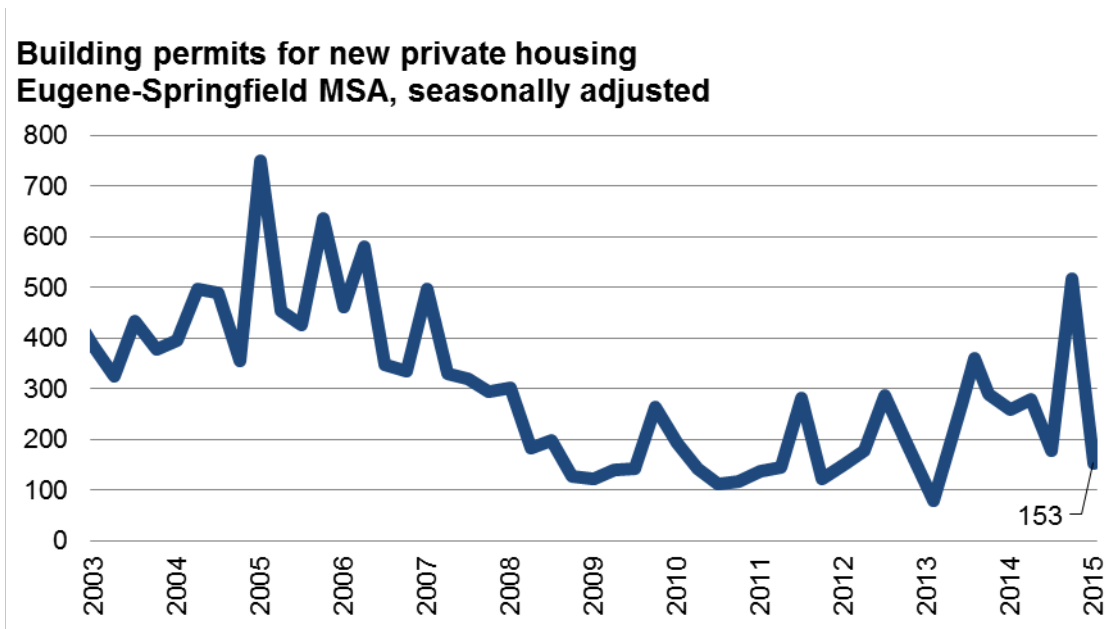
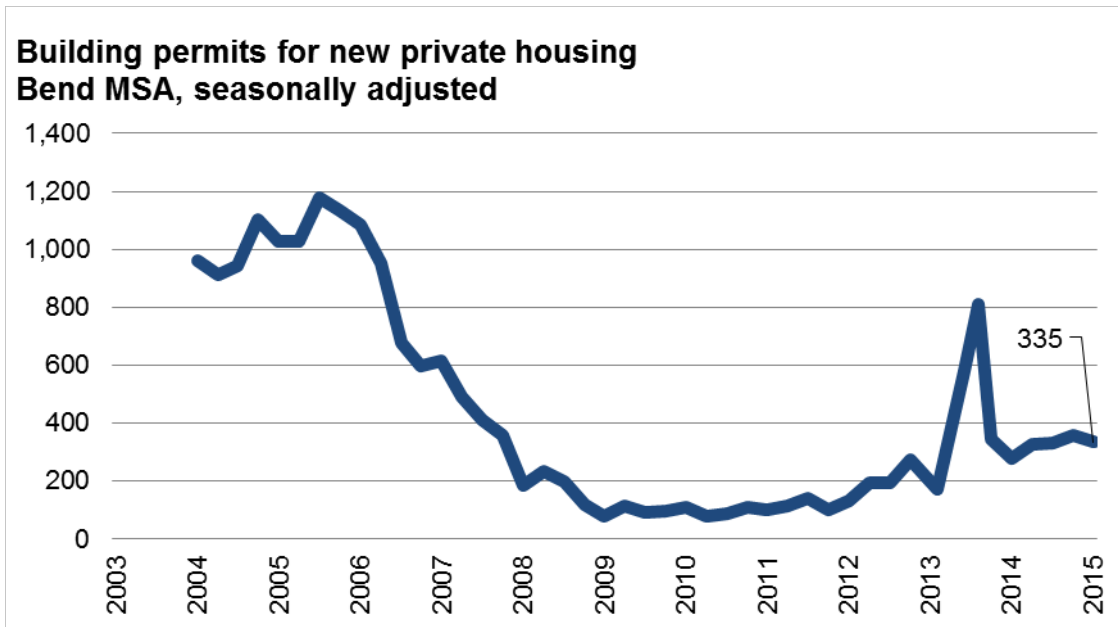
Following a similar pattern, permits issued in the Bend MSA declined from quarter to quarter by six percent, or 22, to 335 permits, a 21 percent year-over-year increase of 57 permits. The Eugene-Springfield MSA experienced a contraction as noteworthy as last quarter's expansion: 70 percent fewer permits were issued in the first quarter of 2015 versus the fourth quarter of 2014, decreasing by 364 to 153 permits (41 percent or 107 fewer year over year). The Medford MSA's total decreased from the prior quarter by 16 percent or 27 to 137 permits, representing 19 percent or 32 fewer than were issued in the first quarter of 2014.

**Building permits for new private housing  
Oregon, statewide, seasonally adjusted**

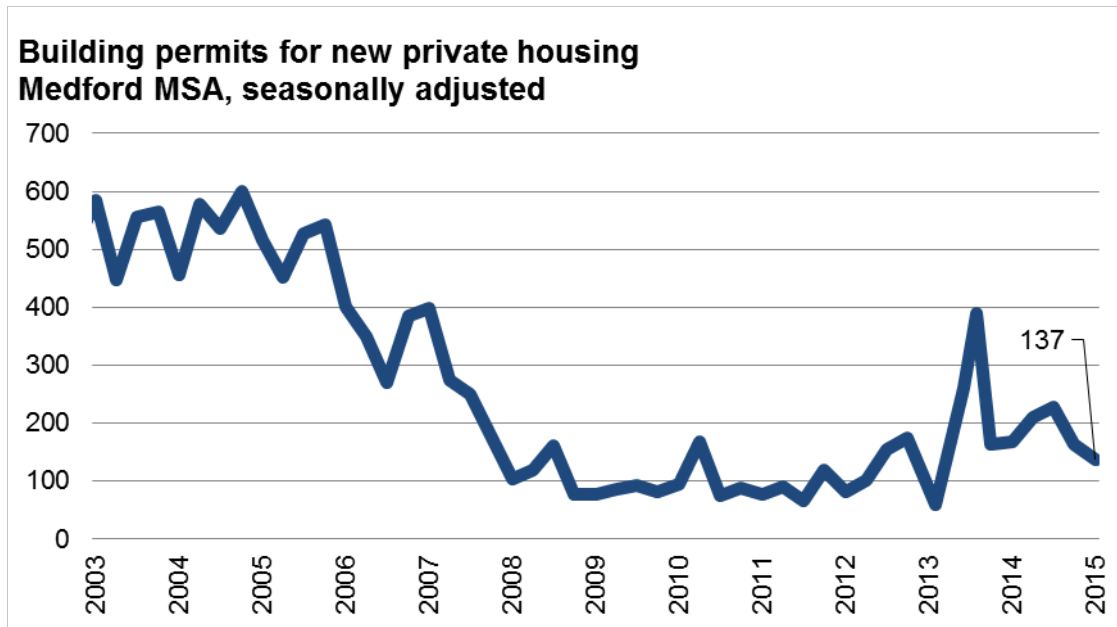


**Building permits for new private housing  
Portland-Vancouver-Hillsboro MSA, seasonally adjusted**









## PORTLAND

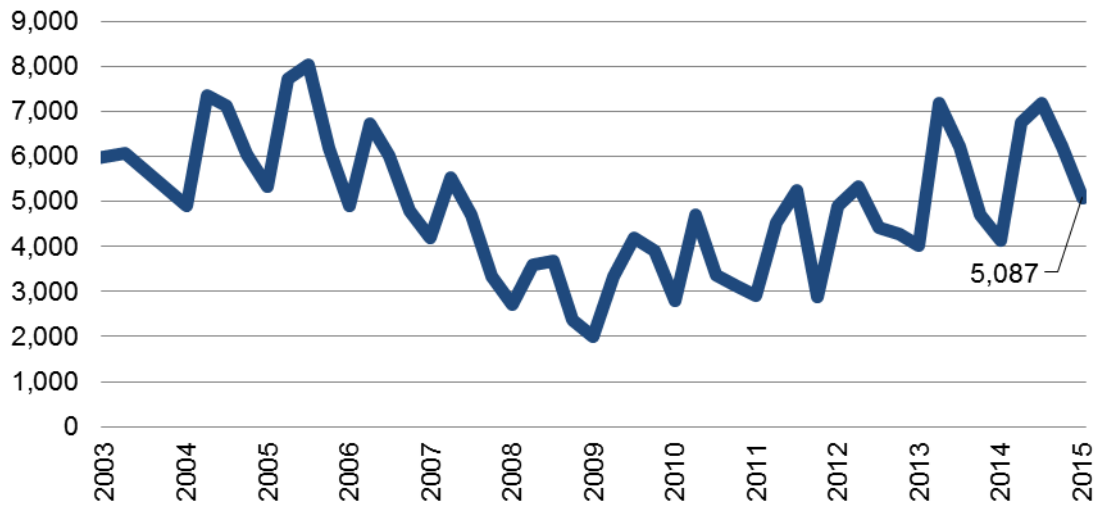
The market for existing homes in Portland continued the cooling trend it exhibited in the fourth quarter of 2014, and also continued the strengthening trend in year-over-year terms.

- 1,134 fewer units transacted versus the fourth quarter for a total of 5,087, an 18 percent drop, yet
- Year-over-year volume was around 23 percent greater.

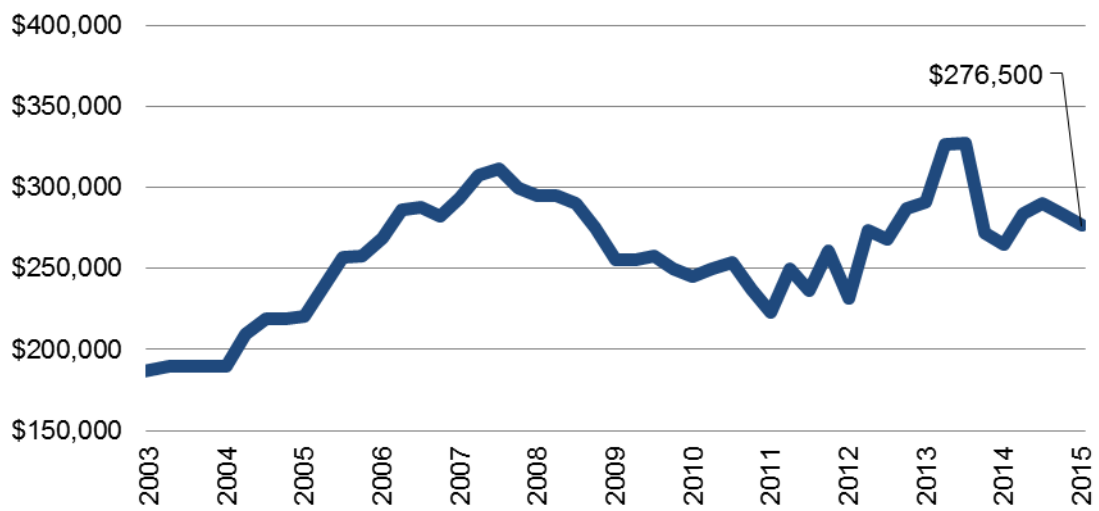
The median price continued declining, falling \$7,500 or three percent to \$276,500. Again on the (slightly) positive side, this is around five percent higher than 2014's first-quarter median price. Although average time on market increased by six percent to 57 days, this too outperforms the first quarter of 2014—by 17 percent. Sellers' realization of 99 percent of final list prices continues unchanged.

Both reported metrics in the new construction market showed improvement, most notably sales price. Buyers closed on seven percent more new detached single family units, bringing the first quarter's total to 585 (around 21 percent greater year over year). The nearly \$400,000 median price sets a new record among the data in this Quarterly publication. The price is \$35,000 (nearly 10 percent) higher than the prior quarter and 14 percent higher than first quarter 2014. This new construction median price has now surpassed its pre-recession peak.

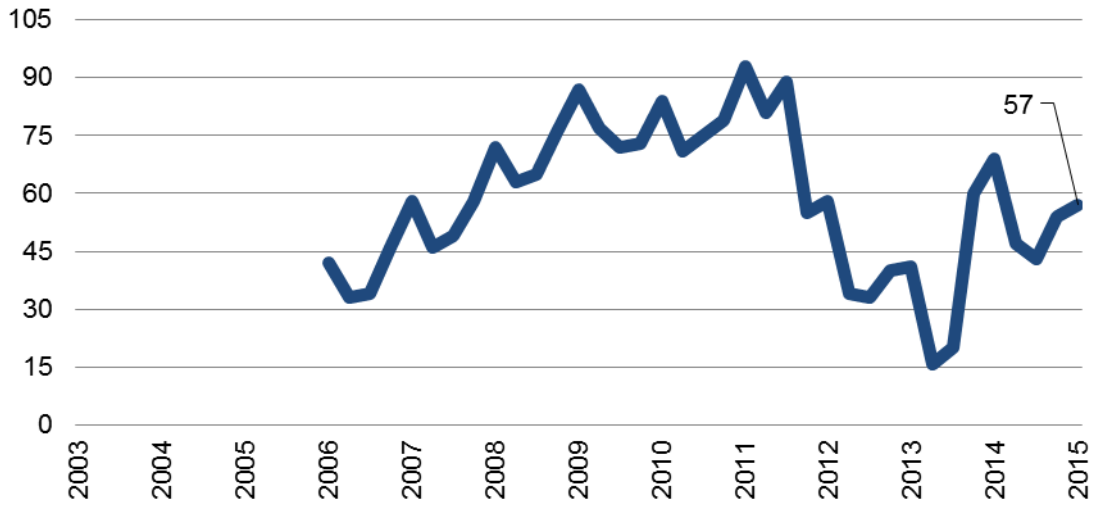
**Number of transactions**  
**Portland metro, existing homes**



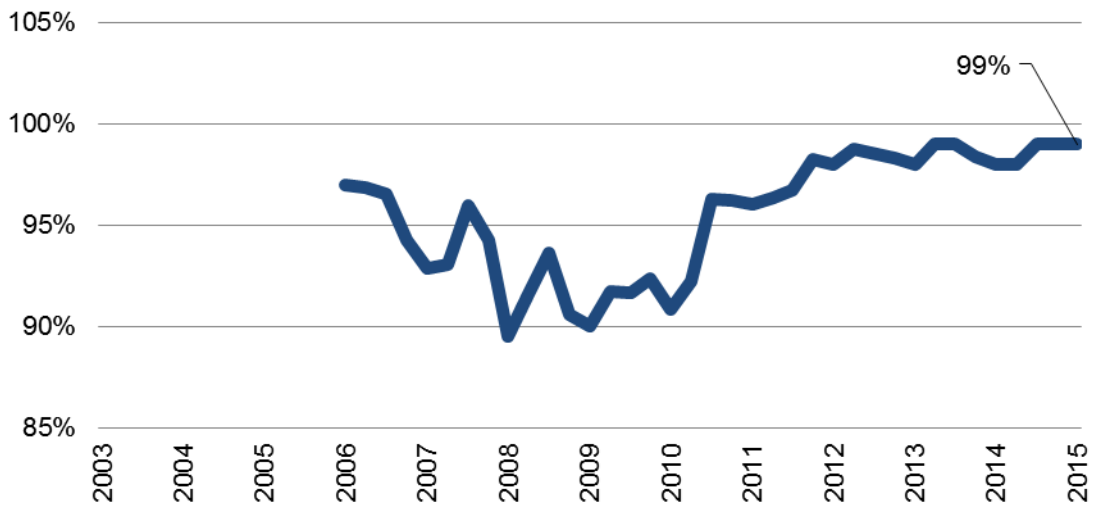
**Median sales price**  
**Portland metro, existing homes**



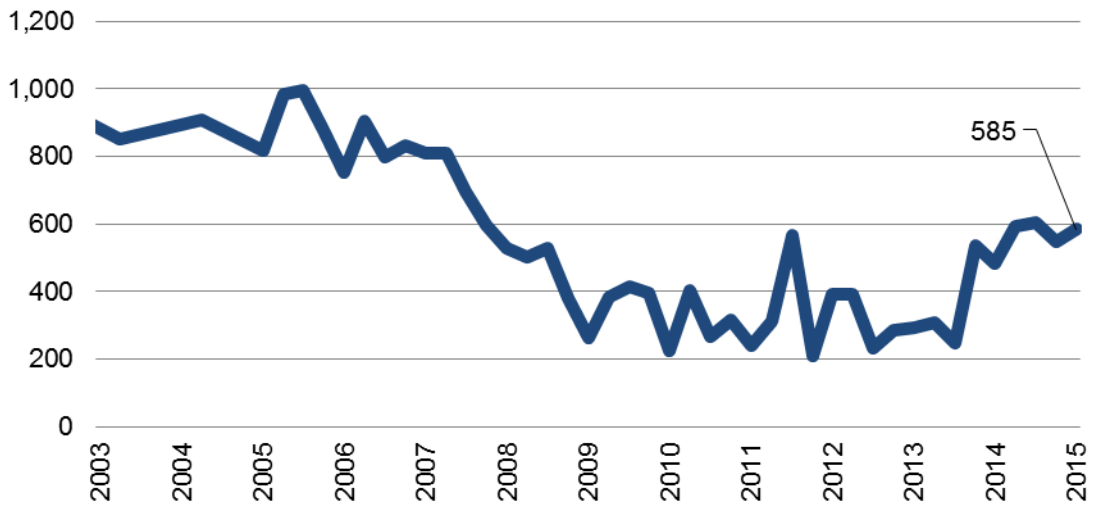
**Days on market**  
**Portland metro, existing homes**



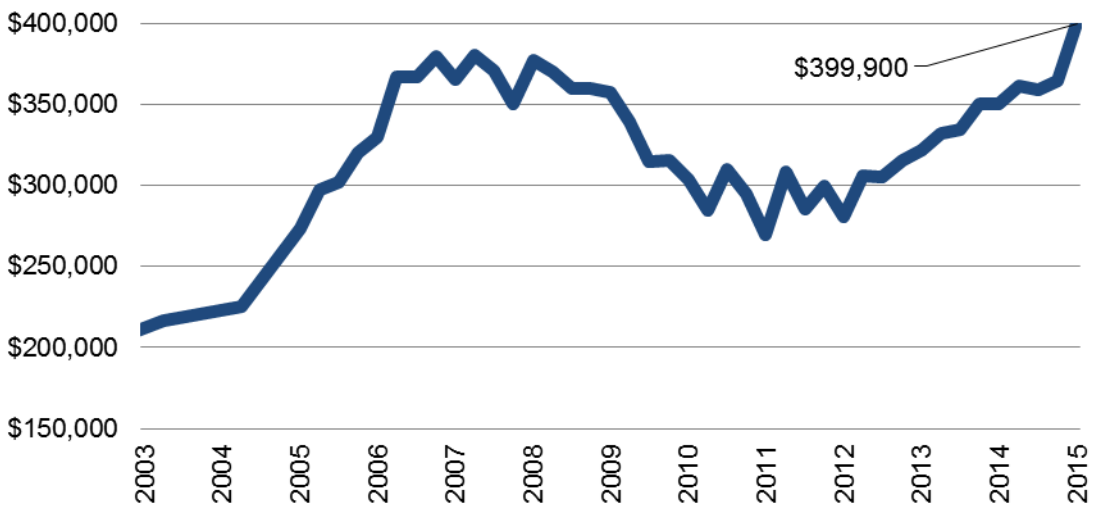
**Ratio of sales price to list price**  
**Portland metro, existing homes**



**Number of transactions**  
**Portland metro, new detached homes**



**Median sales price**  
**Portland metro, new detached homes**

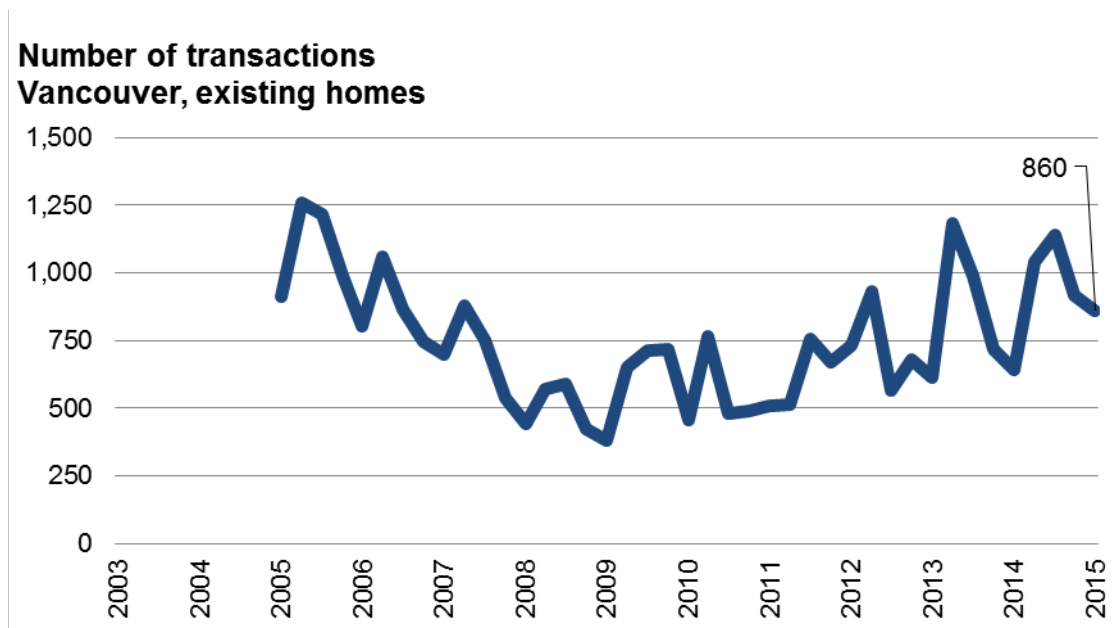


## VANCOUVER AND CLARK COUNTY

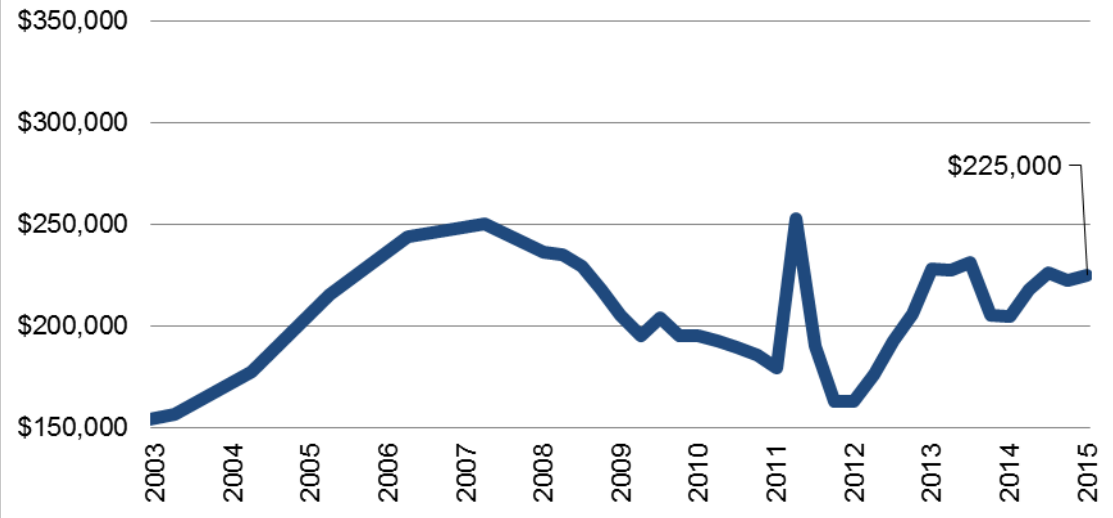
Trends in Vancouver and Clark County's existing housing stock showed many positive movements in the first quarter of 2015. Although transaction volume in Vancouver dropped by 55 units from fourth quarter 2014 to 860 (a decrease of almost six percent), 34 percent more closings were booked versus the first quarter of 2014.

Vancouver's median price nearly regained its losses from the prior quarter-over-quarter period, increasing around one percent or \$2,500 to \$225,000. More encouraging is the fact this price is \$20,550 or 10 percent greater in year-over-year terms. Average days on market increased by nine to 67, but this is 17 days faster than first quarter 2014. Sellers achieved 98 percent of final list prices.

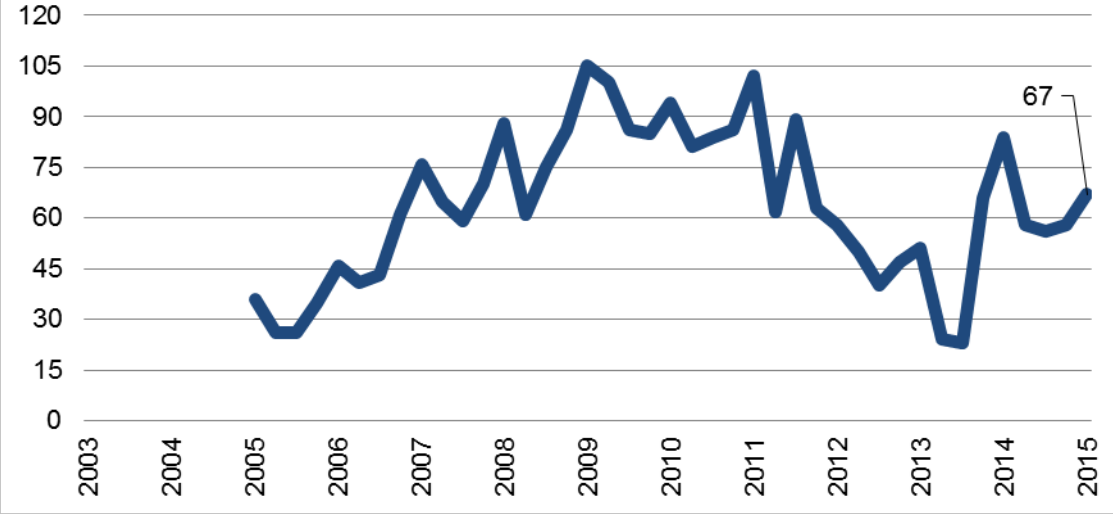
Against the fourth quarter of 2014, transaction volume in Clark County excluding Vancouver decreased by 121 units or 18 percent to 559, yet this is still 28 percent higher than the same period a year earlier. 2015's first quarter median price remained almost constant quarter over quarter, inching up to \$260,590; this is four percent or \$10,590 better than the first quarter of 2014. Houses averaged 84 days on the market, nine more days than in the prior quarter but 10 fewer days than during the first quarter of 2014. Sellers in this region also realized 98 percent of final list prices.



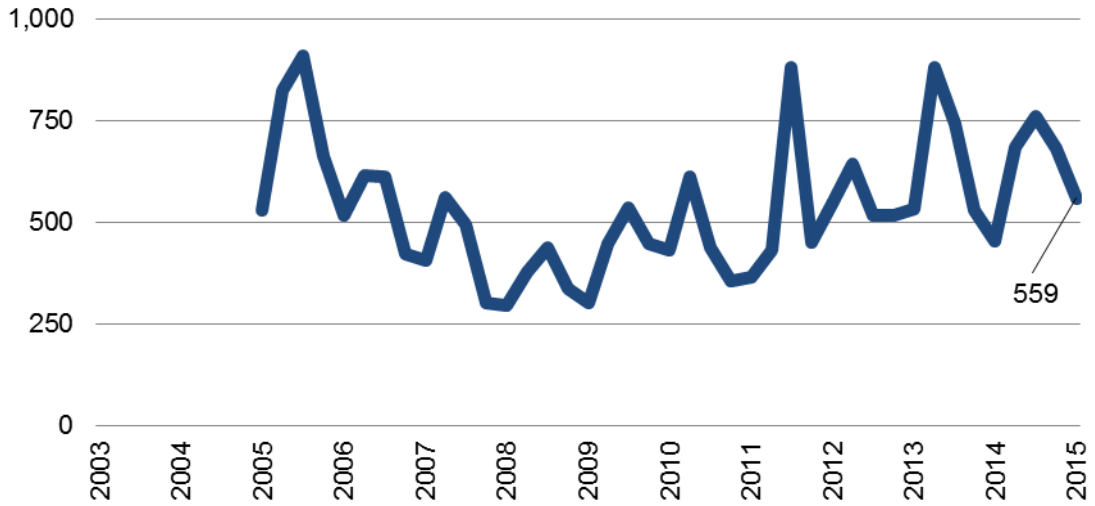
**Median sales price**  
**Vancouver, existing homes**



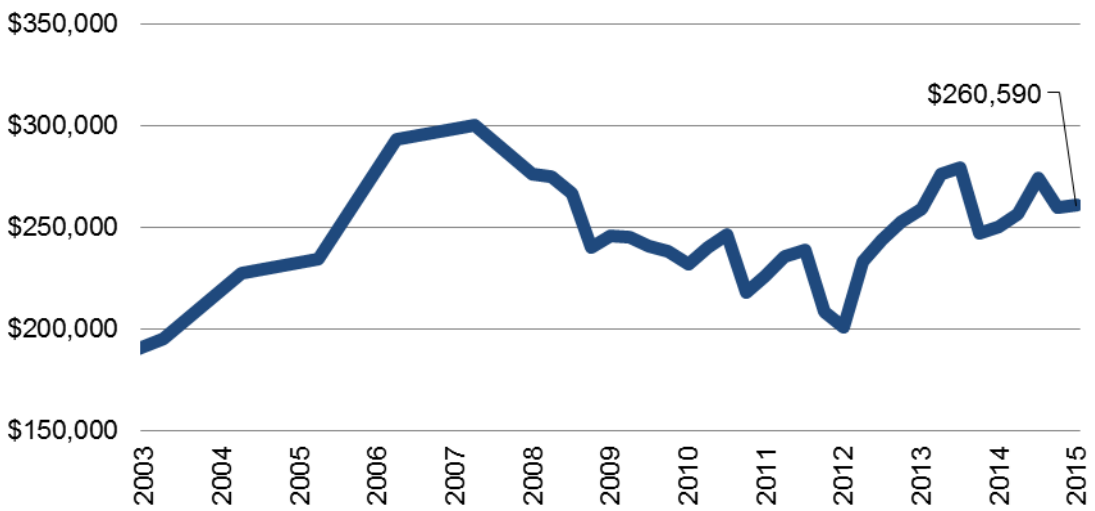
**Days on market**  
**Vancouver, existing homes**

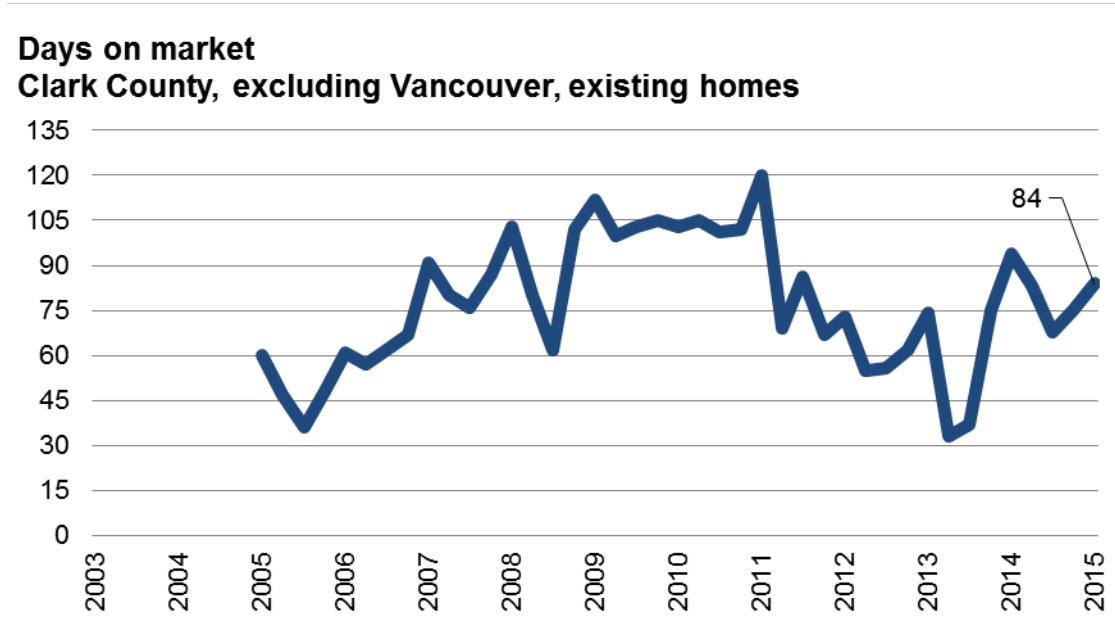


**Number of transactions**  
**Clark County, excluding Vancouver, existing homes**



**Median sales price**  
**Clark County, excluding Vancouver, existing homes**





## CENTRAL OREGON

As reported in the Winter 2015 edition of the Quarterly Report, the annual transaction volume trends of Bend and Redmond over the last two years have followed a distinct geometric pattern of start of the year valleys and mid-year peaks. So far, this pattern continues, as shown in the “Number of transactions” charts below. Note that Redmond’s pattern over the last two years is very symmetrical, with the greater area under the 2014-2015 curve versus the 2013-2014 curve suggesting a market expansion.

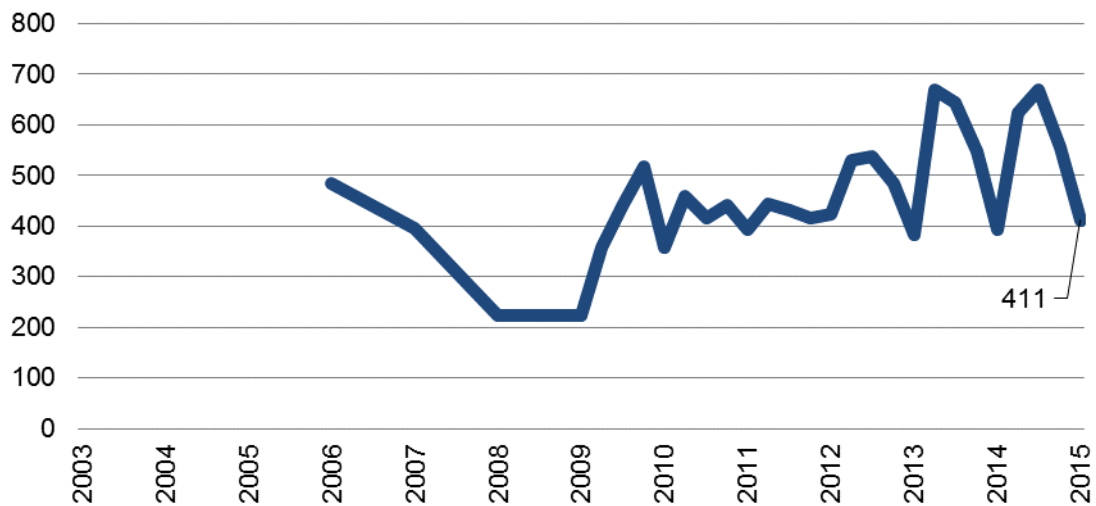
For Bend, total transactions in the first quarter of 2015 fell by 145, to 411 units sold—a 26 percent contraction. This is 19 units or five percent more than were sold in the first quarter of 2014, however. The median sales price continued its upward momentum, increasing from the prior quarter by \$25,050 or nine percent to \$315,000, nearly setting a record. This is \$65,000 or 26 percent greater than first quarter 2014. A median price higher than \$315,000 has not been reported in this publication since the first quarter of 2007. It took sellers longer to realize these



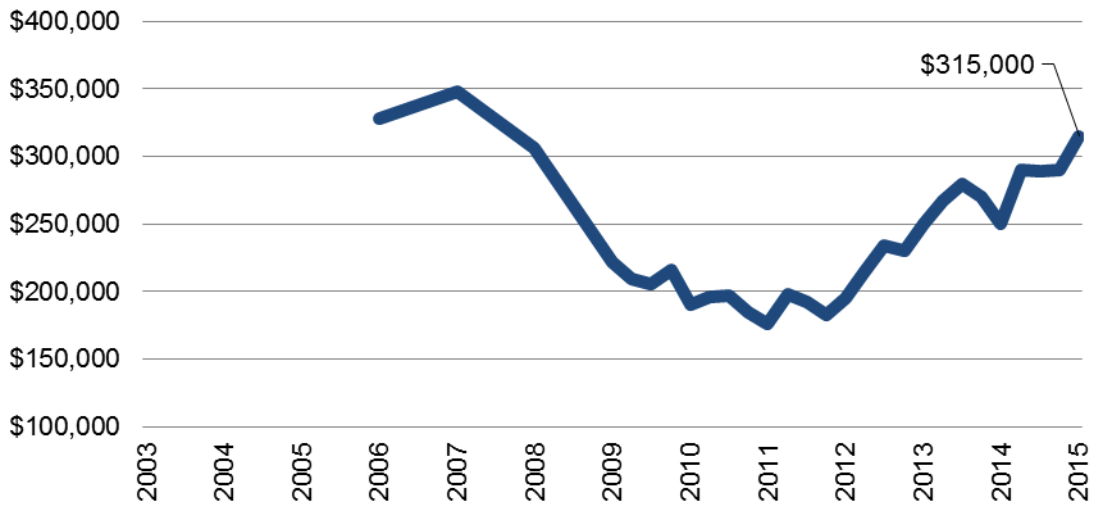
higher prices, however: from the fourth quarter of 2014 average marketing time increased by 22 days to 139; this is 13 days longer year over year.

For Redmond, transaction volume in the first quarter decreased by 20 units or 12 percent to 146 homes, but this is still 14 percent more units sold year over year. The median price rebounded, increasing by 7 percent or \$13,700 to \$209,974, which represents a 17 percent or \$30,000 year-over-year increase. Marketing time increased from fourth quarter 2014 by five days to 130 days on market, representing a slight improvement of two percent (three days faster) versus the first quarter of 2014.

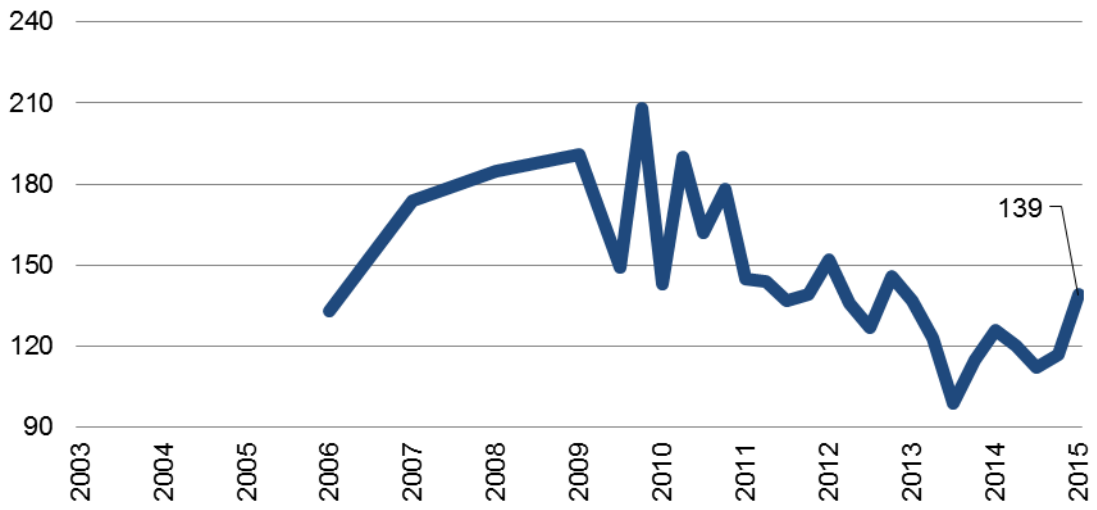
**Number of transactions  
Bend, under 1 acre**

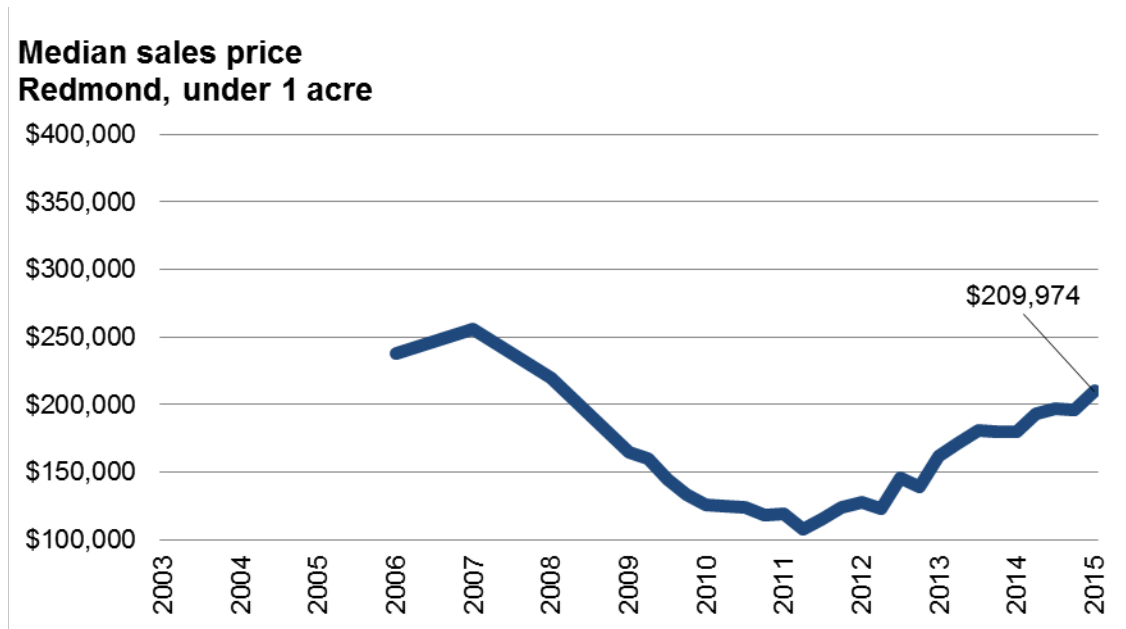
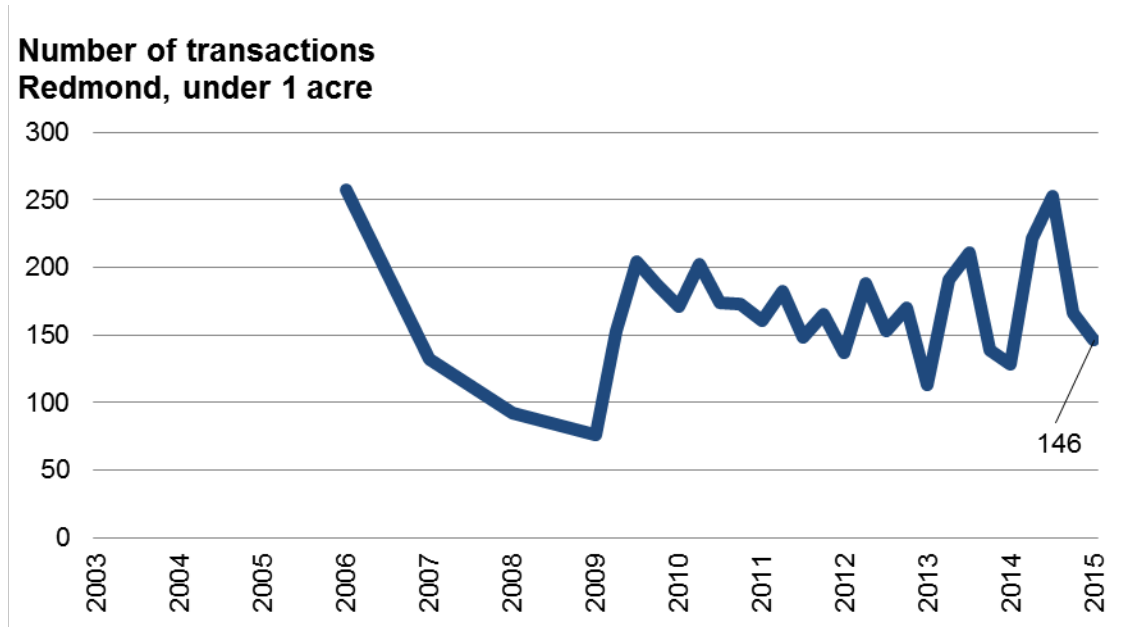


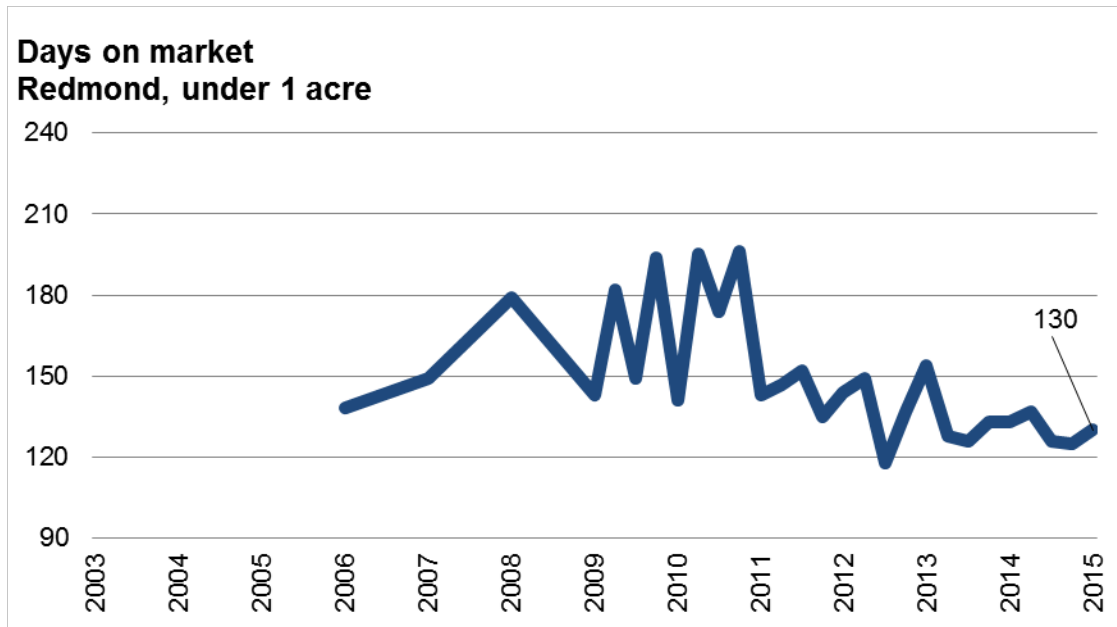
**Median sales price  
Bend, under 1 acre**



**Days on market  
Bend, under 1 acre**



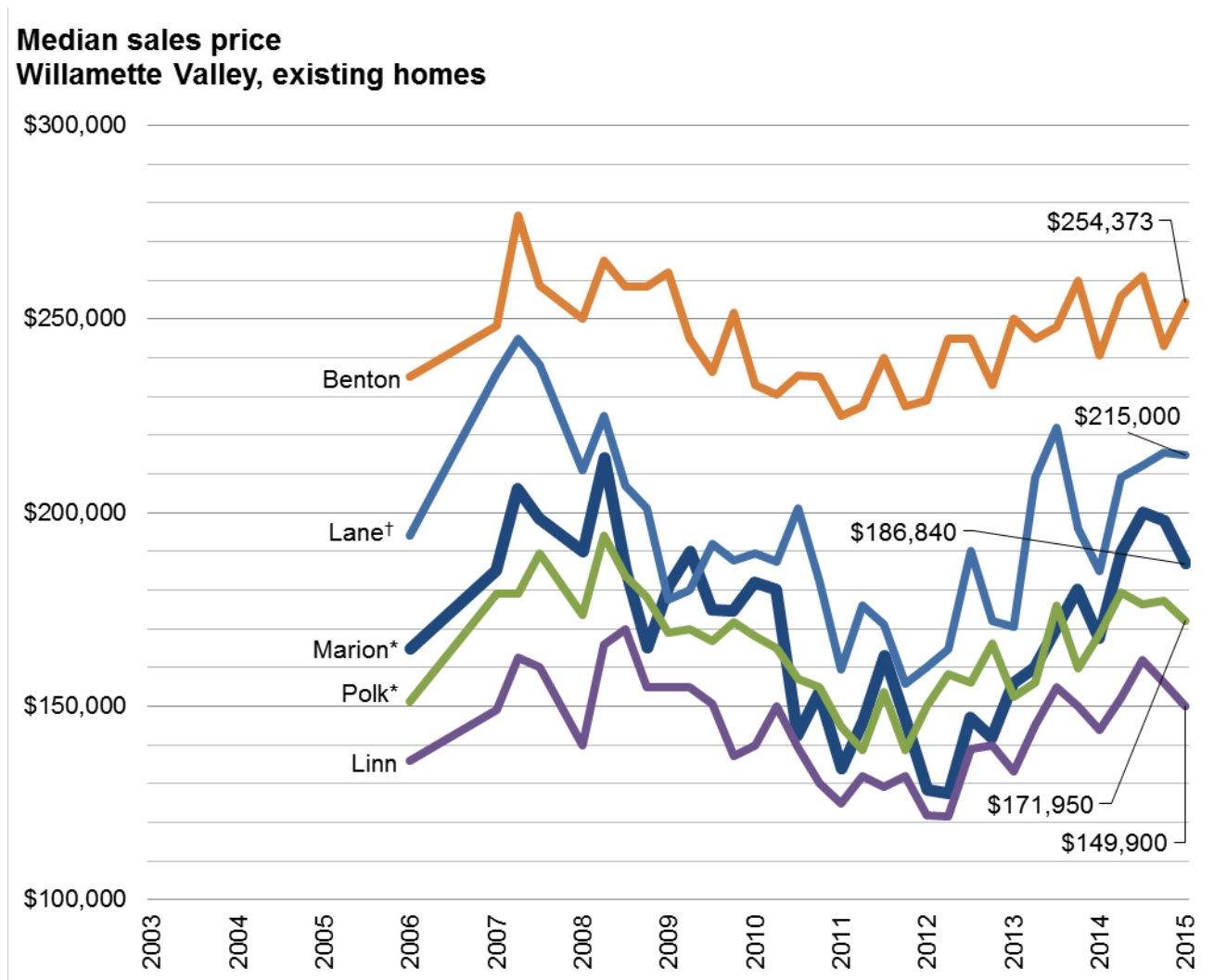




## WILLAMETTE VALLEY

Benton County was the only jurisdiction to post an increase in median sales price during the first quarter of 2015 versus the final quarter of 2014. That being said, the quarter-over-quarter declines in the remaining counties were relatively small, and prices in all five counties grew in year-over-year terms.

- Benton County: \$254,373, five percent increase of \$11,373; six percent increase of \$13,750 year over year
- Lane County (excluding Eugene): \$215,000, less than one percent decrease of \$500; 16 percent increase of \$30,050 year over year
- Marion County (excluding Salem): \$186,840, six percent decrease of \$11,160; 12 percent increase of \$19,390 year over year
- Polk County (excluding Salem): \$171,950, three percent decrease of \$5,300; two percent increase of \$3,250 year over year
- Linn County: \$149,900, four percent decrease of \$6,100; four percent increase of \$6,000 year over year



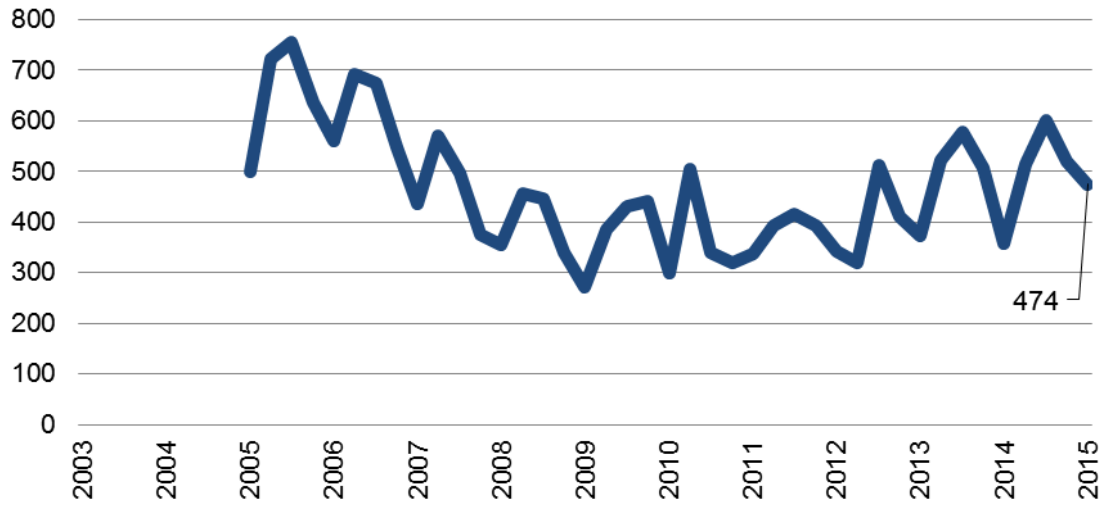
†Excluding Eugene

\*Excluding Salem

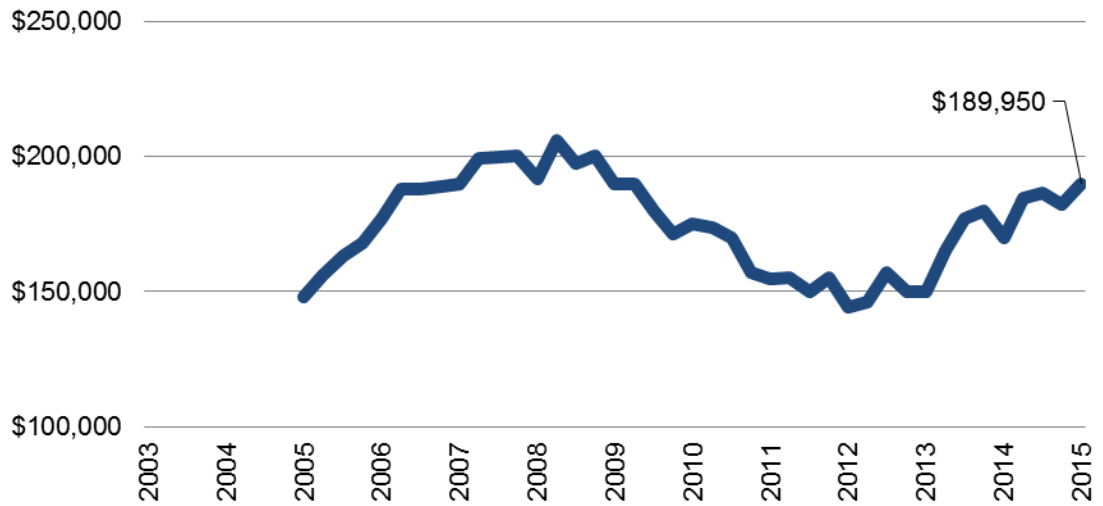
**SALEM**

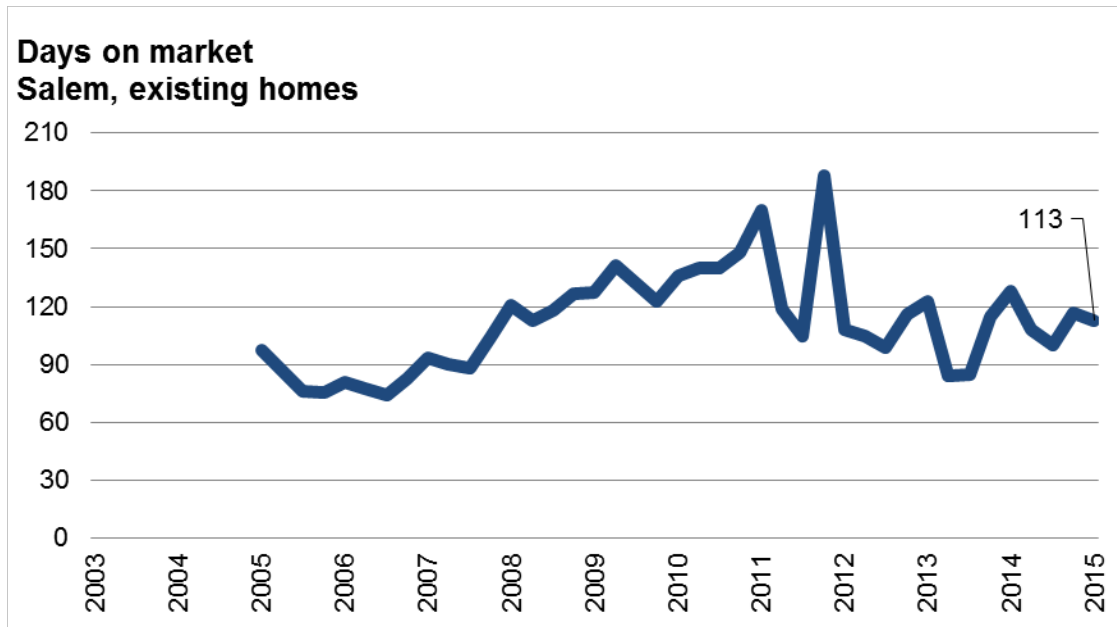
Transaction volume in Salem decreased by 46 units to 474 sales, a nine percent reduction. Year over year, however, the number of transactions is 33 percent stronger. The median price increased over the fourth quarter of 2014 by four percent or \$7,700, reaching \$189,950. This is 12 percent or nearly \$20,000 more than the prior year period. From both time perspectives, homes sold faster in the first quarter: units averaged 113 days on the market, four days and four percent better than the fourth quarter, and 15 days or 12 percent faster than the first quarter of 2014.

**Number of transactions  
Salem, existing homes**



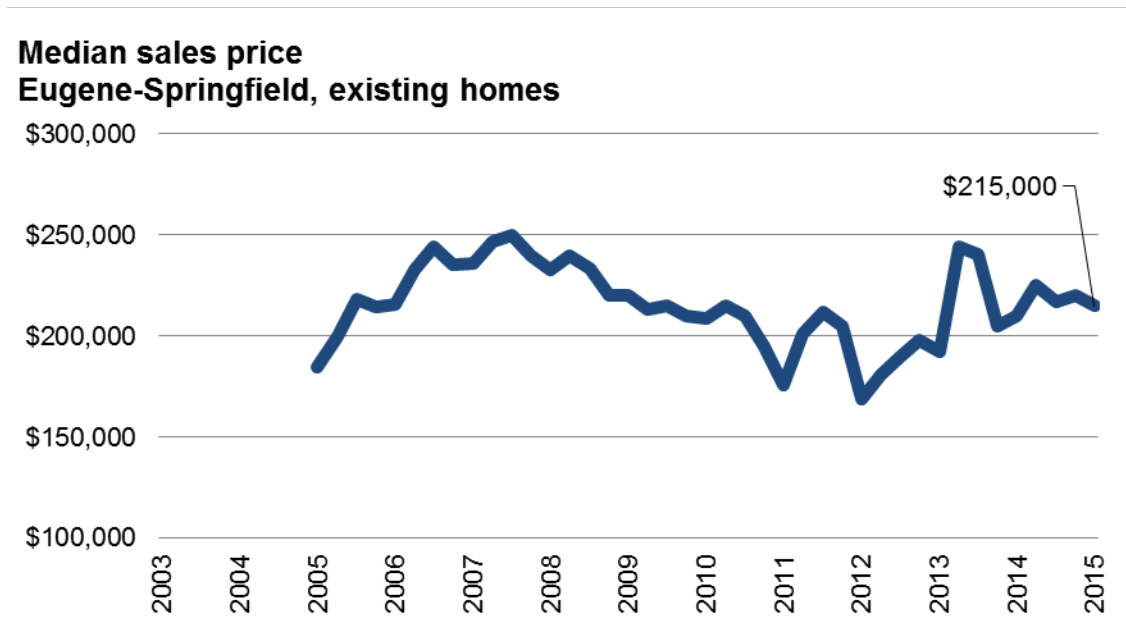
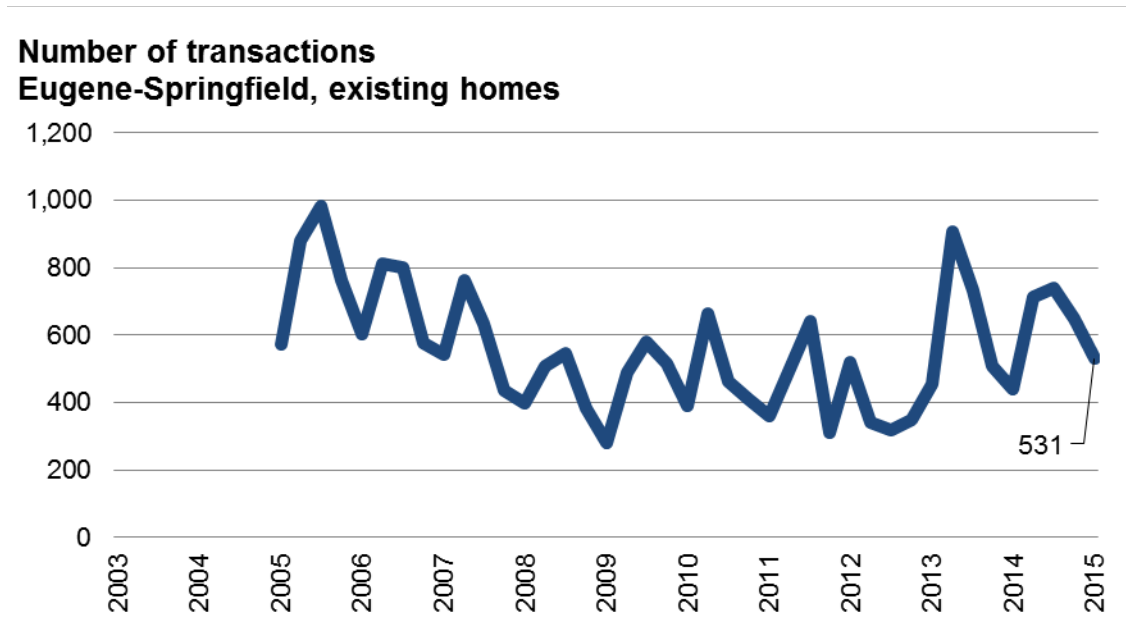
**Median sales price  
Salem, existing homes**





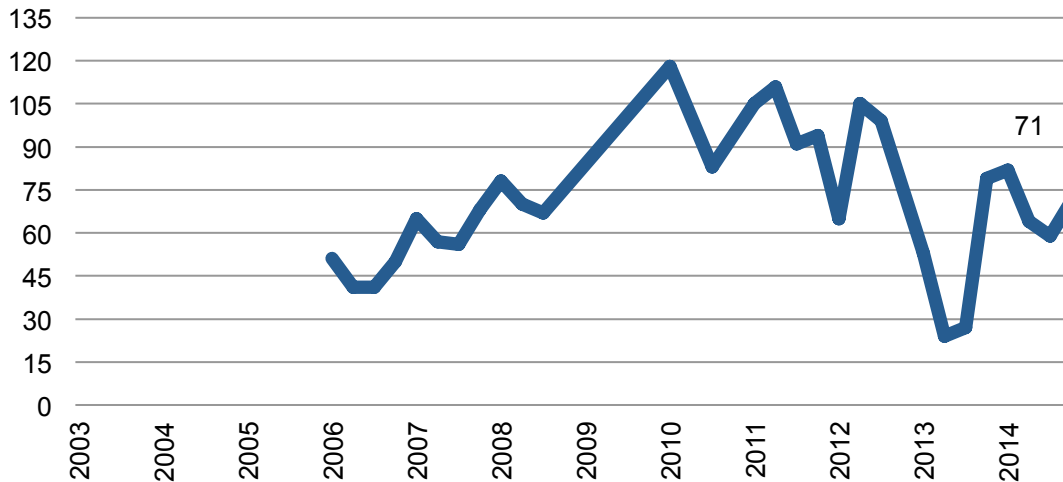
## EUGENE-SPRINGFIELD

Although the Eugene-Springfield market experienced another decline in transaction volume of 110 units to 531 (a 12 percent drop) compared to the prior quarter, this is still 20 percent or 90 more sold units than during the first quarter of 2014. The median sales price fell by \$5,000 or one percent to \$215,000 from the prior quarter, but this price is two percent or \$5,000 better than the first quarter of 2014. While marketing time increased 20% or five days to 76 days in the short term, this is seven percent or six days shorter in year-over-year terms.





### Days on market Eugene-Springfield, existing homes



## SOUTHERN OREGON

Data for southern Oregon comes to us on a rolling three month basis, thus the following information pertains to the period December 1, 2014 through February 28, 2015.

During this time, Josephine County posted a median sales price of \$183,500, marginally better than the prior quarter but nine percent or \$14,750 greater than the same period a year earlier. 118 sales closed, four percent fewer than fourth quarter 2014 but 37 percent more year over year. Properties spent longer on the market during the most recent period, averaging 81 days listed; this is 12 days or 17 percent more than the prior period but 15 days or 16 percent faster year over year.

Meanwhile, Jackson County's median price is reported at \$209,000, two percent or \$4,000 more than the prior quarter and 11 percent or \$21,500 more year over year. 419 sales closed, 127 units or 23 percent fewer than the prior quarter but 74 units or 21 percent more year over year. Properties also seem to be taking longer to sell in Jackson County lately, averaging 73 days on the market—17 days or 30 percent longer than the prior quarter and 9 days or 14 percent longer year over year. ■

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## MULTIFAMILY MARKET ANALYSIS

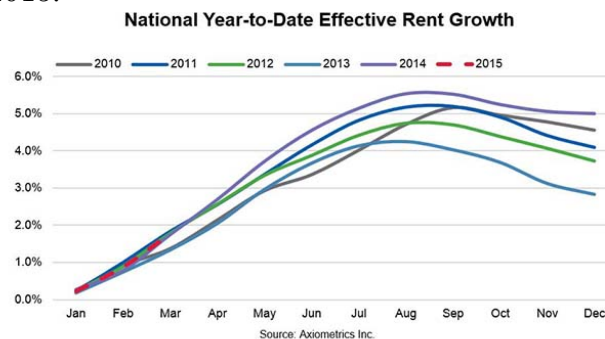
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CLANCY TERRY

RMLS Student Fellow  
Master of Real Estate Development Candidate

At the national level, annual effective rent growth in the multifamily sector has displayed some of the strength that it does in Portland. As reported by Axiometrics, the growth rate was five percent or above for two consecutive months by March 2015, reaching a level not seen since the summer of 2011. This national rent growth rate was nearly the same as that seen in February 2015, and was the highest registered since March 2011.

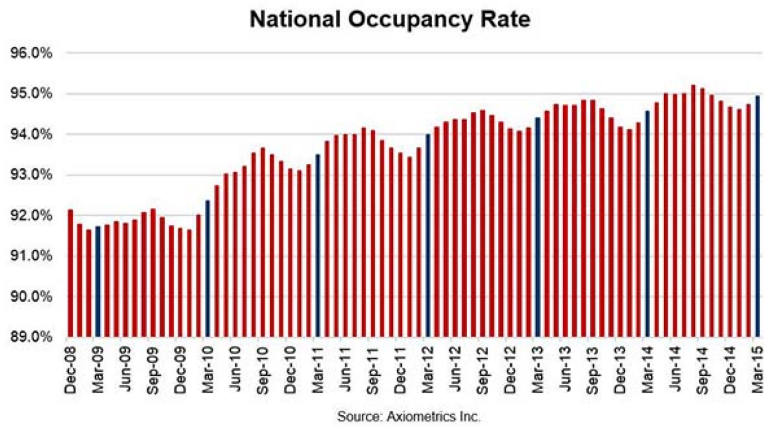
Axiometrics points out that “the second quarter is usually the strongest of the year for rent growth, as shown by the chart below, so the next three months will likely be crucial to the fate of 2015.”



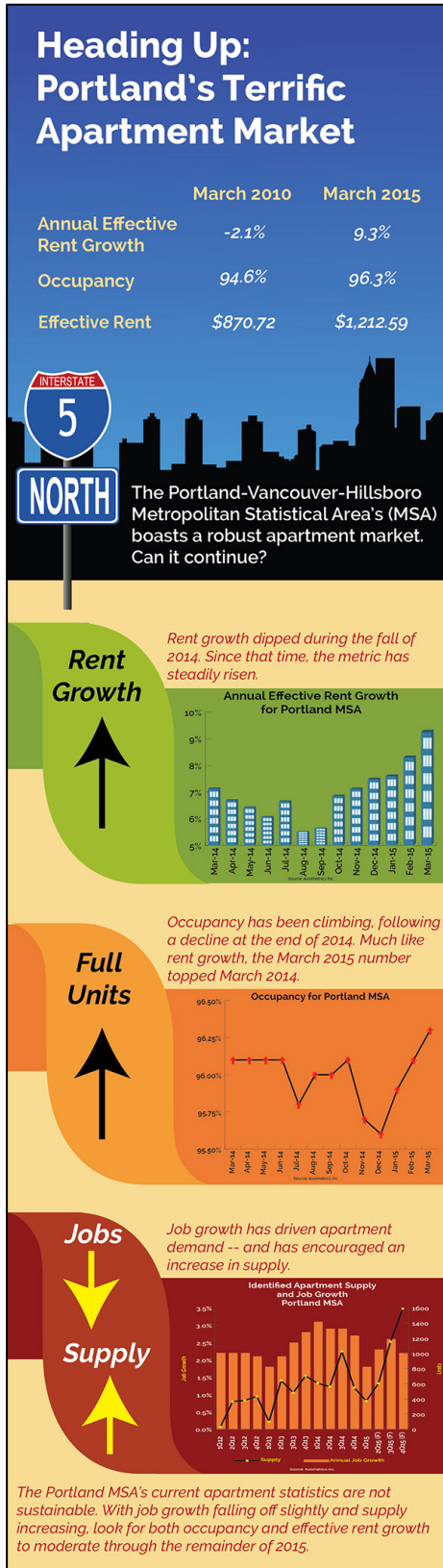
■ Clancy Terry is a current Master of Real Estate Development candidate through a joint program of Portland State University’s School of Business Administration and School of Urban Studies and Planning. He is the 2015 RMLS Student Fellow at PSU’s Center for Real Estate. Any errors or omissions are the author’s responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.



In terms of apartment occupancy across the U.S., the national rate in March 2015 was 94.9 percent, a slight improvement over both the prior quarter and the prior year’s same timeframe. The increase has also now been trending for two consecutive months, beginning to correct a five-month series of decreases beginning August 2014.



## PORTLAND APARTMENT MARKET



The infographic at left is courtesy of Axiometrics. It summarizes many of the aspects of Portland's current multifamily market that are regularly reported. Two points are interesting. The first is that while job growth continues, the rate at which employment is growing slowed during the first quarter. Second, the piece asserts the market's performance is "not sustainable." This is likely reasonable given the long-term impact of robust supply deliveries and other factors. And yet, with the structural changes brought to the Portland economy in general due to large population in-migration, the multifamily market's statistics could moderate to more stable growth indicators in the long term, rather than undergo major downward correction.

The 9.3 percent annualized effective rent growth is specific to Axiometrics' March 2015 measurements. For that month, this growth rate places Portland fifth among 50 metros examined, behind only Oakland (15.33 percent), San Jose (11.97 percent), Denver (11.47 percent), and San Francisco (11.12 percent). From a quarterly perspective, the Portland MSA places sixth in annualized effective rent growth terms: first-quarter effective rent growth in Portland, per Axiometrics, was 8.2 percent. The only MSAs outpacing Portland in the first quarter were Oakland (14.9 percent), San Francisco (12.6 percent), Denver (11.9 percent), San Jose (11.3 percent), and Sacramento (8.4 percent).

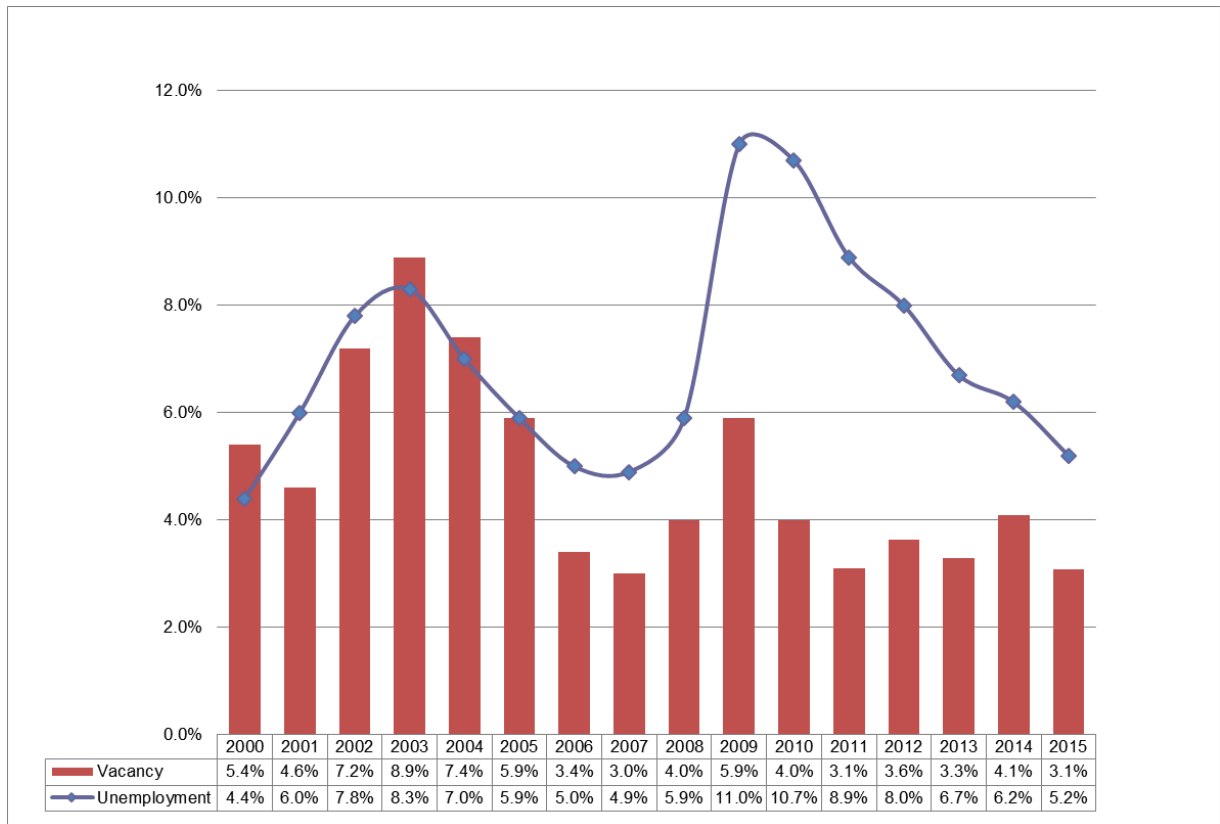
The Barry Apartment Report for spring 2015 pegs Portland's apartment vacancy at the sixth lowest in the U.S. as of the end of the fourth quarter of 2014. The Barrys point to the most recent Multifamily Northwest Apartment Report's findings that vacancy in Portland has fallen to roughly three percent, a decrease from the fall of 2014. 17 of the 20 submarkets surveyed in that Report registered vacancies under four percent. The highest vacancies were reported in downtown, as well as in Tigard and Aloha in centers outside of Portland. New construction in Portland's downtown core appears to be having an impact on vacancy, bringing a small measure of relief to a market constrained by previously existing supply and very robust demand. The

Barrys predict vacancies will settle somewhere between 4 percent and 4.75 percent in 2016.

Meanwhile, Colliers International Portland office is forecasting another strong year in the local multifamily market, with several fundamentals resembling their 2014 performance. For example, the group predicts key segments of both the Millennial and Baby Boom generations will either continue to prefer renting or begin to find it attractive. Job growth and general expansion in the local and regional economy are predicted to continue supporting strong demand for apartments and Portland renters’ ability to keep pace with rising rents.

The graphic below displays Multifamily Northwest’s measurement of the Portland metro’s apartment vacancy at 3.09 percent (a marked drop reflecting continued strong absorption) and the Oregon Employment Department’s unemployment rate for the Portland-Vancouver-Hillsboro Metropolitan Statistical Area in March 2015 at 5.2 percent.

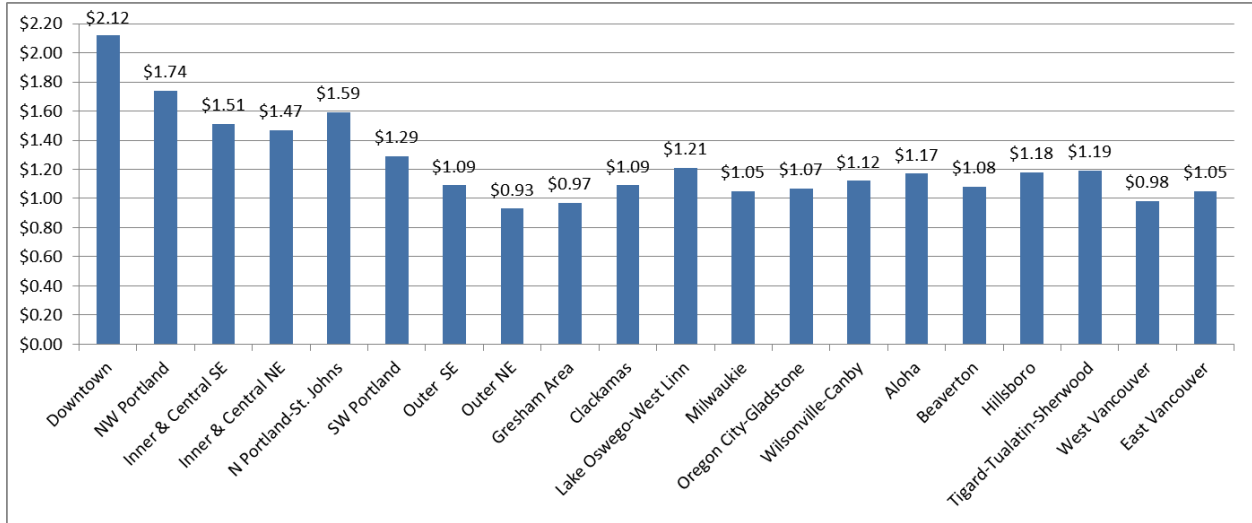
**Unemployment and multifamily vacancy  
Portland metropolitan area**



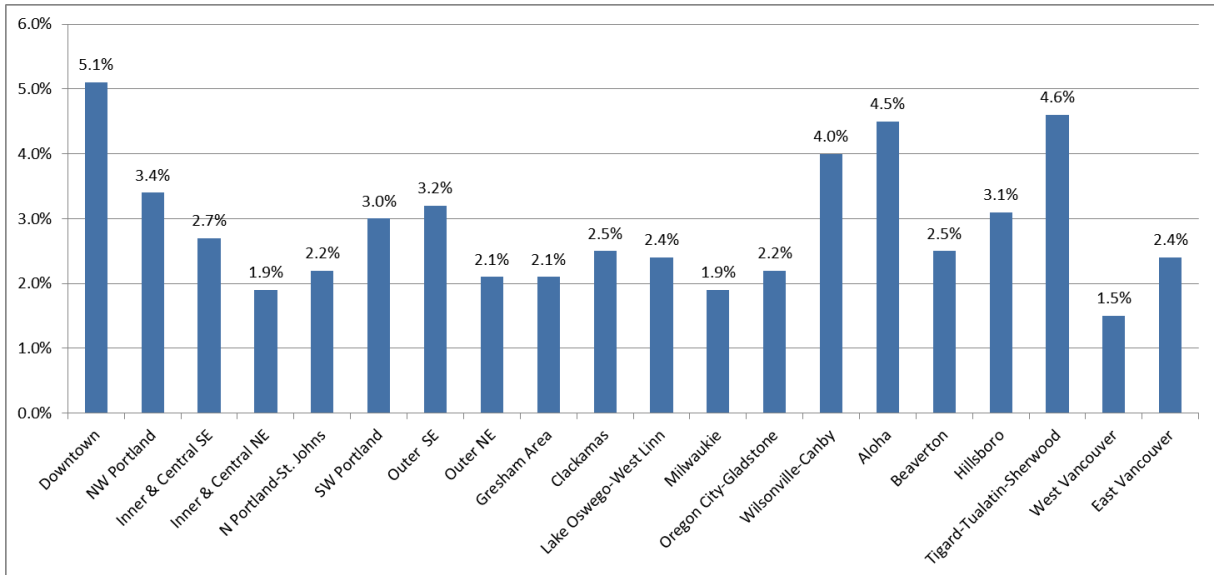
Source: Multifamily Northwest; Oregon Employment Department

Below are representations of Multifamily NW's average rents per square foot and average vacancy rates for the 20 Portland submarkets that publication surveys.

**Rent/SF by Submarket, Spring 2015**



**Vacancy Rate by Submarket, Spring 2015**



## TRANSACTIONS

Sperry Van Ness | Bluestone & Hockley has compiled the following data on multifamily transactions over \$450,000 for the first quarter of 2015:

In January 2015, 21 properties traded versus January 2014's 18 sales. Volume totaled \$164,289,570—52 percent greater than January 2014. Averages for these 21 transactions are as follows: 44.3 units, \$7,823,313 price, \$184,960/unit, 1,202.3 square feet/unit, \$152.10/square foot, 5.57 percent average reported cap rate.

In February 2015, 25 properties traded versus eight in February 2014. Dollar volume reached \$142,281,600 or 195.4 percent greater than February 2014. Averages for these 25 transactions are as follows: 46.2 units, \$5,691,264 price, \$128,297/unit, 839.5 square feet/unit, \$159.52/square foot, 6.12 percent average reported cap rate.

In March 2015, 21 properties traded compared to 13 in March 2014. Dollar volume was again up, reaching \$126,497,025. Averages for the 21 transactions are as follows: 48.1 units, \$6,023,668 price, \$125,245/unit, 908.6 square feet/unit, \$145.50/square foot, 5.21 percent average reported cap rate.

Year to date through March 2015, total dollar volume of sales reached \$468,622,575 on 74 total transactions.

Colliers Portland reports the following significant trades in the first quarter:

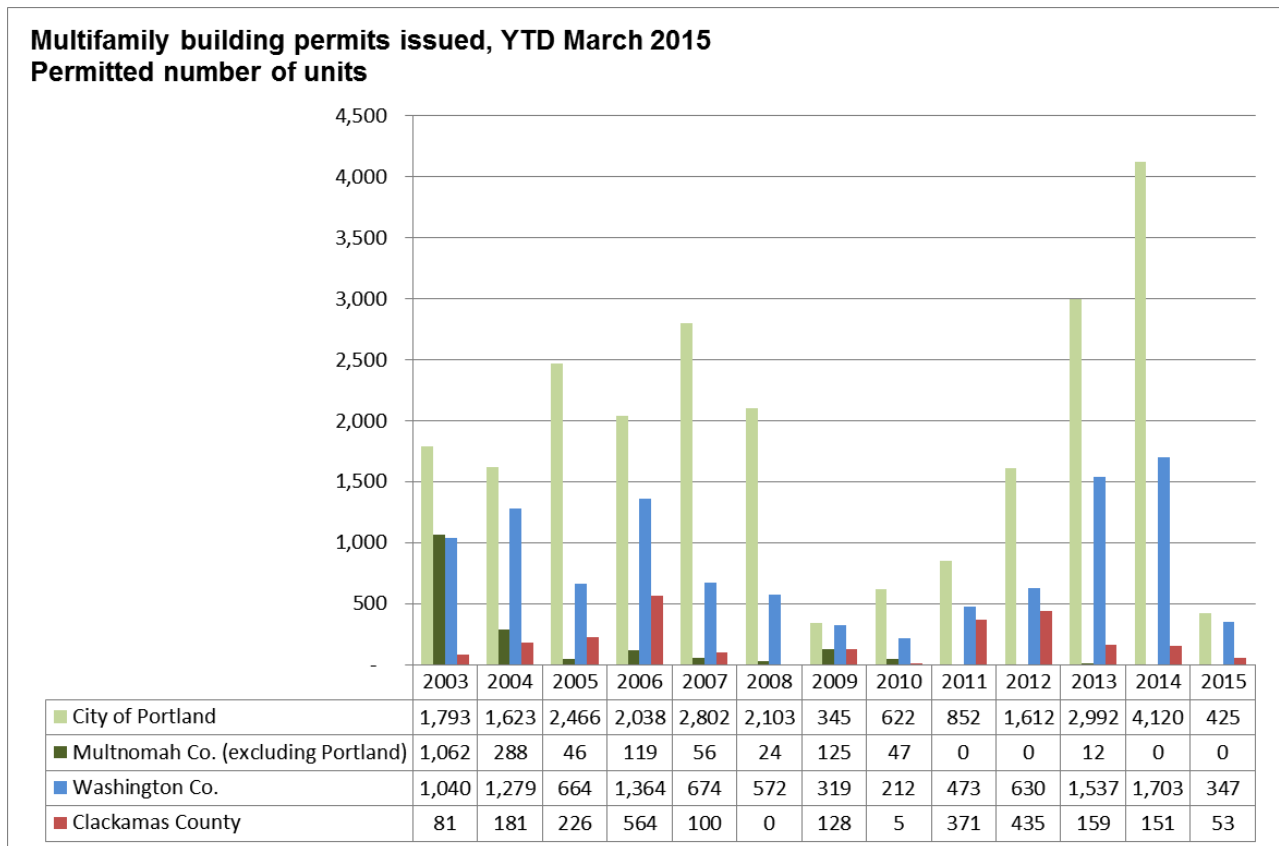
Project	City	Sale Date	Sales Price	# Units	Price/Unit	Price/SF	Cap Rate
Jory Trail at the Grove	Wilsonville	2/27/2015	\$59,000,000	324	\$ 182,099	\$ 144.08	6.00
Element 170	Beaverton	1/27/2015	\$39,000,000	244	\$ 160,494	\$ 200.62	
Central Eastside Lofts	Portland	1/4/2015	\$18,945,000	70	\$ 270,643	\$ 311.34	4.82
Harbour Court Apartments	Portland	2/27/2015	\$17,700,000	99	\$ 178,788	\$ 185.50	5.00
Willow Grove Apartments	Beaverton	2/27/2015	\$17,300,000	119	\$ 145,378	\$ 155.49	
Jasper Place	Beaverton	2/27/2015	\$14,800,000	100	\$ 148,000	\$ 150.25	
Jasper Square	Beaverton	2/27/2015	\$12,900,000	83	\$ 155,421	\$ 159.85	
Westover Tower Apartments	Portland	2/24/2015	\$12,400,000	70	\$ 177,143	\$ 398.53	4.59
Beaumont Village Apartments	Portland	2/25/2015	\$11,500,000	50	\$ 230,000	\$ 372.42	5.25
Gardenbrook Apartments	Beaverton	2/24/2015	\$ 9,800,000	120	\$ 81,667	\$ 159.82	
Colonial Gardens Apartments	Portland	2/27/2015	\$ 9,250,000	72	\$ 128,472	\$ 144.11	
Willowcreek Apartments	Beaverton	2/17/2015	\$ 8,300,000	77	\$ 107,792	\$ 89.79	
The Timbers	Vancouver	1/7/2015	\$ 7,830,000	45	\$ 174,000	\$ 125.55	

ABR Winkler Real Estate Services reports the following multifamily sales statistics through the period ended March 2015:

Average price per foot	\$126
Median cap rate	6.37%
Dollar volume of sales	\$300,014,512
Median gross rent multiplier	8.46
Median price per unit	\$94,243
Average price	\$6,040,405
Average number of units	46

## PERMITS

The proportional relationships among the four jurisdictions covered in this section—City of Portland, Multnomah County excluding Portland, Washington County, and Clackamas County—remained unchanged in terms of number of multifamily permits issued for buildings with five or more units. 425 multifamily units in such developments were issued in Portland, zero were issued in the balance of Multnomah County, 347 units were permitted in Washington County, and 53 units were permitted in Clackamas County.



Source: U.S. Census Bureau

## NEW CONSTRUCTION

Looking back at 2014, the Barry Apartment Report indicates that the rate of apartment construction was brisk throughout the year. Permits were issued for 6,800 new apartment units in the four-county metro area, an increase from 2013’s 5,800 permitted units. Over 60 percent of the permits for new units were issued in Multnomah County alone, making 2014 the most robust year ever for apartment construction in Multnomah County—permits were issued there for 4,225 new units.



Construction activity virtually did not occur in Clackamas County and East Multnomah County.

For 2015, new multifamily construction is predicted by the Barrys to continue strongly throughout the year. Their assessment of recent permitting trends leads to a prediction of 12,000 to 16,000 new multifamily units in 2015 and 2016. Again, the majority of permitting and construction is likely to occur in or near Portland's urban core. This localization of development in the central city sets the most recent construction activity apart from previous cycles. Apart from Hillsboro and certain pieces of Beaverton and Vancouver, there is little construction in suburban areas. Many regions have not seen new multifamily development since 2007. ■

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## OFFICE MARKET ANALYSIS

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A. SYNKAI HARRISON

Portland State University

Statewide employment is growing at three percent annually according to the State of Oregon Employment Department, a percentage point faster than the rest of the country. The Oregon Office of Economic Management is predicting that job growth should continue at a rate of 2.9 percent in 2015 and continue on that pace for the next few years. In Oregon, professional and business services employment grew by 11,500 jobs over the past year, a 5.3 percent increase. Unemployment in the Portland metro area dropped to 5.2 percent, the lowest in seven years. In addition, wages and income in the state grew faster than the rest of the nation in 2014.

The Portland Business Journal recently reported that Portland is attracting significant interest from institutional investors. Portland's office market continues to benefit from an influx of startup and tech firms locating to the Portland area. With relatively low vacancy rates and steadily increasing rents, institutional investors are investing heavily in the Portland market. The recent sale of the Overton Pearl, at \$500 per square foot, is evident that Portland's office market is robust and continues to grow.

■ **A. Synkai Harrison** is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions are those of the author solely and do not represent the opinions of any other person or entity.

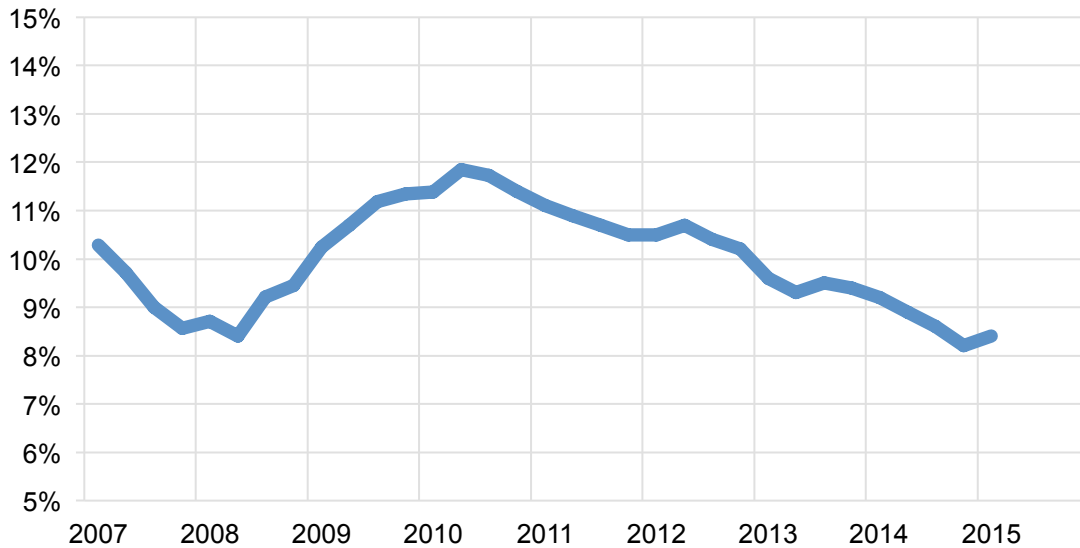
## VACANCY

Overall office vacancy continues its downward trend as limited deliveries are unable to keep with demand. Kidder Mathews reports that overall average vacancy rate for Portland's office market at the end of the first quarter of 2015 was 8.4 percent.

This was a slight increase over the previous quarter of 8.2 percent, and a significant improvement over the first quarter of 2014 when the overall average vacancy rate was 9.2 percent. According to CoStar, Class A properties experiencing an overall vacancy rate of 9.9 percent down from 10.1 percent in the previous quarter and 10.7 percent at the end of the first quarter of 2014.

At the end of the first quarter Class B properties reported an average vacancy rate 8.7 percent, up slightly from the previous quarter at 8.6 percent. Vacancy rates for Class C properties reported an average vacancy rate of 5.8 percent down from 5.9 percent at the end of the fourth quarter of 2014.

**Figure 1: Portland Office Market Vacancy Rate, 2007–2015**



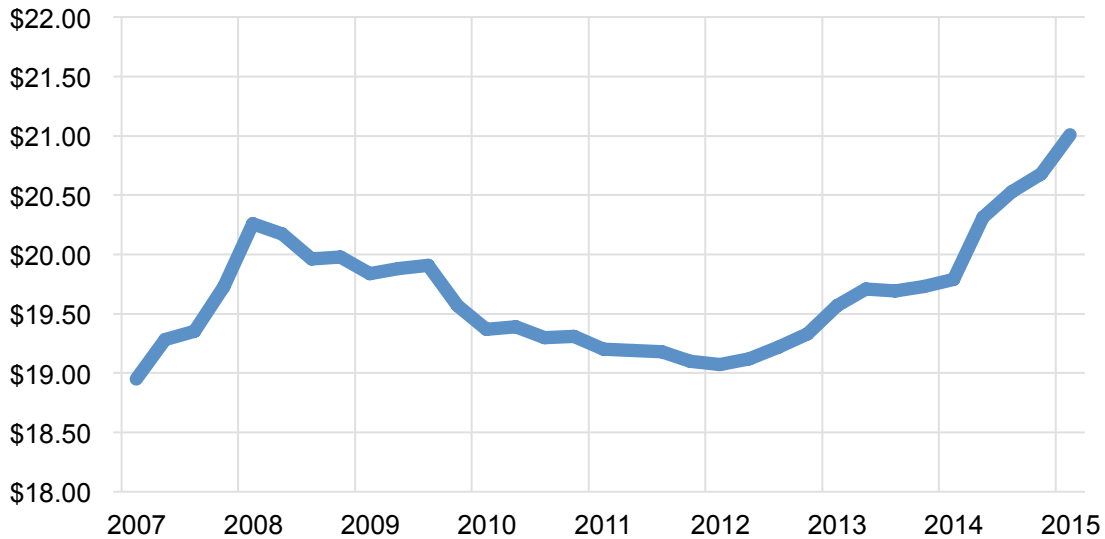
Source: Kidder Mathews

## RENTAL RATES

The average quoted asking rental rate for the first quarter of 2015 was \$21.01 per square foot up from \$20.68 per square foot at the end of the fourth quarter of 2014 according to Kidder Mathews. The first quarter of 2014 ended with an average asking rental rate of \$19.79 per square foot.

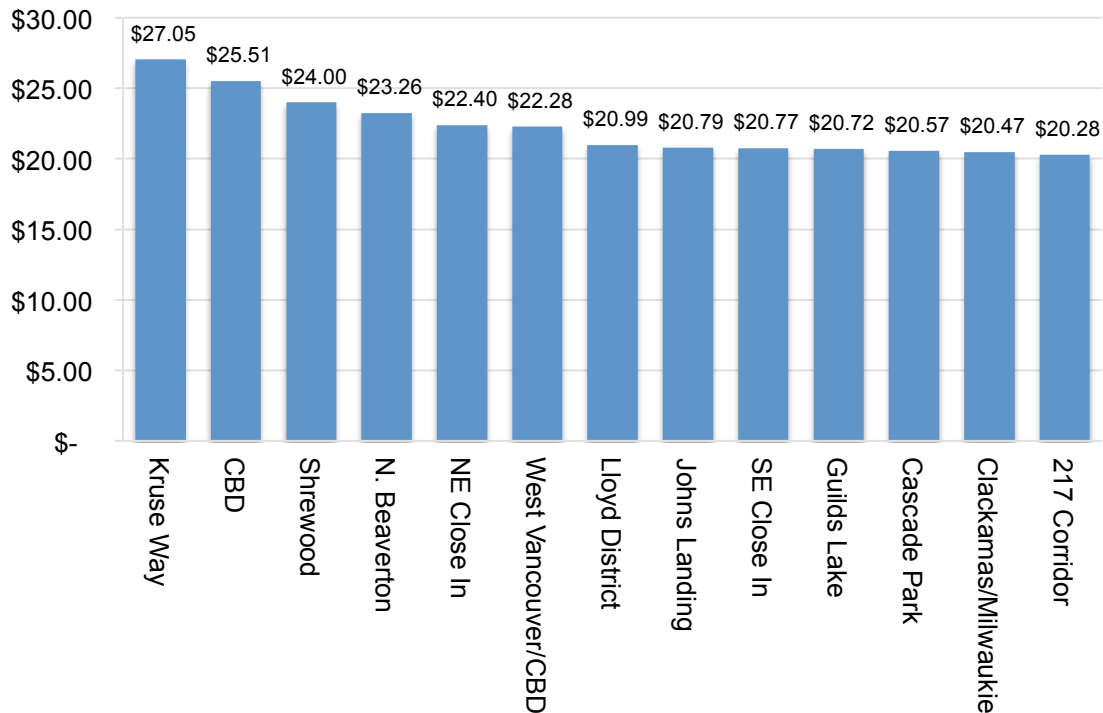
Class A properties reported an average asking rental rate of \$25.46 per square foot during the first quarter of 2015 compared to \$25.15 per square foot at the end of the fourth quarter of 2014. Class B properties reported an average asking rates of \$20.36 per square foot as opposed to the previous quarter where properties reported an average asking rate of \$19.37 per square foot. Class C properties reported an average asking rate of \$16.84 per square foot for the first quarter of this year. Properties in the CBD reported an average asking rental rate of \$25.51 per square foot compared to suburban markets which reported \$19.97 per square foot.

**Figure 2: Portland Office Market Average Asking Rents, 2007–2015**



Source: Kidder Mathews

**Figure 2: Highest Office Market Average Asking Rents in Portland Area Submarkets, first quarter 2015**



Source: CoStar

## ABSORPTION AND LEASING

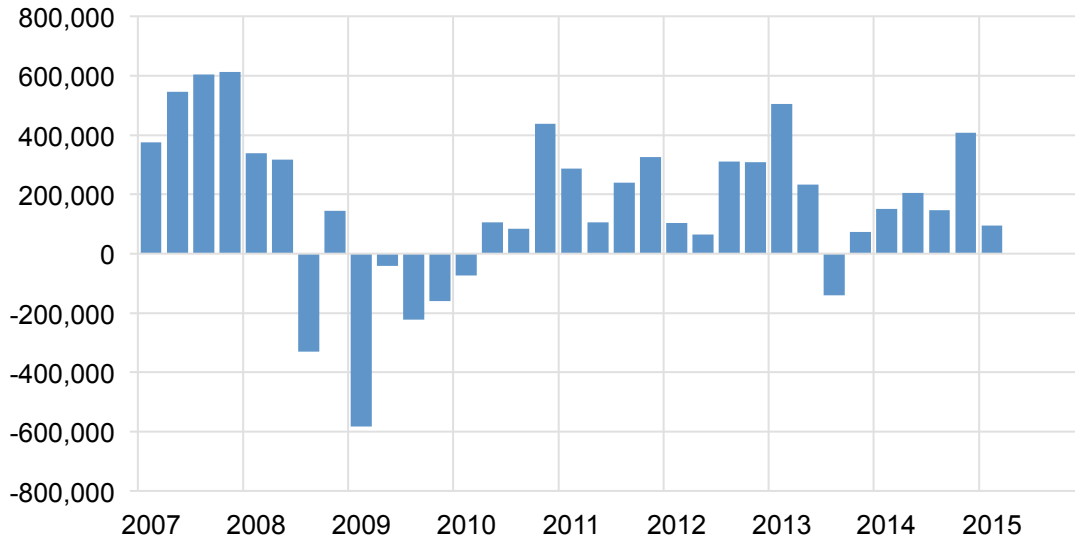
At the end of the first quarter of 2015, Portland's office market experienced 95,627 square feet of positive net absorption according to Kidder Mathews. This is compared to previous quarter where net absorption was positive 407,079 square feet. The first quarter of 2014 saw 150,789 square feet of positive net absorption.

Class A properties reported 44,911 square feet of positive net absorption during the first quarter of 2015 according to CoStar. During the fourth quarter of 2014, the Class A market experienced 213,459 square feet of positive net absorption compared to first quarter of 2014 where there was 68,289 negative net absorption. During the first quarter of 2015, the Class B properties reported 36,189 square feet of positive net absorption where as in the previous quarter Class B properties reported 37,400 square feet of negative net absorption.

Out of all of the Portland metro area office submarkets, the Close-in southeast significantly outperformed all others with 124,359 square feet positive of net absorption followed by the Clackamas/Milwaukie submarket with 27,180 square feet of positive net absorption. Tigard and Lloyd District experienced the largest

amounts of negative net absorption with 38,229 and 36,402 respectively all according to CoStar.

**Figure 3: Portland Office Market Net Absorption, Square Feet, 2007–2015**



Source: Kidder Mathews

**Table 1: 2015 Q1 Notable Lease Transactions**

<b>Tenant</b>	<b>Address</b>	<b>Market</b>	<b>Sq. Ft.</b>
Planar Systems	AmberGlen Corp. Dr.	Sunset Corr	72,000
DiscoverOrg	805 Broadway	West Vancouver	27,043
Zapproved	Machine Works	CBD	19,258
Norris Stevens, Inc	Standard Ins. Ctr	CBD	14,470
Parson’s Brinkerhoff	Pacific Center	CBD	13,780
Smith Optics	200 SE MLK Jr. Blvd	Lloyd District	12,889
Guild Mortgage	Kruse Way Plaza I	Kruse Way	12,263

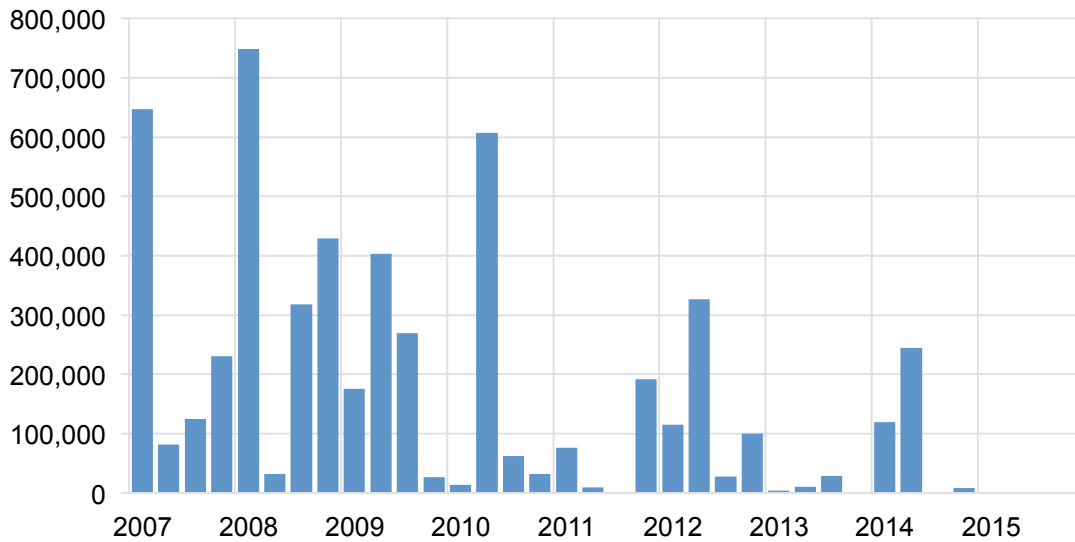
Source: Colliers International

**Table 2: 2015 Q1 Notable Sales Transactions**

<b>Tenant</b>	<b>City</b>	<b>Price</b>
KOIN Center	Portland	\$88,000,000
One Pacific Center	Portland	\$48,500,000
2100 SW River Parkway	Portland	\$35,350,000
The Overton Pearl	Portland	\$30,890,000
Mason Ehrman	Portland	\$14,500,000
321 Glisan	Portland	\$9,300,000

Source: Colliers International

**Figure 4: Portland Office Market Deliveries, Rentable Building Area, Square Feet, 2007–2015**



Source: Kidder Mathews

## **DELIVERIES AND CONSTRUCTION**

Two office building were delivered to market by the end of the first quarter of 2015 according to Kidder Mathews for a total of 93,348 square feet, compared to 1 building last quarter with only 8000 square feet. The first quarter of 2014 saw four buildings delivered totaling 81,521 square feet. Currently there are ten buildings under construction in the Portland metro office market with a total rentable area of 990,673 square feet. ■



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# INDUSTRIAL MARKET ANALYSIS

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A. SYNKAI HARRISON

Portland State University

CBRE recently reported that fundamentals in Portland's industrial market remain strong going into 2015 as asking rents continue to rise, vacancy rates continue their downward trend and absorption remains robust. Construction activity has increased with over a million square feet delivered to market during the past two quarters. Even though Portland is seeing more speculative construction, new construction is still low compared to historic levels.

## VACANCY

The overall vacancy rate for the Portland metro area industrial market continues its downward trend. The first quarter of 2015 ended with an overall vacancy rate of 4.7 percent down from 5.0 percent at the end of the fourth quarter of 2014 according to Kidder Mathews. Portland's overall industrial vacancy rate has decrease 15 percent since the first quarter of 2014.

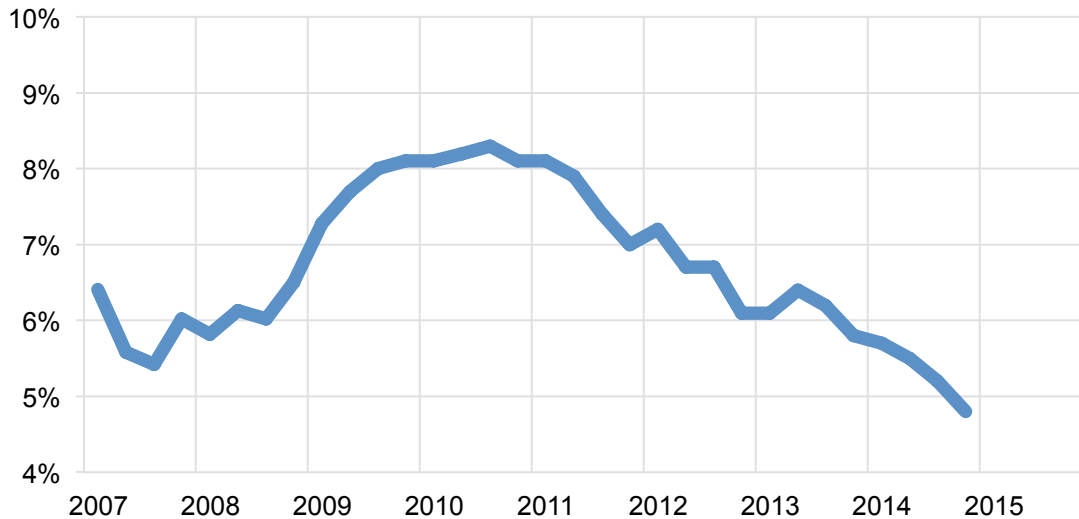
The overall vacancy rate for flex properties ended the first quarter of 2015 at 11.6 percent down slightly from 11.5 percent at the end of the previous quarter. The vacancy rate for the flex market has increased by 1.4 percent since the first quarter of 2014 according to CoStar.

The warehouse sector reported an overall vacancy rate of 4.4 percent, down four tenths of a percentage point from the fourth quarter of 2014. The fourth quarter of 2014 ended with a 5.6 percent vacancy rate. Of all the metro submarkets, the

■ **A. Synkai Harrison** is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions are those of the author solely and do not represent the opinions of any other person or entity.

Northwest and I-5 corridor reported the lowest vacancy rates. Properties in northwest reported 3.1 percent vacancy out of a total inventory of 13,800,535 square feet followed by the I-5 Corridor with 3.6 percent with a total inventory of 28,859,757 square feet according to CoStar.

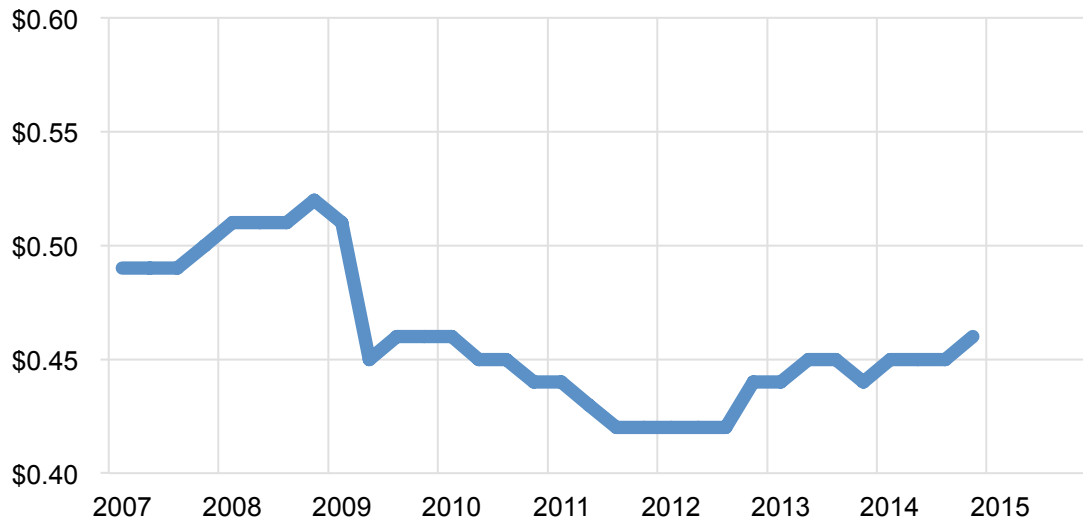
**Figure 1: Portland Industrial Market Vacancy Rate, 2007–2015**



Source: Kidder Mathews

## RENTAL RATES

Kidder Mathews reports the average asking rental rate, triple net, for the overall industrial market increased just over 2 percent during first quarter of 2015 to \$.46 per square foot per month from \$.45 per square foot per month in the previous quarter. The flex sector ended the first quarter of this year at \$.99 per square foot per month up from \$.98 per square foot per month at the end of final quarter of 2014. Over the past year rental rates in the flex market have increased 6.8 percent, up from \$.93 per square foot per month at the end of the first quarter of 2014 according to CoStar.

**Figure 2: Portland Industrial Market Average Quoted Rates, 2007–2015**

Source: Kidder Mathews

## ABSORPTION AND LEASING

Portland's overall industrial market ended the first quarter of 2015 with 1,085,258 square feet of net positive absorption compared to 811,667 square feet of net positive absorption at the close of the fourth quarter of 2014. The market's performance was a significant improvement over the first quarter of 2014 which ended with 226,367 square feet of negative net absorption as reported by Kidder Mathews.

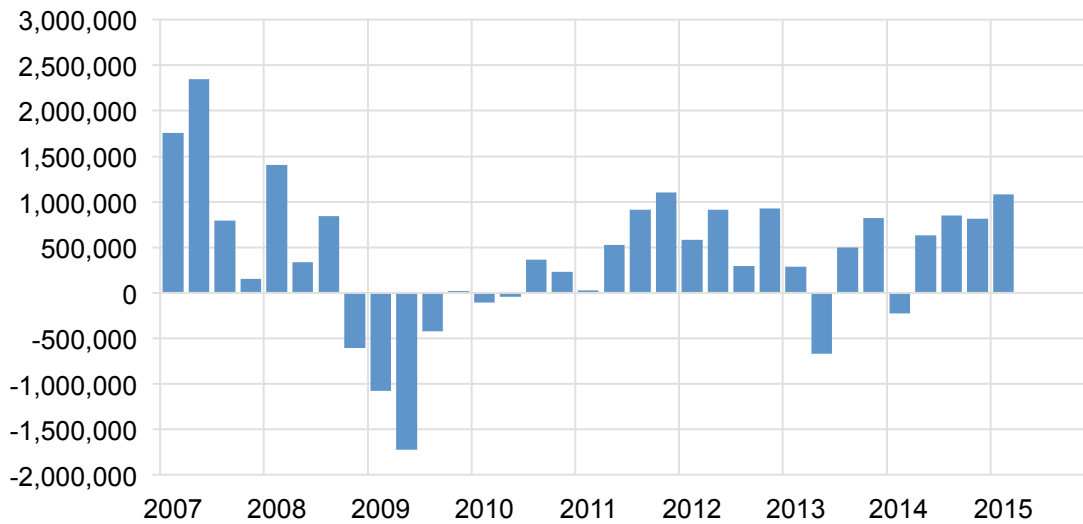
The flex market reported net negative absorption of 16,410 square feet at the end of the first quarter of 2015 whereas the warehouse market did significantly better with 1,016,516 of positive net absorption. Within the flex market, the submarket that experienced the greatest amount of positive absorption was the Westside with 46,354 square feet. The southwest market saw the largest amount of negative absorption at 43,151 square feet all according to CoStar.

According to Norris, Beggs and Simpson, the Northeast was the most robust submarket in the Portland metro area during the first quarter. Cardinal Health preleased 125,542 square feet in the Gateway Corporate Center which was brought to market in February. Terminal Transfer moved in to 101,131 square foot space and also during the last quarter American Tire Distributors moved into an 110,000 square foot facility. According to CoStar, the Northeast market saw the largest amount of square footage delivered at 407,800 square feet and the greatest amount of absorption at 298,349 square feet. KeHE had one of the largest reported lease signings of the quarter with its renewal of the company's 166,503 square foot facility at Chirgwin Distribution Center. In Hillsboro, Laika animation studios is expanding

its current space, a 150,000 square foot former warehouse, by an additional 105,000 square feet.

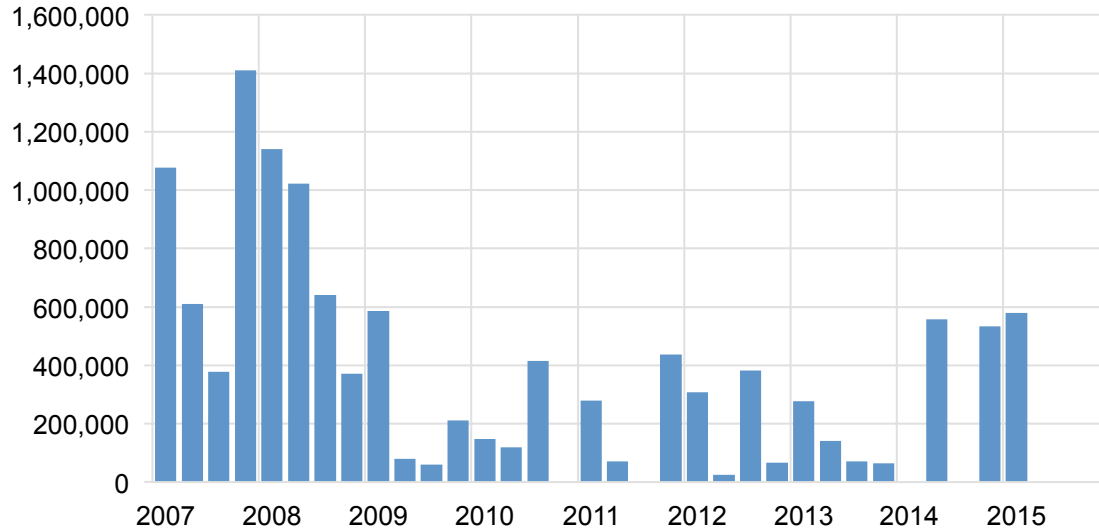
CRBE reports that the average deal size in the Portland industrial market has been decreasing. Transactions averaged 11,786 square feet during the first quarter of this year, where the ten year average is 16,069 square feet.

**Figure 3: Portland Industrial Market Net Absorption, Square Feet, 2007–2015**



Source: Kidder Mathews

**Figure 4: Portland Industrial Market Deliveries, Rentable Building Area, Square Feet, 2007–2015**



Source: Kidder Mathews

**Table 1: Notable Q1 2015 Industrial Lease Transactions**

<b>Tenant</b>	<b>Address</b>	<b>Market</b>	<b>Size</b>
KeHE	Chirgwin Distribution Center	Clackamas	166,503
Cardinal Health	Gateway Corp. Center	E. Columbia Corr.	125,542
Terminal Transfer	Rivergate Logistics Center	Rivergate	101,131
Solar World	Sunset Corr. Industrial Bldg.	Sunset Corr.	80,470
Perfect 10, Inc.	Airport Way Commerce Park	E. Columbia Corr.	45,000

Source: Colliers International

**Table 2: Notable Q1 2015 Industrial Sales Transactions**

<b>Building</b>	<b>City</b>	<b>Price</b>
1140 SE 7 <sup>th</sup> Ave	Portland	\$5,450,000
11555-11633 NE Sumner St	Portland	\$5,002,000
Wilsonville Business Center	Wilsonville	\$4,600,000
Swan Island Industrial Ctr	Portland	\$4,350,000
17230 NE Sacramento St	Gresham	\$3,750,000
18332 NE San Rafael St	Portland	\$3,750,000

## **DELIVERIES AND CONSTRUCTION**

Jones Lang LaSalle reports that the NE Columbia Corridor has seen increased activity over the past five years with five significant projects due to deliver this year. They include the Interstate Crossroads Distribution Center with 492,554 square feet, the Colwood Industrial Park Building 1, 418,979 square feet, the Cameron Distribution Center, 320,795 square feet, the Gateway Corporate Center Building F, 215,250 square feet and Prologis PDX 20 with 270,800 square feet. Evergreen Plastic Company, which relocated from Portland to Clark County, delivered its 53,930 square foot building during the first quarter of this year. ■

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## RETAIL MARKET ANALYSIS

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A. SYNKAI HARRISON

Portland State University

The US economy got off to a very sluggish start in 2015 as gross domestic product grew only by 0.2 percent compared to 2.2 percent in the first quarter of 2014. This is largely due to decreased exports because of a strong dollar and a harsh winter that put a damper on consumer spending and a lack of investment from energy companies as oil prices continued to decline. According to Market Watch, experts expect a repeat of 2014, where first quarter growth was lackluster as GDP declined 2.1 percent but gained ground in the spring and summer with 4.6 percent and 5 percent growth.

Oregon's seasonally adjusted unemployment rate dropped to 5.4 percent in March from 5.8 percent February and 6.3 percent in January. The unemployment rate for the Portland metro area came in lower at 5.2 percent in March. Nationally, Personal Consumption Expenditures, a primary measure of inflation, rose by .2 percent in March and when excluding food and energy, the rate only rose by .1 percent. Since June 2014 gas prices have declined 39.5 percent, couple that with low inflation and robust gains in employment, Portland area retailers could likely to see strong consumption growth in the coming months.

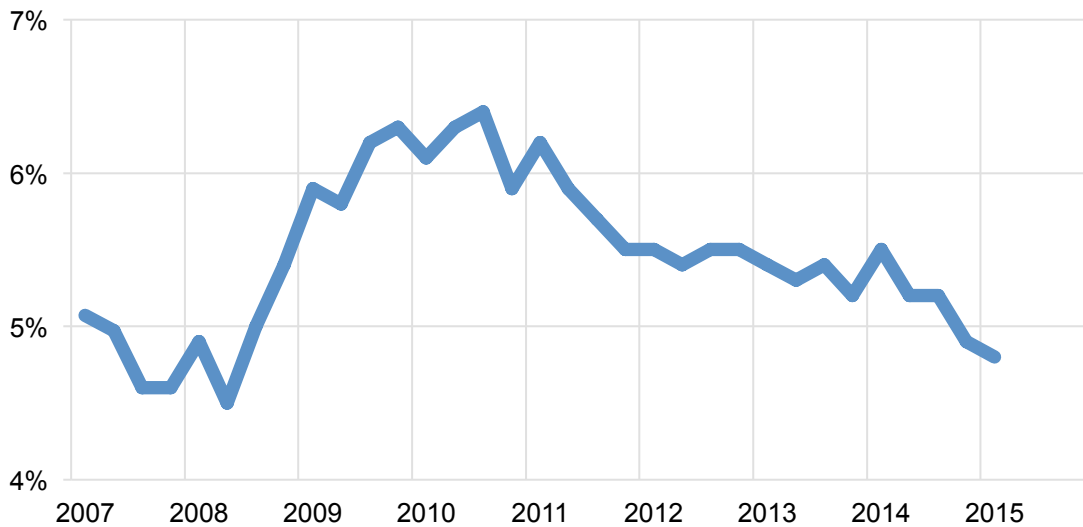
■ **A. Synkai Harrison** is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions are those of the author solely and do not represent the opinions of any other person or entity.

## VACANCY

Portland’s overall retail vacancy rate decreased by one-tenth of one percent during the first quarter of 2015 according to Kidder Mathews. The quarter ended at 4.8 percent compared to 4.9 percent at the end of the fourth quarter of 2014. The overall vacancy rate for general retail was 3 percent for a total of 1,608,169 square feet out of over 54 million in total inventory according to CoStar. Power centers performed well coming in with a vacancy rate of 4.3 percent followed by the mall market at 4.4 percent. According to Kidder Mathews, the retail market in Portland is experiencing its lowest vacancy rate since the fourth quarter of 2007.

The retail submarkets with the lowest vacancy rates were NE Close In at 1.8 percent, Airport Way with 1.8 percent and Tualatin at 1.9 percent. A few of the areas with the highest vacancy rates were St. Johns/Central Vancouver at 8.6 percent, CBD/West Vancouver at 8.2 percent and Orchards at 9.0 percent all according to CoStar.

**Figure 1: Portland Retail Market Overall Vacancy Rate, 2007–2015**



Source: Kidder Mathews

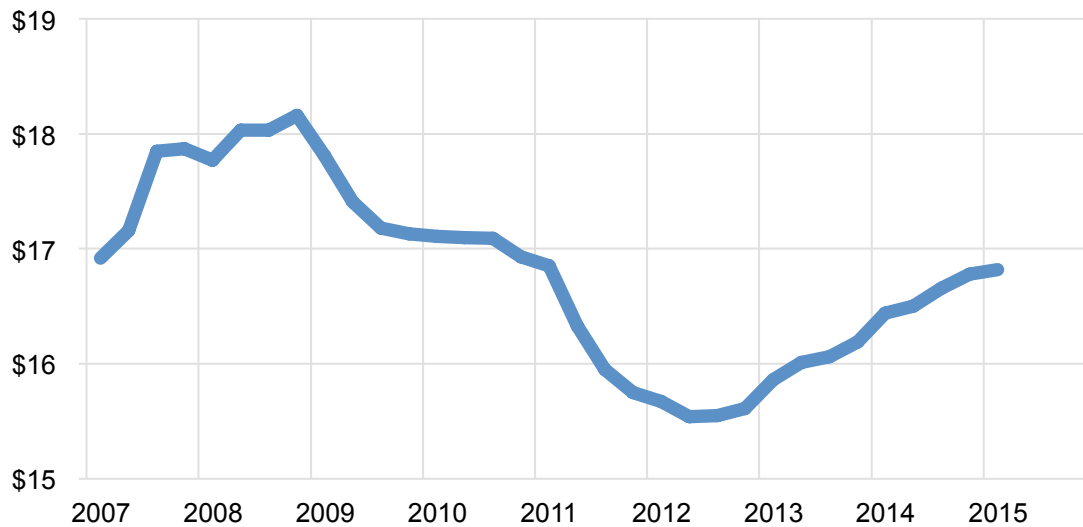


## RENTAL RATES

At the end of the first quarter of 2015, overall asking rental rate for the retail sector was \$16.82 per square foot per year up from \$16.78 per square foot the previous quarter. The current asking rental rate is a 6.25 percent increase over the first quarter of 2014, which ended with an average asking rate per square foot of \$16.44 according to Kidder Mathews.

Power Centers ended the first quarter of this year with the highest overall asking rental rate of \$20.03 per square foot per year, followed by the mall market with \$19.36 per square foot per year and the shopping center market with \$17.37 per square foot per year.

**Figure 2: Portland Retail Market Average Quoted Rates, 2007–2015**



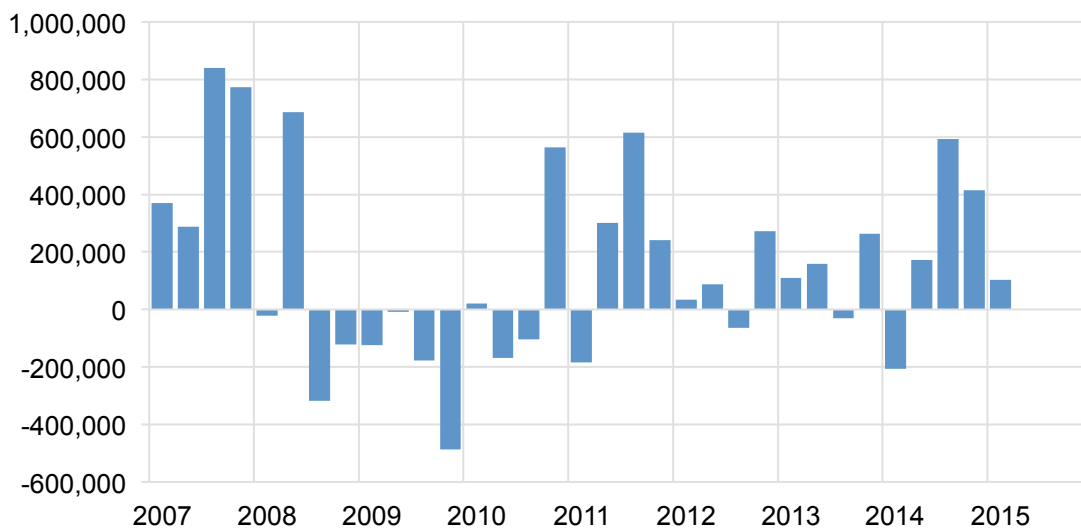
Source: Kidder Mathews

## ABSORPTION AND LEASING

Kidder Mathews is reported 104,082 square feet of net positive absorption at the end of the first quarter of 2015 compared to 415,278 square feet net positive absorption at the end of the fourth quarter of 2014. Despite this decrease, the market is performing better than the first quarter of 2014, which experienced 205,455 of negative absorption.

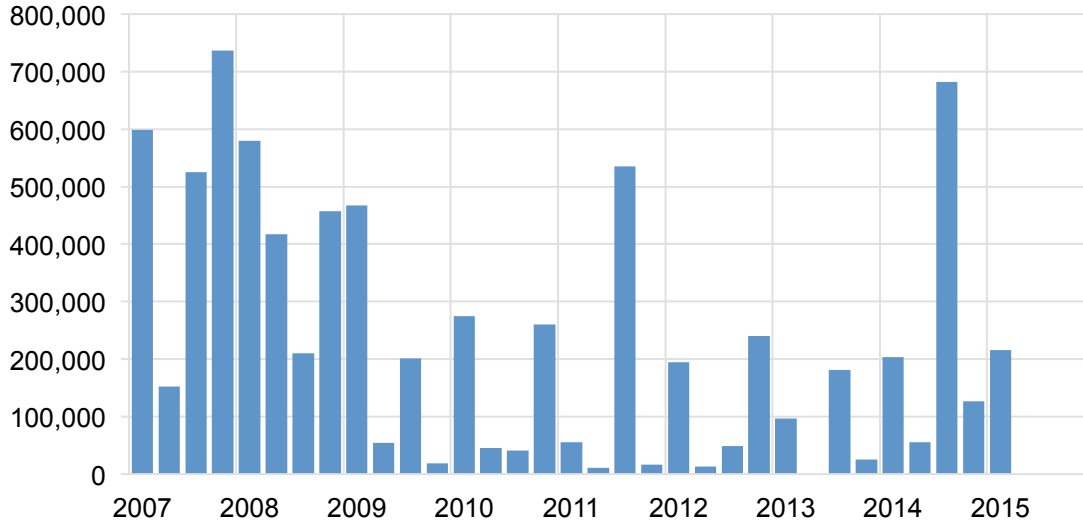
According to CoStar, shopping centers experienced the greatest amount of net absorption with 134,922 square feet followed by power centers with over 48,470 square feet. Malls saw over 1000 square feet of negative absorption at the end of the first quarter of this year. The Portland Central Business District experienced the largest amount of net negative absorption at 44,681 square feet. The Camas/Washougal submarket saw the greatest amount of net positive absorption at 44,597 square feet.

**Figure 3: Portland Retail Market Net Absorption, Square Feet, 2007–2015**



Source: Kidder Mathews

**Figure 4: Portland Retail Market Deliveries, Net Rentable Building Area, Square Feet, 2007–2015**



Source: Kidder Mathews

**Table 1: 2015 Q1 Notable Retail Lease Transactions**

<b>Building</b>	<b>Tenant</b>	<b>Submarket</b>	<b>Sq. Ft</b>
Village Square	Victory Outreach Church	Mall 205	23,500
8124 SW Barbur Blvd	Natural Grocers	Capital Hwy	15,400
Bakery Block	Z Haus Brewery	Clackamas	10,750
Anderson Plaza	The River Church	Camas/Washaugal	10,746

Source: CoStar

**Table 2: 2015 Q1 Notable Investment Transactions**

<b>Property</b>	<b>City</b>	<b>Sq. Ft</b>	<b>Sale Price</b>
Starbucks & Pacific Dental	Vancouver	5,000	\$2,620,000
Mattress Discounters & Zoom Care	Vancouver	6,500	\$2,400,000
915 NW 21 <sup>st</sup> Ave	Portland	4,731	\$2,100,000

## **DELIVERIES AND CONSTRUCTION**

At the end of the first quarter of 2015, nine buildings were delivered for a total of 122,734 square feet according to CoStar. At the end of the fourth quarter of 2014, seven buildings were delivered totaling 126,825 square feet. During the first quarter 2014, fourteen buildings were delivered for a total 221,859 square feet.

Power Centers saw 42,000 gross leasable area delivered followed by general retail which saw 30,279 square feet delivered. The Fred Meyer at 2011 W Burnside Street delivered its 38,455 square foot addition during the first quarter of this year as well as a 42,000 square foot LA Fitness which is 100 percent occupied. ■