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CENTER FOR REAL ESTATE

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CENTER FOR REAL ESTATE Quarterly Report

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SUMMARY AND EDITORIAL

ERIC FRUITS

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The past year has been a tumultuous one for housing policy in the Portland metropolitan area. Our regional government, Metro, has been engaged in determining whether the Urban Growth Boundary should be expanded. Apartment rents and home prices in the region have reached new historic highs, even after accounting for the 30 percent decline in prices following the Great Recession. Developers have responded with a flurry of apartment construction in central neighborhoods in Portland, leading to a strong reaction by neighborhood organizations and activists. Portland mayor has proposed a tax on demolition permits, and a city commissioner has proposed a tax on office development to subsidize affordable housing construction. With this much activity and proposals in play **Gerard Mildner** discusses the fundamentals of the economics of housing and local governments' policy proposals to promote affordable housing.

Oregon's **residential market** continues its strong performance, especially in the Portland area. Number of sales are stable, prices are rising, and days on the market are shrinking. Even so, home ownership in Oregon and the U.S. as a whole has hit 50-year lows. While demographics explain some of the decline, the rapid growth of

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home prices in the face of stagnant wage growth has made home ownership more difficult.

The **multifamily market** brings mixed messages regarding affordability. On the one hand, Axiometrics concludes that although rental rates have grown at more than double the rate of household income growth, average rents in Portland remain below the rule of thumb 30 percent housing-expense-to-income ratio. On the other hand, NAI Norris, Beggs & Simpson find that market fundamentals such as shrinking vacancy rates and rising rent levels have driven up both property values and institutional acquisitions. These conditions have also given rise to new developments that have mostly targeted the highest end of the Class A market, effectively "pricing out" many middle- and working-class renters. In Portland area submarkets, areas with some of the lowest rents also have the lowest vacancy rates. Looking forward, there is an increasing likelihood that areas such as Gresham and Outer Northeast will see rising rental rates and—in turn—declining affordability.

The **office market** report finds vacancy to be at its lowest rate since the fourth quarter of 2007 but projects vacancy rates to increase to historic average rates as new construction and redevelopment projects deliver.

Portland's **industrial market** continues to exhibit strong fundamentals. Despite over 1.2 million square feet of new space delivered in the quarter, net absorption is keeping pace with deliveries. Industrial vacancies remain at historic lows. Rental rates remained at or near historic highs. These trends are expected to continue as tenant demand for small and large spaces remains strong.

The Portland **retail market** has been buoyed by the barriers to entry imposed by Oregon's system of urban growth boundaries and by Portland's increasing urban housing density. Retail growth is projected to continue in central Portland, particularly from ground-floor retail in urban, mixed-use, multitenant buildings and grocery anchors looking to locate or expand in inner Portland. In contrast, observers expect to see a slight decrease in demand for suburban grocery-anchored centers.

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. ■

THE GENTRIFICATION PLAN FOR METRO PORTLAND

GERARD C. S. MILDNER

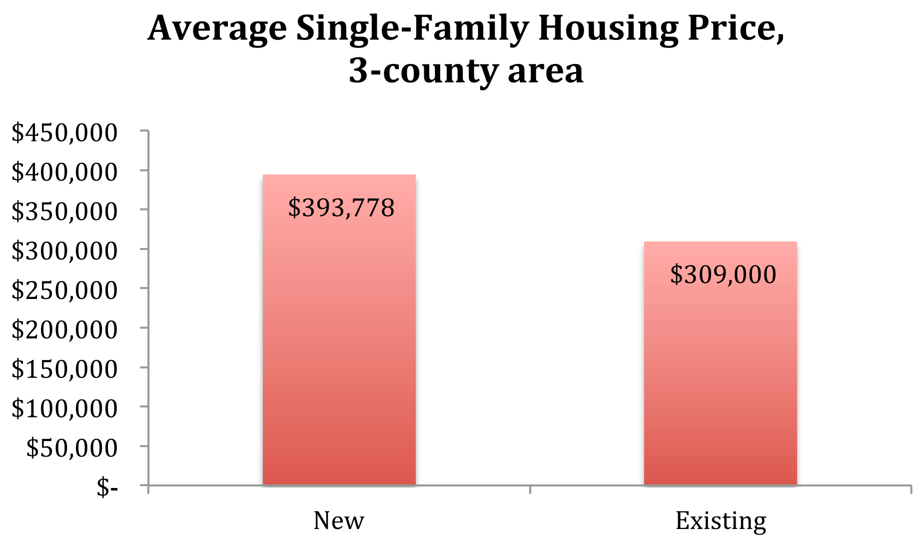
Academic Director, Center for Real Estate, Portland State University

The past year has been a tumultuous one for housing policy in the Portland metropolitan area. Our regional government, Metro, has been engaged in determining whether the Urban Growth Boundary should be expanded. Apartment rents and home prices in the region have reached new historic highs, even after accounting for the 30 percent decline in prices following the Great Recession. Developers have responded with a flurry of apartment construction in central neighborhoods in Portland, leading to a strong reaction by neighborhood organizations and activists. Portland Mayor Charlie Hales has proposed a tax on demolition permits, and city commissioner Dan Saltzman has proposed a tax on office development to subsidize affordable housing construction. With this much activity and proposals in play it's worth some time to discuss the fundamentals of the economics of housing and our policies to promote affordable housing.

■ **Gerard Mildner, Ph.D.** is an associate professor of real estate finance and the academic director of the Center for Real Estate at Portland State University. Dr. Mildner has an undergraduate degree from the University of Chicago and a Ph.D. in economics from New York University. His research is focused on land use regulation, growth managements, rent control, urban transportation and the economics of local government. 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.

COST OF NEW VS. EXISTING HOUSING

A first principle of housing policy is the idea that existing housing is almost always more affordable than new housing. Using numbers calculated by our Master degree student, Clancy Terry, in the last issue of the *Quarterly Report*, we find that the average new single family home sold for $85,000 more than the average existing single family home, or about 25 percent additional cost (Terry, 2015a). There are two main reasons. First, as incomes have risen over the past 100 years, houses have become larger and contain more amenities than in the past. Features like garage door openers, air conditioners, and built-in trash compactors didn't exist in the 1920s, yet today's new homebuyer demands them. Second, housing structures depreciate over time—roughly at a rate of 2 percent per year. It's simply not possible to build a new house with a mossy roof, a cracked sidewalk, or worn out carpets.

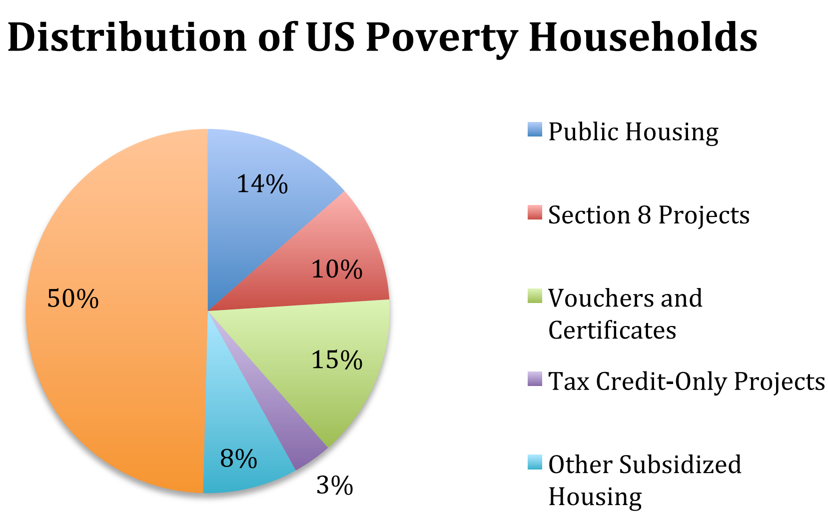


The implication for housing policy is that today's affordable housing is a vintage product that is made available as the result of new housing construction adding to total supply. Households with higher than median incomes can afford the new construction, and as they move into those new homes, older homes are freed up for less affluent households. So, just as households of modest means shop for affordable transportation on 82nd Avenue or look for affordable furniture on Craigslist, they look for affordable housing from the stock of existing housing being vacated by more affluent households. And if we want more affordable housing (meaning more low cost housing), we need to encourage rapid new housing construction, even if the new housing appears to be out of the financial reach of lower income households.

Unfortunately, this essential lesson of housing economics is lost on many of today's affordable housing advocates, who continue to lobby for new construction of "affordable housing." However classified, new homes are costly and cannot be built at lower cost without sacrificing quality, compliance with building standards, durability, or steep subsidies. As a result, new apartments cost much more per square foot than the average apartment in the region. To give a well-known example, Bud Clark Commons, a 130 studio apartment complex built by the public agency Home Forward in 2011 in downtown Portland, cost over $300,000 per studio apartment, much more than the average single family home price at that time (Meinhold, 2013). Public housing authorities would serve their clients better by issuing housing vouchers that would allow their clients to shop for existing homes and apartments closer to their preferred location.

MARKET RENTS MATTER

A second overlooked conclusion from the housing policy literature is that most low-income households pay market rents. We can compare the 9.6 million households below the poverty line in the United States to the 1.3 million households living in public housing, 1.0 million living in Section 8 projects, 1.4 million using housing vouchers, 300,000 in low-income tax credit housing, and 800,000 living in other subsidized housing programs (US Department of Housing and Urban Development, 2015, US Census Bureau, 2015). That leaves 4.8 million households (or 50 percent of the households in poverty) renting at market prices.

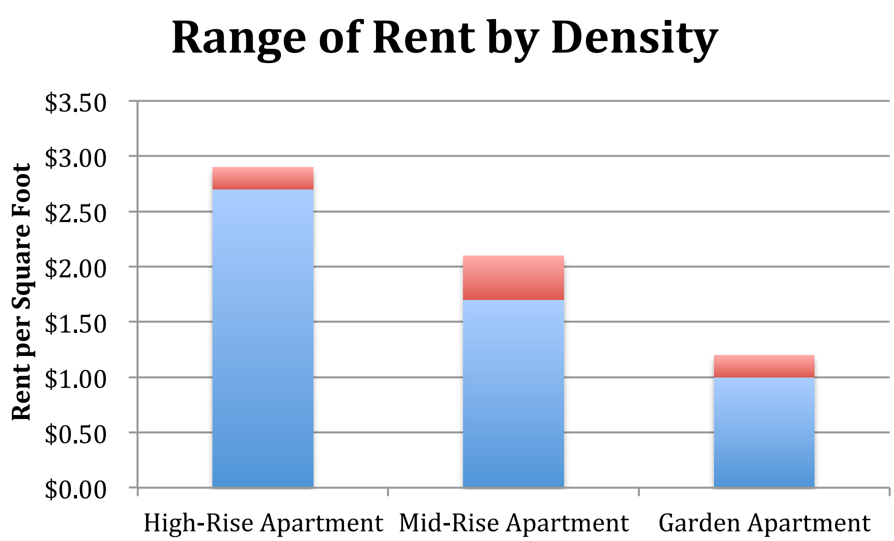


Note that many housing projects receive help from multiple subsidy programs, but the compilation by HUD accounts for that, which is why one category is called "tax credit-only." Also, not every subsidized housing tenant is categorized as below the poverty line, so the percentage of poverty households living at market rents is higher than the 50 percent estimated by these numbers.

The conclusion from this data is that we must be sensitive to trends in market conditions if we want to protect low-income households from unreasonable housing cost burdens. Affordable housing advocates often decry the lack of government support for subsidized projects, but the reality is that inherently high cost of housing necessitates the rationing of subsidy budgets. Thus, not everyone who qualifies for housing assistance receives a subsidized unit, only the first in line. Consequently, subsidization of housing projects is a policy that is inherently inequitable. On the other hand, reducing the market price of housing by promoting (or not impeding) more production creates a tremendous benefit to all low-income households given the size of housing costs in the household budget of low income households.

HIGH DENSITY MEANS HIGH COST

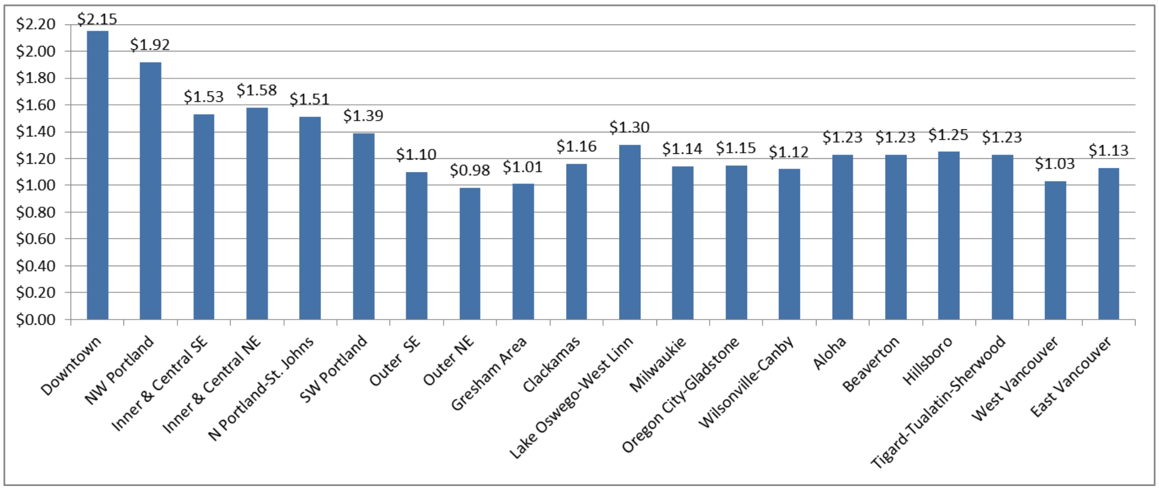
An important conclusion from the urban economics and the housing economics literature is that high density development is more costly to build and provides fewer consumer amenities. It only occurs naturally when site values are very high, and household incomes are high enough to permit the product to be marketed. We can see this from the table of apartment rents below that was generated from a study the Center undertook for the Holland Partner Group in 2014.



As part of that study, we collected pro formas from a large number of recently constructed housing projects in the Portland metropolitan area. The blue bars represent the low end of the range and the red bars represent the high end of the ranges. We separated he projects according to whether they were garden apartments (typically two-story wood construction), mid-rise apartments (typically four stories of wood construction over a concrete podium), or high-rise apartments (typically steel and concrete construction, greater than five stories). Then, we calculated the average apartment rent on a dollar per square foot basis. The projects that were least expensive to rent (per square foot per month) were the low-density garden apartments and the most expensive were the high rise apartments.

Apartment rents in most metropolitan areas are greatest at the center of that metropolitan area. And as you would expect, the high-rise construction projects are only found in Portland's Central City, which has the highest rents in the region. The mid-rise apartments were built largely within three miles of downtown, and the low-rise apartments were mostly built outside that perimeter.

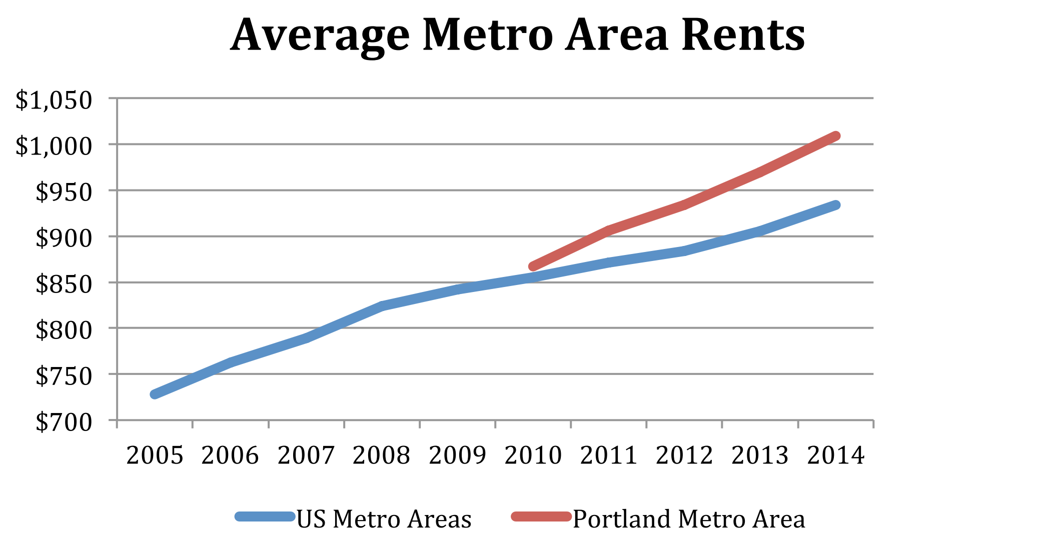
This pattern of apartment rents and locations can also be found in the work that Clancy Terry produced in this issue of the *Quarterly Report* (Terry, 2015b).



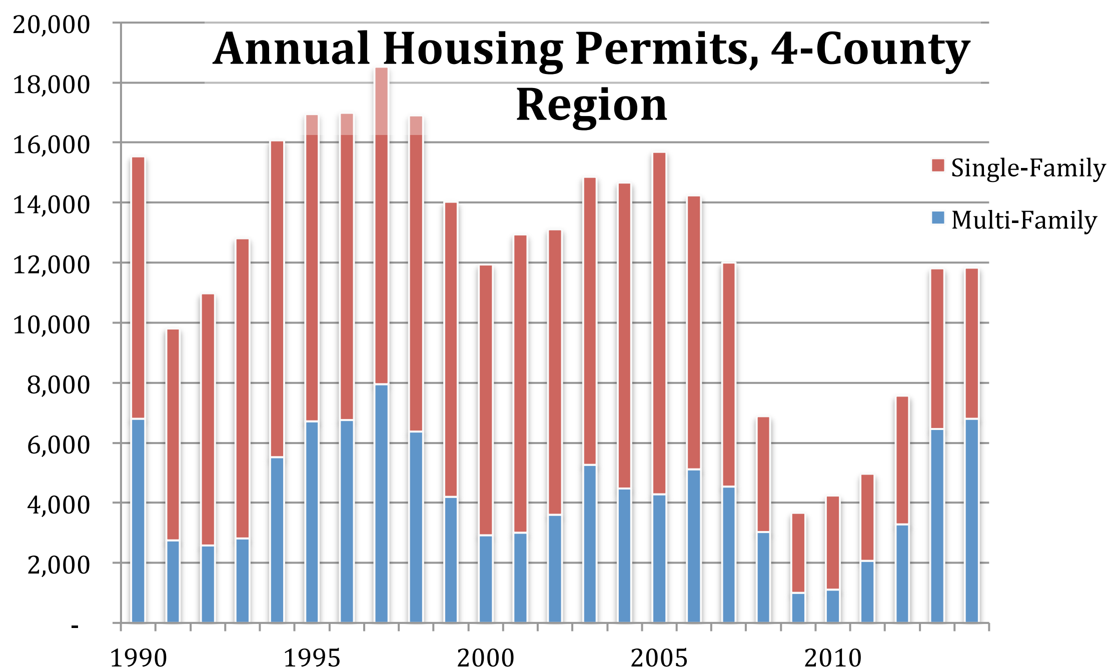
In the chart, districts are arrayed from the most central locations on the left and the most remote locations on the right. The information in the two charts isn't directly comparable, however, since the project pro forma rents reflect the price of new units and the average rent data reflect all apartments, including older ones. In any case, these are the markets that developers are building into, and it takes $2.00 per square foot average rents for existing apartments in downtown Portland to justify $2.70 rents for new high rise construction. Conversely, it's hard to imagine anything besides garden apartments being built in Outer Southeast Portland or Outer Northeast Portland when average rents are $1.09 and $0.93, respectively. More on that later.

PORTLAND'S ANEMIC HOUSING PRODUCTION

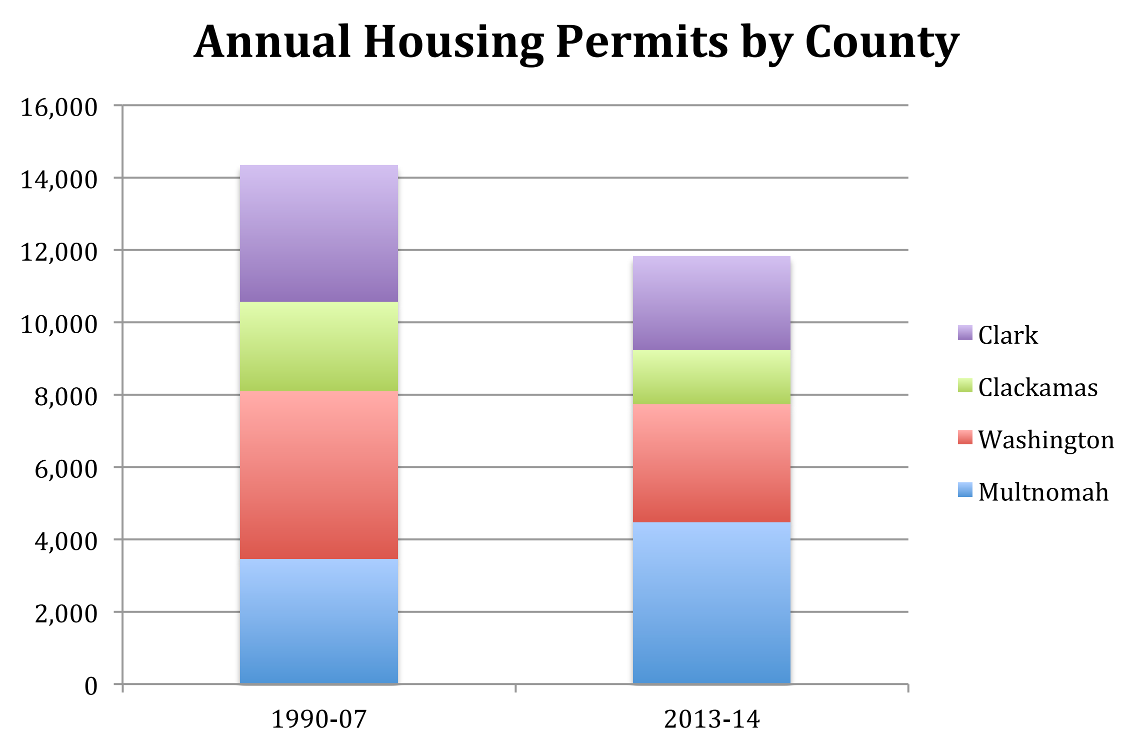
Given these observations, it seems critical for the Portland metropolitan area to boost housing production to moderate the trend in apartment rents and home prices. Rents in the Portland metro area, which have lagged national averages historically, now exceed those averages. Data prior to 2010 for the Portland metro aren't available, but statewide numbers suggest that Portland apartment rents were much lower than national averages prior to 2009.



At the same time, housing production in the region has fallen compared to the levels during the housing boom. We are producing 20 percent fewer units in the last two years compared to the period from 1990 to 2007. This is very surprising, given that home prices have now fully recovered to their peak prior to the housing bust and apartment rents have reached their highest levels ever.



Looking more deeply at these numbers, we find that multi-family construction has returned to normal levels, with a large shift from suburban construction to construction in the City of Portland. However, there has been a large decline in single family construction in all the counties in the metropolitan area. This could be a change in tastes. Additionally, household incomes and mortgage credit access declined sufficiently during the recession to shift demand away from the single-family market. However, in the Portland region this likely reflects the fact that building sites are in short supply due to minimum density regulations and regional supply constraints. That lack of new suburban housing production has led many of the new residents wanting single-family living to seek housing in the gentrifying neighborhoods of Southeast and Northeast Portland.



The two shifts from single-family to multi-family construction and the shift from suburban to central city construction create negative consequences for housing affordability. Apartments in the central city tend to be higher density, and higher density construction tends to be more expensive. And given that the aggregate number of housing units produced is reduced, less supply implies higher housing costs.

INCLUSIONARY ZONING, LINKAGE FEES, AND HOUSING SET ASIDES

Given these trends and the economics of affordable housing, the efforts of Portland's City Council seem woefully inadequate, if not misguided. As mentioned previously, the Mayor has proposed a tax on demolition, which is a necessary precursor to redevelopment. This policy could have significant impacts given Metro's reliance on redevelopment and infill for 90 percent of the City of Portland's housing capacity in the next 20 years. Others on the city council have lobbied for a lifting of the statewide ban on inclusionary zoning and the imposition of a commercial office linkage fee for affordable housing. Finally, the city council has raised the subsidized housing set aside in urban renewal areas from 30 percent to 50 percent.

Inclusionary zoning and commercial office linkage fees should be seen as development taxes geared to raise funds (or produce units) for subsidized housing. In the case of inclusionary zoning, developers of a particular number of units or more are expected to provide a percentage of housing units at a particular rent level for a particular period of time. In that formulation, there are several unknowns: (1) the unit threshold, (2) the percentage of below market units, (3) the amount of subsidization per unit, and (4) the period of time of subsidization. Given these four variables, inclusionary zoning ordinances can be written very strictly and present an onerous burden on development, or they can be written in a gentle way and impose a small burden. And in some jurisdictions, the developer is allowed to pay money into a subsidized housing fund, rather than build below market units directly.

However, regardless of the intent, an inclusionary zoning requirement is a burden on development and should be seen as a development tax. Developers will take a loss on the subsidized units for the "privilege" of building market rate units. As such, it's a very peculiar and harmful tax.

Because high apartment rents result in part from lack of supply, it seems strange to tax housing supply which, if effective, would only drive rents higher. This counter-productive feature of inclusionary zoning has led some housing market analysts to interpret its intent as "exclusionary zoning," due to its negative impact on housing production. Most jurisdictions implementing inclusionary zoning are higher income (e.g., Montgomery County, Maryland and Boulder, Colorado), and this critique suggests that their unstated goal is to prevent growth, not build subsidized housing.

Commercial office linkage fees represent a similar strategy. In this case, fees are levied on the construction of commercial office buildings to pay for subsidized housing projects. The conception of the fee as a development tax is clearer in this example. The few jurisdictions that implement this fee represent very strong office markets such as San Francisco. Local residents perceive new office development driving up apartment rents, and they may get support from existing property owners who want less competition. However, to generate significant amounts of revenue, the linkage fee will likely reduce economic activity within the city, which would seem counter-productive from the point of view of helping residents achieve the income to pay housing costs.

Finally, both of these two policies—inclusionary zoning and linkage fees—are usually associated with the construction of new subsidized housing units, which limits the number of incremental units produced. Cities would be better off with a policy that liberates additional development sites and, if any income redistribution is warranted, it would be better to offer portable vouchers to support rental payments on any unit, rather than particular housing units. This would stimulate new production in the aggregate and free up older units.

Fascination with subsidized housing units also limits the effectiveness of the City of Portland's urban renewal policy. Urban renewal is designed for blighted city neighborhoods to receive new infrastructure and private economic development. Historically, urban renewal has been used to develop road, transit, and sewer infrastructure, allowing neighborhoods like Portland's Downtown, Pearl District, South Waterfront, and Airport Way to become economic engines for the region. The city makes public infrastructure investments and the additional property tax on the new private investment pays for the infrastructure.

Unfortunately, the Portland City Council in 2006 imposed a requirement that 30 percent of the public investment in an urban renewal district has to be set aside for subsidized housing, which neither attracts private investment nor pays property tax. Earlier this year, the Council raised this percentage to 50 percent. While this policy may force some subsidized housing to be built, the potential for catalytic public investments, such as a new road, a new bridge, a new transit line, or repairing a decaying eyesore property is made less likely. And because the subsidized housing pays no property tax, it generates no incremental revenue to finance public improvements.

METRO'S BET ON HIGH DENSITY

In this environment of policy turmoil, Metro has finished a multi-year process to decide whether to expand the Portland Metro Urban Growth Boundary (UGB). Earlier this month, the Metro council endorsed the Urban Growth Report which determined that the existing boundary contained 20 years of developable land. Metro council ultimately decided not to expand the UGB. This determination was based on the assumptions that the future presages smaller households that earn less money and have less need or financial ability to live in single-family housing. Thus, the concept of what constitutes a housing unit for the purpose of meeting UGB capacity 20-year capacity requirements was conveniently redefined to compress the anticipated future population into the existing UGB dimensions.

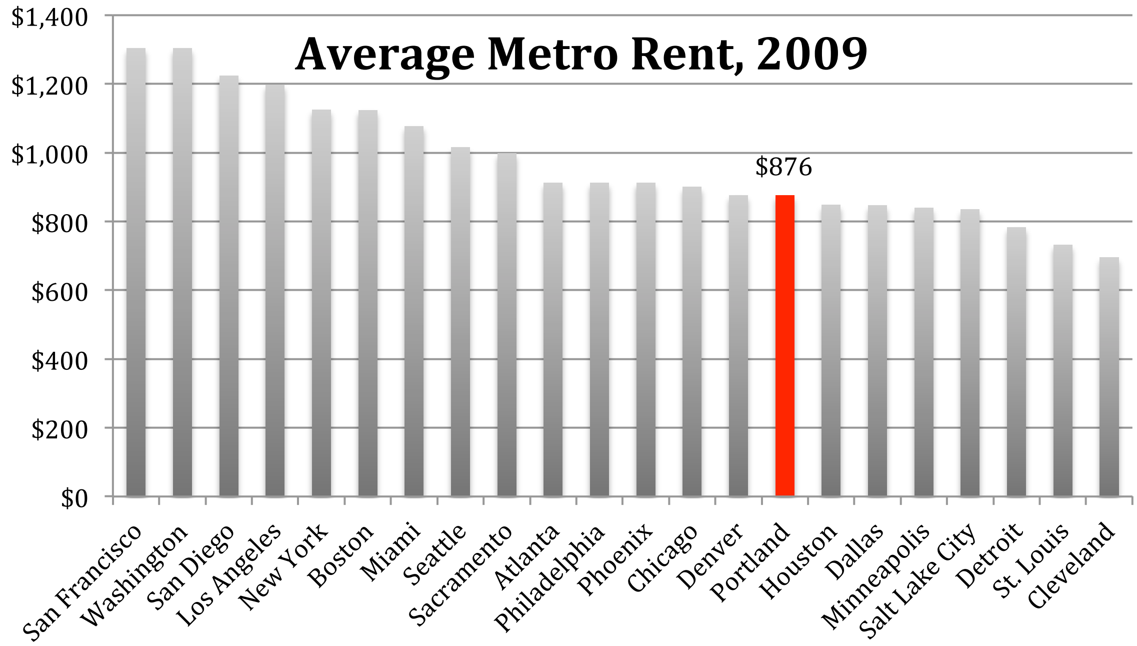
As I have argued previously in the *Quarterly Report*, the conclusion of zero-expansion was hot-wired by the process that Metro used to calculate the capability of the UGB to meet the anticipated housing and employment needs of the region for the next 20 years. Metro planners were given the directive to work with existing zoning given by the jurisdictions, regardless of whether that development capacity would be economically feasible. From there, anticipated housing units were assigned to that theoretical capacity, rather than located outside the UGB.

Figure 5. BLI Housing Development Capacity

As can be seen above diagram from the City of Portland, much of their future housing capacity is claimed in districts like Gateway, 82nd Avenue, Rockwood, and Montavilla. However, very little development activity is taking place in those communities, as they are some of the lowest rent districts in the region. As we noted earlier, apartment rents in Outer Southeast and Northeast Portland are only about $1.00 per square foot. To reach the conditions where mid-rise or high-rise development could take place, rents in these neighborhoods would need to rise to $2.00 or $3.00 per square foot. And if prices are that high in East Portland, they will be astronomical in higher income neighborhoods of the region. In essence, Metro planners treated zero-expansion of the Urban Growth Boundary as an absolute constraint, with housing rents forced to become the free variable to make that result possible. The resulting gentrification of East Portland is a policy outcome that is both unstated and inevitable.

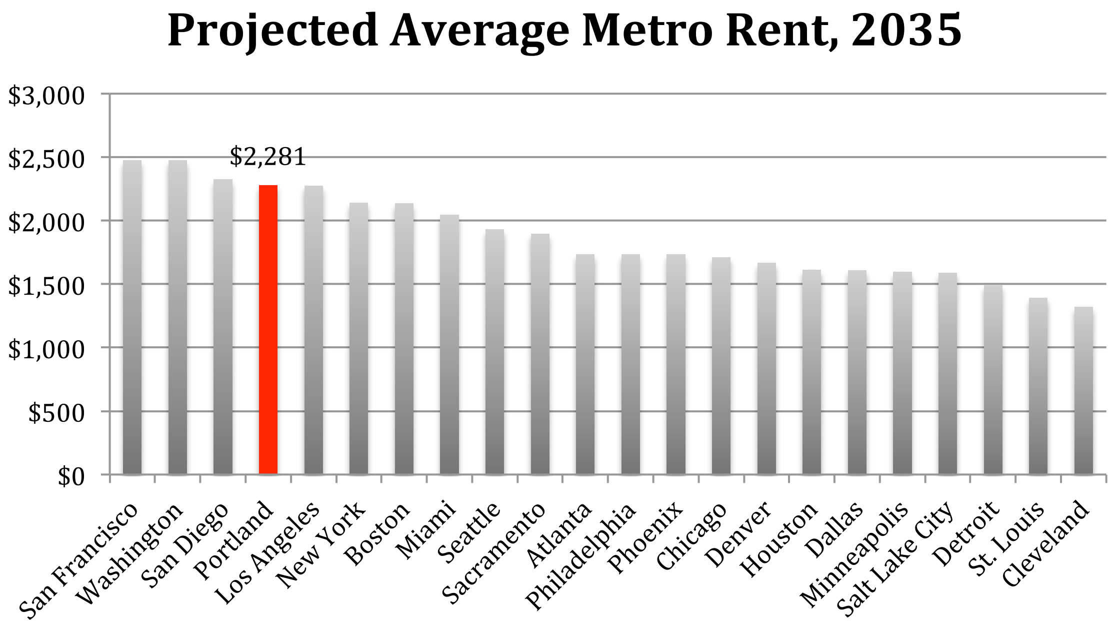
To their credit, Metro's planners have estimated the housing prices and apartment rents that would need to be achieved to reach those development targets. They anticipate that average rents in the Portland region to rise by 37 percent in inflation-adjusted terms in 20 years. Factoring in a 2.5 percent annual inflation factor, that would mean that rents would rise by 124 percent—more than doubling the current level. Home prices would rise even faster in Metro's estimation—148 percent in 20 years.

To assess what that level of appreciation would mean, I've arrayed the median gross rent in the Portland metropolitan area in 2009 against 21 other US metropolitan areas, selected for their size and location.



In that diagram, we find that the rents in the Portland region are somewhere in the lower half of the distribution, competing with large metropolitan areas such as Chicago and Dallas, and west coast competitors like Phoenix, Denver, and Salt Lake City. More importantly, Portland area rents are substantially below those in the major cities in California, such as San Francisco and Los Angeles, which are important sources of employment growth for this region. Economic development agencies in the region routinely recruit Bay Area software firms, arguing that while Portland may not have the same cultural or climate amenities of California, our housing is one-third less expensive and we're a short airplane flight away. Put differently, the software firm in Bay Area can convince some of their engineers to move to Portland, knowing that the engineer can afford to buy a nice house.

However, with the rent and price increases anticipated by Metro's 20-year plan, that value proposition evaporates. If rents in Portland rise by 37 percent more than the rate of inflation for apartments elsewhere, the large discount relative to the California cities vanishes. The engineer in Silicon Valley won't readily accept a move to Portland, and our competitors in Denver, Phoenix, Salt Lake City, and Austin will win those firm relocation opportunities.



In practice, the strategy of absolute containment of the region's population is likely to result in reduced employment opportunities and slower economic growth. Workers will require compensation for accepting jobs in a high cost, modest amenity region. If firms cannot achieve significant cost savings from locating in Portland, expansion will occur in other cities, whether that's our mountain state competitors, cities in Texas, or cities in the Southeast US, such as Atlanta and Charlotte. Children who grow up in the Portland area will more likely move to those cities to find employment, creating what I call the "Santa Barbara Effect."

Our city will remain a nice place with amenities, but it won't be a dynamic place where new employment and technology are developed. Homeowners will feel richer, but the resulting increase in home equity won't matter until they retire and move to Arizona or Nevada. Additionally, the brunt of the transition to Metro's policy to appreciate real property assets will be felt most harshly by the poor, who don't own property. Low-income households have been shown to be losers in regions that constrained spatial expansion in the face of population growth pressure. (Pozdena, 2002)

MOVING FORWARD

Metro officials justify their dedication to the zero expansion policy by arguing that they received only one proposal by a city that wanted to expand the urban growth boundary, Wilsonville, to accommodate new growth. And Metro is wary of expanding the UGB in places where there isn't a willing jurisdiction to plan for new growth. The largest UGB expansion that Metro has authorized in the last 35 years happened in 1999 when 24,583 acres in Damascus were added. However, very little housing was developed in that area, due to a combination of lack of freeway access, lack of local infrastructure (i.e., arterial streets and sewers), and a new jurisdiction whose residents prefer to remain rural.

However, the housing problems of the region cannot wait for jurisdictions to step forward and sacrifice for the region. Housing markets tend to be regional in scope. If prices rise in Wilsonville, they will tend to rise in Tualatin and Tigard at the same time. And if Wilsonville agrees to allow new housing, the increase in supply will reduce prices in Wilsonville, Tualatin, Tigard, and many other communities, too, and Wilsonville will be left with the infrastructure cost. As a result, it's important for Metro to correct the incentives. The counties and the Metro regional government need to create a funding mechanism—such as a county-wide gasoline tax—to fund new road development. Revenue from the tax could be used to match local system development charge funds so that towns accepting new housing development can get assistance to cover the extra infrastructure costs. The cities that accept new growth would be rewarded for doing their part to solve a regional problem.

Finally, we need a new regional planning process that tests multiple scenarios, not just the single "zero expansion policy" that Metro has modeled. We need to accept that values that we hold—a protected resource economy, vibrant shopping districts, quiet residential neighborhoods, and housing that's affordable—exist in some conflict, with trade-offs between goals. The latest Urban Growth Boundary decision shows that housing cost impacts are ignored and no one is responsible for the gentrification that will ensue. ■

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THE STATE OF THE ECONOMY

Adam Seidman

Portland State University

The third quarter was full of mixed signals locally and globally. In its latest release, the Oregon Office of Economic Analysis continued to describe Oregon's economy as at "full-throttle growth." Year-over-year employment growth remained strong for Oregon and the Portland metro area, with rates of 2.9 percent and 3.6 percent respectively, driven by continued growth in high-paying professional services and high-tech manufacturing industries. However, the unemployment rate ticked up in the quarter in both Oregon and Portland, and in September the state lost more jobs than it had in a month in over 5 years.

Nationally, low oil prices likely helped boost consumer spending, but output growth was relatively weak in the quarter as business pulled back in reaction to global conditions and a strong dollar put a brake on exports. The Federal Reserve did not raise interest rates, but hinted that it would by the end of the year.

There was significant volatility globally in the third quarter, especially in China, which saw its stock market rise and fall sharply, sending shockwaves across equity markets. The IMF revised its growth estimates downwards for the global economy. Yet China's economy is still projected to grow at a relatively strong (albeit slowing) clip, and moderate growth is forecasted for the major advanced economies.

■ Adam Seidman 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.

Table 1: Key Economic Indicators, Portland MSA, Oregon, and US Q3 2015

	Q3 2015/ Sept 2015	Q2 2015/ June 2015	Q3 2014/ Sept 2014
GDP Growth (annualized)			
US	1.5%	3.9%	4.3%
Unemployment Rate			
US	5.1%	5.3%	5.9%
OR	6.2%	5.5%	6.9%
Portland MSA	5.6%	5.4%	6.4%
Job Growth Rate (12-mo growth)			
US	2.0%	2.2%	2.0%
OR	2.9%	3.0%	2.8%
Portland MSA	3.6%	3.6%	2.8%
Inflation (12-mo unadjusted)			
US	0.1%	0.0%	1.8%
Interest Rates			
Federal Funds Rate	0.1%	0.1%	0.1%
10-Year Treasury	2.2%	2.4%	2.5%

Sources: BEA, BLS, Federal Reserve, Oregon Employment Department

GLOBAL TRENDS

The International Monetary Fund (IMF) revised its global growth projection down again for 2015 to 3.1 percent, based on weaker than anticipated activity across the globe. It notes that downside risks have risen, due to declining commodity prices, depreciating emerging market currencies, and increasing financial market volatility. However, growth is expected to be positive in all regions of the world except for Russia and Brazil, which are believed to be in recession.

All eyes were on China in the third quarter, with a roller coaster ride in its equity and property markets, devaluation of its currency, and unsuccessful attempts at government intervention to stop the volatility. China is still expected to have strong growth, albeit at a slowing rate. The IMF projects GDP growth in China of 6.8 percent in 2015 and 6.3 percent in 2016. According to the Oregon Office of Economic Analysis, China is now Oregon’s top export market, accounting for approximately 20 percent of all of the state’s exports. Clearly, the state of the Chinese economy has spillover effects to the local economy, especially for Oregon’s high-tech companies.

In large part due to the volatility in China and an overall slowdown in global economy, the United States Federal Reserve did not raise interest rates in the third quarter, as had widely been expected.

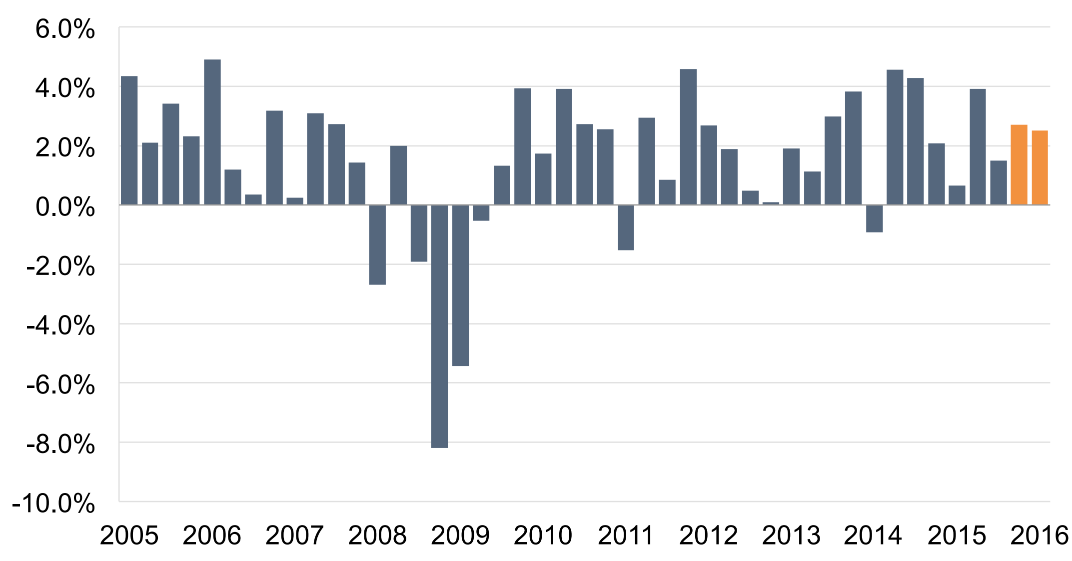
After rising 25 percent in the second quarter, oil prices in the United States fell by 24 percent in the third and are at or near six-year lows. This decline may have helped spur consumer spending in the United States, which once again was a major component of GDP growth. On the global stage, falling oil prices hurt countries with commodity-drive economies, such as Russia.

The dollar continued to show strength versus foreign currencies, and has appreciated about 18 percent since the middle of 2014. This has continued to impact the prices of US exports as well as the value of foreign sales of US-based firms, and may have led to a slowdown in export sales in the third quarter.

GDP/OUTPUT

According to the "advance" estimate from the Bureau of Economic Analysis (BEA), United States GDP grew by an annualized 1.5 percent in the third quarter. This follows growth of 3.9 percent in the second quarter (revised upwards from the "advance" estimate of 2.3 percent). Growth in the quarter was driven primarily by consumer expenditures, exports, government spending, the housing sector, and business investments. The slower growth in the third quarter was likely due in part to the stronger dollar (impacting exports), the weaker global market, and business pullback in investments as a result of these and other trends. Looking ahead, The Wall Street Journal Economic Forecasting Survey projects annualized GDP growth of 2.5 percent to 2.7 percent for the next two quarters.

Figure 1: Gross Domestic Product, United States, Annualized Percent Change, 2005–2016 (Forecast)



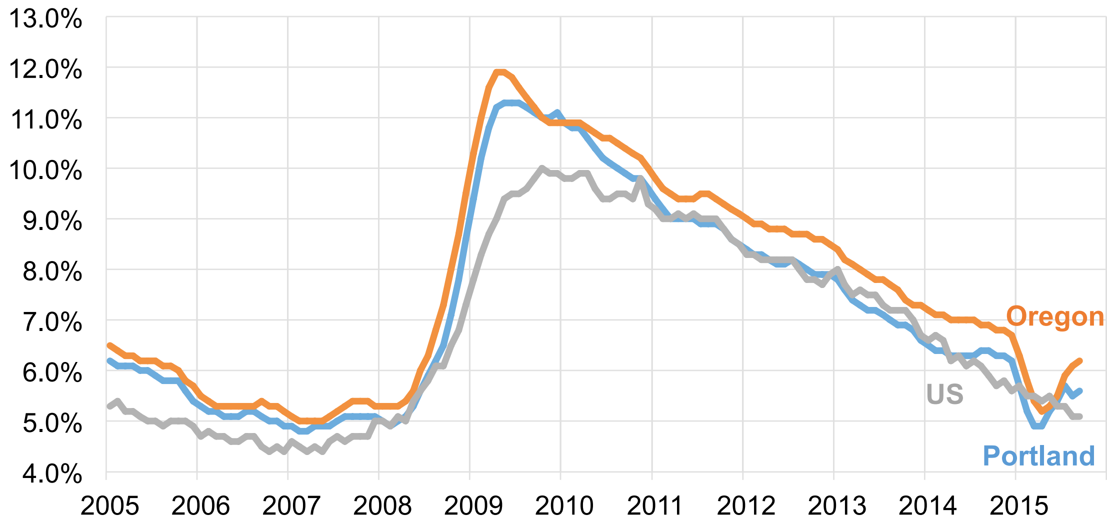
Source: Bureau of Economic Analysis (blue bars) and Wall Street Journal Economic Forecasting Survey (orange bars)

EMPLOYMENT

The Bureau of Labor Statistics (BLS) reported that total U.S. nonfarm employment increased by 142,000 in September and unemployment remained at 5.1 percent. The last time that the national unemployment rate was this low was in April 2008.

The unemployment rate for both Oregon and the Portland Metropolitan Statistical Area (MSA) ticked up slightly in September, to 6.2 percent and 5.6 percent respectively. For both areas, this continues a 6-month trend of rising unemployment rates. According to the Oregon Office of Economic Analysis, the increases bring the figures back in-line with their post Great Recession trends and may reflect overstatements of unemployment drops earlier in the year.

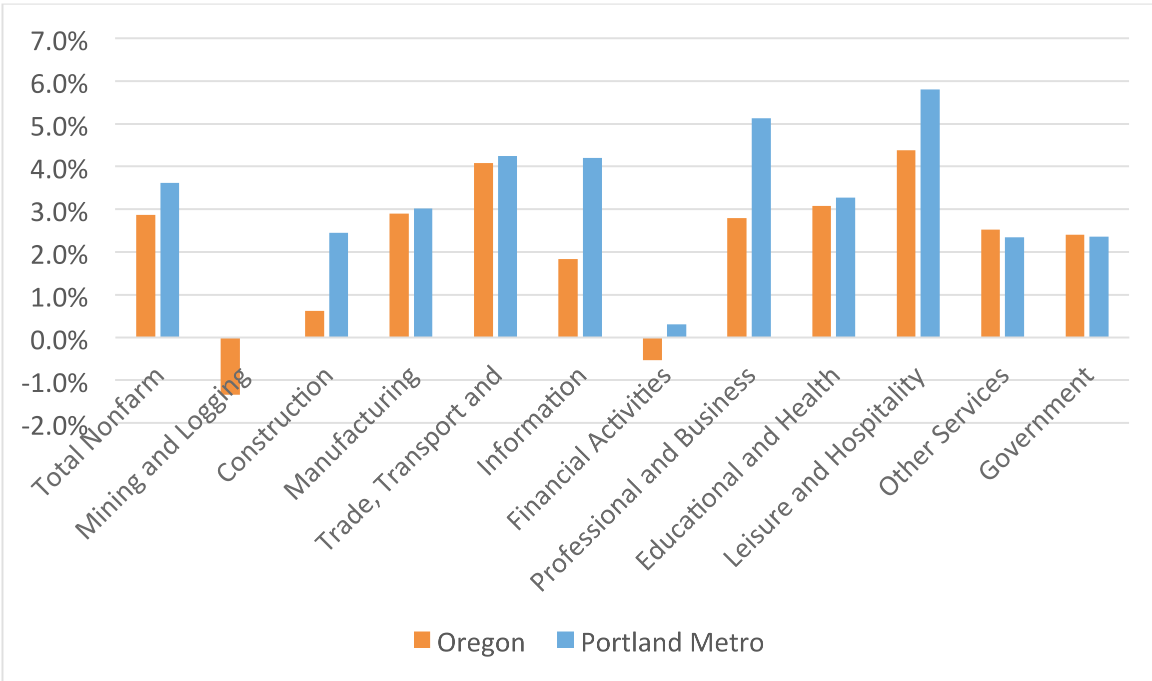
Figure 2: Unemployment Rate, Portland MSA, Oregon and United States, 2005-2015



Source: Bureau of Labor Statistics

Oregon shed 5,300 jobs in September, the first decline in statewide employment in 36 months and the largest monthly job loss since July 2010. The Portland MSA added just 600 jobs in September, and actually lost 2,200 private-sector jobs (offset by gains of 2,800 government jobs). However, taking a longer view, job growth has been strong year-over-year – in the 12 months to September 2015, Oregon's job growth rate was 2.9 percent and that of Portland MSA was a robust 3.6 percent. Both of these rates compare favorably to the national growth rate of 2.0 percent over the same time period, and the Portland MSA rate is one of the highest of all of the top metropolitan areas in the country.

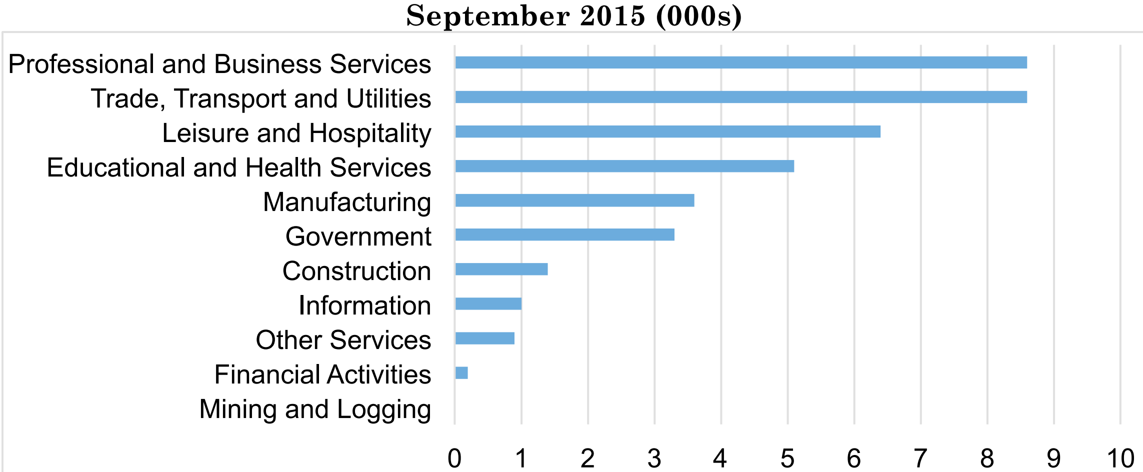
Figure 3: Employment Growth Rate by Sector, Portland MSA and Oregon, 12 Months to September 2015



Source: Oregon Employment Department

Oregon added 49,500 jobs over the past 12 months, with over 39,000 of those *coming from the Portland MSA. Employment growth in the Portland MSA has been* relatively broad-based and has been led by strong growth in Professional and Business Services, Trade, Transportation and Utilities, and Leisure and Hospitality.

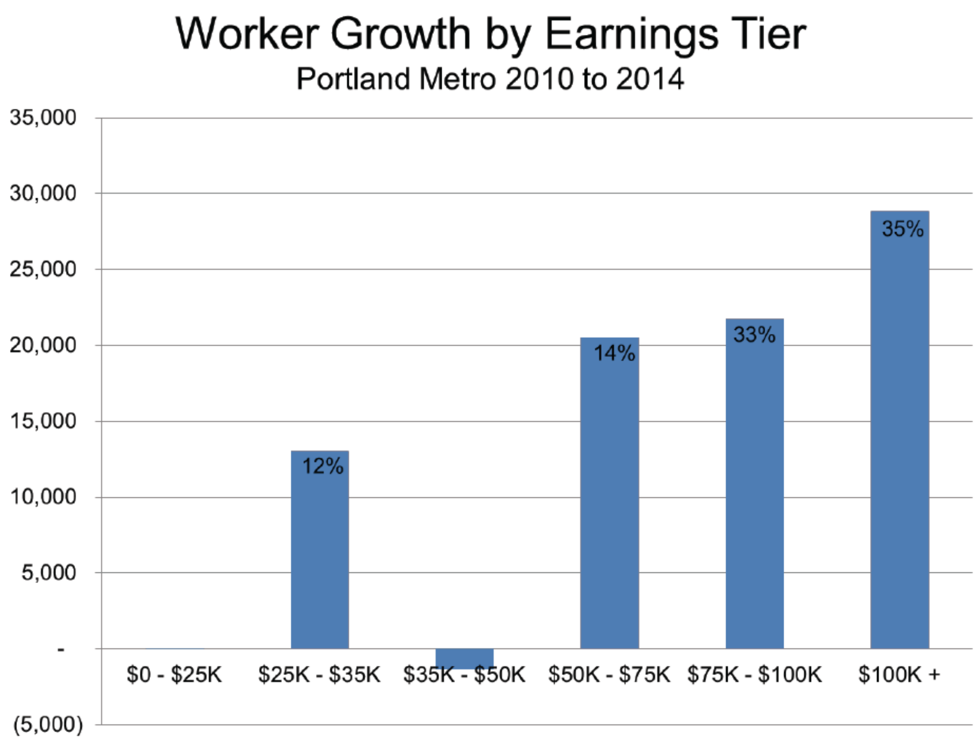
Figure 4: Employment Growth by Sector, Portland MSA, 12 Months to September 2015 (000s)



Source: Oregon Employment Department

According to the Oregon Employment Department, job growth in the Portland MSA since 2010 has been heavily weighted towards high-wage positions. Nearly 70 percent of job growth between 2010 and 2014 came from those earning $75,000 or more per year, and 35 percent came from those earning $100,000 or more. Many of these new jobs are found in the high-tech manufacturing sector, professional and business services, and education and health services.

Figure 5: Employment Growth by Earnings Tier, Portland MSA, 2010-2014



Source: Oregon Employment Department (from October 28, 2015 Presentation)

Growth in the high-wage sectors has pushed the average annual wage growth in Oregon to nearly 8 percent, according to the Oregon Office of Economic Analysis (OEA). However, average wage growth per worker is closer to 3 percent-4 percent year-over-year. The OEA notes that wage gains are increasing at rates above inflation for all Oregon workers except for hourly workers, which have seen virtually no real gains in inflation-adjusted per-capita income. This trend is similar to that seen nationally.

Job growth in Oregon and Portland is expected to continue, driven by projected population growth. The Oregon Office of Economic Analysis expects job growth of over 3 percent annually from 2015 to 2017. Other forecasters, such as IHS, are less bullish about growth prospects after this year.

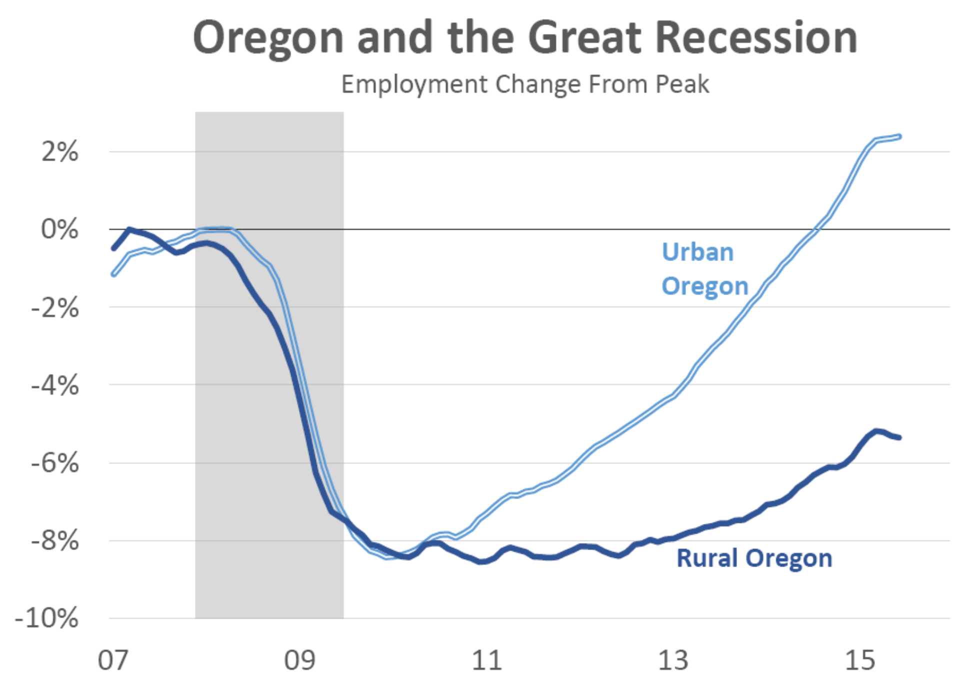
Table 2: Employment Growth Forecasts, Oregon, 2015-2017

Forecaster	2015	2016	2017
Oregon Office of Economic Analysis	3.4%	3.1%	3.1%
IHS Economics	2.9%	1.5%	1.6%
Western Blue Chip Consensus	3.1%	2.7%	-

Source: Oregon Office of Economic Analysis

Job growth has occurred across sectors and regions in the state over the past 5 years. However, job growth in Oregon's urban areas have brought their total employment above pre-recession levels, while the state's rural areas (with the exception of the Columbia Gorge) remain about 5 percent below their peak job levels.

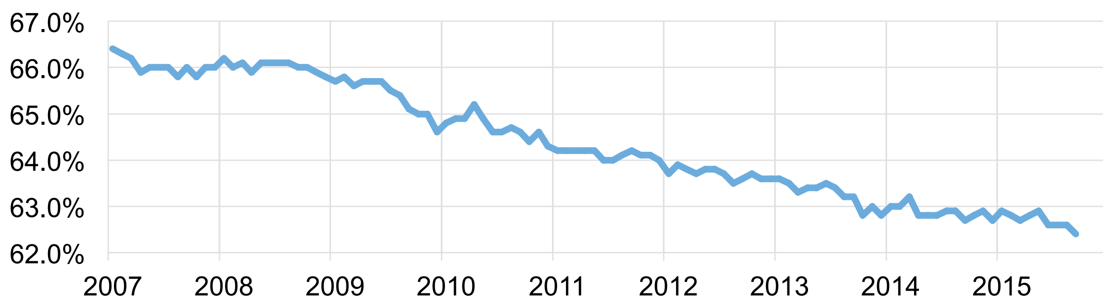
Figure 6: Employment Change from Peak, Oregon, 2007-2015 (June)



Sources: Oregon Employment Department, Oregon Office of Economic Analysis

The labor force participation rate remains a concern to state economists. Oregon's labor force participation rate was 60.2 percent in June, the lowest rate since records began in 1976. This trend is similar to the national trend, which at 62.4 percent is the lowest it has been since 1977.

Figure 7: Labor Force Participation Rate, United States, 2007-2015



Source: Bureau of Labor Statistics

INFLATION

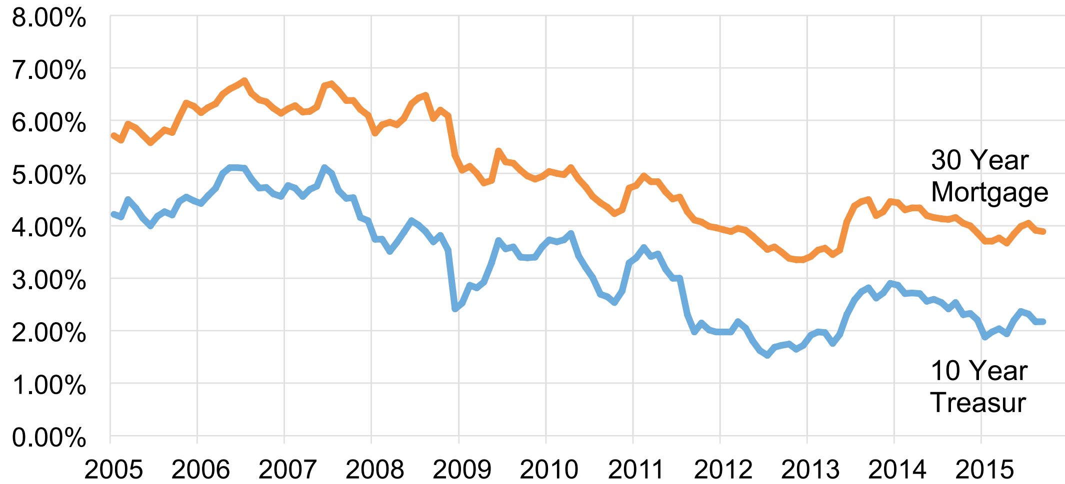
The United States Consumer Price Index (CPI-U) decreased 0.2 percent in September on a seasonally-adjusted basis and essentially 0 percent for the 12 months to September on a non-adjusted basis. Rising prices for food and other items were more than offset by decreases in energy, driven by a sharp drop in gasoline prices. The energy index is down more than 18 percent over the past year. The Wall Street Journal's Economic Forecasting Survey projects that the unadjusted 12-month CPI will increase by 0.8 percent in December 2015.

INTEREST RATES

The Federal Funds Rate remained virtually unchanged in the third quarter at 0.14 percent. The Federal Reserve did not raise rates in September, citing the global economic slowdown, but left open the possibility of an increase by the end of 2015. It is still widely believed that the Federal Reserve will raise the rate before the end of the year, and the Wall Street Journal's Economic Forecasting Survey projects that the rate will increase to 0.32 percent by December 2015 and 0.72 percent by June 2016.

The 10-year Treasury remained unchanged at 2.17 percent and the 30-year mortgage rate ticked down in the third quarter, ending September at 3.89 percent respectively. Both of these measures remain below their September 2014 levels.

Figure 8: Treasury and Mortgage Rates, United States, 2005-2015



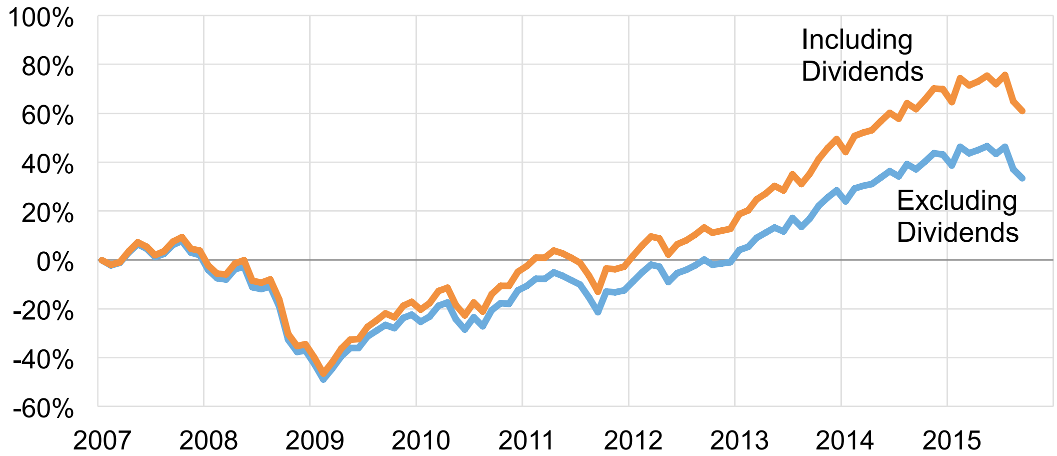
Source: Federal Reserve

CAPITAL MARKETS

The US Treasury yield curve flattened in the third quarter, with shorter-term rates moving higher and longer-term rates declining 20 to 30 basis points.

The big news in the capital markets in the third quarter was the increased volatility in global equity markets, reaching levels not seen in years. Responding to macroeconomic and geopolitical news, especially fears concerning the Chinese economy, the S&P declined 6.4 percent in the quarter, with the NASDAQ falling by 7.4 percent.

Figure 9: Standard & Poor's 500 Index, 2007–2015



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

LOOKING AHEAD

Does the rise in unemployment levels in Oregon and Portland signal a trend, or will these markets continue with their strong growth of the past few years? Does the volatility in China signal a change in its economy, or will it continue to have strong (albeit declining) growth? Will the Federal Reserve raise interest rates by year end? Will Oregon's minimum wage be raised significantly? These are all questions that impact the Oregon and Portland economies, and economists and real estate investors will be watching to see what trends emerge over the next few quarters. ■

RESIDENTIAL MARKET ANALYSIS

CLANCY TERRY

RMLS Student Fellow
Master of Real Estate Development Candidate

In general, the gains nationally and in local Oregon markets reported for the third quarter of 2015 are more modest than those that drove the second quarter's results. Housing in particular is quite cyclical in accordance with the seasons, meaning it may be useful to interpret the third quarter's results by shifting focus to year-on-year improvements. As winter approaches, volumes will display rather normal contractions. That being said, most of the Oregon markets surveyed continue to perform strongly.

Axiometrics reports that nationally in July, single-family permitting decreased by 1.9 percent from the prior month to a Seasonally Adjusted Annual Rate (SAAR) of 679,000 units, a 6.1 percent increase year over year. Single-family starts increased 12.8 percent from the prior month to 782,000 units, which is 19.0 percent higher in year-over-year terms. Single-family completions totaled 627,000 units for the 12 months ending in July 2015.

The National Association of Realtors (NAR) reports the median sale price for existing single-family homes registered at $235,500, a 5.8 percent premium over July 2014. Transaction volume was also up in year-over-year terms by 2.7 percent to a SAAR of 4.96 million units. Unsold inventory of all home types at the end of July

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tightened to a 4.8-month supply, down 0.4 percent from 4.9 months in June. First-time homebuyers represented a 28 percent share of the market in July.

National single-family permitting increased again in August, this time by 2.8 percent over the prior month to a SAAR of 699,000 units, an 8.7 percent year-over-year increase. For the consecutive 12 months ending in August 2015, single-family starts decreased 3.0 percent to 739,000 units (still 14.9 percent better than one year prior). Completions rose 5.4 percent to 646,000 units annually.

In August, a SAAR of 4.69 million existing single-family homes transacted, around six percent greater in year-over-year terms. The median price for these units came in at $230,200, a five percent gain year over year. Unsold inventory of all home types increased from the prior month to a 5.2-month supply. First-time homebuyers represented an improved 32 percent of the market in August.

In September, national single-family transaction volume increased again, to a SAAR of 4.93 million units, nearly 10 percent more than one year prior. The median sale price for existing homes reached $223,500, nearly seven percent higher year over year. National unsold inventory dropped in September to a 4.8-month supply. The share of first-time homebuyers in the market decreased to 29 percent during the month, backing off from the record set so far in 2015 in August (32 percent).

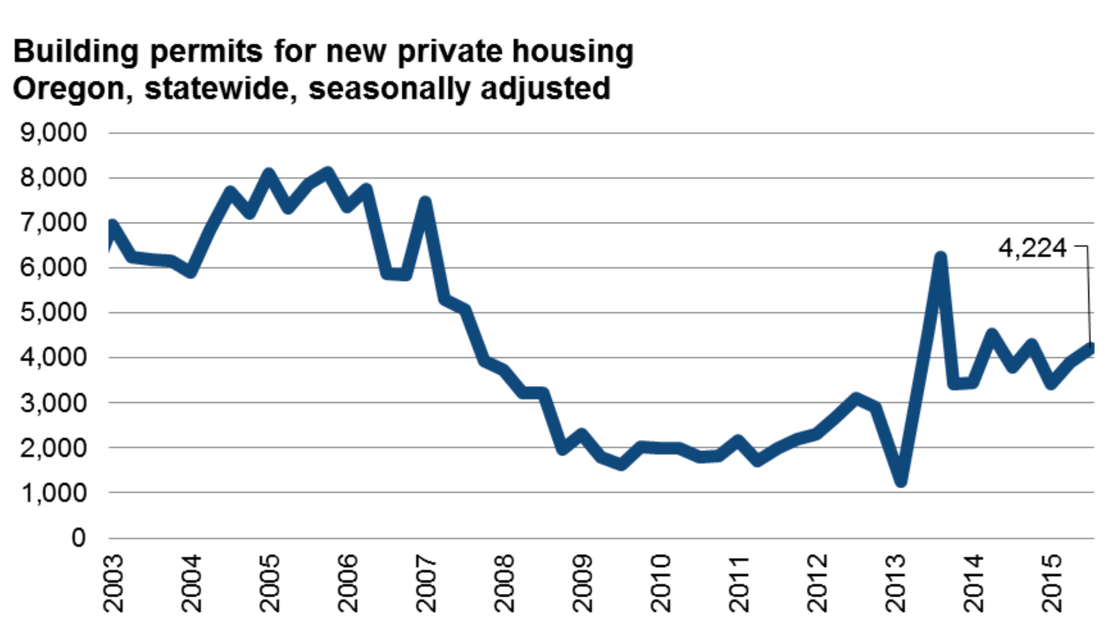
Berlinberg Properties reports that, from a national perspective in the third quarter, mortgage rates increased in July and then fell back in August and September amid concerns over turbulence in global markets and uncertain growth. The group shares that Freddie Mac's most recently reported average commitment rates are as follows:

- 30-year fixed rate: 3.91 percent
- 15-year fixed rate: 3.11 percent
- 5/1 adjustable rate: 2.92 percent

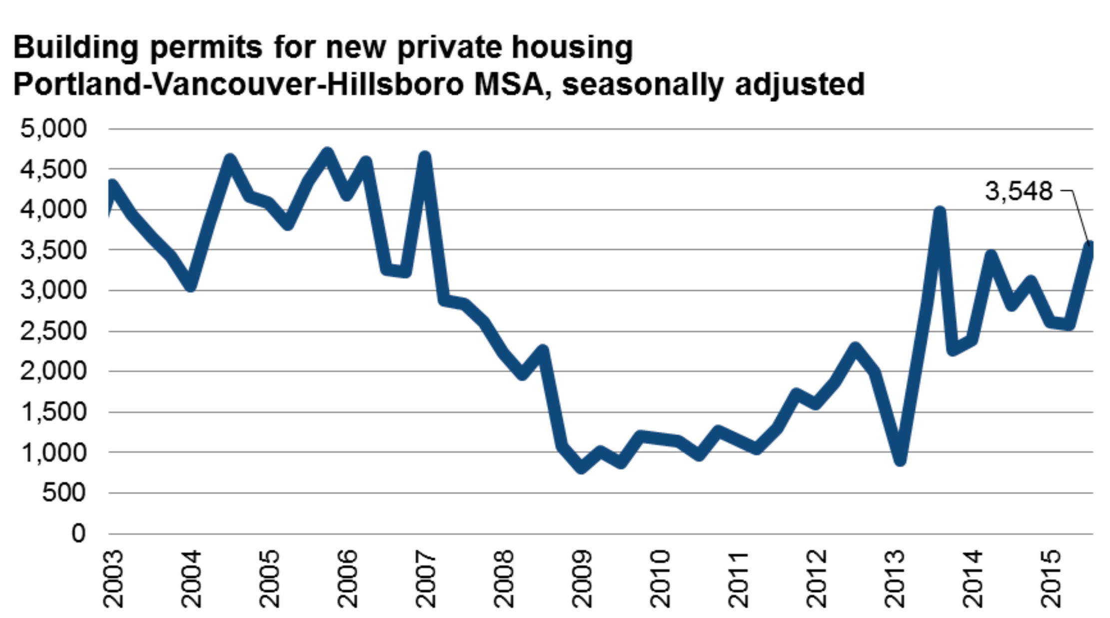
Citing the U.S. Department of Commerce, RealtyTrac's August Housing News Report indicates the national homeownership rate has fallen for the eighth consecutive year, arriving at 63.4 percent in the second quarter of 2015. This is the lowest rate of homeownership in the U.S. since 1967. The 50-year average rate is 65.3 percent. As previously documented, young adults are an important driver of this trend as they face uncertain employment prospects, relatively high personal debt burdens, "wage growth that hasn't kept up with surging home prices," and exacting mortgage underwriting standards. Of course, generationally unique tastes and preferences play a role as well.

LOCAL PERMITTING

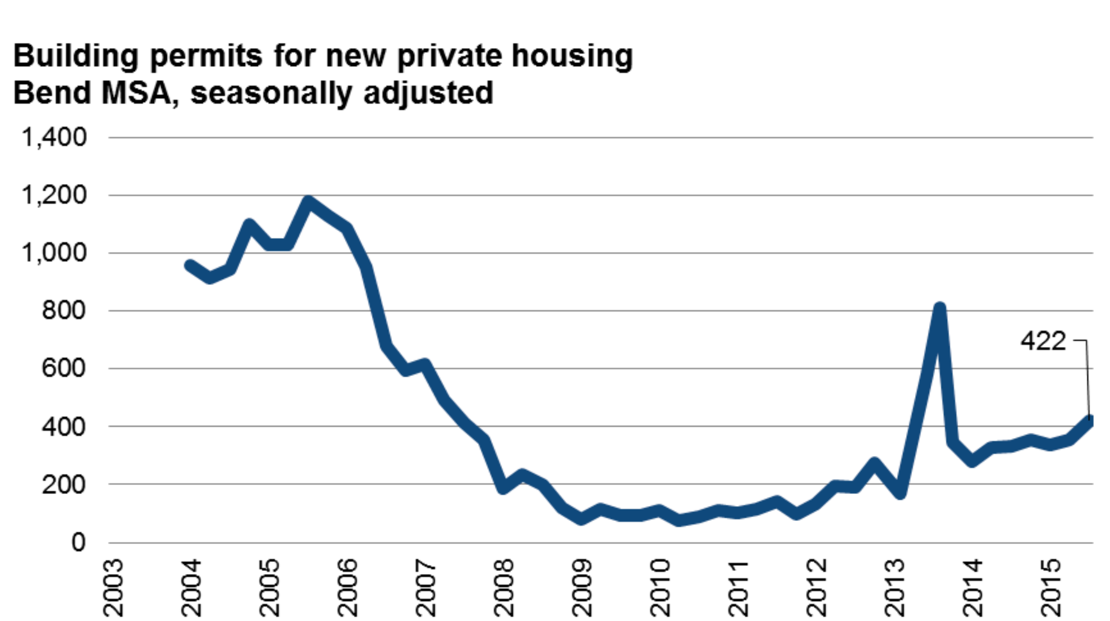
In the third quarter of 2015, 4,224 building permits for new private housing units were issued in total across Oregon. Despite quarter-over-quarter and year-over-year increases, statewide permitting activity has been relatively stable for the past two years.



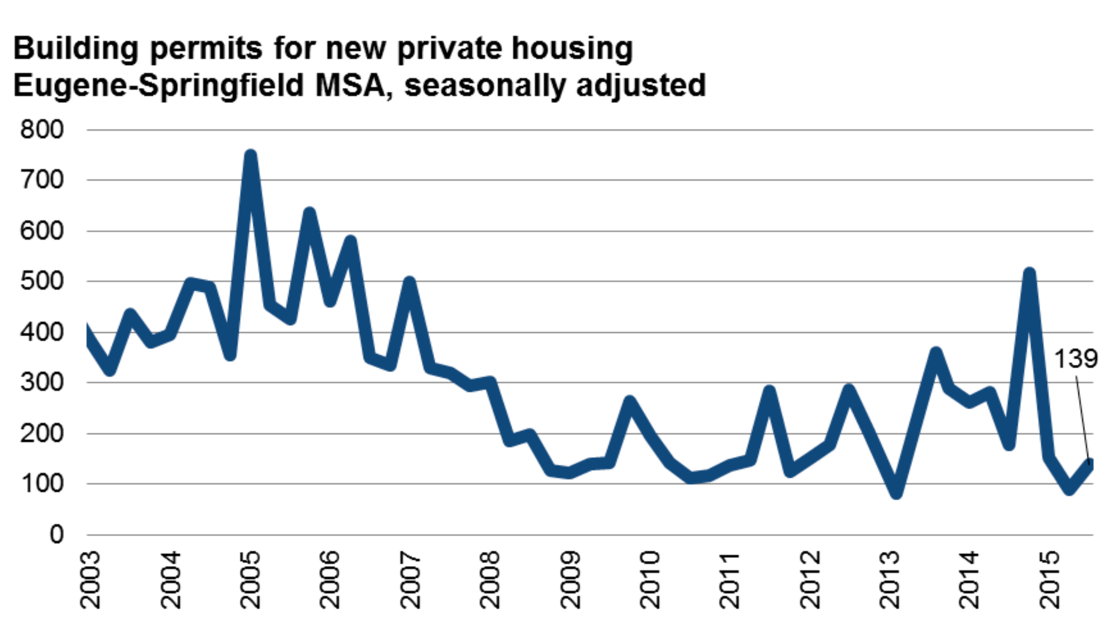
3,548 permits for new private housing units were issued in the Portland-Vancouver-Hillsboro Metropolitan Statistical Area (MSA) in the third quarter. This is a substantial increase in quarter-over-quarter and year-over year terms: 37 percent or 960 permits greater versus 2015's second quarter, and 26 percent or 725 permits more than 2014's third quarter.



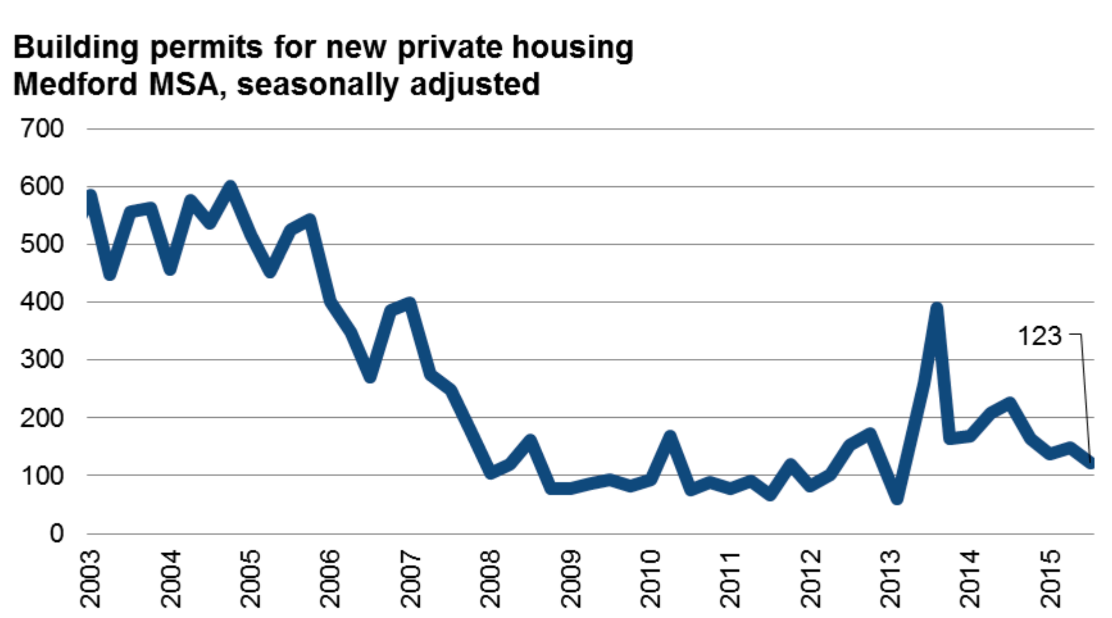
The Bend MSA received 422 permits for new private housing units. In consecutive-quarter and year-over-year comparisons, this represents much stronger gains than were reported in the second quarter. 422 permits in the third quarter represent 19 percent more than were issued in the second quarter of 2015 and 27 percent more than were issued in the third quarter of 2014.



The Eugene-Springfield MSA's third-quarter results are mixed. Permitting for new private housing units totaled 139, 54 percent more than the prior quarter but 22 percent fewer year over year.

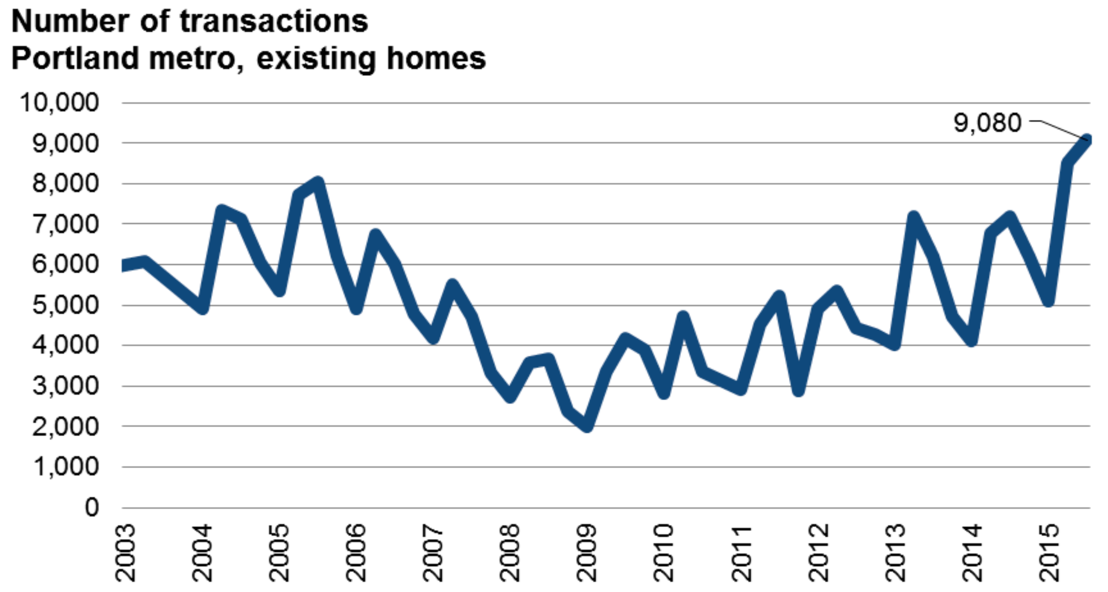


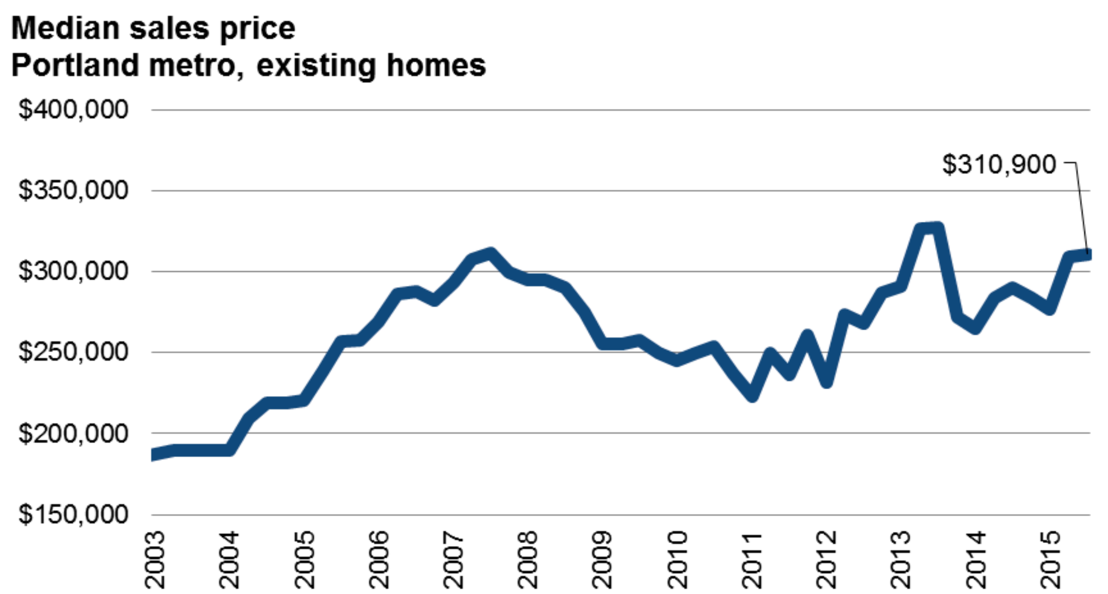
The Medford MSA is the only market to see declines in permitting of new private housing units from both perspectives in the third quarter. 123 such permits were issued, 17 percent less than the prior quarter and 46 percent less in year-over-year terms.

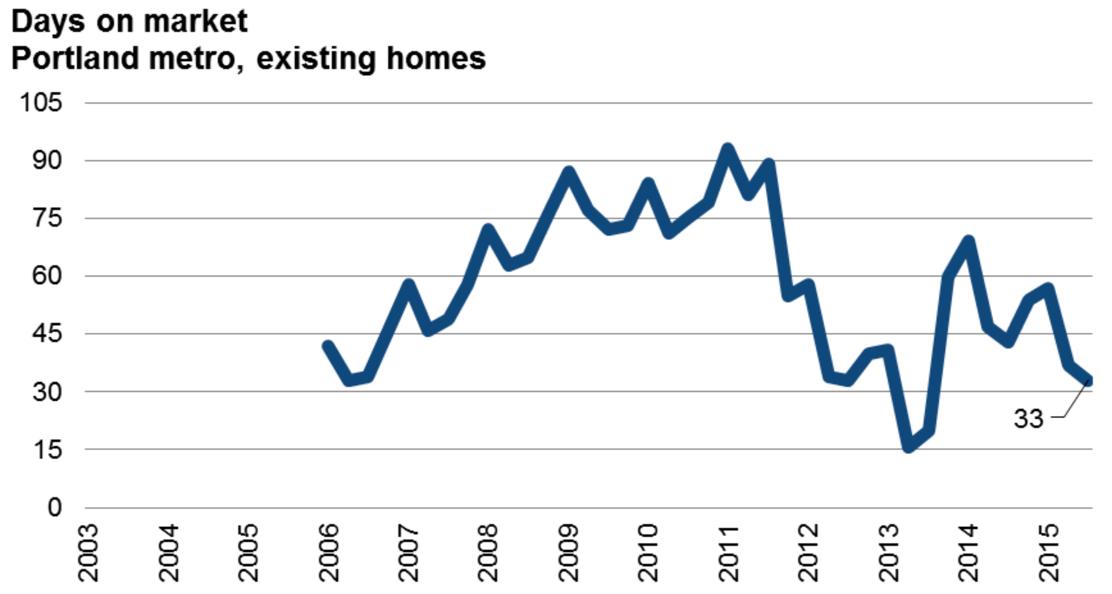


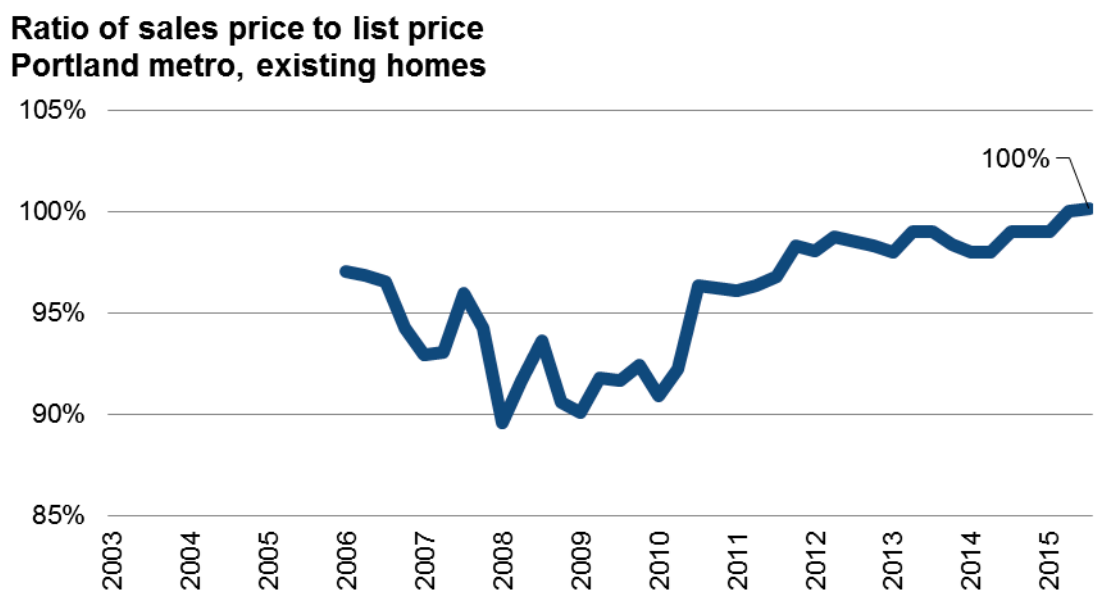
PORTLAND TRANSACTIONS

The Portland market has show another quarter of strong growth n the residential market. In the quarter, 9,080 sales were recorded, seven percent more than the second quarter and 26 percent more than the third quarter of 2014. The median sale price inched up to $310,900, around one percent higher than the prior quarter and seven percent higher year over year. Units averaged 33 days on the market, an 11 percent shorter timeframe than the prior quarter and two percent less time than the third quarter of 2014. Sellers continued to command 100 percent of list prices in realized sale prices.

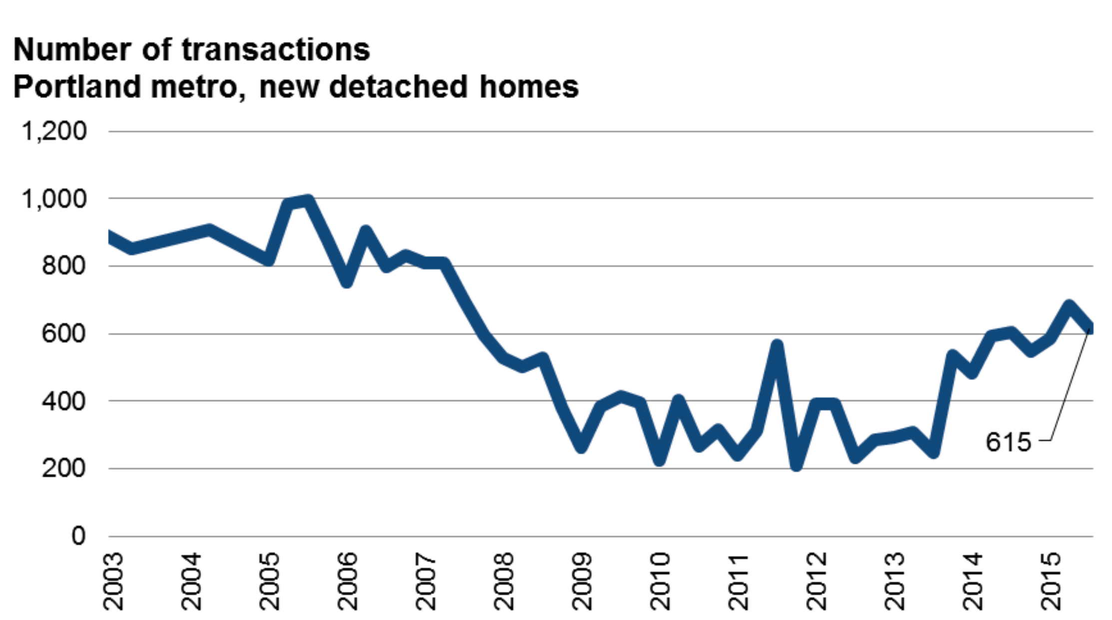

Number of transactions
Portland metro, existing homes
10,000
9,000
8,000
7,000
6,000
5,000
4,000
3,000
2,000
1,000
0
9,080
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015

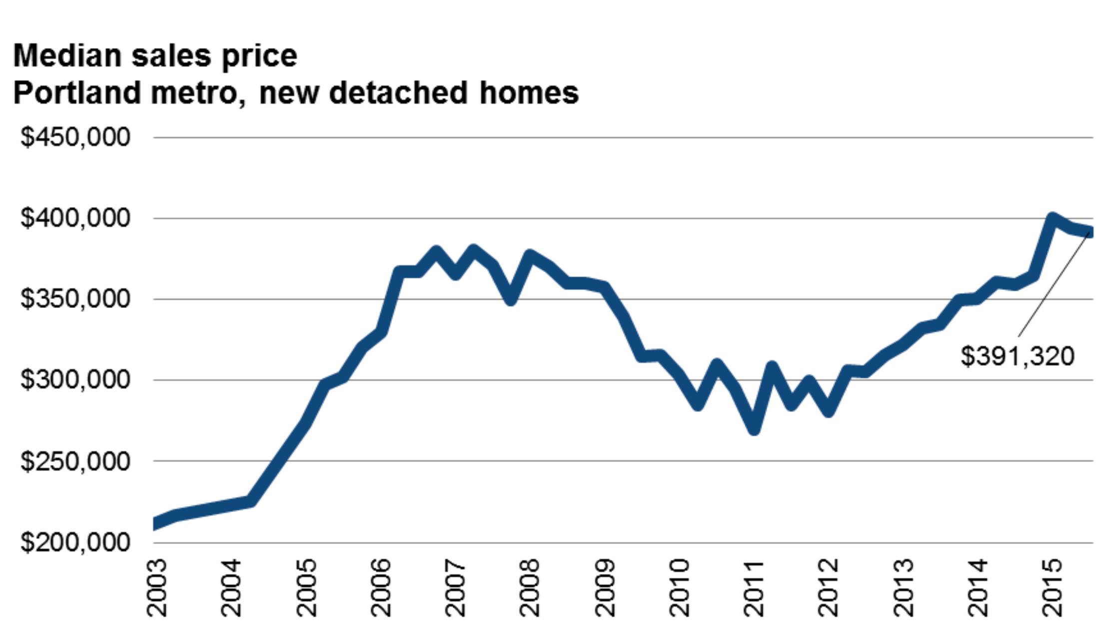

Median sales price
Portland metro, existing homes
$400,000
$350,000
$300,000
$250,000
$200,000
$150,000
$310,900
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015





In the market for newly built detached single-family units, sales volume and median price displayed modest reductions versus the second quarter and modest gains versus the third quarter of 2014. 615 new homes sold in the third quarter of 2015, 10 percent fewer than during the second quarter and two percent more than third quarter 2014. The median sale price floated down to $391,320, around one percent lower than second quarter but still nine percent better than third quarter 2014.

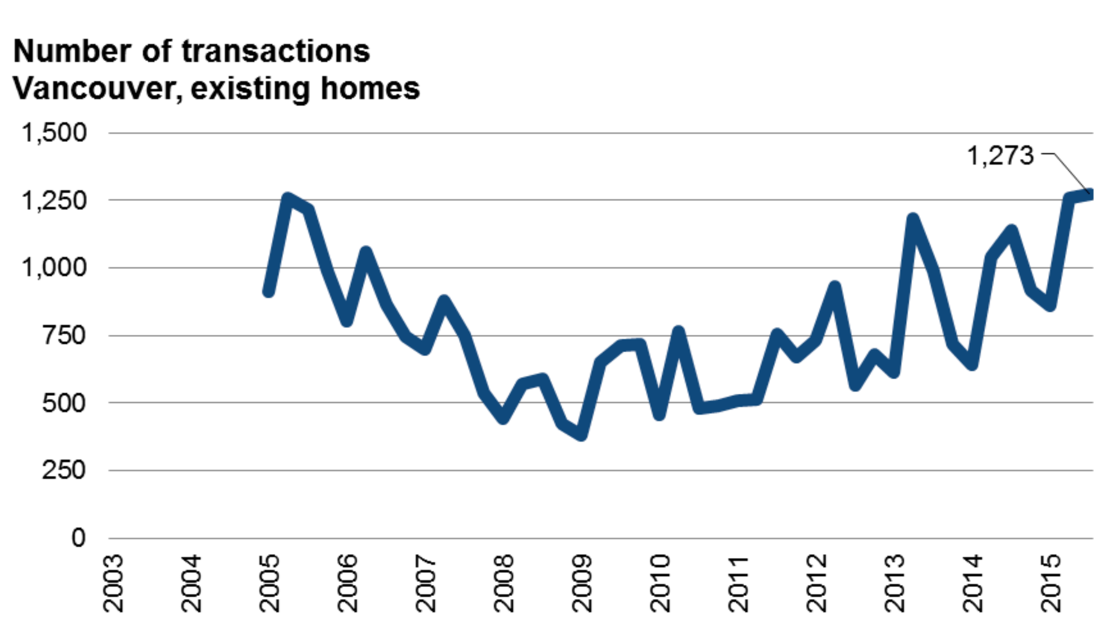


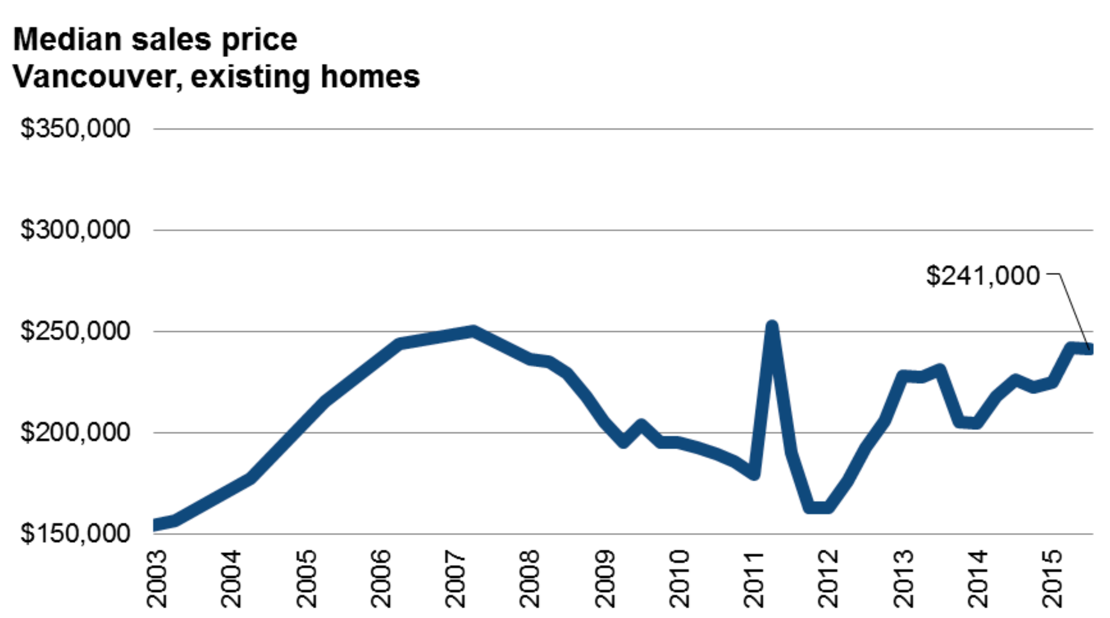


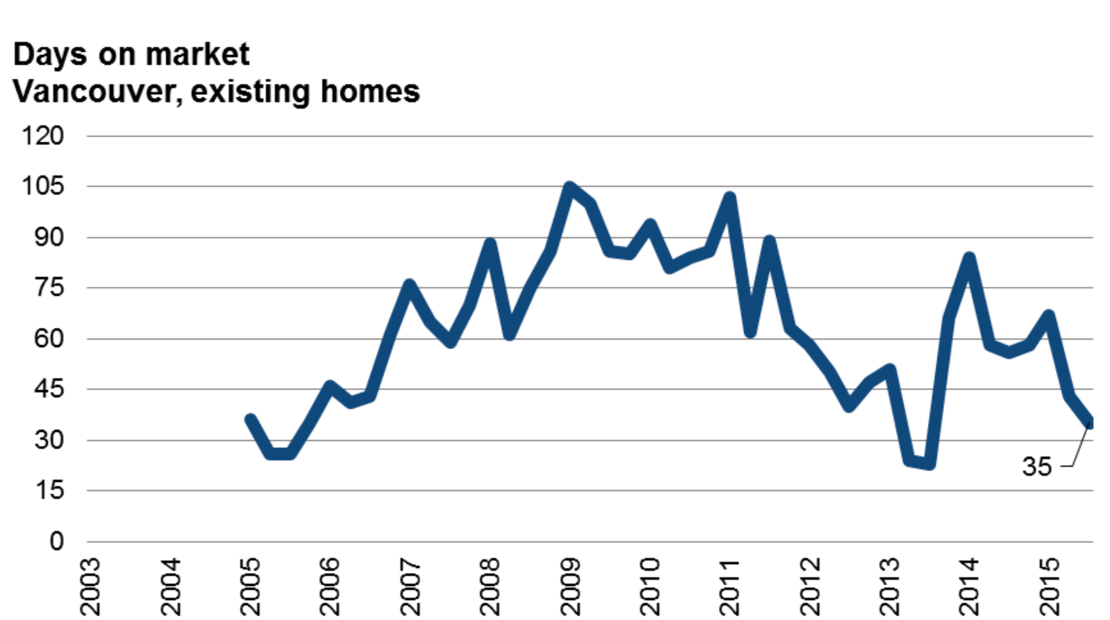
VANCOUVER AND CLARK COUNTY TRANSACTIONS

The trend patterns in the Vancouver and Clark County markets for existing single-family units show a mixed bag of generally modest gains in the third quarter.

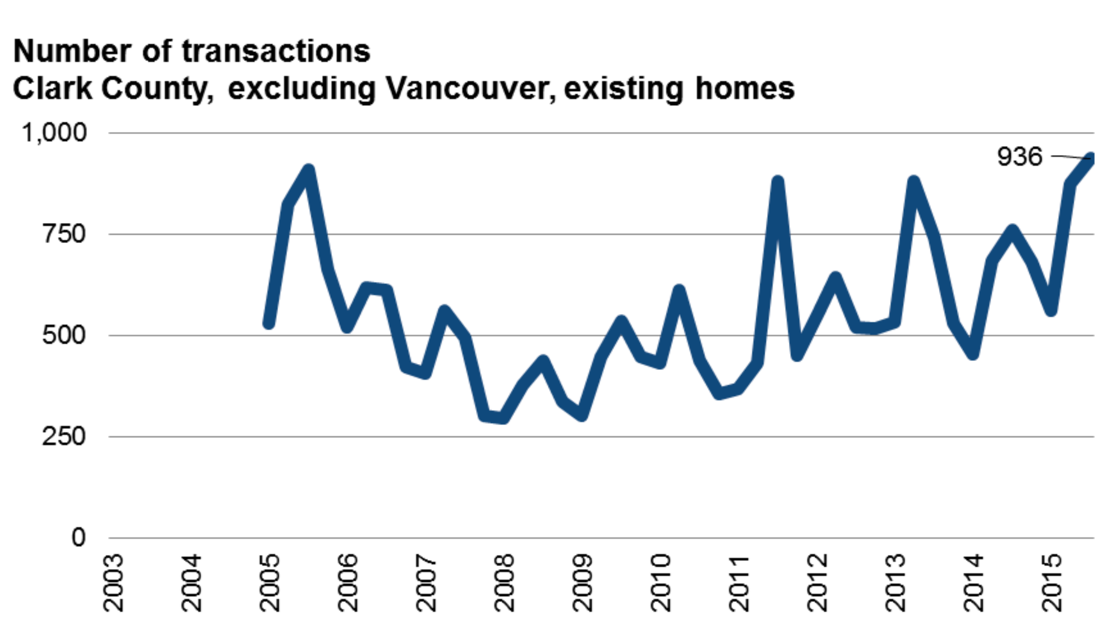
1,273 existing units sold in Vancouver, a one percent increase over the prior quarter and a 12 percent increase year over year. The median sale price barely moved, declining from the prior quarter less than one percent to $241,000, a price seven percent greater than third quarter 2014. Units averaged 35 days on the market, which is 19 percent faster than the second quarter and 38 percent faster than third quarter 2014.

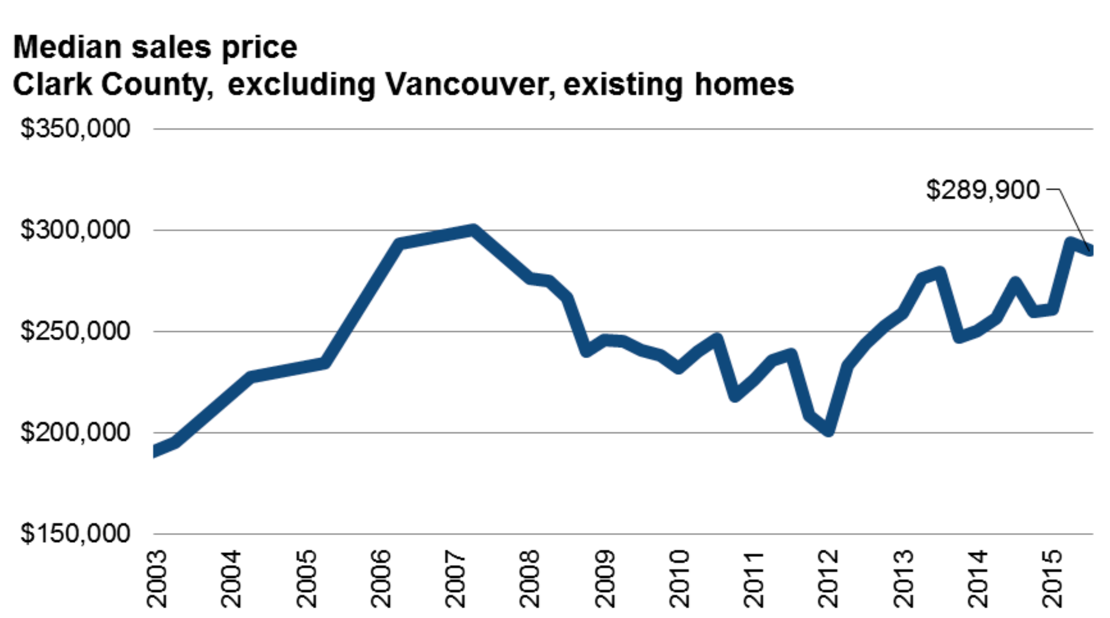


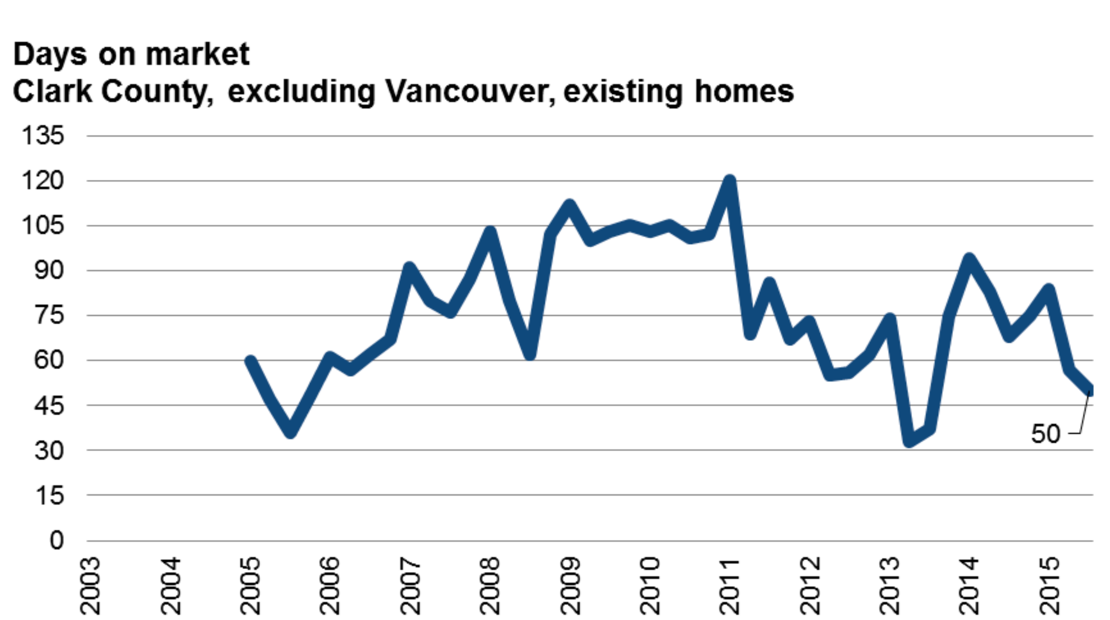

Median sales price
Vancouver, existing homes
$350,000
$300,000
$250,000
$200,000
$150,000
$241,000
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015


Days on market
Vancouver, existing homes
120
105
90
75
60
45
30
15
0
35
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015

Similarly, 936 existing units sold in the balance of Clark County excluding Vancouver during the third quarter, a seven percent increase over the second quarter and 23 percent more than third quarter 2014. The area's median price drifted down from the prior period by one percent to $289,900, a price six percent greater year over year. The units that ultimately sold averaged 50 days on the market, which is 12 percent faster than the second quarter statistic and 26 percent less time year over year.



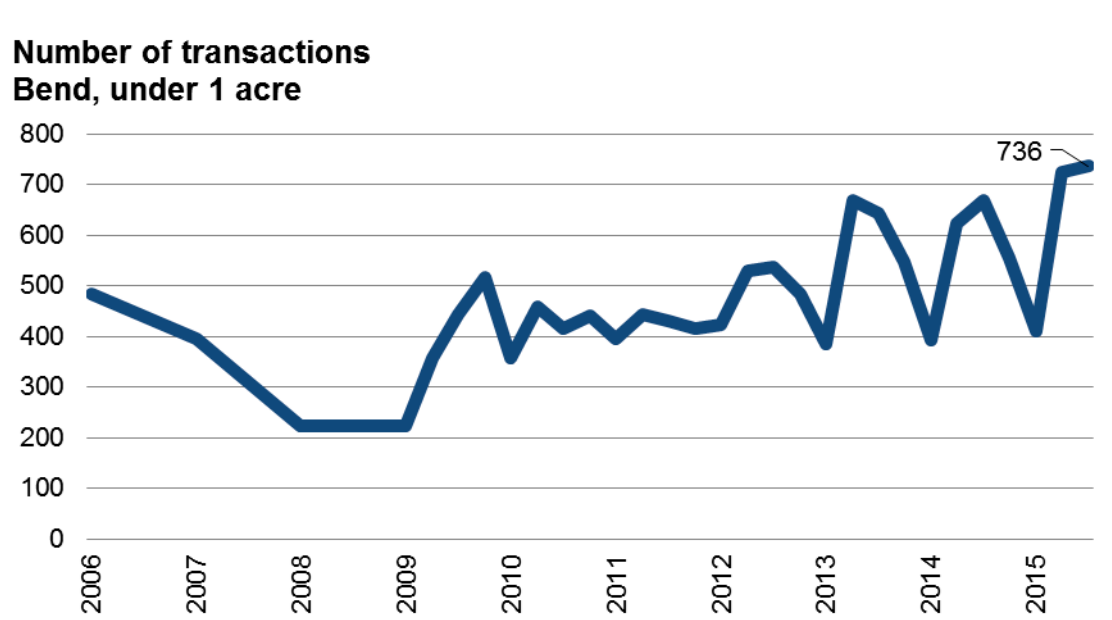

Median sales price
Clark County, excluding Vancouver, existing homes
$350,000
$300,000
$250,000
$200,000
$150,000
$289,900
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015

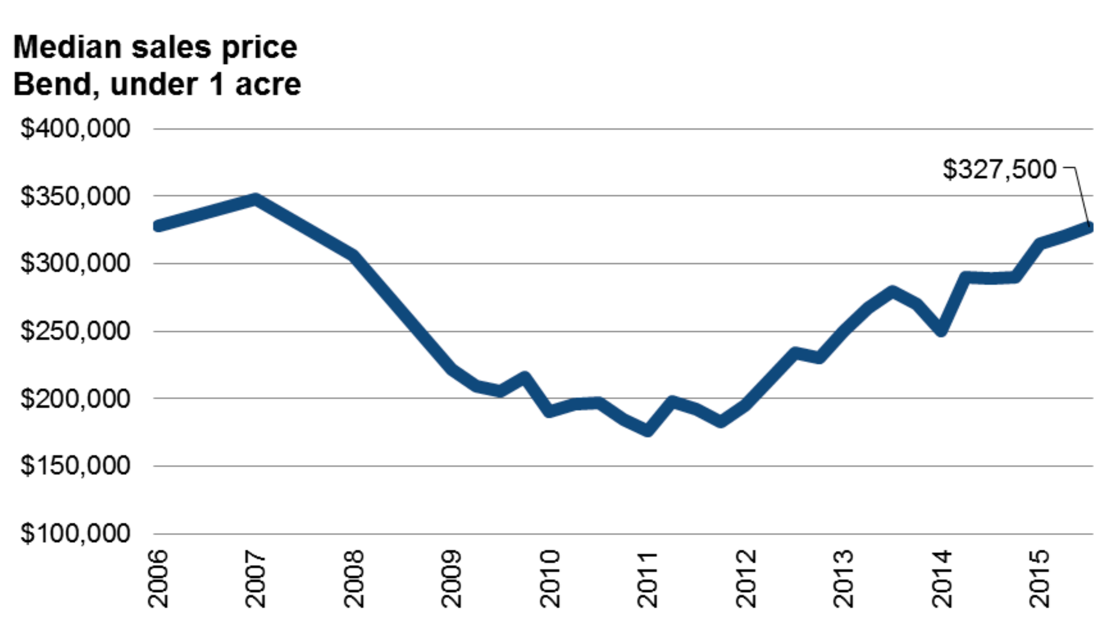

Days on market
Clark County, excluding Vancouver, existing homes
135
120
105
90
75
60
45
30
15
0
50
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015

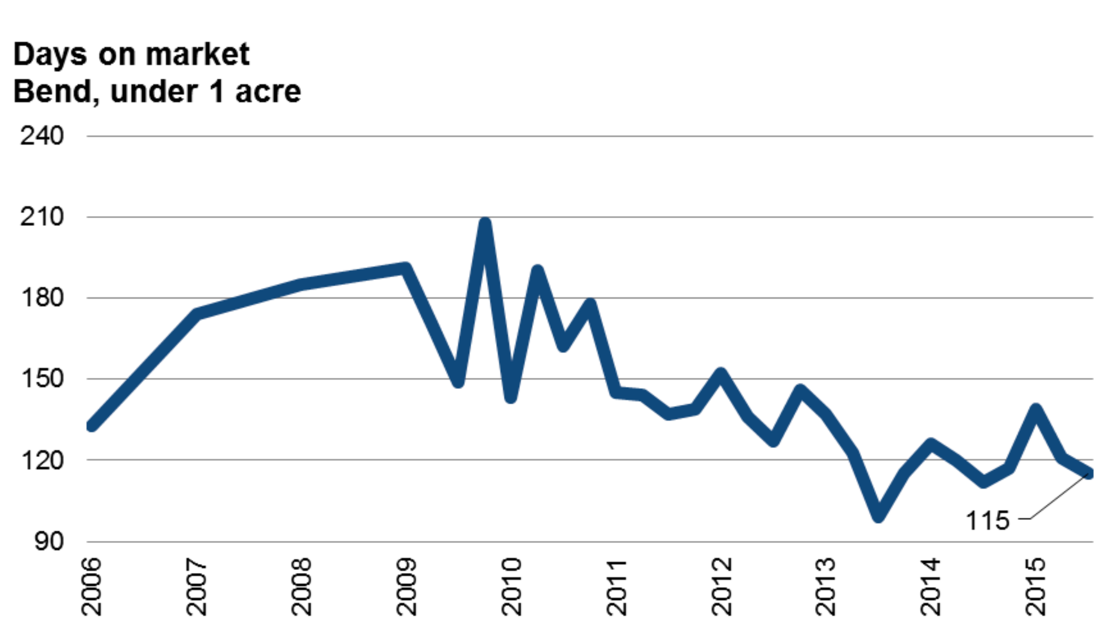
CENTRAL OREGON TRANSACTIONS

Like its northern neighbors Portland and Vancouver, Central Oregon's market indicators generally revealed growth in the third quarter, but not at the robust rates seen during the second quarter.

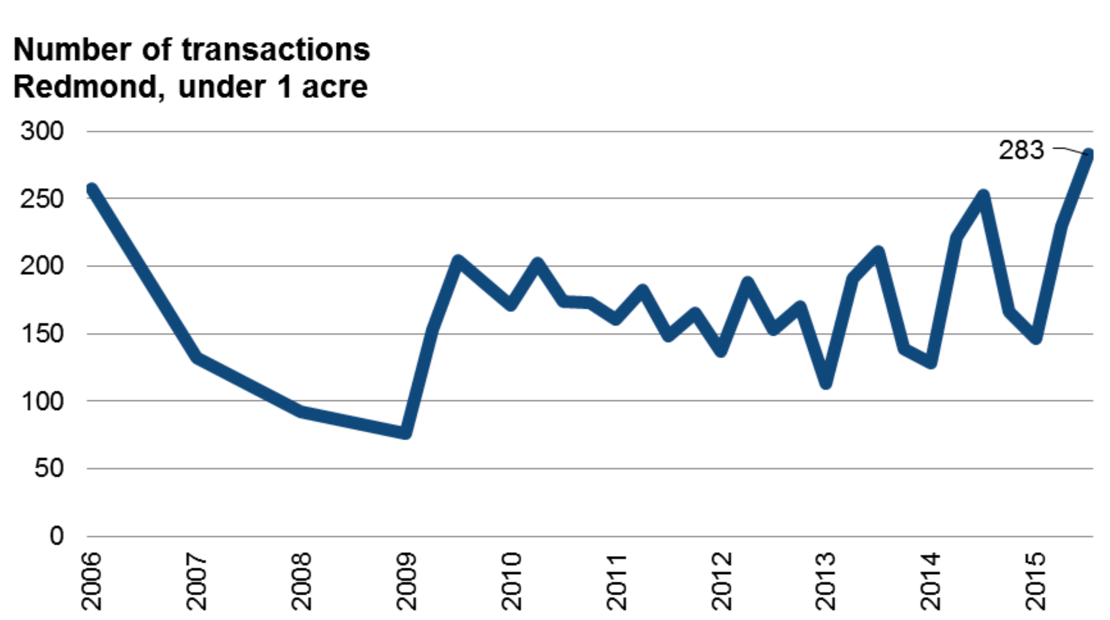
The third quarter in Bend saw 736 trades of existing homes. This is one and a half percent more than the second quarter and 10 percent more year over year. The median sale price rose two percent from the prior period to $327,500, a price 13 percent above third quarter 2014. Transacted units averaged 115 days on the market, five percent faster than in the second quarter but three percent slower than the third quarter of 2014.

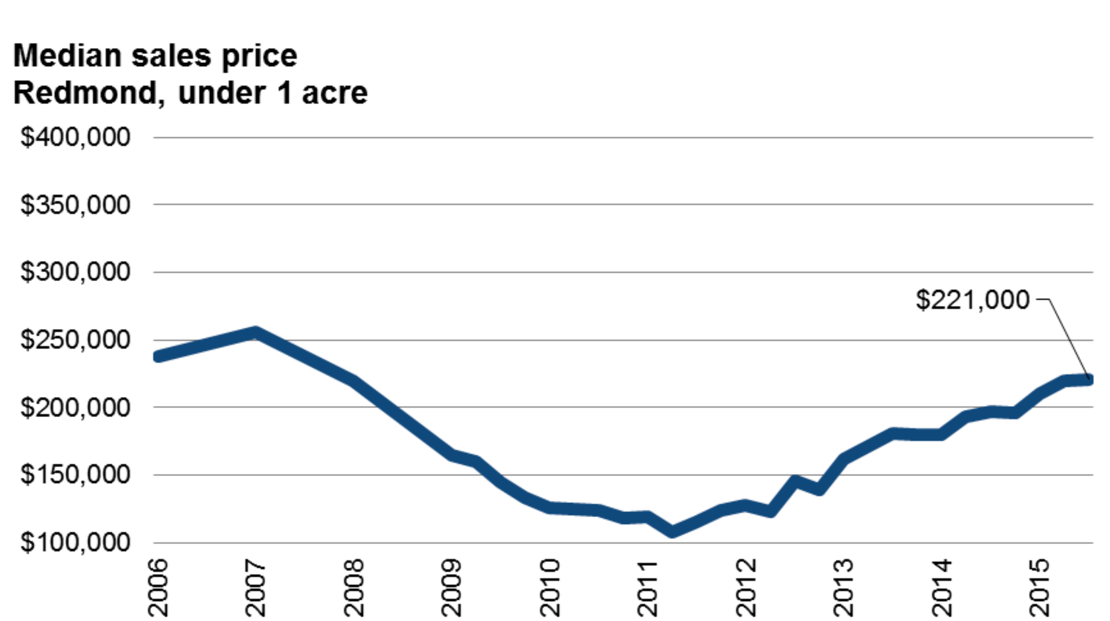


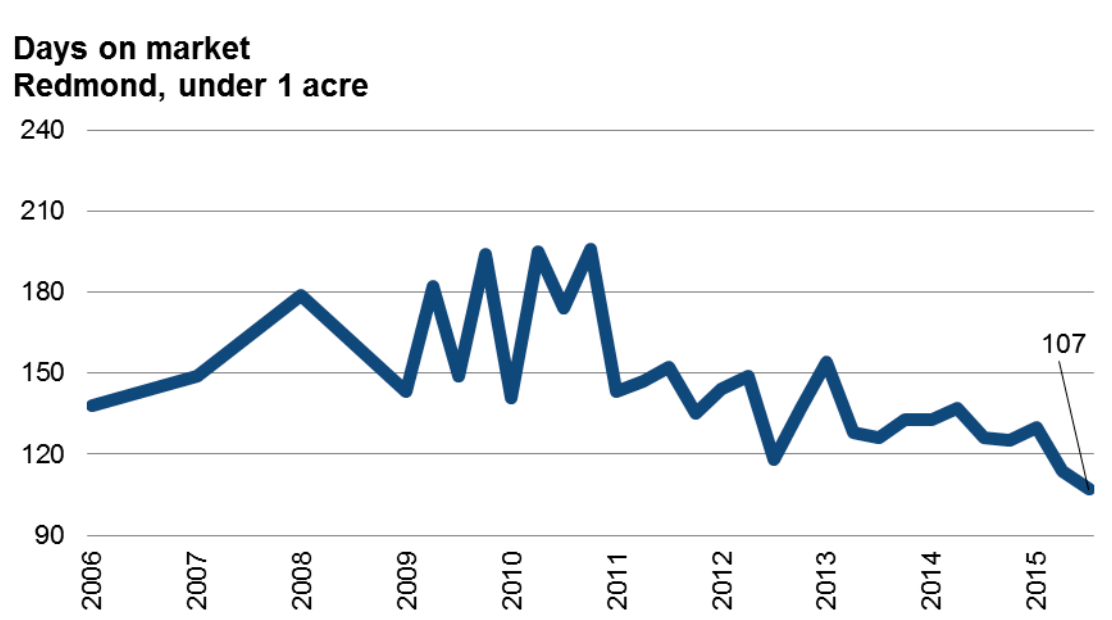




Redmond's existing single-family transaction total for the third quarter is 283 units: 23 percent more than the second quarter and 12 percent more than third quarter 2014. The median sale price increased from the prior period less than one percent to $221,000, a price that is 12 percent higher than the level reached in third quarter 2014. Sold units averaged 107 days on the market, six percent faster than second quarter and 15 percent faster year over year.



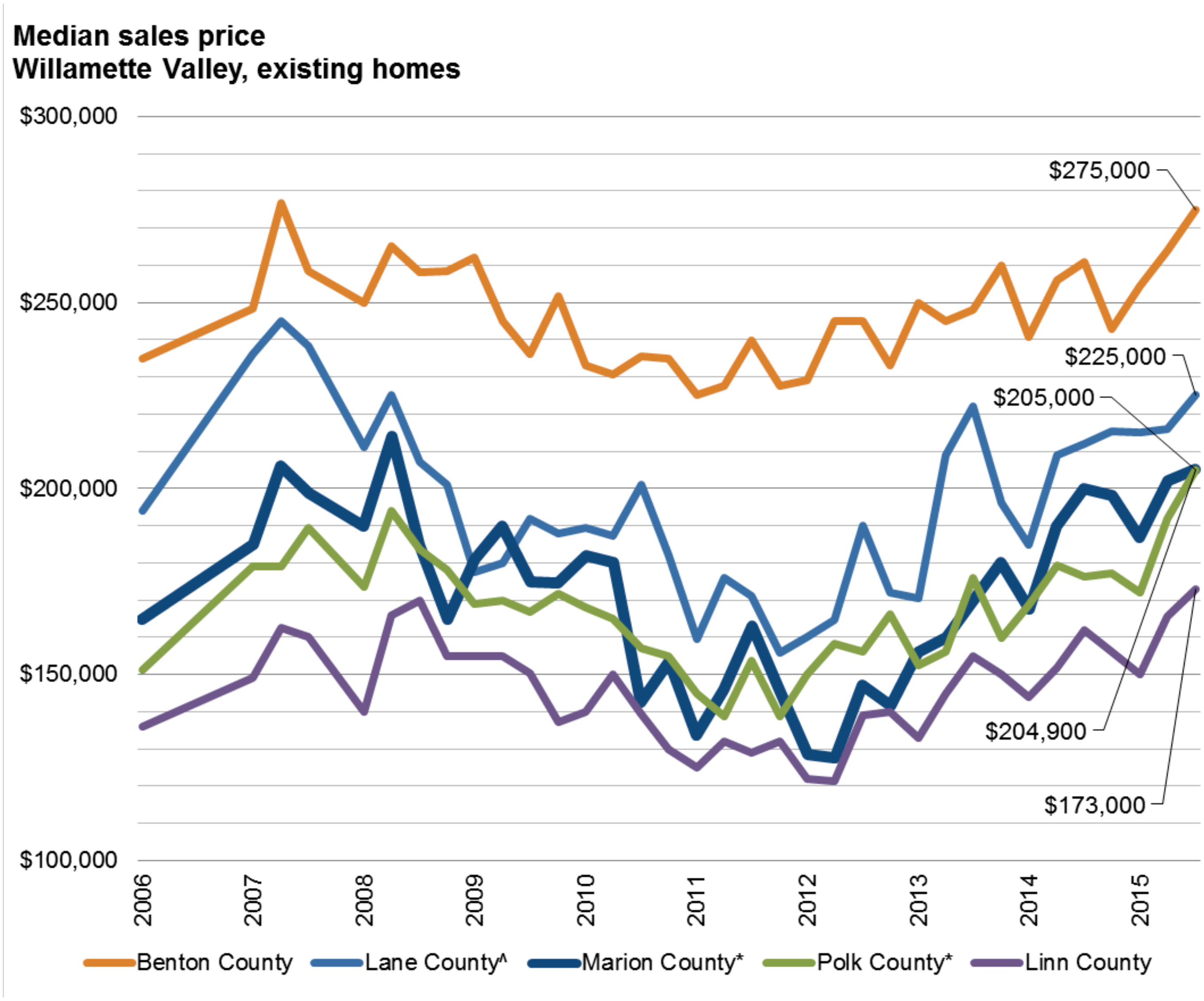




WILLAMETTE VALLEY TRANSACTIONS

As in the second quarter of 2015, all measurements of median sale prices in the Willamette Valley counties made positive movements in the third quarter. Also similar: Linn and Polk Counties posted the most substantial increases versus the second quarter, and Linn County showed the greatest year-on-year growth.

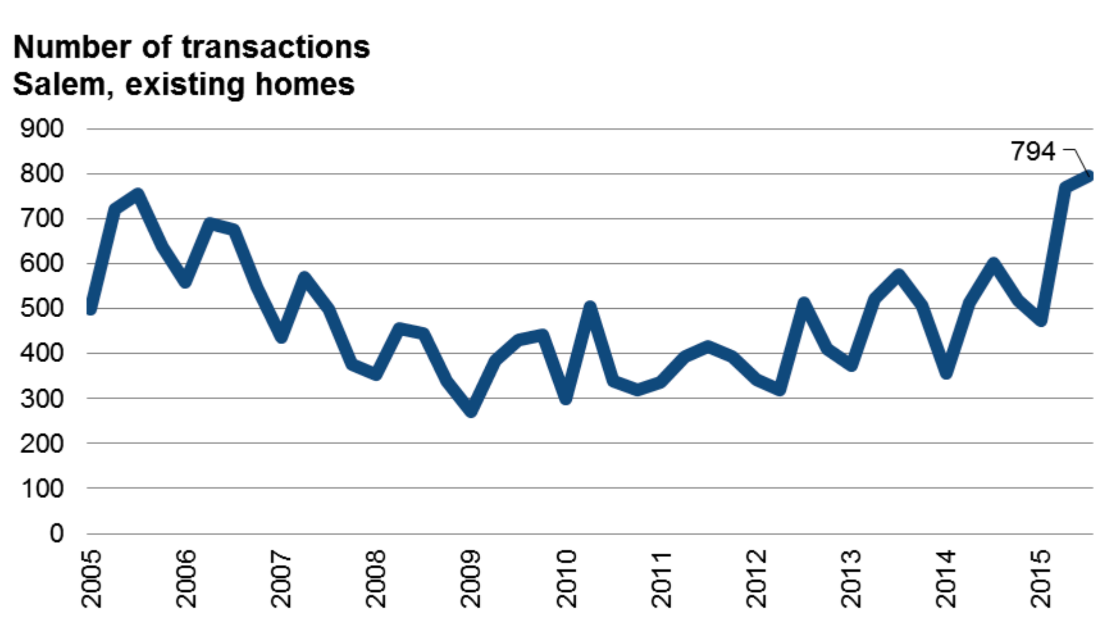
- Benton County: $275,000 median price, a four percent increase of $11,122 from the prior quarter and a five percent increase of $14,000 year over year
- Lane County (excluding Eugene): $225,000 median price, a four percent increase of $9,000 from the prior quarter and a six percent increase of $13,000 year over year
- Marion County (excluding Salem): $205,000 median price, a one and a half percent increase of $3,000 from the prior quarter and a three percent increase of $5,100 year over year
- Polk County (excluding Salem): $204,900 median price, a seven percent increase of $12,900 from the prior quarter and a 16 percent increase of $28,500 year over year
- Linn County: $173,000 median price, a four percent increase of $7,250 from the prior quarter and a seven percent increase of $11,00 year over year

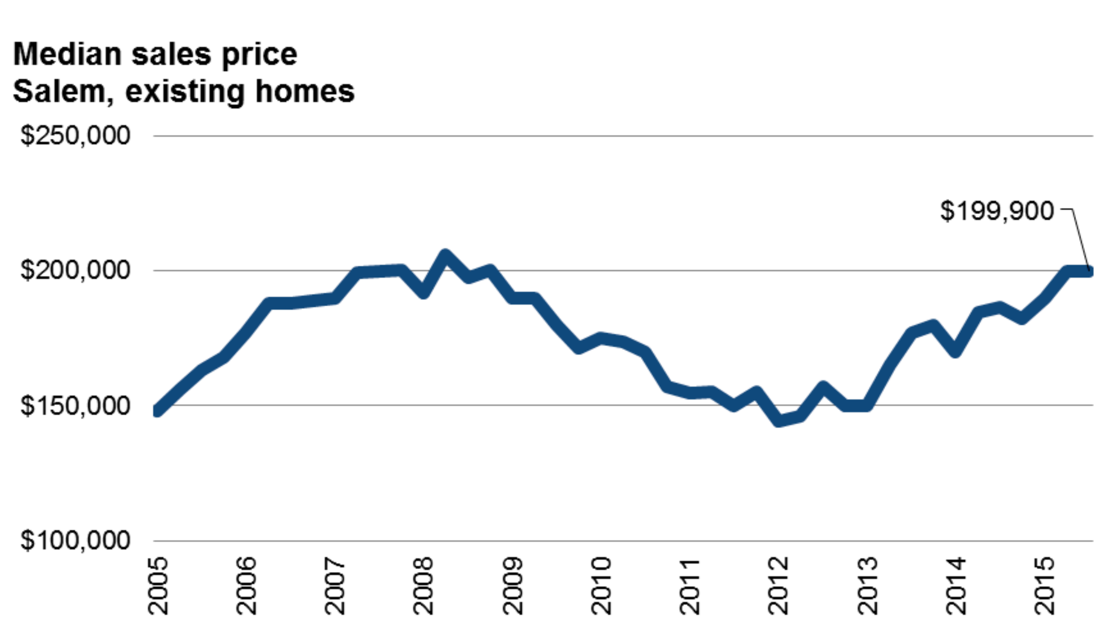


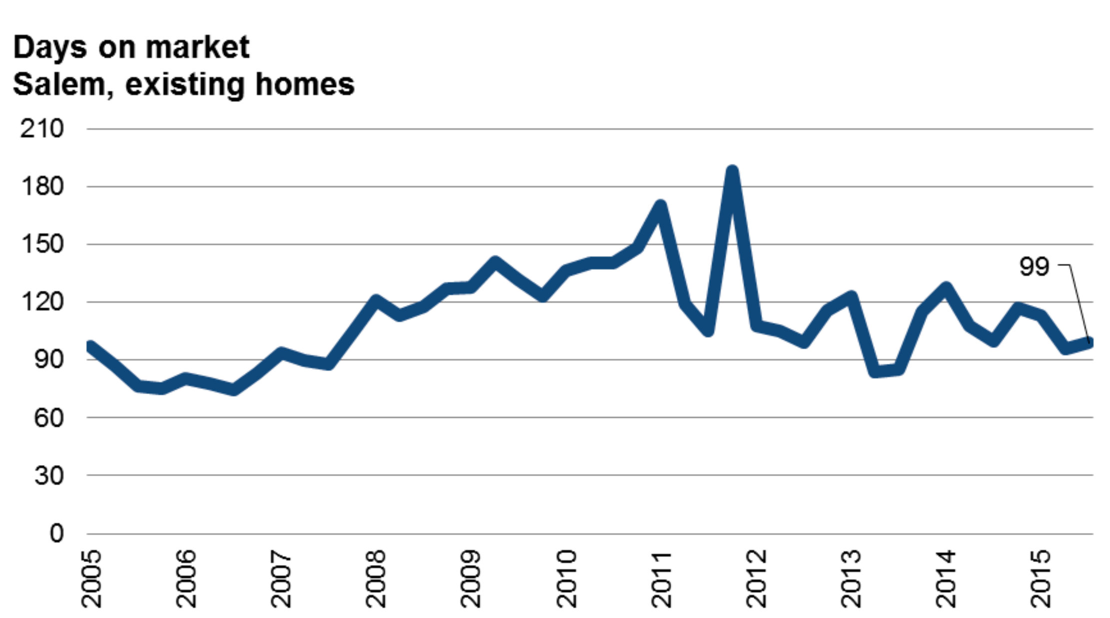
^Excluding Eugene *Excluding Salem

SALEM TRANSACTIONS

Transaction volume in Salem increased from the second quarter by three percent or 25 transactions to reach 794 sales. This is also a 32 percent increase of 194 sales versus the third quarter of 2014. The median price did not change from the second quarter, remaining at exactly $199,900. This is seven percent or $13,400 more than the prior-year period. Units averaged 99 days on the market, three days or three percent slower than the second quarter, but one day or one percent faster than the third quarter of 2014.


Number of transactions
Salem, existing homes
900
800
700
600
500
400
300
200
100
0
794
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015

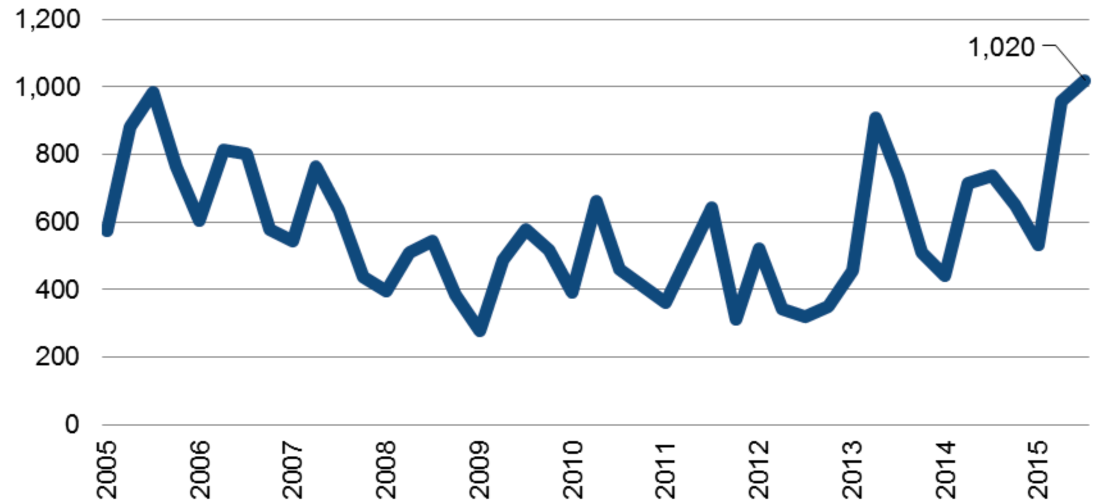

Median sales price
Salem, existing homes
$250,000
$200,000
$150,000
$100,000
$199,900
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015



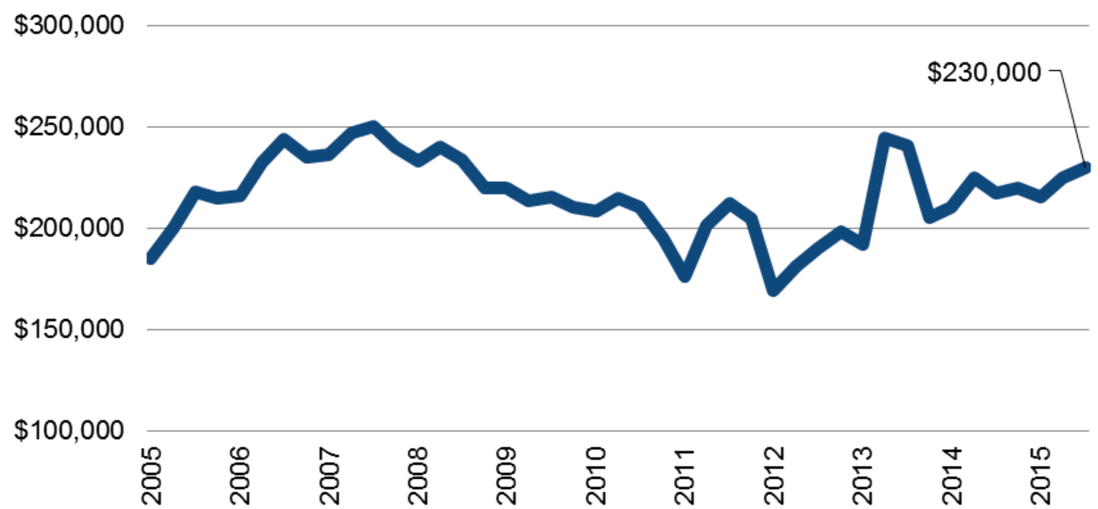
EUGENE–SPRINGFIELD TRANSACTIONS

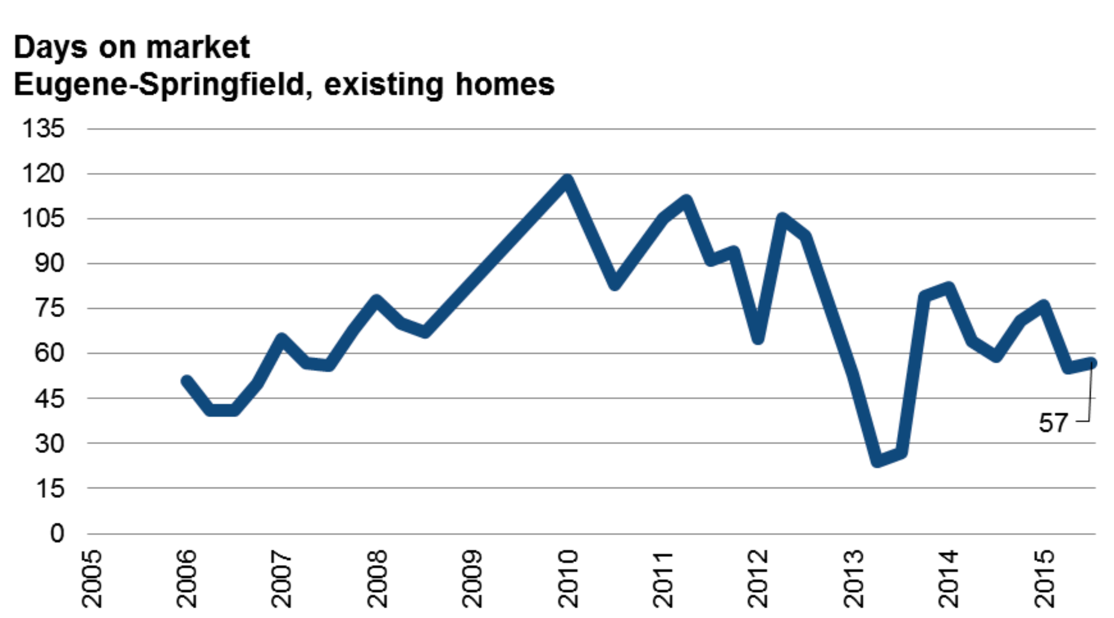
As with most markets surveyed for the third quarter, Eugene-Springfield posted modest gains. 1,020 existing single-family units sold in the third quarter, six percent more than transacted in the second quarter and 38 percent more than third quarter 2014. The median price increased by two percent to $230,000, six percent better than the third quarter of 2014. These sales averaged 57 days on the market, four percent slower than second quarter 2015 but three percent faster than the third quarter of 2014.

Number of transactions
Eugene-Springfield, existing homes



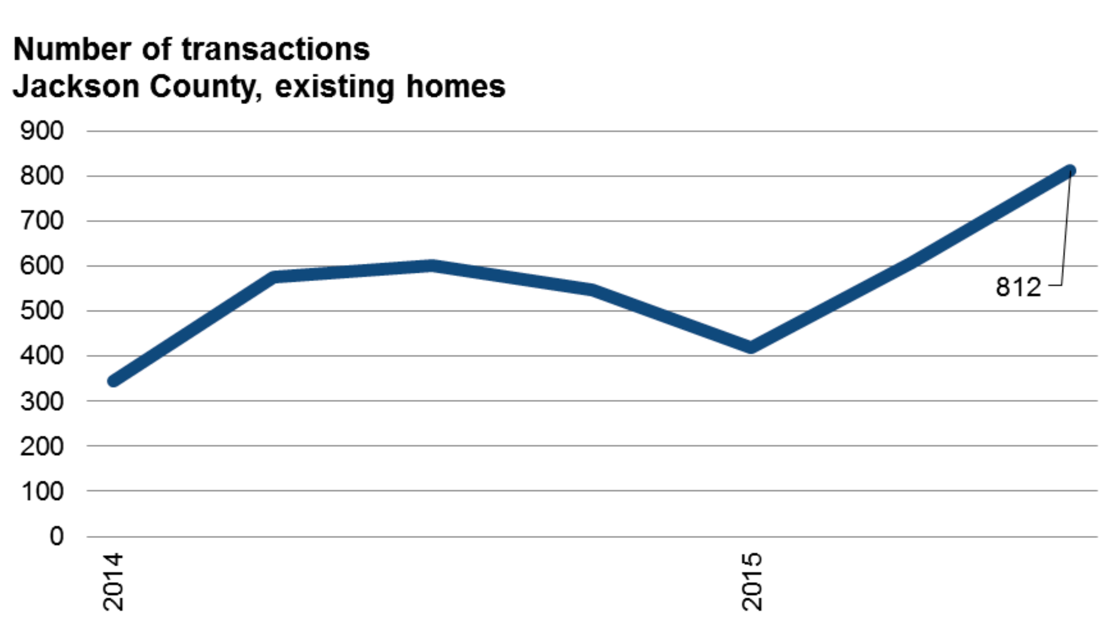
Median sales price
Eugene-Springfield, existing homes

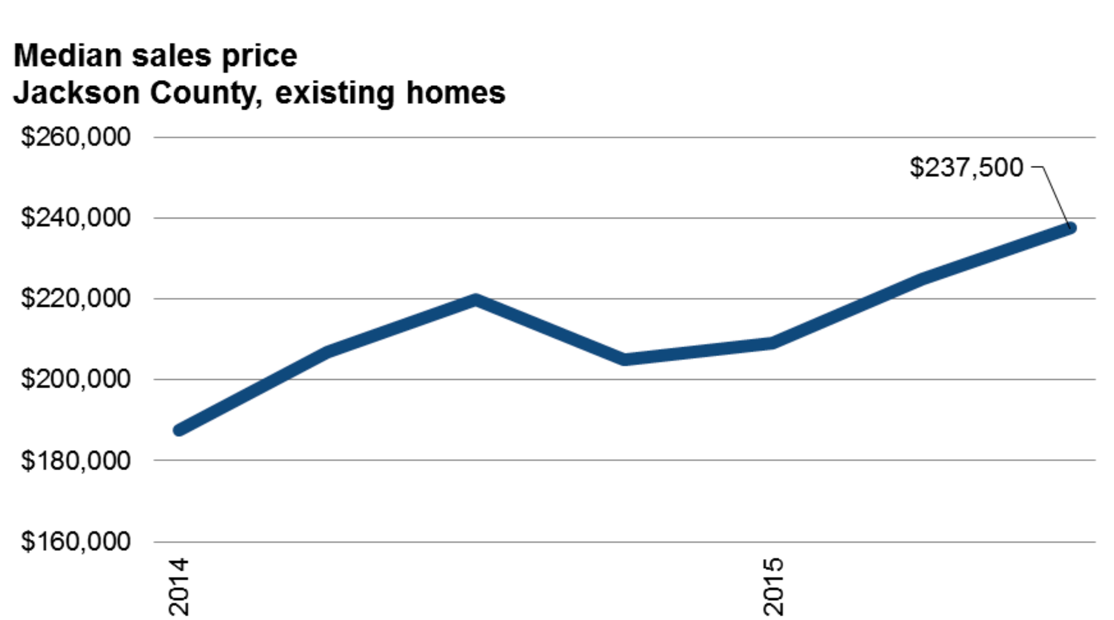


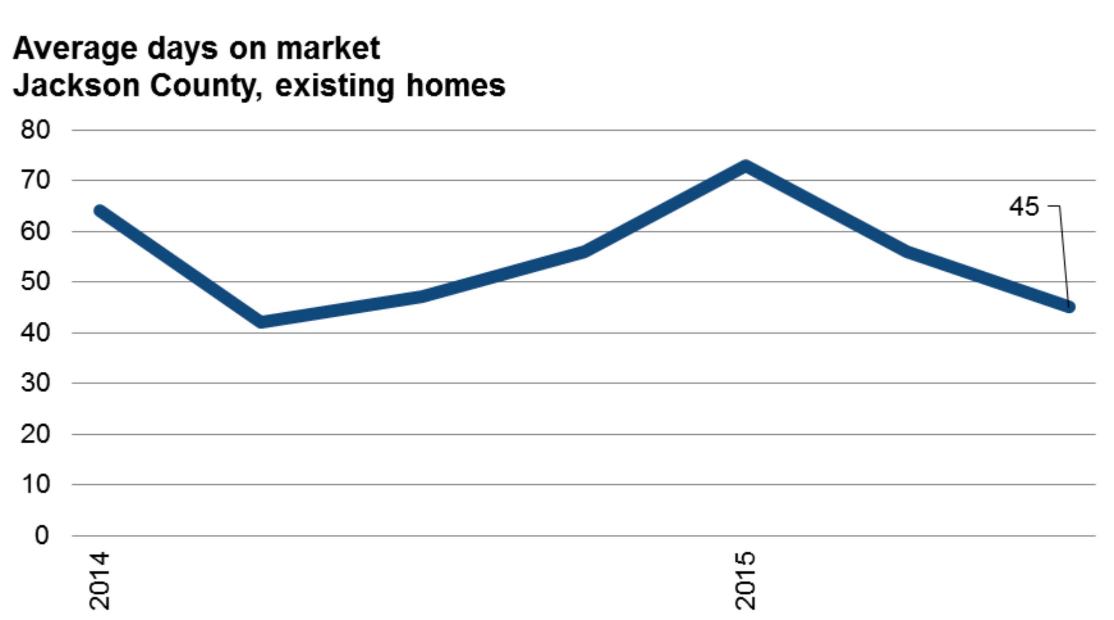

Days on market
Eugene-Springfield, existing homes
135
120
105
90
75
60
45
30
15
0
57
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015

SOUTHERN OREGON TRANSACTIONS

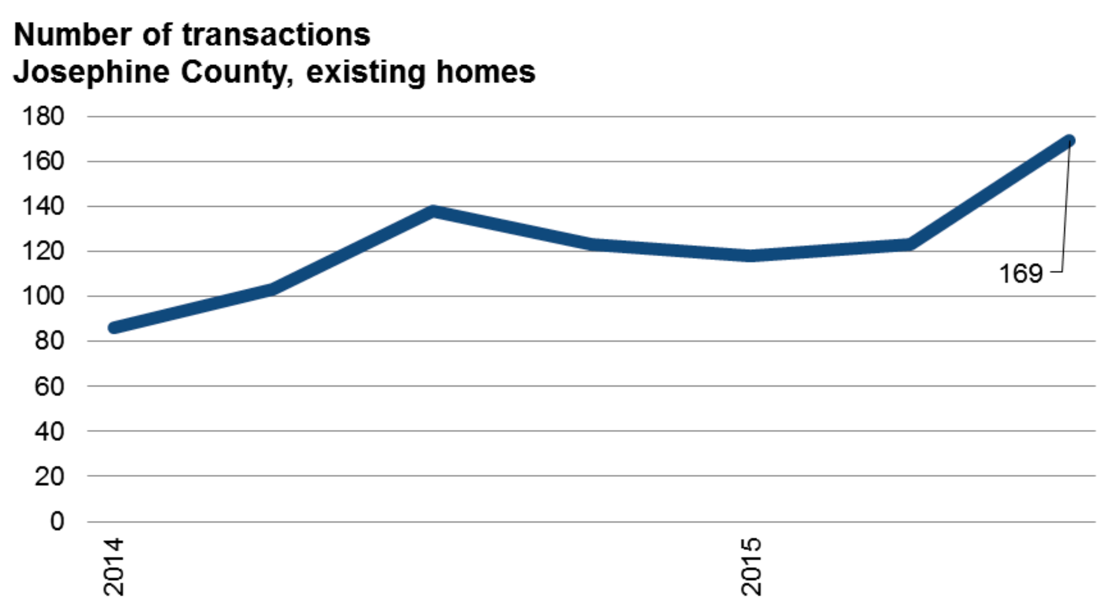
Data for southern Oregon is provided in rolling three-month groupings, and the most recent dataset available for this region covers the May 1, 2015 – July 31, 2015 time period. The following figures display the data for Jackson County.

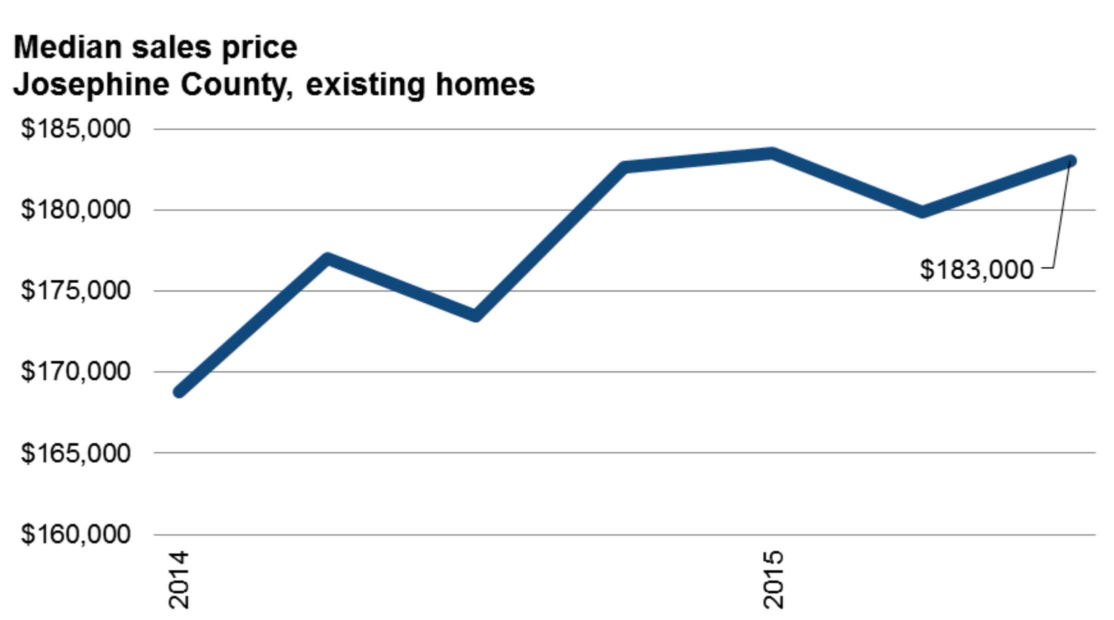


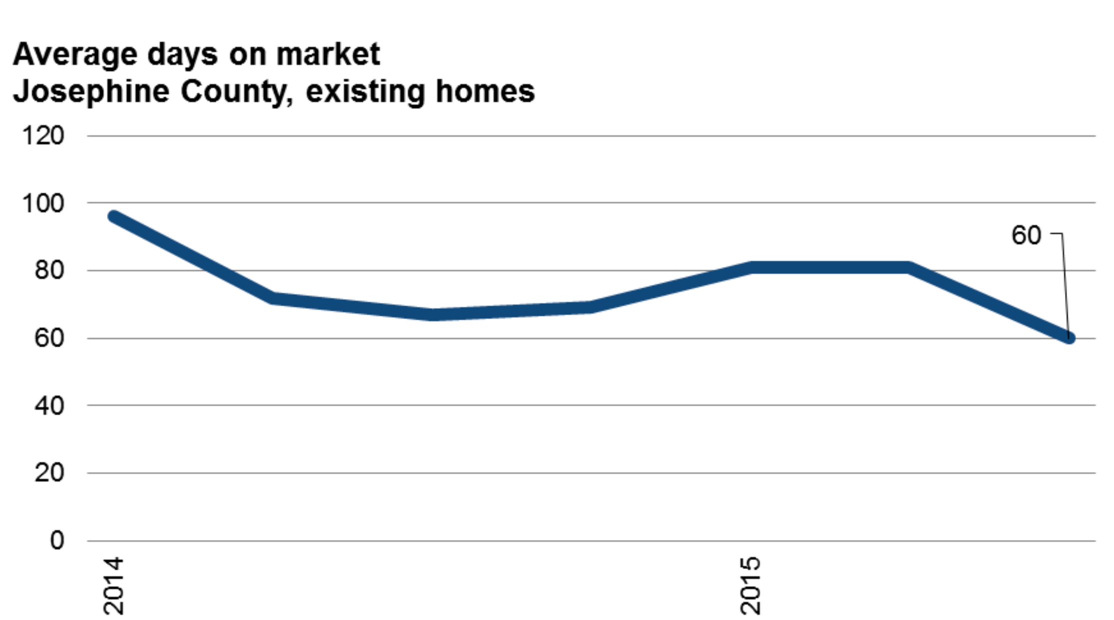




The following figures display the data for Josephine County.




Median sales price
Josephine County, existing homes
$185,000
$180,000
$175,000
$170,000
$165,000
$160,000
$183,000
2014
2015


Average days on market
Josephine County, existing homes
120
100
80
60
40
20
0
60
2014
2015

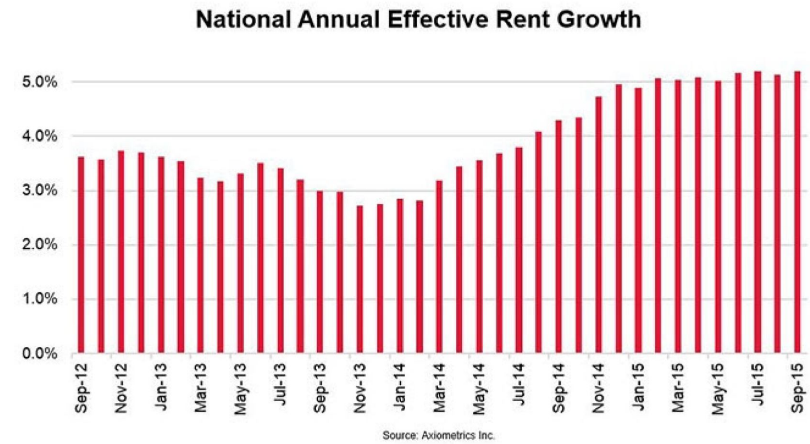
MULTIFAMILY MARKET ANALYSIS

Clancy Terry

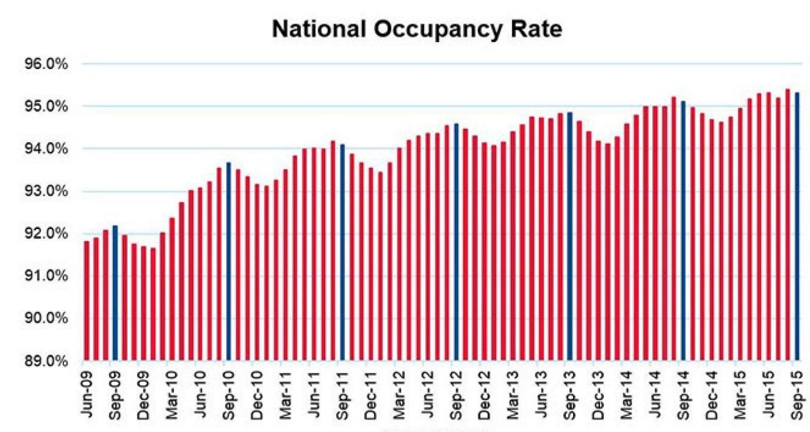
RMLS Student Fellow
Master of Real Estate Development Candidate

At the national level, annual effective rent growth has once again strengthened. The national rate of rent growth was 5.2 percent in September, greater than both the 5.1 percent achieved in August and the 4.3 percent observed in September 2014. The rate has now been at or above 5.0 percent for eight consecutive months according to Axiometrics, from whom this data is derived. At 5.8 percent, year-to-date effective rent growth in September is at its highest level during the entire post-recession period. Meanwhile, national vacancy registered at 4.7 percent in September 2015, the third strongest month of the year by this measure.

■ 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.


National Annual Effective Rent Growth
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
Sep-12
Nov-12
Jan-13
Mar-13
May-13
Jul-13
Sep-13
Nov-13
Jan-14
Mar-14
May-14
Jul-14
Sep-14
Nov-14
Jan-15
Mar-15
May-15
Jul-15
Sep-15
Source: Axiometrics Inc.

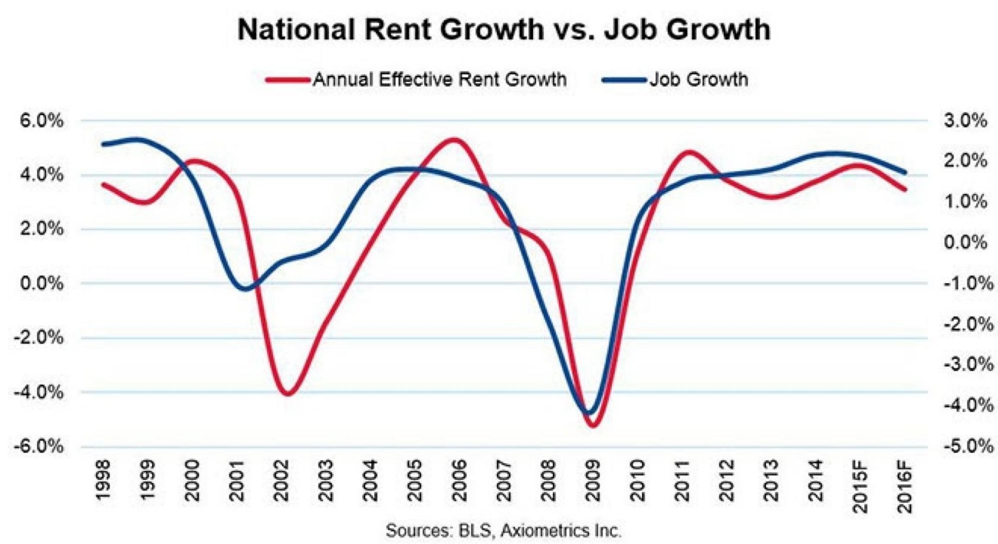

National Year-to-Date Effective Rent Growth
2010
2011
2012
2013
2014
2015
7.0%
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
Jan
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec
Source: Axiometrics Inc.


National Occupancy Rate
96.0%
95.0%
94.0%
93.0%
92.0%
91.0%
90.0%
89.0%
Jun-09
Sep-09
Dec-09
Mar-10
Jun-10
Sep-10
Dec-10
Mar-11
Jun-11
Sep-11
Dec-11
Mar-12
Jun-12
Sep-12
Dec-12
Mar-13
Jun-13
Sep-13
Dec-13
Mar-14
Jun-14
Sep-14
Dec-14
Mar-15
Jun-15
Sep-15
Source: Axiometrics Inc.

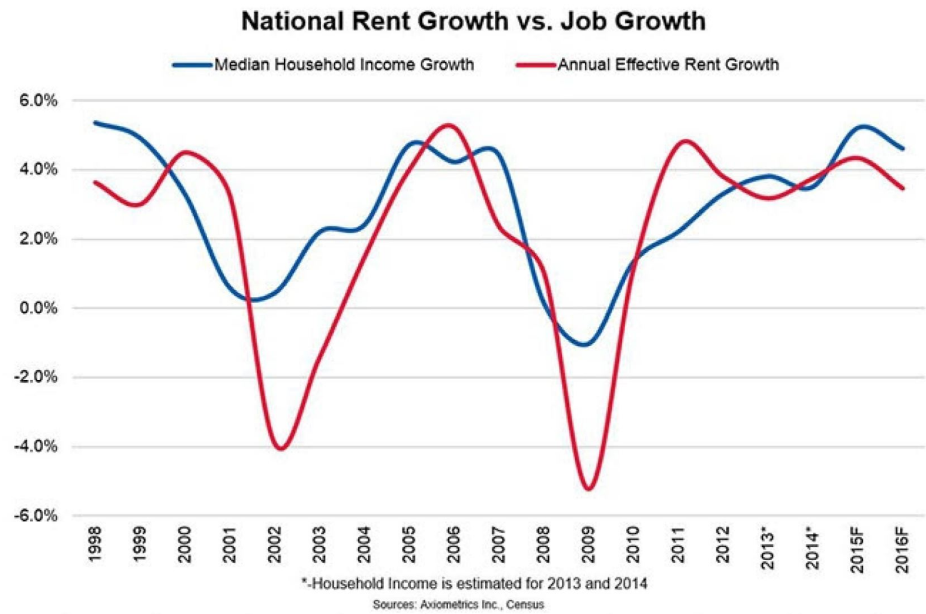
Axiometrics finds the "surge" in multifamily permitting in the second quarter drove a higher-than-expected level of housing starts in September. Multifamily starts totaled 454,000 units on a seasonally adjusted annual rate (SAAR) basis, 28.6 percent more than September 2014. A SAAR of 369,000 multifamily units were permitted in September, 14.6 percent less than August 2015 and 1.3 percent less than September 2014. Multifamily completions totaled 378,000 units, a 20.4 percent year-over-year increase.

AFFORDABILITY

In a special feature, Axiometrics has reviewed apartment affordability nationally and in Portland. With annual effective rent growth making continual headlines, a question on many minds pertains to the sustainability of such rental rate increases vis-à-vis renters' incomes. That is, will renters continue to be able to afford increasing apartment rents? To begin to answer the question, Axiometrics explains that job growth is a fundamental driver of effective rent growth. As job growth has occurred in 2014 and 2015 across the country, relative effective rent growth has also taken place:



Nevertheless, there is a distinction between job growth, wage growth, and total dollars flowing into households. During the 10 years prior to the Great Recession, growth in median household income averaged 3.0 percent while average annual effective rent growth was 2.1 percent; incomes were outpacing rents. After the Recession, however, household income growth has occurred at 2.8 percent while annual effective rent growth has averaged 3.3 percent. Axiometrics forecasts both rates of growth may lessen through 2016, as displayed in the following figure:



From another perspective, housing is generally considered "affordable" provided households are spending no more than 30 percent of incomes on housing payments. In 1998, national rent affordability was 27.2 percent, and has never surpassed 30 percent since then. In Portland, rent growth after the Recession, from 2011 to 2014, has averaged 5.8 percent, while household income growth has averaged 2.4 percent during the same period. Even so, the ratio of rent to median household income in Portland has remained below 24 percent since at least 1998. Thus, against the standard 30 percent gauge, rents in Portland are not at risk of becoming unaffordable over the next few years:

This is an aggregate perspective on the whole of Portland's housing economy, of course, and therefore does not reveal differing experiences in this housing market. NAI Norris, Beggs & Simpson's (NAI-NBS) third-quarter multifamily report to clients points to the market's arrival as acceptable to institutional investment and recent multifamily development trends as some of the factors contributing to valid concerns over housing affordability. NAI-NBS reports that market fundamentals such as vacancy rate and rent levels and growth have driven up both property values and institutional acquisitions. These conditions have also given rise to new developments that have mostly targeted the highest end of the Class A market, effectively "pricing out" many middle- and working-class renters. The firm also points to research indicating severely cost-burdened renters paying more than 50 percent of household income on housing payments could increase nationally by 25 percent over the next decade, as the above trends are not exclusive of Portland. As a final example of this ongoing trend, the firm reports average monthly rent for a two-bedroom, one-bathroom apartment in Portland reached $1,183 in the third quarter, a 15.3 percent year-over-year increase from the $1,026 seen in third quarter 2014.

PORTLAND APARTMENT MARKET

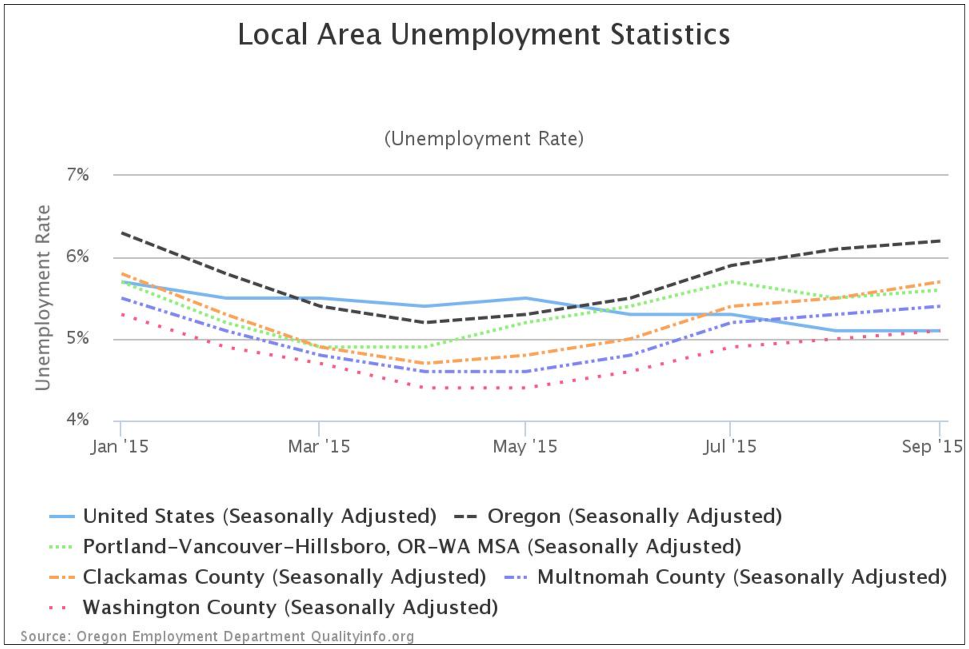
The multifamily market in the Portland-Vancouver-Hillsboro Metropolitan Statistical Area (MSA) continued to reach new milesones in the third quarter.

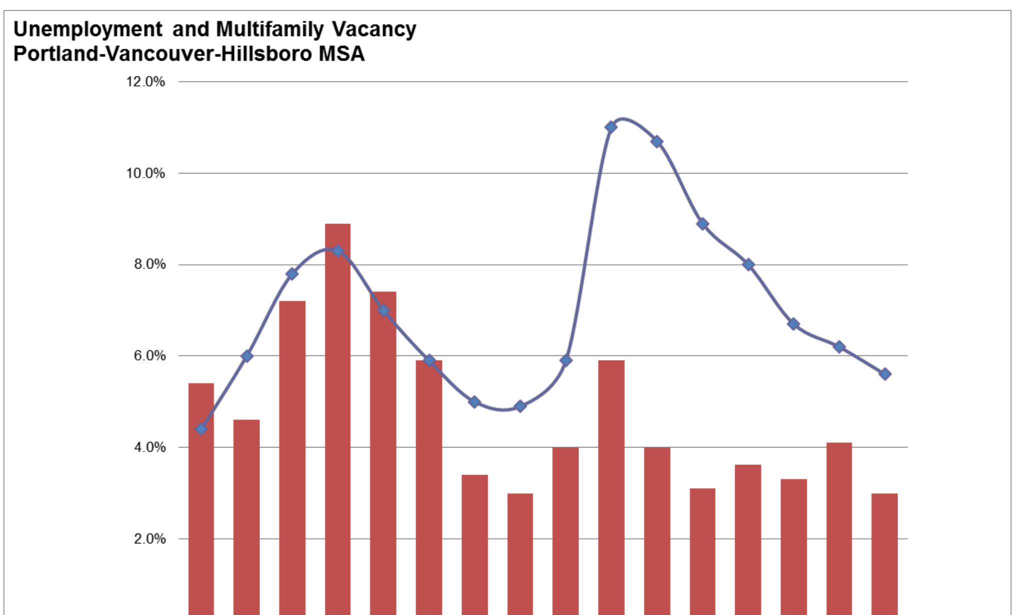
In September 2015, Axiometrics measured the Portland-Vancouver-Hillsboro MSA's annual effective rent growth at 14.31 percent. This puts Portland in first place among the 50 metros studied by the research firm. Runners up were Oakland, CA (13.03 percent), San Franciscio, CA (11.30 percent), Sacramentro, CA (9.95 percent), and San Jose, CA (9.33 percent).

Examining the third quarter as a whole, Axiometrics again ranks the Portland MSA in first place for annualized effective rent growth at a rate of 14.8 percent, ahead of Oakland in second place at 13.7 percent. From another perspective, Portland ranks in second place nationally for quarterly effective rent growth at 5.3 percent, behind San Franciscio-Redwood City-South San Fransisco MSA at 5.6 percent. Axiometrics pegs multifamly occupancy for Portland at 96.5 percent (a 3.5 percent vacancy rate). NAI-NBS measured the vacancy rate at 2.45 percent. We will report 3 percent here as the vacancy rate for the third quarter.

Colliers International reports that rising multifamily property values are supporting increased mortgage debt loads in the sector. The firm's Portland office reveals that total year-to-date sales volume reached approximately $1.7 billion at the close of the third quarter, already surpassing 2014's full-year total of $1.5 billion. Third-quarter multifamily transactions totaled $686 million. Also, absolute average rents grew from $1,023 in the first quarter of 2012 to $1,366 in the second quarter of 2015. And, $85 million in multifamily sales were recorded in the third quarter along the newly opened TriMet Max Orange Line light rail alignment.

The following charts display local unemployment trends and overlays of multifamily vacancy reported for the second quarter (3.0 percent) and the most recent unemployment statistic for September 2015 in the Portland MSA from the State of Oregon Employment Department (5.6 percent).

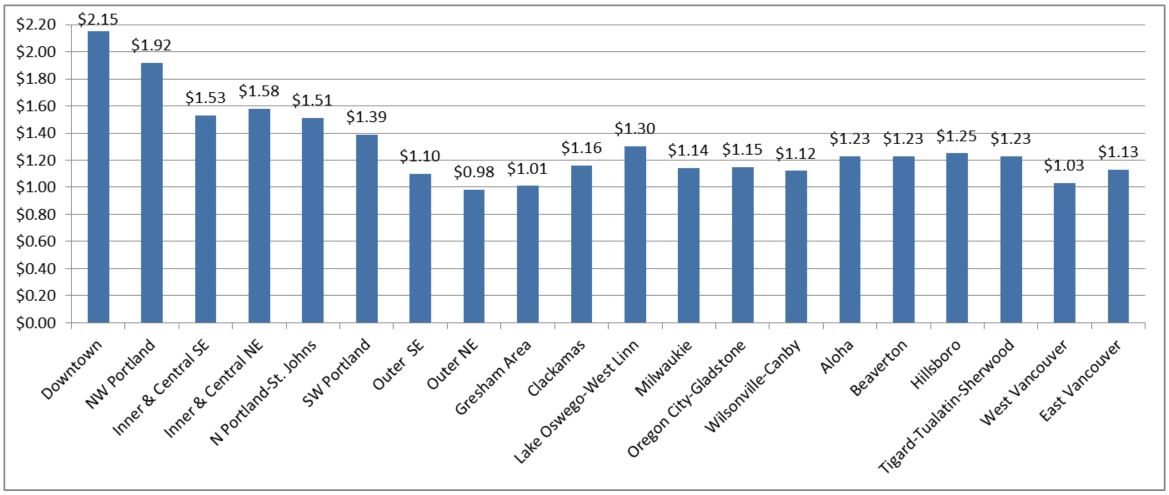




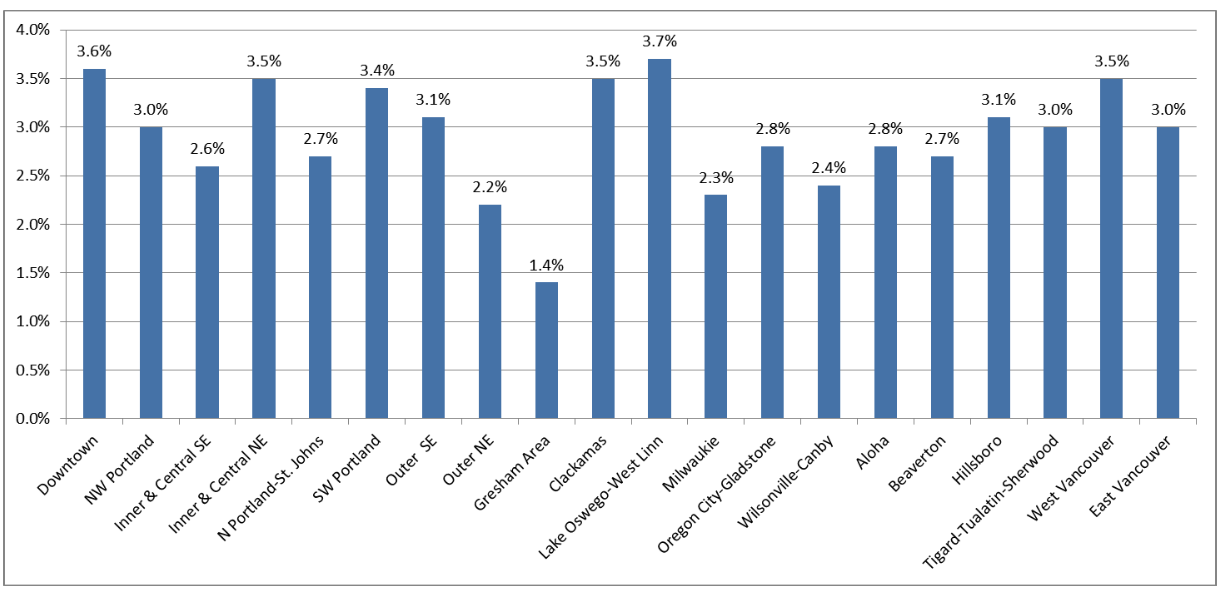
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Vacancy	5.4%	4.6%	7.2%	8.9%	7.4%	5.9%	3.4%	3.0%	4.0%	5.9%	4.0%	3.1%	3.6%	3.3%	4.1%	3.0%
Unemployment	4.4%	6.0%	7.8%	8.3%	7.0%	5.9%	5.0%	4.9%	5.9%	11.0%	10.7%	8.9%	8.0%	6.7%	6.2%	5.6%

Below are representations of Multifamily NW's average rents per square foot and average vacancy rates for the 20 Portland submarkets in its most recently published survey.

Rent/SF by Submarket, Fall 2015



Vacancy Rate by Submarket, Fall 2015



TRANSACTIONS

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

In July, 20 properties traded compared to 14 in July 2014. Dollar volume totaled $221,447,600, 254.4 percent greater than July 2014. Averages for these 20 transactions are as follows: 74.1 units, $11,072,380 price, $149,526/unit, 879.3 square feet/unit, $175.31/square foot, 6.81 percent average reported cap rate.

In August, 17 properties traded compared to 20 in August 2014. Dollar volume totaled $168,423,880, 55.0 percent less than August 2014. Averages for these 17 transactions are as follows: 56.1 units, $9,907,287 price, $176,545/unit, 972.4 square feet/unit, $195.78/square foot, 5.36 percent average reported cap rate.

In September, 30 properties traded compared to 14 in September 2014. Dollar volume totaled $261,222,822, 344.3 percent greater than September 2014. Averages for the 30 transactions are as follows: 62.6 units, $8,707,427 price, $139,022/unit, 918.7 square feet/unit, $150.73/square foot, 5.42 percent average reported cap rate.

Year to date through September 2015, total dollar volume of sales over $450,000 reached $1,681,959,925 on 212 transactions. The averages for these 212 transactions are: 55.1 units, $7,933,773 price, $125,428/unit, 900.9 square feet/unit, $146.82/square foot, 5.83 percent average reported cap rate.

Colliers International Portland reports the following significant Q3 trades:

Project	City	Sale Date	Sale Price	# Units	Price/Unit	Price/SF	Cap Rate
Terrene at the Grove	Wilsonville	8/31/2015	$59,500,000	288	$ 206,597	$ 205.86	5.00
Miramonte Lodge	Portland	7/21/2015	$55,835,462	231	$ 241,711	$ 340.16	5.00
The Cordelia	Portland	7/13/2015	$47,750,000	135	$ 353,704	$ 442.13	4.07
Madison Bridge Creek	Wilsonville	9/24/2015	$47,611,226	315	$ 151,146	$ 169.54	4.85
Madison Boulder Creek	Wilsonville	9/24/2015	$44,739,438	296	$ 139,320	$ 169.23	4.85
Burnside 26	Portland	8/4/2015	$41,500,000	135	$ 307,407	$ 436.84	4.25
Columbia Trails Apartments	Gresham	7/27/2015	$38,400,000	264	$ 145,455	$ 150.38	5.25
The Bluffs	Milwaukie	7/21/2015	$33,114,538	137	$ 241,711	$ 328.40	5.00
Arnada Pointe Apartment Homes	Vancouver	8/11/2015	$28,100,000	200	$ 140,500	$ 146.23	5.50
Alden Apartments	Tualatin	7/16/2015	$28,000,000	210	$ 133,333	$ 171.97	5.70
Prestige Plaza	Vancouver	9/1/2015	$23,300,000	96	$ 242,708	$ 180.40	5.79
Woodspring Apartments	Tigard	7/20/2015	$22,000,000	172	$ 127,907	$ 122.23	5.60
The Addison Apartments	Vancouver	8/13/2015	$21,750,000	147	$ 147,959	$ 131.52	5.60

ABR Winkler Real Estate Services reports the following perspective on multifamily sales through the year-to-date period ended September 2015:

Median price per square foot	$129
Median cap rate	5.60%
Dollar volume of sales	$1,619,232,138
Median gross rent multiplier	9.92
Median price per unit	$107,900
Average price	$9,414,140
Average number of units	55

PERMITS

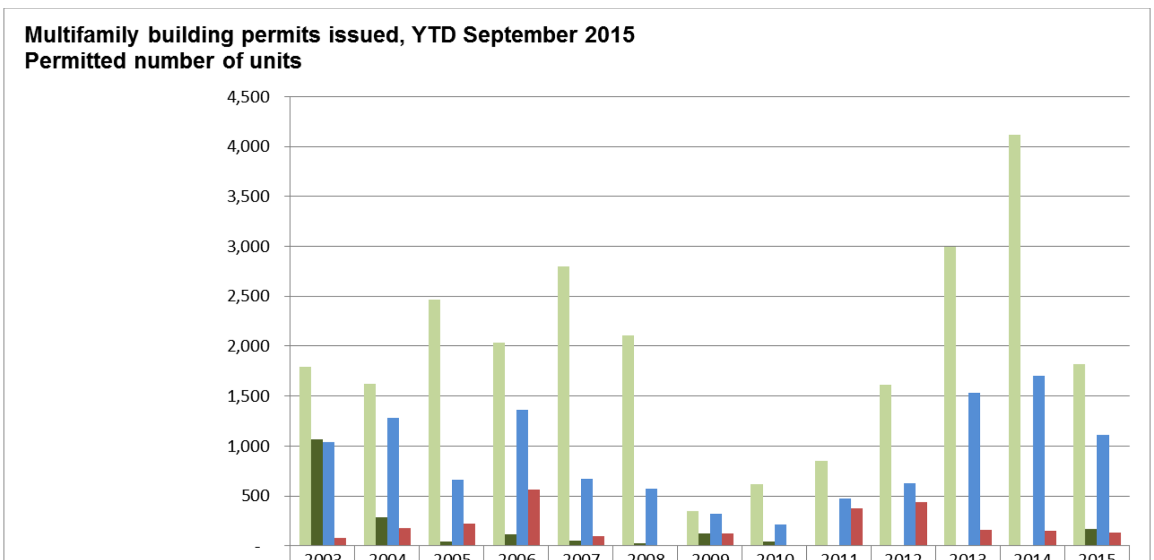
The following information pertains to building permit issuances in the third quarter of 2015 for projects with five or more private housing units.

Portland reclaimed its customary lead in permitting volume, followed in second place by Washington County (which was reported last quarter to have permitted more multifamily units than the City of Portland during that period).

Also, last quarter we reported that for the first time in 2015, multifamily units were permitted in Multnomah County outside of Portland. Additional research indicates that these 17 units were permitted in a single project in the City of Gresham. Significantly more remarkable is the news out of Gresham for the third quarter: a single project was permitted in Gresham in July 2015 containing 155 units. No additional multifamily permits were issued outside of Portland in August or September. This volume of permitting has not been seen in eastern Multnomah County since 2009, and indicates the rapidly rising rents and near-zero vacancy in Portland's suburban submarkets reported last quarter may be driving multifamily development feasibility in these areas.

Third-quarter and year-to-date permit totals for the four areas surveyed are:

Area	Q3 Total
City of Portland	992
Multnomah County Excluding Portland	155
Washington County	238
Clackamas County	60



	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
City of Portland	1,793	1,623	2,466	2,038	2,802	2,103	345	622	852	1,612	2,992	4,120	1,821
Multnomah County (excl PDX)	1,062	288	46	119	56	24	125	47	0	0	12	0	172
Washington County	1,040	1,279	664	1,364	674	572	319	212	473	630	1,537	1,703	1,108
Clackamas County	81	181	226	564	100	0	128	5	371	435	159	151	131

Source: U.S. Census Bureau

NEW CONSTRUCTION

The following totals and samples are courtesy of the Fall 2015 Barry Apartment Construction Report.

Total Units Proposed and Under Construction

	Proposed	Under Construction	Total
North Portland	1,623	912	2,535
Close in East Portland	4,989	1,472	6,461
Close in West Portland	4,674	3,680	8,354
Suburban West	4,146	1,272	5,418
Suburban East	1,190	141	1,331
Suburban South	1,556	180	1,736
Clark County	2,550	1,347	3,897
Total	**20,728**	**9,004**	**29,732**

Total Projects Proposed and Under Construction

	Proposed	Under Construction	Total
North Portland	38	13	51
Close in East Portland	79	30	109
Close in West Portland	47	26	73
Suburban West	23	8	31
Suburban East	25	4	29
Suburban South	10	1	11
Clark County	22	10	32
Total	**244**	**92**	**336**

Sampling of New Construction Completions

North Portland					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
Marvel 29	7227 N Philadelphia Ave	Portland	165	2015	St, 1br, 2br. UG parking, 4 story, grnd floor retail
Wilmore	4357 N Williams Ave	Portland	75	2015	Ground floor retail space, on-site parking
Northwood Apts	8310 N Interstate	Portland	57	2015	4-story, on-site parking, ground floor retail
Monroe Apartments	3035 NE MLK Blvd	Portland	46	2015	In lease up

Close-In Eastside Portland					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
Hassalo on 8th (Lloyd Blocks)	700 NE Multnomah St	Portland	657	2015+	1,200 underground parking spaces, 4 large towers
The Union	304 NE Multnomah	Portland	186	2015+	6-story, ground floor retail, below grade parking
Burnside 26	2625 E Burnside	Portland	135	2014+	4 story, ground floor retail, underground parking
SE Alder Apartments	700 SE Cesar Chaves Blvd	Portland	99	2015	3 story, on-site parking
NE Tillamook Apartments	3910 NE Tillamook St	Portland	75	2015	5 story, underground parking

Close-In Westside Portland					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
Waterline Apartments	2130 NW Front Ave	Portland	244	2015	4 buildings, on-site parking below grade
LL Hawkins Apts	1515 NW 21st Avenue	Portland	113	2015	6-story, mixed use ground floor, on-site parking
Treehouse Apts	3440 SW US Veterans Hosp Rd	Portland	69	2015	7 story, 1/3 of an acre site. On-site parking
The Janey II	1135 NW Everett Street	Portland	62	2015	9-story, ground floor retail, rooftop deck, parking

Suburban West					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
Platform District - Orenco	NW 231st Ave & NE Alder St	Hillsboro	579	2015	Three - 6 story buildings. On max line.
Merlo Village	SW 170th Ave at Baseline Rd	Beaverton	312	2015	3 story flats, large site
West Parc Apartments	15640 NW Laidlaw Rd	Portland	131	2015	4 buildings, 3-5 stories, on-site parking
Springville Oaks	16320 NW Canton Street	Portland	112	2015	Seven buildings

Suburban East					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
Glendoveer Woods	333 NE 146th Ave	Portland	112	2015	Some affordable housing
The Rose Apartments	318 NE 97th Ave	Portland	90	2015	2 - 4-story bldgs, 58 parking spots, workforce housing
Glisan Commons (Phase II)	601 NE 99th Ave	Portland	60	2015	6-story, senior housing, on-site parking
Glisan Commons	9999 NE Glisan St	Portland	127	2014	Some subsidized housing, 1st floor retail space

Suburban South					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
Active Adults at the Grove	8750 SW Ash Meadows Rd	Wilsonville	112	2014+	4 story, 55+ community. 3.41 Acre site
Eddyline at Bridgeport	18055 SW Lower Boones Ferry Rd	Tualatin	367	2014	Completed in phases
Bell Tower @ Old Town Square	30480 SW Boones Ferry Rd	Wilsonville	52	2013	2, 3 & 4 story building - Luxury apts, studio, 1br & 2br
Villebois	28900 SW Villebois Dr	Wilsonville	178	2013	Completed in phases

Clark County					
Name	**Address**	**City**	**Units**	**Complete**	**Notes**
VHA Apartments	16703 SE 1st Ave	Vancouver	152	2015	Low-income
Prestige Plaza	307 E Mill St	Vancouver	96	2014	3-story, studios, 1br, 2br
The Reserve	600 SE Mill Plain Blvd	E. Vancouver	418	2013	Completed in phases
NorthGlen Villas	7101 NE 109th St	NE Vancouver	200	2013	Phased - gas FP, W/D, fitness center, jacuzzi, spa

OFFICE MARKET ANALYSIS

ALEC LAWRENCE

Portland State University

The Portland Metro economy continues to perform strongly, with 3.2 percent job growth over the last 12 months spread over a diverse group of industries. The State of Oregon's Office of Economic Analysis (OEA) has also revised its initial winter estimates with more optimistic projections. Despite a small uptick in unemployment from 5.4 percent in June to 5.7 percent in July due to an influx of "people entering the labor market or who are leaving their jobs voluntarily," unemployment closely trailed the national rate of 5.3 percent in July and sits well below the July 2014 Portland Metro rate of 7.0 percent. Nick Beleiciks, Oregon's state employment economist, notes, "Oregon's economy is adding jobs so fast right now that many of [the recently unemployed] will find work quickly."

The third quarter brokerage reports focused on the strength of the market for landlords and developers:

- **Colliers** highlighted the expanding prospects for a Bioscience District anchored by OHSU in the South Waterfront and OMSI in the Central Eastside and connected by the now open Trimet Orange Line and Tilikum Crossing. OHSU's has proposed one million square feet in construction in addition to its Knight Cancer Institute, which should stimulate additional development.

- **Kidder Mathews** focused on the continued strength of creative office in the Portland Metro with decreasing vacancy, slightly increasing rents, none to minimal free rent offered, and four development proposals during the quarter for creative office.

■ **Alec Lawrence** 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.

- **CBRE** led its report with an analysis of increasing tenant improvement (TI) dollars in the Downtown submarket. CBRE finds three factors at play: 1) while there are a large number of deliveries on the horizon, large tenants in need of space now are looking to Portland's older inventory, and that inventory is often in need of upgrading; 2) new institutional landlords are locked in to meeting high rent requirements but have capital for TIs; and 3) in the race for creative office cachet, tenants are accepting high rents for the right TI and building. CBRE's conclusion: despite higher TIs, tenants are accepting longer terms and higher rates with "landlords squarely in the driver's seat."

- **JLL** leads with an overview of increased development activity. Noting that "developers shift into high gear," with total 2015 deliveries projected to be 532,980 square feet and 1.2 million square feet forecasted for 2016. According to JLL, 50 percent of that development pipeline is already preleased.

VACANCY

CBRE found vacancy to be at its lowest rate since the fourth quarter 2007 but calls for vacancy rates to increase to historic average rates as new construction and redevelopment projects deliver. CBRE's data show Suburban vacancy rates at their lowest rate in Portland's recorded history at 12.8 percent.

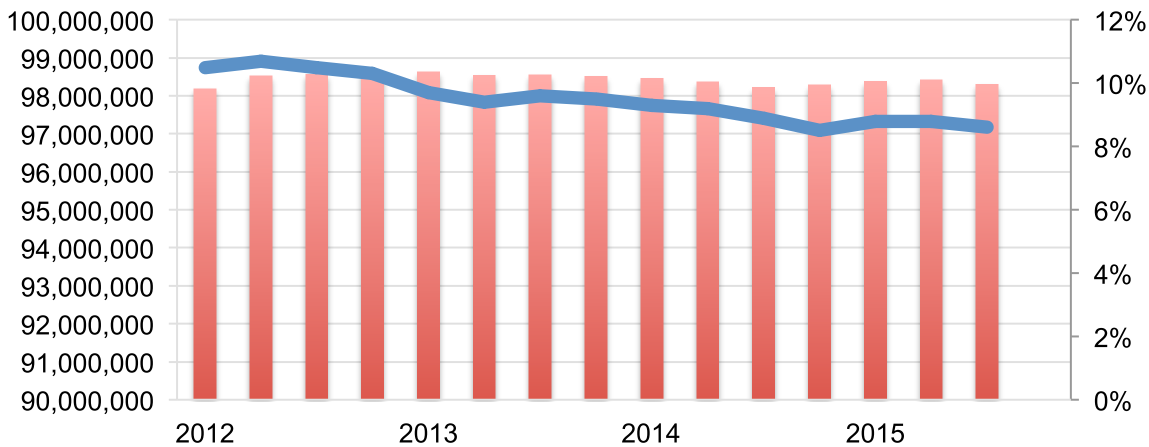
Kidder Mathews mirrored the sentiment, noting the continued "steady pattern of decline" in vacancy, with their data indicating that total Portland Metro office vacancy decreased slightly to 8.6 percent from 8.8 percent during the third quarter 2015. In terms of direct vacancy, the 8.6 percent vacancy rate in the third quarter marks a year-on-year decrease of 30 basis points from 8.9 percent in the third quarter 2014 and the fifth consecutive quarter of below 9.0 percent vacancy rates.

Table 1: Total Vacancy Rates by Brokerage, Class, and Quarter-to-Quarter Change, Third Quarter 2015

Brokerage	Total	CBD	CBD Class A	CBD Class B	CBD Class C	Q-to-Q Change
CBRE	11.0%	9.9%	--	--	--	Decrease
Colliers	9.8%	10.0%	10.0%	10.5%	8.8%	No Change
JLL	9.1%	7.7%	7.4%	7.9%	8.0%	--
Kidder Mathews	10.3%	--	--	--	--	Decrease
NAI	--	10.8%	10.2%	10.0%	13.5%	*Increase

*Change for Central City. Source: Brokerage Quarterly Reports

Figure 1: Portland Office Market Total RBA (square feet) and Direct Vacancy Rate (%), 2012-2015



Source: Kidder Mathews

JLL reported a Portland Metro third quarter 2015 direct vacancy rate of 8.7 percent. Two market areas outperformed the average direct Portland Metro rate: Portland Central City with an average direct vacancy rate of 6.9 percent and the Portland Eastside with an average direct vacancy rate of 8.1 percent. Seven individual submarkets out performed the average direct Portland Metro rate: Lloyd District (4.1 percent), Close In Eastside (4.6 percent), Vancouver Mall (5.1 percent), Sunset Corridor (5.5 percent), the CBD (7.2 percent), Kruse Way 7.2 percent), and Airport Way/Columbia Corridor (7.8 percent).

Table 2: Portland Vacancy Rate Ranked by Market area and Submarket, Third Quarter 2015

Market Area	Submarket	Vacancy
Ranked by Market (Portland Metro Shown for Comparison)		
Portland Central City	Total	6.9%
Portland Eastside Suburbs	Total	8.1%
Portland Metro	**Total**	**8.7%**
Portland Westside	Total	10.5%
Vancouver Suburbs	Total	10.6%
Ranked by Submarket (Portland Metro Shown for Comparison)		
Portland Central City	Lloyd District	4.1%
Portland Eastside Suburbs	Close In Eastside	4.6%
Vancouver Suburbs	Vancouver Mall	5.1%
Portland Westside	Sunset Corridor	5.5%
Portland Central City	Portland CBD	7.2%
Portland Westside	Kruse Way	7.2%
Portland Eastside Suburbs	Airport Way/Columbia Corridor	7.8%
Portland Metro	**Total**	**8.7%**
Portland Westside	SW Close In	9.4%
Vancouver Suburbs	Hazel Dell / Salmon Creek	9.8%
Vancouver Suburbs	CBD/West Vancouver	10.4%
Portland Eastside Suburbs	Clackamas / Milwaukie Totals	10.9%
Vancouver Suburbs	Cascade Park/Camas	11.0%
Portland Westside	Northwest	12.8%
Portland Eastside Suburbs	Outer Eastside	13.5%
Portland Westside	I-5 South Corridor	14.0%
Vancouver Suburbs	St. John's Central Vancouver	14.4%
Portland Westside	217 Corridor / Beaverton	14.7%
Vancouver Suburbs	Orchards/Outer Clark	15.5%

Source: JLL

RENTAL RATES

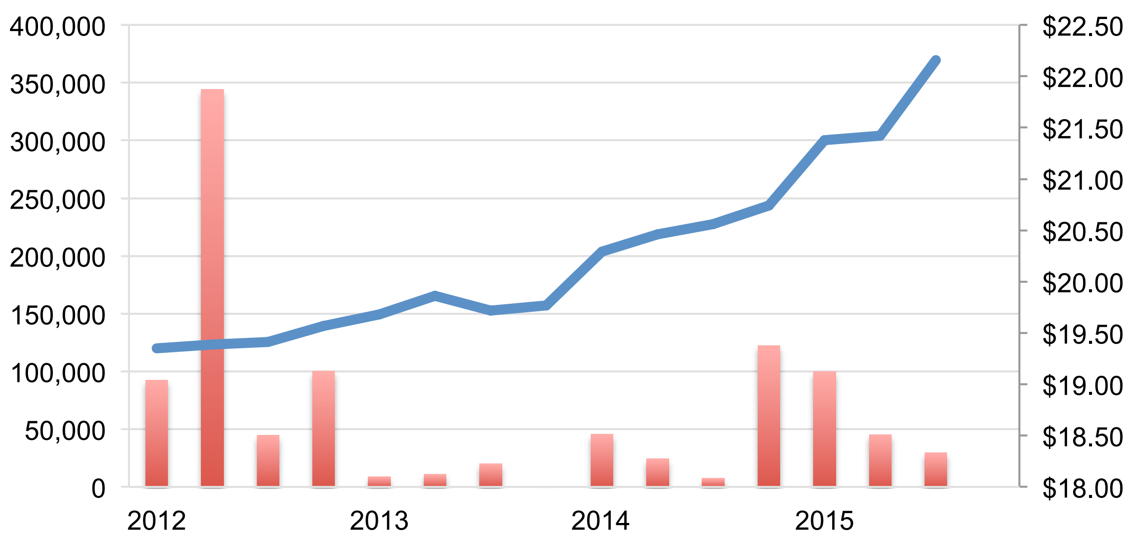
Table 3: Average Quoted Rates ($/SF FSG) by Brokerage, Class, and Quarter-to-Quarter Change, Third Quarter 2015

Brokerage	Average	CBD	Suburban	CBD Class A	CBD Class B	CBD Class C	Q-to-Q Change
CBRE	24.07	27.53	21.29	--	--	--	Increase
Colliers	22.73	27.62	--	29.91	27.42	21.51	Increase
JLL	24.08	28.95	--	31.22	28.38	24.57	Increase
Kidder Mathews	22.16	--	--	--	--	--	Increase
NAI	--	--	--	--	--	--	Increase

Source: Brokerage Quarterly Reports

Kidder Mathews indicates that the overall average quoted FSG rental rates rose to $22.16 for the third quarter. A 7.8 percent year-over-year increase from $20.56 in the third quarter of 2014. CBRE notes this is the 13th straight quarter that rental rates have increased and that rates are increasing at a faster pace than last year (6.7 percent year-over-year increase in 2015 versus a 3.7 percent increase in 2014).

Figure 2: Portland Office Market Average Asking Rents ($) and Deliveries (square feet), 2012-2015



Source: Kidder Mathews

JLL data show the overall Portland Metro average direct asking rent at $24.08. The Portland Central City market area is the only market area outperforming the Portland Metro with an average direct asking rent of $28.60. However, viewed by submarket, JLL data indicate that the Close-In Eastside submarket has the highest overall average direct asking rents at $29.72. Three other submarkets are outperforming the Portland Metro average: Portland CBD ($28.95), Kruse Way ($28.60), and the Lloyd District ($24.92).

Table 4: Portland Average Direct Asking Rent ($/p.s.f.) Ranked by Market Area and Submarket, Third Quarter 2015

Market Area	Submarket	Average Direct Asking Rent ($/p.s.f.)
Ranked by Market Area (Portland Metro shown for Reference)		
Portland Central City	Total	28.60
Portland Metro	**Total**	**24.08**
Portland Eastside Suburbs	Total	23.03
Portland Westside	Total	21.95
Vancouver Suburbs	Total	20.12
Ranked by Market Area (Portland Metro shown for Reference)		
Portland Eastside Suburbs	Close In Eastside	29.72
Portland Central City	Portland CBD	28.95
Portland Westside	Kruse Way	28.60
Portland Central City	Lloyd District	24.92
Portland Metro	**Portland Metro**	**24.08**
Portland Westside	Northwest	23.45
Portland Westside	Sunset Corridor	22.23
Portland Eastside Suburbs	Clackamas/Milwaukie	22.15
Portland Westside	217 Corridor/Beaverton	21.00
Vancouver Suburbs	Hazel Dell/Salmon Creek	20.98
Portland Westside	I-5 South Corridor	20.66
Vancouver Suburbs	Cascade Park/Camas	20.55
Vancouver Suburbs	CBD/West Vancouver	20.47
Vancouver Suburbs	St. John's Central Vancouver	19.87
Portland Eastside Suburbs	Airport Way/Columbia Corridor	19.29
Portland Eastside Suburbs	Outer Eastside	19.08
Portland Westside	SW Close In	18.29
Vancouver Suburbs	Orchards/Outer Clark	18.01
Vancouver Suburbs	Vancouver Mall	16.77

Source: JLL

ABSORPTION AND LEASING

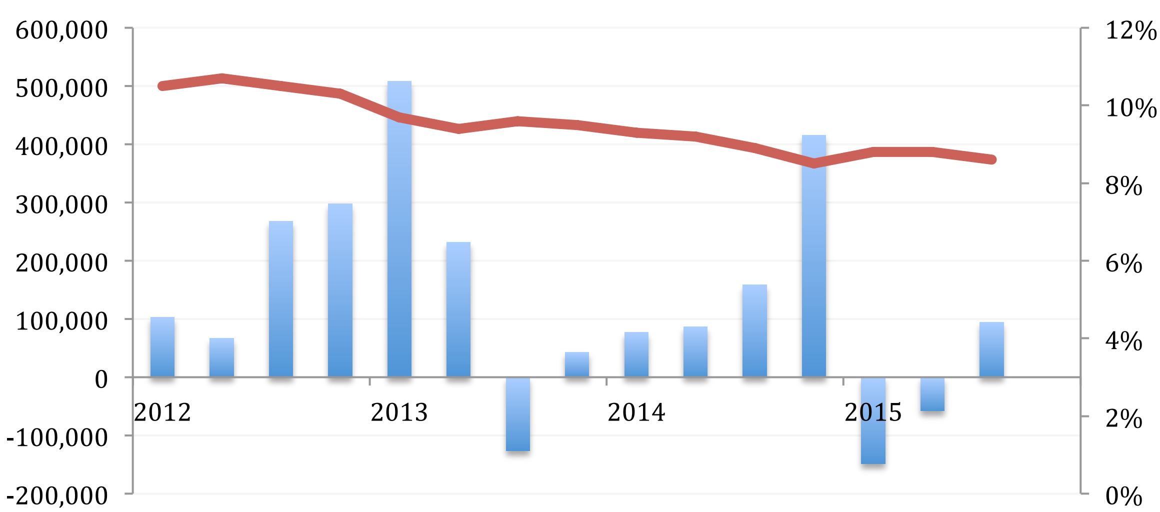
As related by Kidder Mathews, Portland experienced positive net absorption during the third quarter with a total of 94,221 square feet absorbed. Year-to-date absorption rates vary considerably by brokerage house with CBRE data indicating an overall 627,514 year-to-date absorption figure and Norris & Stevens data indicating an overall 1,177 year-to-date absorption figure. CBRE calls for Portland to surpass its 2014 total net absorption and points to potential demand for CBD space of over 500,000 square feet based on its knowledge of current tenants in the market. JLL suggests that weak third quarter absorption is not a product of a sluggish market, instead pointing to limited supply and upcoming deliveries on the horizon that are preventing large tenants from moving as they wait out additional deliveries.

Table 5: Net Absorption (square feet) by Brokerage and Area, Third Quarter 2015

Brokerage	Overall	CBD	Suburban
CBRE	206,796	(18,070)	159,534
Colliers	73,970	(96,602)	--
JLL	24,982	59,201	--
Kidder Mathews	94,221		
NAI	(147,329)	(187,526)	40,197

Source: Brokerage Quarterly Reports

Figure 3: Portland Office Market Net Absorption (square feet) and Vacancy (%), 2012–2015



Source: Kidder Mathews

Table 6: Portland Area Net Absorption Ranked by Submarket, Third Quarter 2015

Submarket	Net Absorption	As A Percent of Rentable Area
Total	**206,796**	**0.5%**
Suburban	159,534	0.7%
Downtown	47,262	0.2%
Beaverton	52,120	1.4%
Lloyd Center	47,891	2.4%
Vancouver	30,837	0.7%
Eastside	26,309	1.0%
Kruse Way	22,754	1.0%
West Hills	19,386	2.4%
WA Square	18,888	1.5%
Northwest	17,441	0.4%
Clackamas	15,644	1.3%
Lake Oswego	7,691	1.3%
Wilsonville	3,251	0.4%
Johns Landing	1,034	0.1%
Barbur Boulevard	-458	-0.1%
Tualatin	-4,643	-0.5%
Airport Way	-7,712	-1.4%
Hillsboro	-9,939	-0.9%
Tigard	-15,628	-0.8%
CBD	-18,070	-0.1%

Source: CBRE

Table 7: Notable Lease Transactions, Third Quarter 2015

Building/Address	Tenant	Market	Square Feet
AmberGlen Business Center	Nike	Sunset Corridor	105,505
CDK Plaza	CDK Global [renewal/expansion]	CBD	90,000
541 NE 20th Ave	Hanna Andersson	Lloyd/Central Eastside	51,335
Kruse Oaks III	Navex	Kruse Way	43,304
Kruse Woods V	Black & Veatch Corporation [renewal/expansion]	Kruse Way	32,671
AmberGlen Corp Center	Kaiser Permanente	Sunset Corridor	31,882
321 Glisan	Pacific Northwest College of Art	NW	31,644
Park Avenue West	Morgan Stanley	CBD	31,448
Pioneer Tower	Geffen Mesher [renewal expansion]	CBD	31,433
Tanasbourne Com. Center	Nike	Sunset Corridor	28,889
Arneson Building	Logical Position	Kruse Way	26,922
Commonwealth Building	Quantum Spatial	CBD	24,252
Fox Tower	Ruby Receptionist	CBD	19,290
Waterfront - Block 6	MJ Murdock	Vancouver	18,000
334 NW 11th Ave	Deskhub	CBD	17,991
2 & Taylor	Jama Software	CBD	17,920
Moda Tower	Moda Health Services Group [renewal/expansion]	CBD	16,700

Source: Colliers International; NAI Norris, Beggs & Simpson; CBRE

SALES TRANSACTIONS

Table 8: Notable Sales Transactions, Third Quarter 2015

Building Address	City	Price	Price/SF	SF
US Bancorp Tower	Portland	$372,500,000	$338.42	1,100,703
Block 300	Portland	$155,252,000	$429.10	361,808
Port of Portland Bldg	Portland	$47,500,000	$395.83	120,001
West End Building	Lake Oswego	$20,100,000	$226.17	88,871
Riverview Tower	Vancouver	$18,750,000	$114.43	163,856
New Market Theater Block	Portland	$15,500,000	$179.70	86,255
The Pettygrove Building	Portland	$8,650,000	$192.22	45,001
Parkway Plaza IV	Vancouver	$8,636,680	$170.00	50,804
221 Molalla Ave	Oregon City	$6,287,260	$182.97	34,362
Parkway Courtyard	Wilsonville	$6,050,000	$258.71	23,385
DHS O ce Building	Oregon City	$5,750,000	$174.50	32,951
19 NW 5th Ave	Portland	$2,750,000	$118.40	23,226

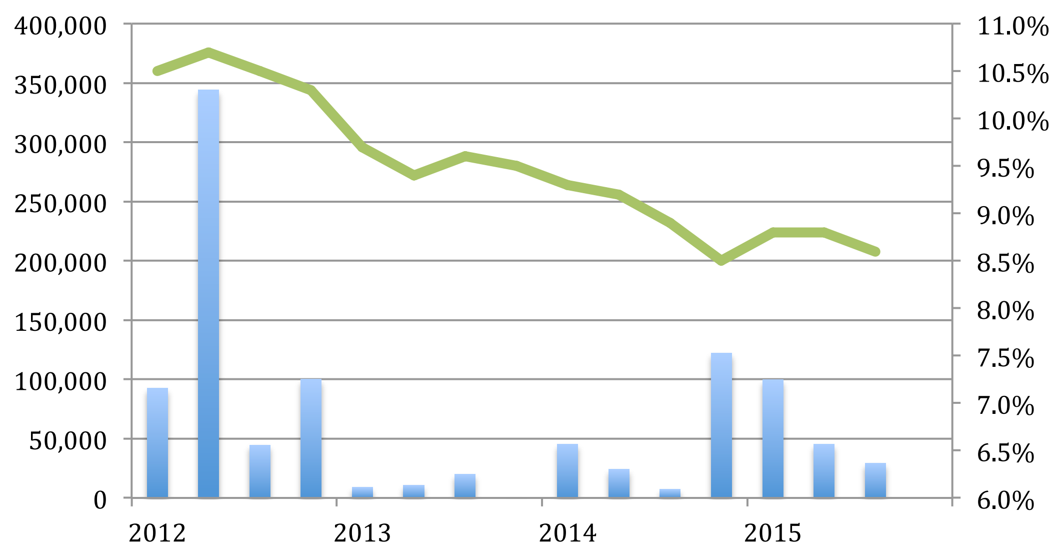
Source: Colliers International; NAI Norris, Beggs & Simpson; CBRE

DELIVERIES AND CONSTRUCTION

JLL is projecting a total of 532,980 square feet of deliveries for 2015, one of the highest figures in recent memory, with another 1.2 million square feet of new deliveries estimated to deliver during 2016. According to JLL, most new developments have taken place in the CBD and close-in submarkets with suburban rents not yet high enough to justify new development.

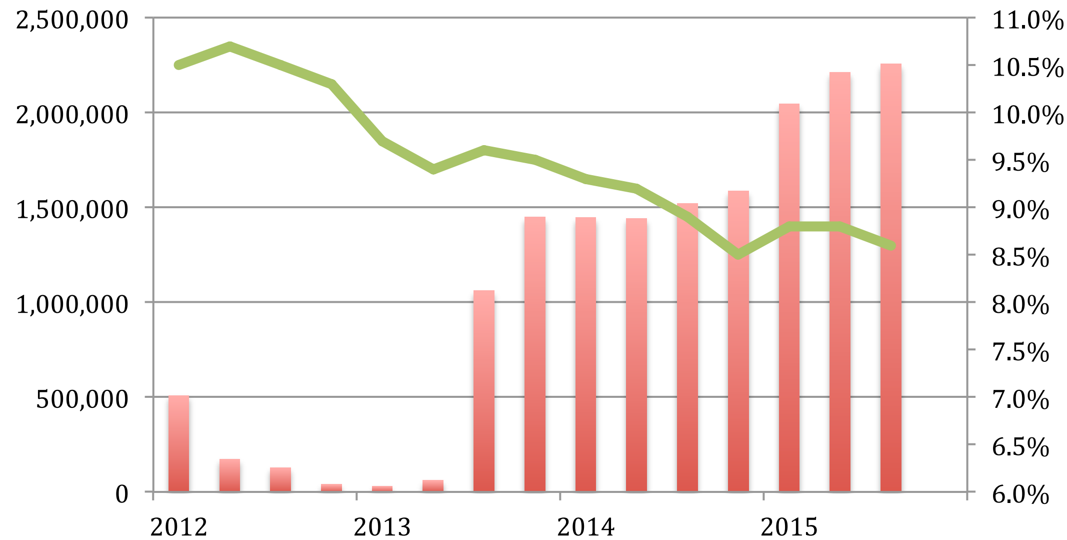
Kidder Mathews points to four creative office developments in the pipeline: the 100,000 square foot renovation of the Towne Storage Building, the 28,000 square foot renovation of The Stagecraft Building, the 45,000 square foot renovation of Laika's former headquarters at 1400 NW Pettygrove Street, and the 75,000 square foot renovation/expansion of the Premier Press building. There were also two new office developments announced: the Field Office, a 270,00 square foot space proposed at NW 17th Avenue and Broadway Tower, a mixed-use building with 170,000 square feet of office at SW Columbia Street and Clay Street.

Figure 4: Portland Office Market Deliveries (rentable square feet) and Vacancy (%), 2012–2015



Source: Kidder Mathews

Figure 5: Portland Office Market Construction (rentable square feet) and Vacancy (%), 2012–2015



Source: Kidder Mathews

Table 9: Portland Office Market Construction by Submarket, Number of Buildings, Total RBA, and Preleasing, Third Quarter 2105

Submarket	Under Construction Inventory				Average Building Size	
	Buildings	Total RBA	Preleased SF	Preleased %	All Existing	U/C
Westside	0	0	0	0	28,821	1,000,000
CBD	5	576,029	372,996	64.8%	71,027	115,206
Northeast	2	300,671	268,567	89.3%	9,173	150,335
Clark County	2	254,000	232,880	91.7%	13,302	127,000
Southeast	1	72,000	0	0.0%	9,288	72,000
Northwest	1	29,933	29,933	100.0%	16,852	29,933
Lloyd District	1	24,400	5,124	21.0%	23,599	24,400
I-5 Corridor	0	0	0	0.0%	16,711	0
Southwest	0	0	0	0.0%	15,996	0
Totals	**12**	**1,257,033**	**909,500**	**72.35%**	**204,769**	**1,518,874**

Source: Norris & Stevens

INDUSTRIAL MARKET ANALYSIS

ADAM SEIDMAN

Portland State University

Portland's industrial market continues to exhibit strong fundamentals in the third quarter. Despite over 1.2 million square feet of new space delivered in the quarter, net absorption kept pace with deliveries and vacancies remaining at historic lows. Rental rates remain at or near historic highs. These trends are expected to continue as tenant demand for small and large spaces remains strong.

VACANCY AND RENTS

In the third quarter, CBRE declared that "Portland's industrial market fundamentals are stronger than ever." Indeed, Metropolitan Portland's industrial market continues to see both occupancies and asking rates at or near historic highs. A review of quarterly research reports from four leading commercial real estate firms reveals a metro-wide vacancy rate of 4.82 percent in the third quarter, 3 basis points below the prior quarter and 59 basis points below the third quarter of 2014. This vacancy rate is especially impressive in light of the delivery of over one million square feet of new, mostly speculative space. Distribution/warehouse vacancy rates remain flat versus the prior quarter and 58 basis points below the prior year, while flex space vacancy stood 60 basis points below the prior quarter and 80 basis points below the prior year.

■ Adam Seidman 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.

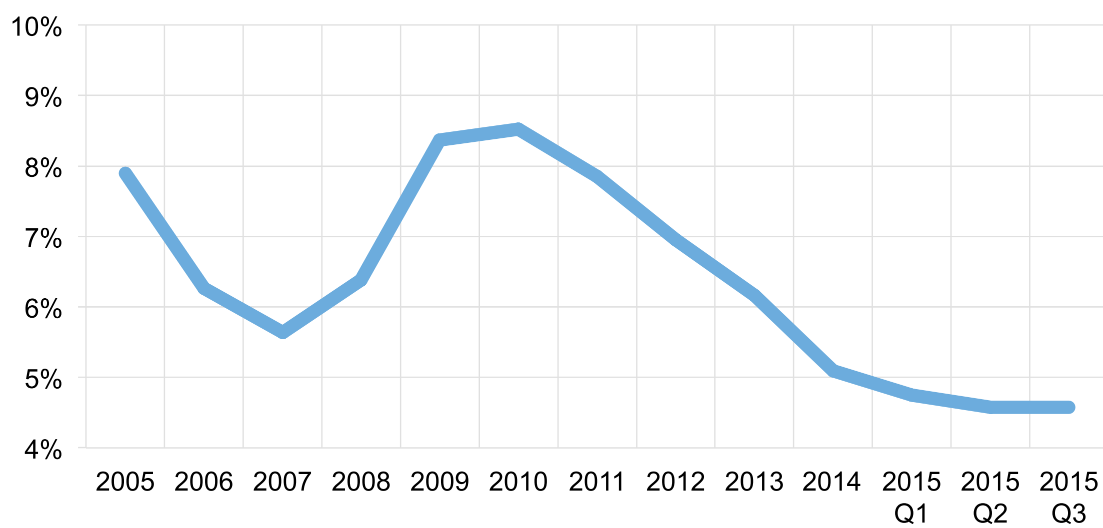
Table 1: Portland Industrial Quarterly Report Survey Q3 2015

	Colliers	JLL	CBRE	Kidder Mathews	Average - Q3 2015	Chg vs Prior Qtr	Chg vs Prior Year
Vacancy							
- Distribution/Warehouse	5.00%	4.20%	4.40%	4.70%	4.58%	00 bps	-58 bps
- Flex	10.20%	9.70%	-	-	9.95%	-60 bps	-80 bps
- Weighted Average	5.47%	4.71%	4.40%	4.70%	**4.82%**	**-03 bps**	**-59 bps**
Rents *							
- Distribution/Warehouse	$0.47	$0.50	$0.41	$0.48	$0.46	-0.5%	3.6%
- Flex	$0.93	$0.97	$1.07	-	$0.99	2.1%	19.1%
- Weighted Average	$0.51	$0.54	$0.47	$0.48	**$0.50**	**-0.2%**	**5.6%**

* Asking rents; Industrial = shell space; Flex = shell and office space
Sources: Quarterly Reports

According to CBRE, this is the ninth consecutive quarter of declining vacancy rates. Kidder Mathews note that there is demand from a broad base of sectors, from the food industry to e-commerce, driven by Portland's strong population growth.

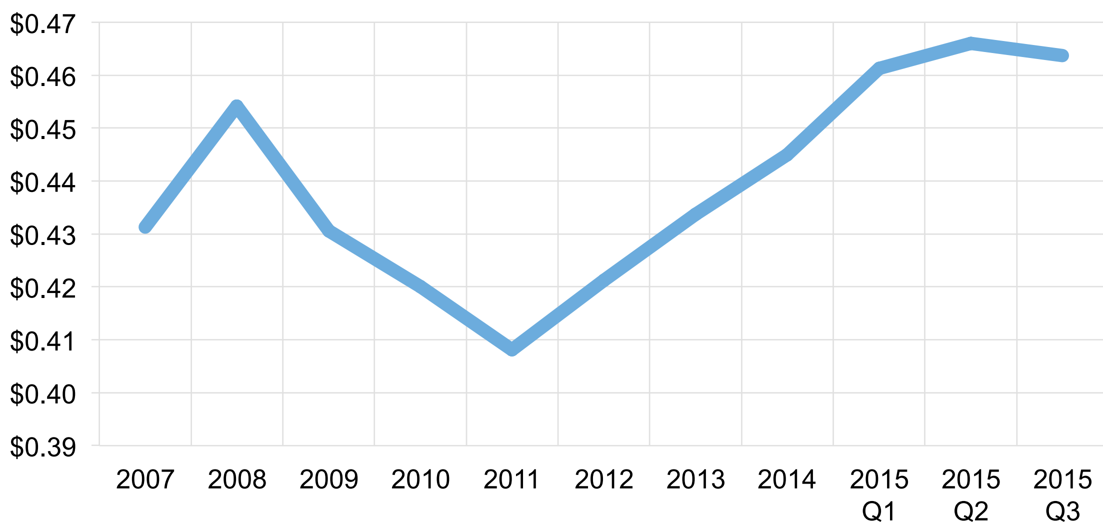
Figure 1: Portland Distribution/Warehouse Market Vacancy Rate, 2007–2015 Q3



Sources: Average of Quarterly Reports from CBRE, JLL, Colliers, and Kidder Mathews

Along with steady vacancy rates, asking rental rates dipped slightly but remained virtually unchanged in the third quarter. The quarterly report survey showed monthly distribution/warehouse asking rates of $0.46/square foot and flex rates of $0.99/square foot, for a combined weighted market average of $0.50/square foot. Distribution/warehouse rates were down 0.5 percent from the second quarter but up 3.6 percent year-over-year. Capacity Commercial Group notes that shell rents for smaller and close-in properties are reaching $0.50/square foot and up. Flex rates increased 2.1 percent from the second quarter and exhibited strong annual growth of 19 percent.

Figure 2: Portland Distribution/Warehouse Market Asking Rents, 2007–2015 Q3



Sources: Average of Quarterly Reports from CBRE, JLL, Colliers, and Kidder Mathews

ABSORPTION AND DELIVERIES

Colliers report positive net absorption of 1.16 million square feet in the third quarter, up from 900,000 square feet in the second quarter. Over the past four quarters, the market has absorbed nearly 4 million square feet of space (2.9 million square feet excluding Intel's Mod1 site). This net absorption run rate is higher than the market's average annual net absorption from 2004-2014 of 2.55 million square feet. With another strong quarter of net absorption expected in the fourth quarter, 2015 is on pace to have the strongest net absorption and deliveries of any year since 2007. Capacity Commercial Group notes that leases totaling 1.1 million square feet are either underway or in active negotiations.

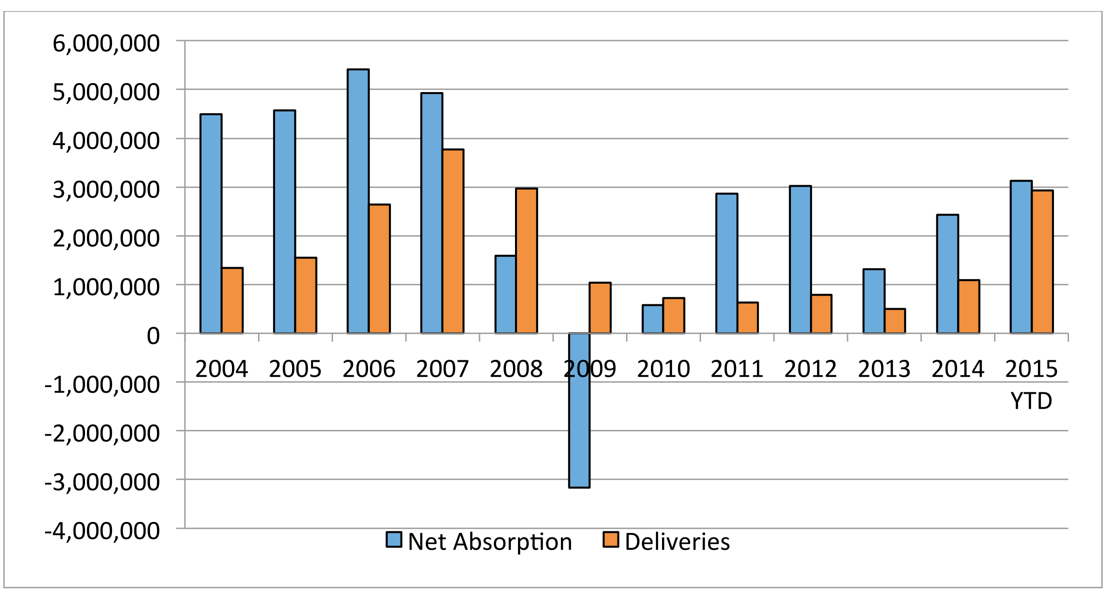
Notable deliveries in the quarter include 493,000 square feet at Specht's Interstate Crossroads Distribution Center, 212,000 square feet for the Swan Island FedEx distribution center, and 145,000 square feet at Trammell Crow's Southwest Industrial Park.

Table 2: Portland Industrial Net Absorption Last 4 Quarters

	Distribution/ Warehouse	Flex	Total
Q4 2014	848,170	14,689	862,859
Q1 2015	1,129,776	-68,708	1,061,068
Q2 2015	-218,400	1,129,200	910,800
Q3 2015	835,434	325,453	1,160,887
Total	2,594,980	1,400,634	3,995,614
w/out Intel	*2,594,980*	*300,634*	2,895,614
AVG 2004-2014			2,549,245
Peak Annual	*2006:*		*5,412,028*
Trough Annual	*2009:*		*-3,169,003*

Source: Colliers International

Figure 3: Portland Industrial Net Absorption and Deliveries, 2004–2015 YTD (Through Q3)



Sources: Colliers Quarterly Report and Colliers/Capacity Commercial Presentation

Table 3: Notable Portland Industrial Lease Transactions Q3 2015

Tenant	Building	Submarket	Size (s.f.)	Type
KeHE Distributors	PDX Logistics Center Bldg 1	Airport Way	383,040	New
Unisource Worldwide	I-84 Industrial Center	East Columbia	226,290	Renewal
LKQ Auto Parts	Interstate Crossroads	East Columbia	225,000	New
Trailblazer Foods	Halsey Crossing	East Columbia	134,400	New
Mergenthaler	Bybee Lake II	Rivergate	123,120	New

Sources: CBRE and Colliers

UNDER CONSTRUCTION

JLL notes that there is known tenant demand for approximately 2.6 million square feet of space, with over 60 percent of this demand coming from users seeking spaces over 100,000 square feet. Capacity Commercial Group notes that leasing activity for large blocks has been occurring mainly in the Airport Way/East Columbia submarket due to its space availability and options.

To meet known and speculative demand, there are over 2.5 million square feet of space currently under construction. This does not include Intel's 1.6 million square feet at Ronler Acres. Much of the future supply, 1.9 million square feet, is located in the Northeast Portland submarkets. This area includes the following notable projects that together represent over 1.3 million square feet of space:

- Cameron Distribution Center: 321,000 square feet, due to deliver Q4 2015
- Colwood Industrial Park: 425,000 square feet in Phase 1, due to deliver 2016; total project could deliver up to 845,000 square feet
- PDX Logistics Center: 355,000 square feet in Building 3, due to deliver 2016
- Gateway Corporate Center: 211,000 square feet in Buildings D and E, due to deliver 2016

INVESTMENT ACTIVITY

Kidder Mathews reports that transaction volume for the third quarter was $188 million, up from $143 million in the second quarter and $121 million in the first quarter. The Kelley Point Distribution Center transaction, at $75 million, accounted for 40 percent of the quarter's sales volume. The average sales price in the quarter was $90.09 per square foot, up from $71.72 in the second quarter and $70.56 in the first quarter. The average market capitalization rate decreased to 5.99 percent in the third quarter, as compared to 6.41 percent in the second quarter and 7.02 percent in the previous quarter.

Capacity Commercial Group notes that investor demand is strong across all categories, from older single-tenant spaces to newer institutional-grade offerings. CBRE notes that close-in spaces are driving up the average per-square foot values, as their sales prices are over $133/square foot, or 45 percent above the market average.

Table 4: Notable Portland Industrial Sales Transactions Q3 2015

Address	Location	Size (s.f.)	Price	Price/s.f.	Type
Kelley Point Distribution Center	Portland	1,034,500	$ 75,518,500	$ 73.00	Investment
Birtcher Center @ Townsend Way	Fairview	397,934	$ 34,500,000	$ 86.70	Investment
Ogden Business Park	Vancouver	300,583	$ 18,050,000	$ 60.05	Investment
Quad 217 Corporate Center	Beaverton	77,592	$ 6,600,000	$ 85.06	Investment
Wubben Industrial Park Bldg E	Vancouver	54,600	$ 6,250,000	$ 114.47	Investment

Sources: Colliers and Kidder Mathews

LOOKING AHEAD

With Portland's economy in an expansionary phase, the near- to mid-term fundamentals for the industrial sector look strong. 2.5 million square feet of mostly speculative space are in the pipeline and should be delivered over the next four quarters. Given historical trends as well as known demand in the market for larger spaces, most of this space will likely be absorbed by the end of 2016, leaving vacancy rates virtually unchanged from their current low levels. This amount of new space, coupled with low vacancy rates, should also lead to an increase in the overall shell rates of distribution and warehouse spaces over this time period. The market continues to watch for the potential impact of marijuana legalization on the industrial market; this will likely begin to impact the market over the next four quarters as businesses and investors look to find space for warehousing and distribution needs.■

RETAIL MARKET ANALYSIS

ALEC LAWRENCE

Portland State University

After an improved 3.9 percent annualized GDP growth rate for the second quarter, growth in the US economy slowed to a 1.5 percent annualized growth rate during the third quarter—that according to the advance estimate released by the US Department of Commerce. While this marks a marked slowdown from the second quarter, the rate is just below the market estimate of 1.6 percent and the Department of Commerce credits the decrease to an inventory glut forcing production to slow rather than to worsening market fundamentals. Fourth quarter estimates are optimistic, with economists calling for a pick up in GDP growth.

Consumer spending grew at a 3.2 percent rate during the third quarter—a decrease from the 3.6 percent rate of growth during the second quarter. However, the growth rate in disposable income actually increased during the third quarter to 4.8 percent from 3.4 percent during the second quarter.

The Portland metro economy continues to perform strongly, with 3.2 percent job growth over the last 12 months spread over a diverse group of industries. The State of Oregon's Office of Economic Analysis (OEA) has even increased its winter estimates from original projections. Despite a small uptick in unemployment from 5.4 percent in June to 5.7 percent in July due to an influx of "people entering the labor market or who are leaving their jobs voluntarily," unemployment closely trailed the national rate of 5.3 percent in July and sits well below the 7.0 percent rate in July 2014.

The Integra Realty Resources (IRR) highlights several trends in Portland's retail market. According to IRR, the Portland retail market is buoyed by the barriers to

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entry imposed by Oregon's system of urban growth boundaries and by Portland's increasing urban housing density. IRR sees strong retail growth in central Portland, particularly from ground-floor retail in urban, mixed-use, multitenant buildings and grocery anchors looking to locate or expand in inner Portland. In contrast, IRR sees a slight decrease in demand for suburban grocery-anchored centers.

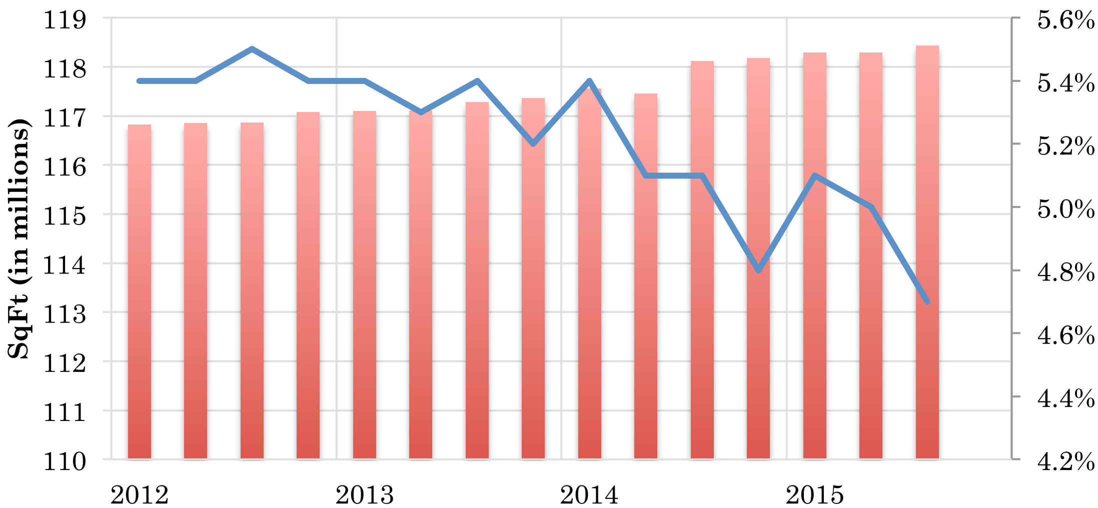
As of October 1, 2015, Portland's growing bevy of marijuana dispensaries opened their doors to recreational sales. According to an extrapolation based upon limited sales numbers collected by the Oregon Retail Cannabis Association, Oregon dispensaries brought in $11 million during the first week of recreational sales alone. If true, this number could indicate much stronger sales than anticipated, leading to higher tax revenues and potentially greater interest in additional marijuana tenanted real estate.

Portland's retail market is also likely be impacted by Haggen's Chapter 11 bankruptcy filing. The filing follows Haggen's botched purchase of 146 stores that Albertsons and Safeway were ordered to sell in exchange for federal approval of their merger. NAI Norris, Beggs, & Simpson reports that Haggen will close 12 of its Oregon stores, including those in Ashland, Baker City, Beaverton, Milwaukie, Sherwood, Springfield, and Tigard.

VACANCY

Kidder Mathews reports that vacancy continued a steady but slow decline, with the direct vacancy rate ending at 4.7 percent for the third quarter. This marks the lowest retail vacancy rate on record since at least 2008 as compared to Kidder Mathews' annualized historic vacancy rates. The spread between the vacancy rate and availability rate was unchanged from the second quarter, holding steady at 1.1 percent over the direct vacancy rate, ending at 5.8 percent in the third quarter. NAI Norris, Beggs & Simpson reported a total availability rate of 6.1 percent.

Figure 1: Portland Retail Market Net Rentable Area (NRA) and Vacancy (percent), 2012-2015



Source: Kidder Mathews

NAI, Norris, Beggs, & Simpson, reported the weakest total vacancy rates in the 122nd/Gresham and Vancouver submarkets, at 9.9 percent and 8.3 percent respectively, and the strongest performance in the Southwest and Eastside submarkets, at 3.8 percent and 4.4 percent respectively—trends unchanged from the previous quarter.

Table 1: Vacancy Ranked by Submarket, Third Quarter 2015

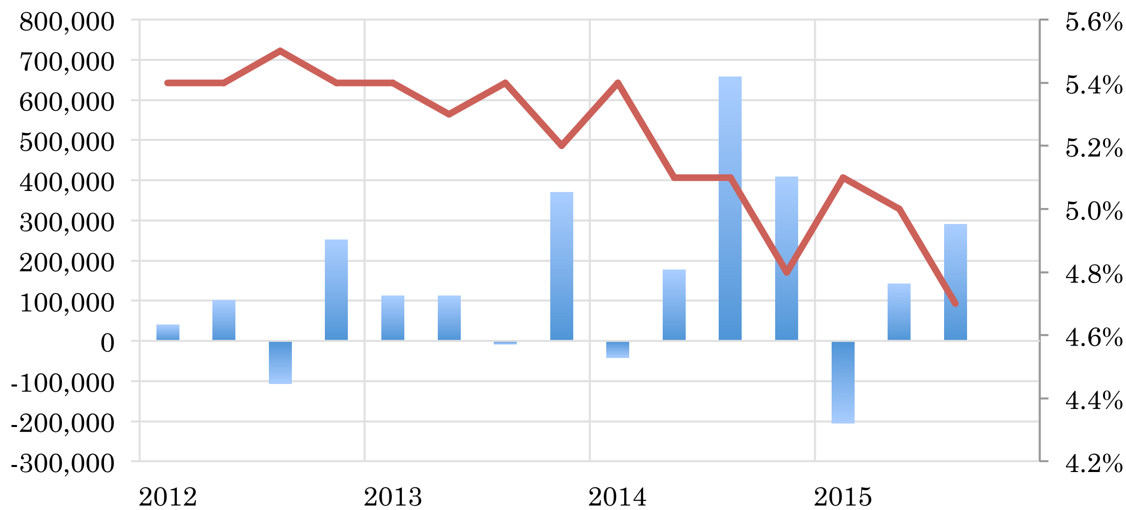
Submarket	Vacancy
Southwest	3.8 percent
Eastside	4.4 percent
Sunset Corridor	5.1 percent
Central City	5.7 percent
Southeast/East Clackamas	5.7 percent
Total	**6.1 percent**
Vancouver	8.3 percent
122nd/Gresham	9.9 percent

Source: NAI Norris, Beggs & Simpson

ABSORPTION AND LEASING

Kidder Mathews reports a strong net absorption of 290,109 square feet for the quarter, 43 percent higher than the average quarterly net absorption rate over the past three years. NAI Norris, Beggs & Simpson reported net absorption of 170,836 square feet for the quarter.

Figure 2: Net Absorption Rate (square feet) and Vacancy (percent), 2012-2015



Source: Kidder Mathews

Safeway recently closed two Portland Metro stores: its Wilkes East store in Gresham and its Oak Grove store in Milwaukie. Shleifer Furniture also announced it would close after 80 years with an announced conversion of the SE Grand Avenue building to a hotel by Beam Development. Green Zebra moved forward with two new stores, a 4,200-square-foot location at SW Broadway and Mill Street in an agreement with PSU as well as an 8,023-square-foot location at the Hassalo on Eighth development. Whole Foods will open its 365 by Whole Foods concept in Lake Oswego—one of just five locations to be announced so far. The format targets value and quality conscious customers in a smaller format and will feature its 365 Everyday Value brand. Analysts are interpreting the concept as a move to target Millennials.

Table 2: Net Absorption Ranked by Submarket, Third Quarter 2015

Submarket	Absorption
Total	**170,836**
Vancouver	152,674
Southwest	30,529
Southeast/East	
Clackamas	19,334
Eastside	32
Central City	(432)
122nd/Gresham	(1,847)
Sunset Corridor	(29,454)

Source: NAI Norris, Beggs & Simpson

Table 3: Notable Retail Lease Transactions, Third Quarter 2015

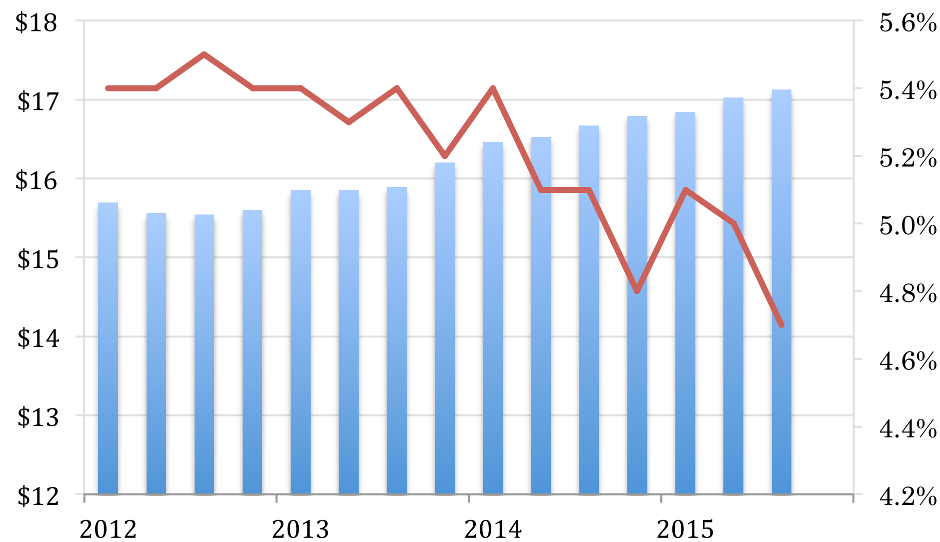
Building	Tenant	Submarket	Sq. Ft
Tigard Triangle Center	Party Fair	Southwest	9,509
Hassalo on Eighth	Green Zebra Grocery	Eastside	8,203
Barrows Crossing	Dogstar	Southwest	5,540

Source: NAI Norris, Beggs & Simpson

RENTAL RATES

Kidder Mathews reports that rents continued a nine-quarter climb, ending at $17.12 per square foot NNN per year. This marks a 2.7 percent year-to-year increase. Norris & Stevens reported average quoted rents at $17.41 per square foot per year, a 2.87 percent year-to-year increase according to its data.

Figure 3: Portland Retail Market Average Quoted Rates ($/SF/Yr/NNN) and Vacancy (percent), 2012-2015



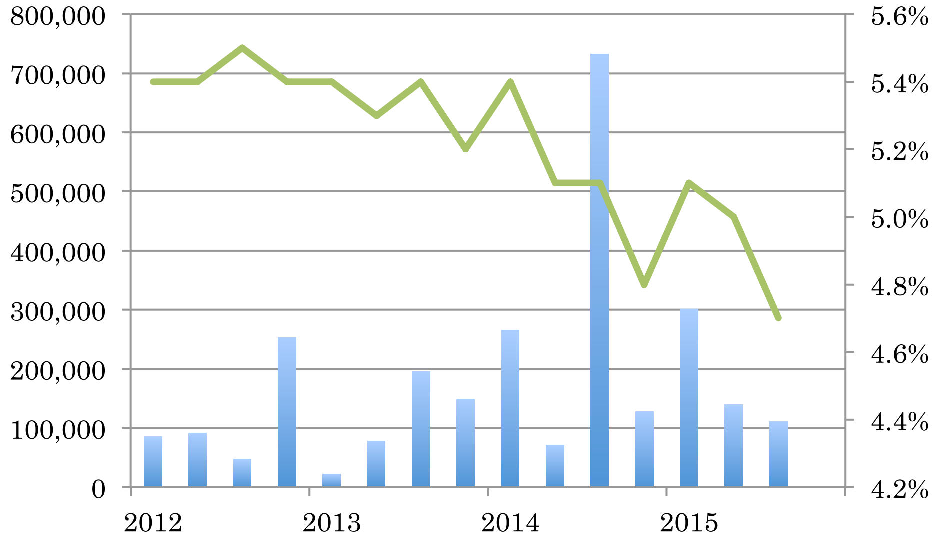
Source: Kidder Mathews

DELIVERIES AND CONSTRUCTION

Kidder Mathews reported a total of 15 buildings and 111,001 square feet delivered for the quarter, NAI, Norris, Beggs, & Simpson reported three buildings completed and 168,250 square feet, and Norris & Stevens reported 14 buildings and 100,717 square feet.

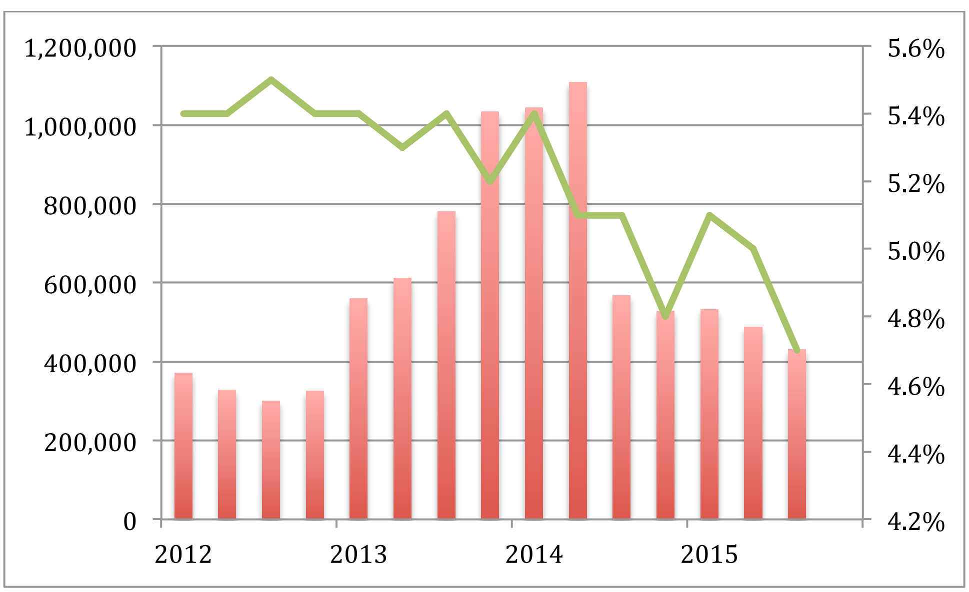
Kidder Mathews reports a total of 20 projects under construction, for a total of 430,918 square feet. This is down from 488,227 square feet last quarter. The construction pipeline continues to sit below late 2013 and early 2014 levels that stood at over 1,000,000 square feet. NAI Norris, Beggs & Simpson reports a total of 45,267 square feet under construction and Norris & Stevens reports a total of 146,445 square feet.

Figure 4: Portland Retail Market Deliveries (square feet) and Vacancy (percent), 2012-2015



Source: Kidder Mathews

Figure 5: Portland Retail Market Construction (square feet) and Vacancy (percent), 2012-2015



Source: Kidder Mathews

SALES

Kidder Mathews reported $202.47 million in transactions during the third quarter, an increase from the 2014 quarterly average of $169.1 million and reports expectations of growth in total 2015 transactions over 2014. Marcus & Millichap reports capitalization rates of five percent for drug stores in the CBD with a 25 basis point increase for surrounding areas, a high-six to low-seven percent rate for strip centers increasing for surrounding areas, and fast-food restaurants as low as 4 percent.

Table 4: Notable Investment Transactions, Third Quarter 2015

Property	City	Sale Price	Square Feet	Price/SF
Tigard Promenade & Sunnyside	Portland	$38.5 M	117,695	$327
Dealership Portfolio	Portland	$32.25 M	116,681	$276
Trails End Marketplace	Oregon City	$20 M	105,191	$190
Winco Foods	Portland	$15 M	105,000	$143
Mt. Baker Building	Portland	$3.55 M	NA	NA
419 E Burnside St.	Portland	$2.795 M	NA	NA

Source: Kidder Mathews and NAI Norris, Beggs & Simpson