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IN SEARCH OF THE MISSING CONDOS: AN ANALYSIS OF THE CONDO DEVELOPMENT MARKET IN THE PORTLAND AREA

Adam Seidman

Portland State University

Since the Great Recession, there has been significant multifamily development activity in the Portland metropolitan area and across the country – but it has almost exclusively been rental housing and not for-sale multifamily (i.e. condominium) product. This article will attempt to uncover the main causes of this lack of condominium development in the local market and will also seek to answer if this trend is likely to continue over the next few years. In addition, we will explore if these issues are unique to the Portland market.

The analysis revealed that there are three core reasons underlying the lack of condominium development in the Portland metro:

1. A significant shift towards rental housing demand since the Great Recession, due to factors such as demographics, shifting preferences, changing home and work patterns, higher quality rental supply, and increased standards for qualifying for home mortgages.

2. The impact of failed or challenging condo projects on regulations and perceptions (for the developer, investor, and lender), and the resulting difficulty in

■ 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.

obtaining capital for condo projects in the current cycle – both for developers and for prospective buyers of condo units.

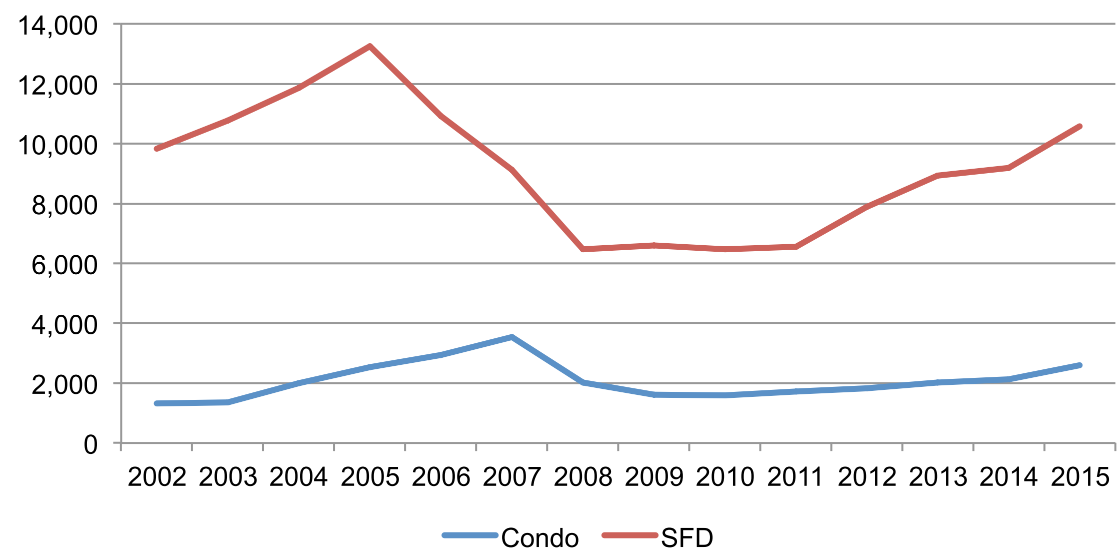
3. The impact of construction defect liability claims on developer perceptions and on project risk and financial feasibility.

We will first examine the current state of Portland's condo market and will then dive deeper into each of the core issues outlined above.

PORTLAND'S CONDO MARKET

After peaking at 3,500 sales in 2007, condo sales (of existing and new product) declined in Multnomah County for three straight years before beginning a steady five-year rebound, according to RMLS. Sales volume increased 22% in 2015 to 2,600 sales. Similar trends can be seen in sales of single family homes in Figure 1.

Figure 1: Total Sales Volume, Multnomah County, 2002-2015



Source: RMLS

As with sales volume, median condo prices have been rising for five straight years. At nearly $300,000 as of the first quarter of 2016, values have risen above the pre-recession peaks. A similar trend can be seen in the single family market, although prices have been rising at a faster rate – putting median condo prices at just over 80% that of single family homes, the lowest ratio in 15 years (RMLS).

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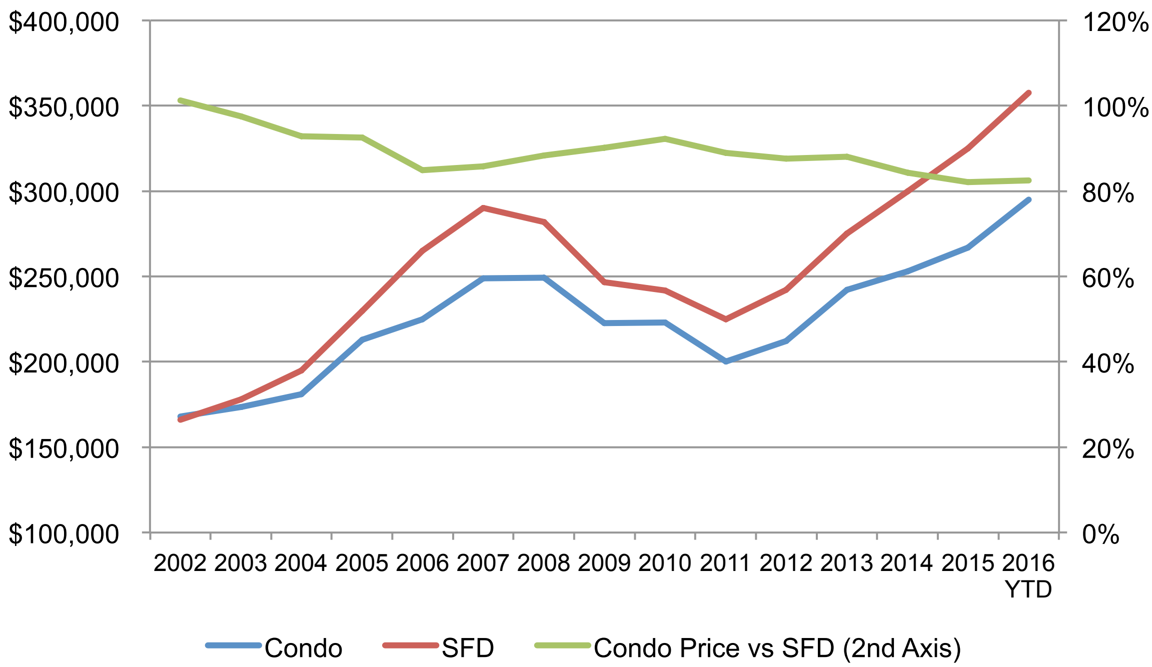
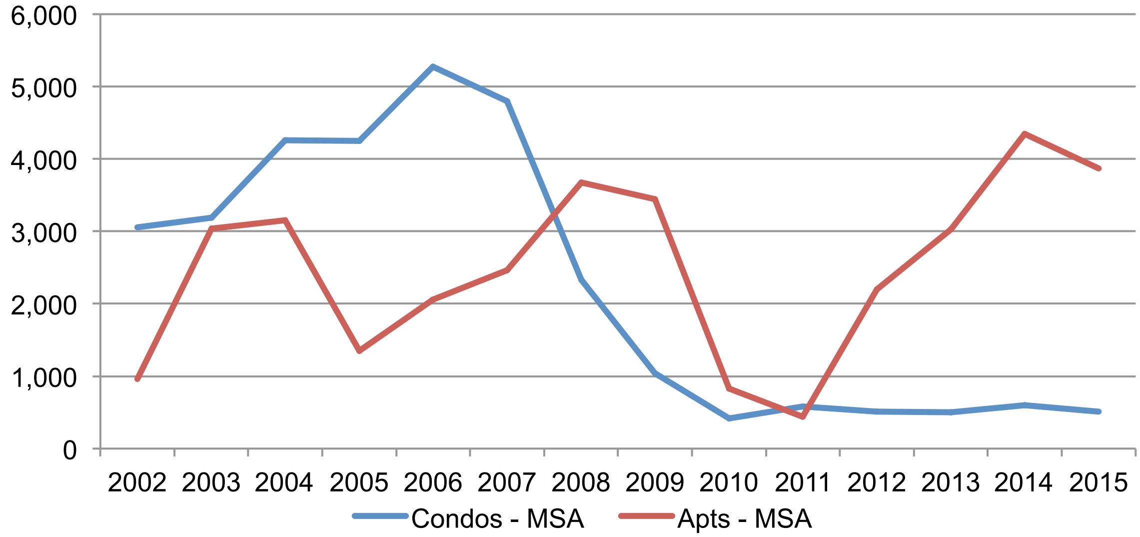
One of the reasons that condo prices have been rising more slowly than single family prices may be due to the age of the housing stock – there have been very few new condos built since 2008. According to RMLS, after averaging nearly 3,900 new condo units built per year between 2002 and 2008, the Portland metropolitan area has since seen the average plummet to 600 units built per year. Multnomah County has seen only 160 new condo units built per year between 2009 and 2015. In contrast, apartment production has ramped up significantly in the MSA and the County since 2011 (CoStar).

Figure 2: Median Sales Price, Multnomah County, 2002-2016 YTD



Source: RMLS

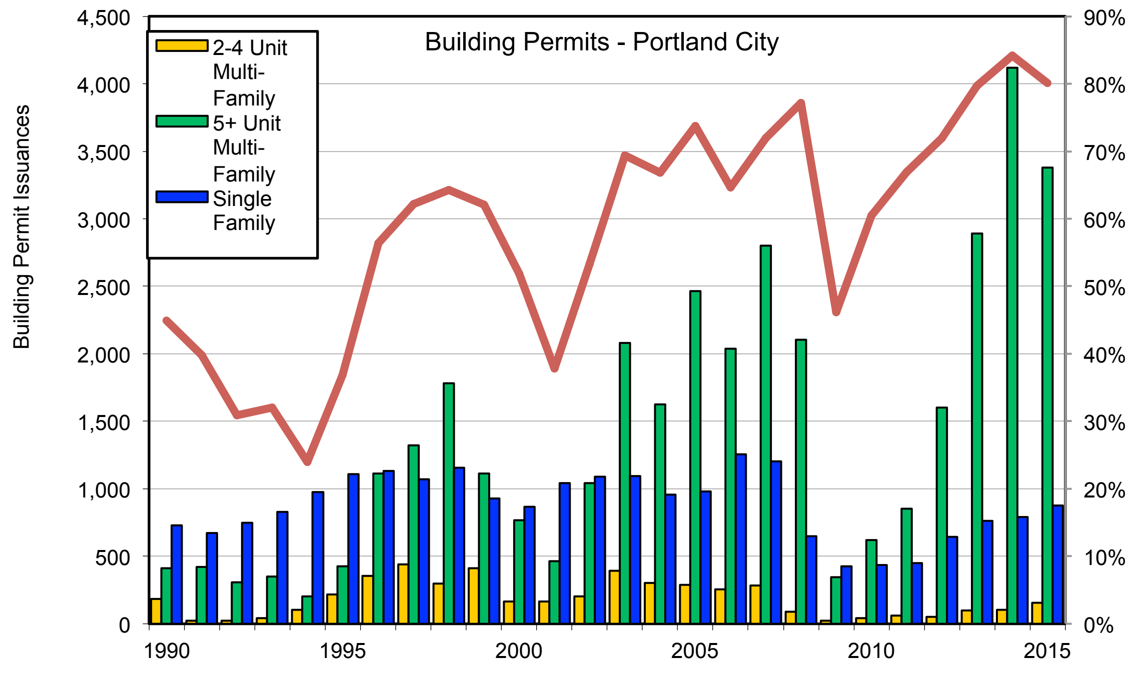
Figure 3: Housing Units Built, Portland MSA, 2002-2015



Source: RMLS, CoStar

This trend looks set to continue, as multifamily permits are at or near record highs in Portland – but nearly all of the planned units are rentals and not for-sale condos (SOCDS).

Figure 4: Building Permits Issued, Portland City, 1990-2015

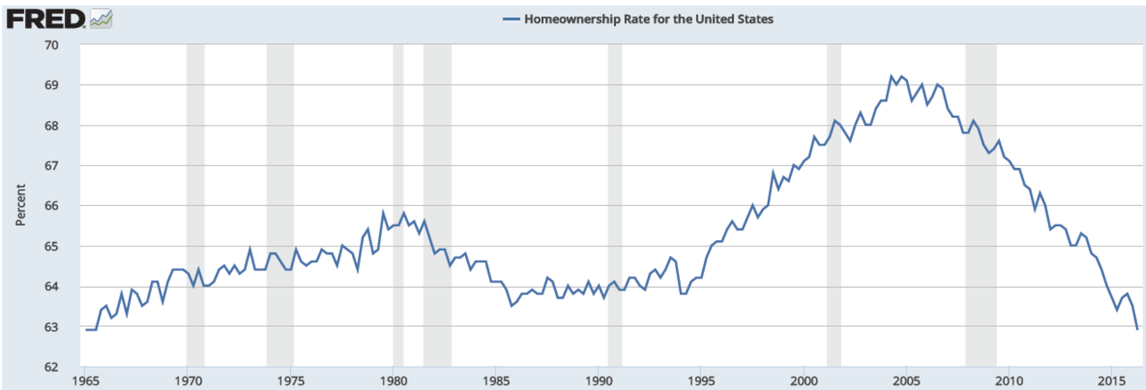


Source: SOCDS (HUD)

SHIFT TOWARDS RENTAL HOUSING

Since the financial crisis and Great Recession that began in late 2007, homeownership in the United States has declined from a peak of 69% to under 63% in the second quarter of 2106 - levels not seen since 1993, according to the most recent U.S. Census figures.

Figure 5: Homeownership Rates, United States, 1965-2016

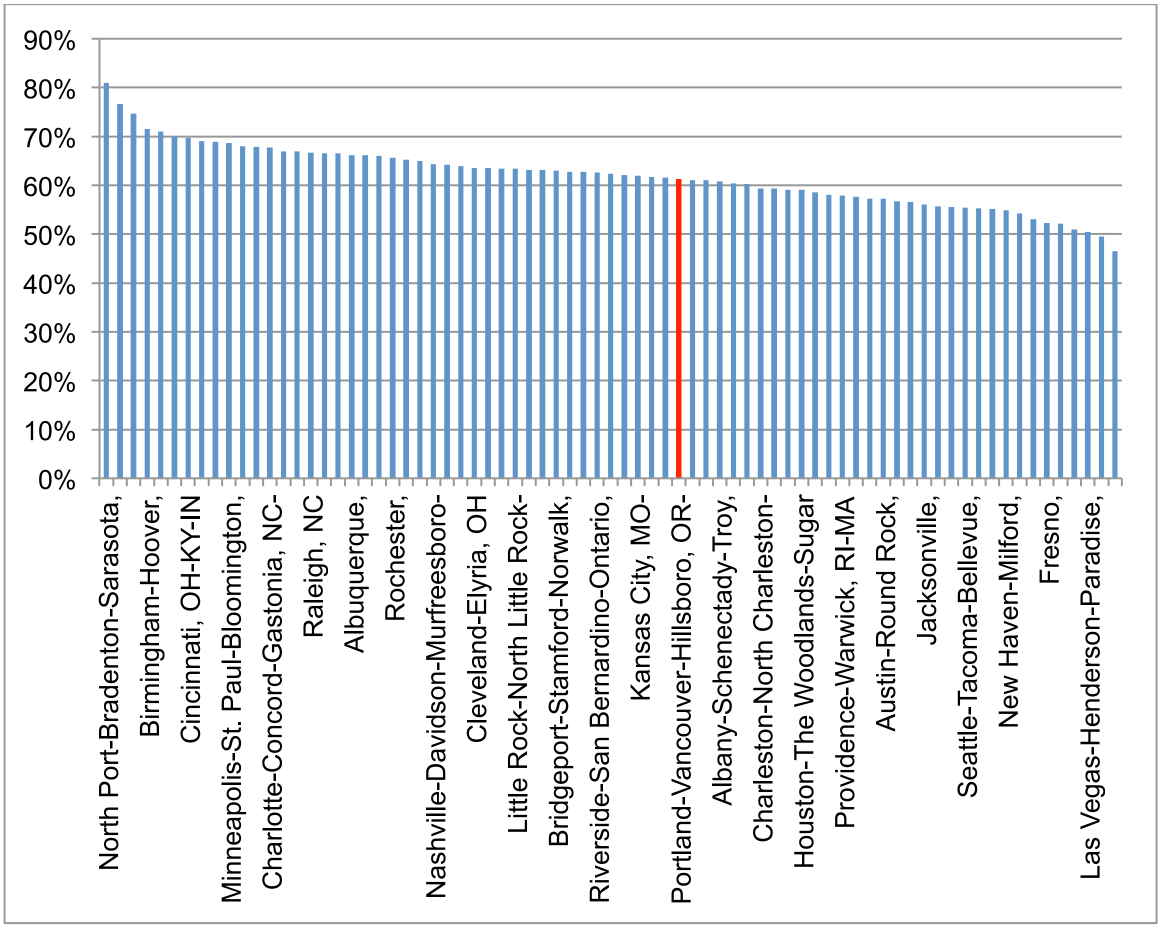


Source: U.S. Census Homeownership Report

Oregon and the Portland MSA have largely followed this trend, and as of the second quarter of 2016 the homeownership rate in the Portland metro sits at just over 61% - down from a peak of nearly 73% in 2005. The Portland MSA is about in the middle of the pack in terms of homeownership rates compared to other metros.

Harvard's Joint Center for Housing Studies' "State of the Nation's Housing" report outlines some of the reasons for the decline in national homeownership rates, including: the negative impacts of the Great Recession on potential or existing homeowners (such as reductions in homeowner equity and credit scores), tighter lending requirements, declines in household incomes, increases in student debt, the aging of both the Baby Boomer and Millennial generations, and shifts in household composition (i.e. more singles and unmarried couples). In addition, changes in work type and tenure and in attitudes towards renting have also likely impacted the overall homeownership rate trend (Harvard 2015).

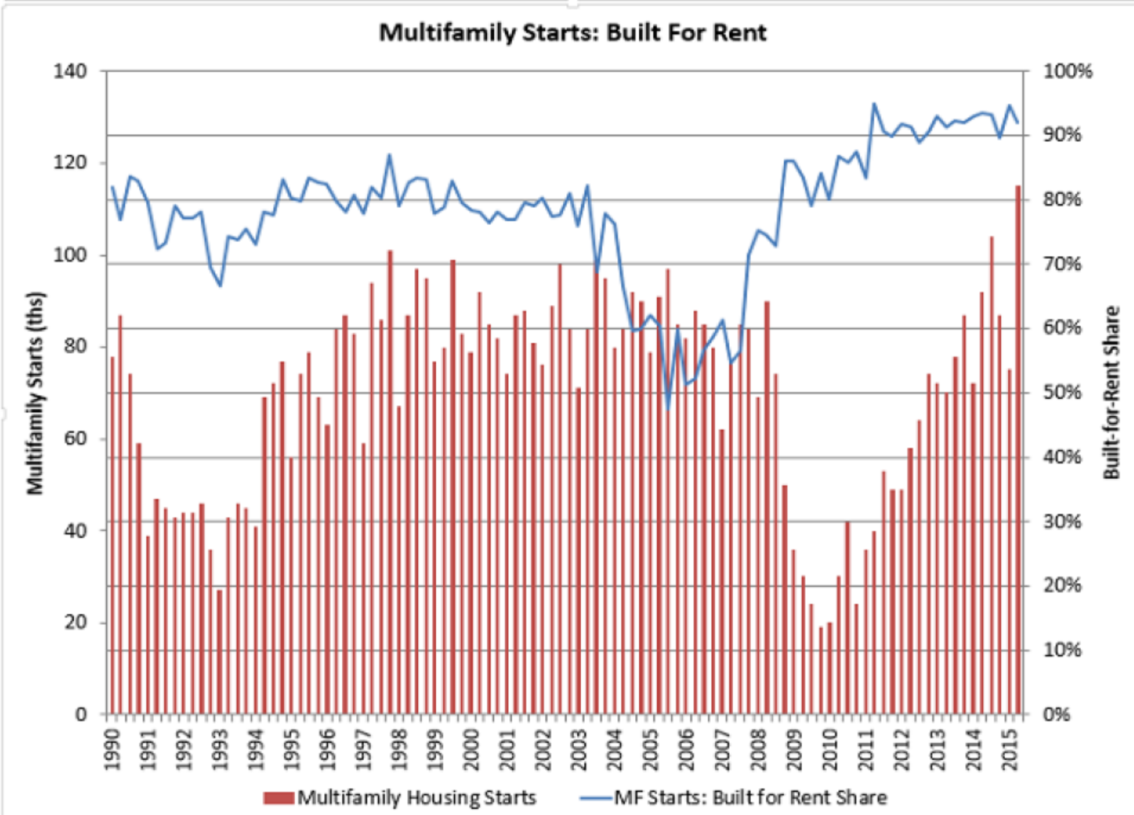
Figure 6: Homeownership Rates, Top MSAs, United States, Q2 2016



Source: U.S. Census Quarterly Vacancy and Homeownership Rates

Because of many of the reasons cited above, key target groups for condo developers, including first-time homebuyers, are increasingly choosing to rent instead of own their housing. This trend has been a headwind against new condo development in the Portland market and nationally. The result is that multifamily development has been dominated by rental product – nationally, accounting for over 90% of all multifamily starts over the past 5 years, versus a historical average of 80% (and a dip to 50-60% during the condo development boom in the mid-2000s). Overall, construction of condo units is running at about half of its pre-boom pace (Anderson 2015; Dietz 2015).

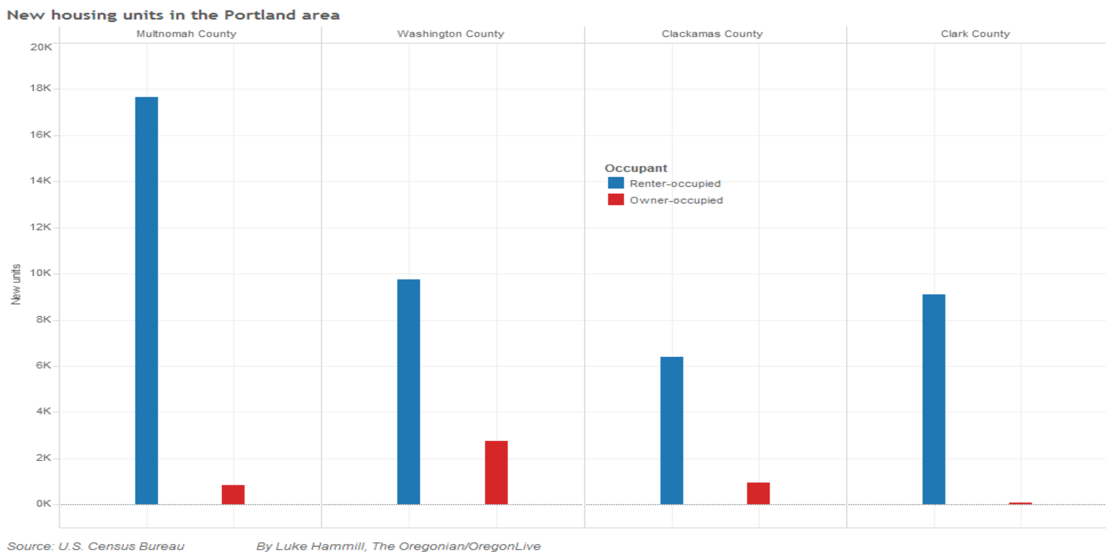
Figure 7: Multifamily Housing Starts and Apartment Share, United States, 1990-2015



Source: U.S. News & World Report, based on data from U.S. Census

This also has been the case in the Portland metro, as we saw in our review of Portland's condo market. In fact, an analysis of new housing units in the metro's largest counties reveals that most of the new housing units built in the past 5 years have been renter-occupied – suggesting that in addition to the purpose-built rental products (i.e. apartments) in the market, renters have also been occupying new units traditionally built for ownership (i.e. single family homes) (OregonLive).

Figure 8: Occupancy Type of New Housing Units, Top Counties, Portland MSA, 2005-2014



Source: Oregonlive, based on data from U.S. Census

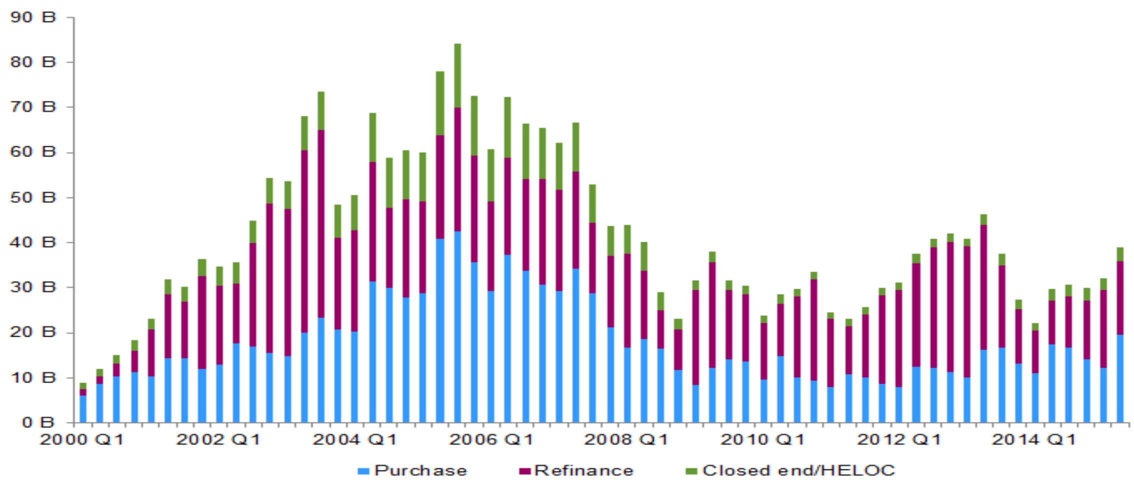
RESTRICTED CAPITAL

The Great Recession clearly had a significant impact on condo development in Portland and nationally. Condos were disproportionately impacted during the downturn, as many investors who speculated on price increases in condo towers were unable to make loan payments once demand (from both potential renters and future buyers) froze up, or in some cases walked away from purchases before closing. This impacted perceptions and subsequent actions of banks, developers, and government entities. Many banks, especially ones that had to deal with foreclosed condo units, simply stopped lending to both developers (for construction) and prospective buyers (for purchases of units). Most developers, unable to receive traditional financing and concerned about lack of demand for units, stopped developing condo projects.

Perhaps most significantly, the main Government Sponsored Enterprises – Fannie Mae, Freddie Mac, and the FHA – changed their policies after the Great Recession in ways that made it harder to purchase condo units. As the main purchasers of mortgages in the United States, accounting for half of all mortgage securitization nationally, these policy changes impacted all lenders. These policies included restricted limits on such things as the percentage of units that could be rented in a project, the number of units that could be owned by a single entity, and the percent of units late in paying their condo association dues. The result of these policies is that many condo projects became "unwarrantable" – in other words, the GSEs would not "warrant" them because they did not fit the new criteria – and this meant that loans effectively couldn't be made on units in these projects (U.S. HUD 2015; Fannie Mae 2014; Freddie Mac; Gibbs 2014; Glink 2013).

As financing became difficult or impossible to find for purchasing condos, the share of units purchased entirely with cash (and no loan) nationally increased from around 27% prior to the downturn to a peak of 62% of all units in 2012 (Yao 2015). The past few years have seen an increase in loan originations for condos and a decrease in all-cash purchases, in part a result of the GSEs easing up their policies. However, financing remains difficult to access, and all-cash sales are still significantly higher than prior to the downturn.

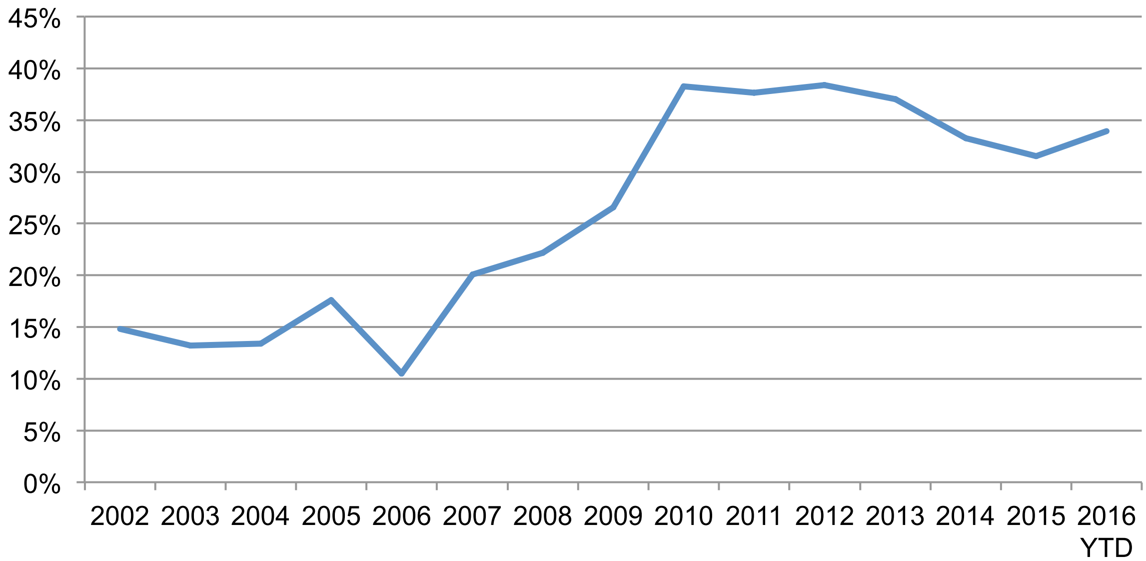
Figure 9: Condo/Co-Op Mortgage Originations, United States, 2000-2015



Source: CoreLogic

Multnomah County reflects these national trends: all-cash sales have been between 30%-40% of all condo sales since 2009, compared to rates below 20% before 2007 (RMLS).

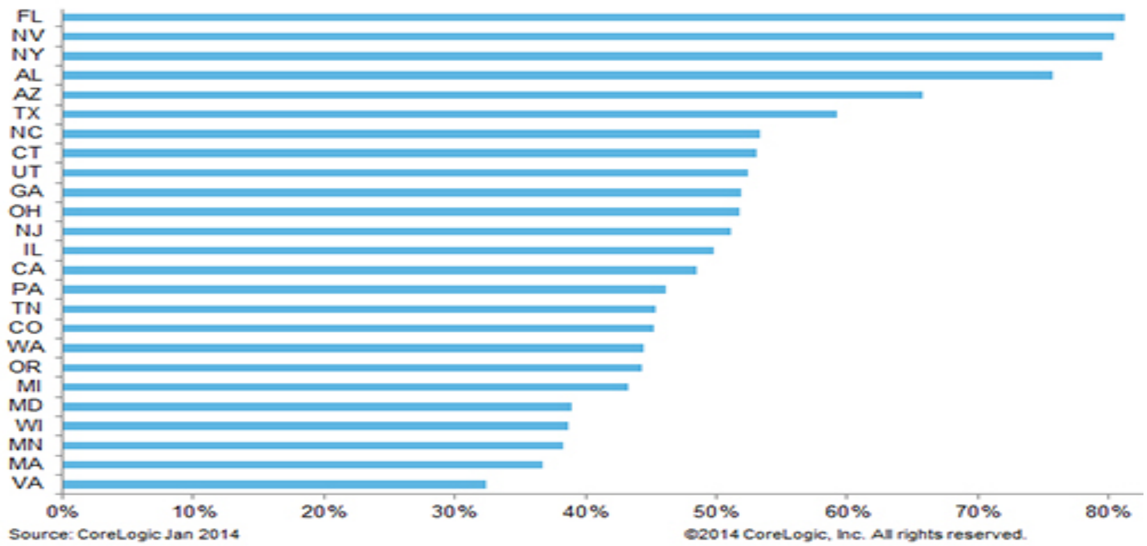
Figure 10: All-Cash Share of Total Condo Sales, Multnomah County, 2002-2016 YTD



Source: RMLS

Nationally, there are a number of core condo markets (including Florida, Nevada, and New York) whose all-cash sales have been between 70%-80% of total condo sales – a sign that in the more built-up markets that had more distressed sales after the downturn, financing for purchasing a condo unit is especially difficult (Vitlo 2014).

Figure 11: All-Cash Share of Total Condo Sales, Various States, 2014

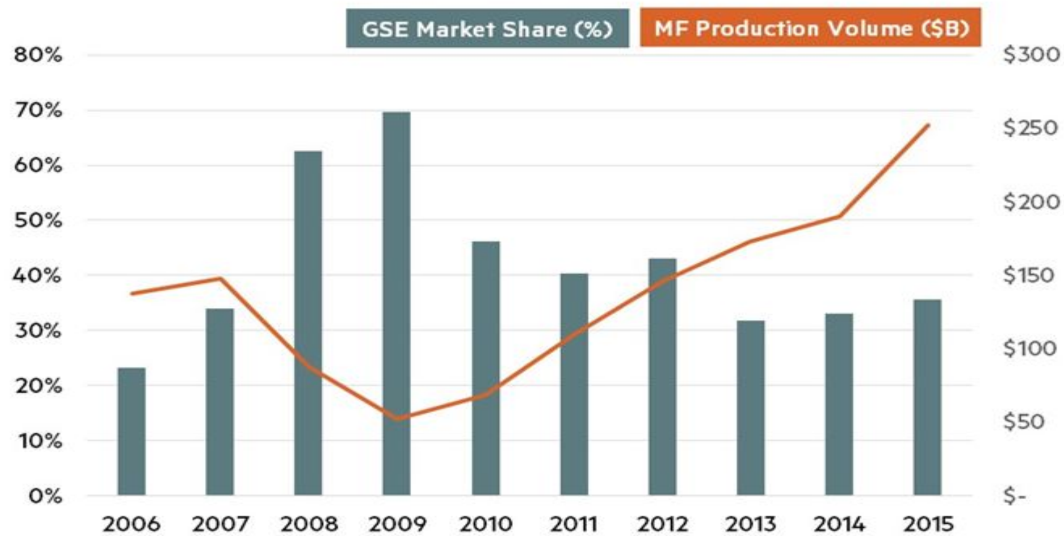


Source: CoreLogic

The John Ross Tower in Portland is a local example of the impact of the Great Recession on condo development. The 303-unit tower in Portland's South Waterfront neighborhood opened its sales office in 2005 – and took reservations for 229 units in 6 days. However, as the beginning elements of the recession and housing downturn came on in 2007, many of those reservations backed out of their sales closings. Unit buyers couldn't get mortgages, and some got scared that prices would no longer keep going up. By 2009, the project's developers lost the project to its lender, which then proceeded to auction off units at prices that were 50% off the original list prices. The developers lost their property (and the investment of their equity partners), the bank had to auction off the units at cut-rate prices, and early buyers saw their home values plummet once the auction re-established market prices for the building (Frank 2010). Fast forward to the present: Homer Williams, owner of one of the development companies behind the John Ross project, told the Portland Business Journal that condo development is "not a path that we're on at all." According to Williams, many developers got stung in the downturn and have not warmed to the idea of a large condo project (Bell 2015). In addition, margins can be higher for apartment projects, which also have fewer complications (i.e. liability) as compared to condo projects.

Banks and other capital providers (including the GSEs) have increased multifamily lending every year since 2009 (Urban Institute 2016). However, as apartments now represent over 90% of multifamily starts nationally, the bulk of this financing for development is going towards building apartments and not towards condos.

Figure 12: Multifamily Mortgage Market and GSE Share, United States, 2006-2015



Source: Urban Institute, using data from GSEs and MBA

LIABILITY ISSUES

In addition to the challenges presented by changes in demand and in available capital, developers of condo projects must also face another obstacle – liability issues. Following the Great Recession, there was an uptick nationally and in Oregon in construction defect lawsuits brought on by homeowner associations against developers and contractors. In Oregon, there is a 10-year statute of limitation on liability (the "statute of repose"), so developers and their insurers have a responsibility for a decade after a project is developed. In fact, it is common for homeowner associations to bring on lawsuits around Year 8 or 9, just prior to the end of the statutes of limitations, and in many cases the associations may even be found liable for breach of fiduciary duty if they do not file lawsuits within this timeline (Oregonlaws.org; Eyth 2016).

Developers can mitigate their risk by purchasing "wrap-up" insurance policies (also known as Owner or Contractor Controlled Insurance Product), where one policy covers all the participants in a development, including the developer, his general contractors, and sub-contractors. However, these policies often have various limits and exclusions which can still leave developers open to legal liability. In addition, these policies are an added cost – and can be a burden on the financial pro forma, especially for smaller projects or developments with lower-priced units. For larger projects, the cost per unit in Oregon tends to be $2,000-$4,000, or generally about 1%-2% of the unit sales price, and coverage is typically $25,000-$50,000 per unit (Page 2016). The added cost and risk and coverage limits likely favors the development of higher-priced condo units and larger developments in many markets – and that is what we are seeing in Portland. Hoyt Street's Cosmopolitan project is the first significant condo project in the Portland metro since the financial downturn. The 28-story tower in the north end of the Pearl District features 150 luxury units – 36 of which are priced over $1 million, in a market which saw just 48 condo sales of over $1 million in 2015 (Abragan 2016).

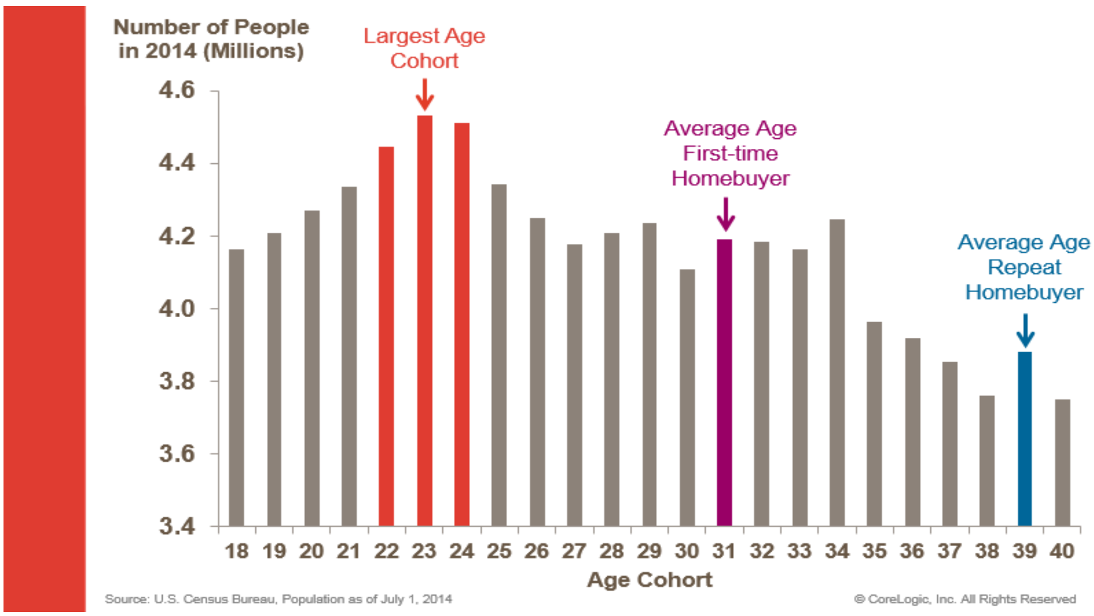
The potential liability, as well as the time and cost that could be involved in litigation, can be a deterrent of development. Chris Nelson, Principal of Portland-based developer Capstone Partners, told the Portland Business Journal: "the insurance, the reserves you have to set aside for future claims and the management of all that stuff, I have no interest" (Bell 2015). The Portland market has seen its share of construction defect lawsuits, including an ongoing case involving leaky plumbing valves in multiple buildings. Importantly, when a project is involved in litigation – which could take years, as is the case with the plumbing lawsuits – lenders will typically not issue loans for units in the project (Njus 2015). This leads to difficulty in selling units and is one of the reasons that all-cash purchases have become increasingly common in Portland and across the country.

Developers in other states must also deal with construction defect liability issues, and there have been recent attempts to mitigate the impact of these laws. Nevada passed the Homeowner Protections Act in 2015, which restricts the definition of what constitutes a home defect, repeals a provision allowing attorney fees and costs in a home defect judgment, requires specific descriptions of defects, and, importantly, reduces the statute of limitations to 6 years (from up to 10 years in current law) (Hudson 2015). Cities across Colorado have also recently enacted legislation to mitigate construction defect laws, with the express intent of encouraging condo development, especially at relatively affordable price points. Denver's City Council adopted a law at the end of 2015 that requires consent of a majority of homeowners (and not just Board members) before litigation can be pursued, requires alternative dispute resolution (arbitration or mediation), eliminates technical code violations as causes for action, and requires that actual damages, injury, or risk be demonstrated (Fernandez 2015).

LOOKING AHEAD

Despite the challenges outlined in the above sections, there are many potential tailwinds that should help to boost condo development in Portland and across the country. First, demographics favor homeownership in the long-term. According to CoreLogic, household formation across the country doubled in 2015 compared to 2014 as an improving economy allowed more young people to get into the labor force and out of their parent's house. The youngest members of the Millennials, who are helping to drive growth in the rental markets, will enter prime first-time homebuying years over the 5-8 years – and surveys consistently show that members of this generation have similar desires to own homes as their parents' generation. Affordability issues, delayed family formation, and desire for proximity to work and amenities should mean that many of these future first-time buyers will be looking at condo units as choices for homes – if they can find condos that meet their needs and budgets. In fact, the NAR reports that the older segment of Millennials are currently the largest group of home buyers, but that they are not finding affordable product in city centers; the NAR's chief economist, Lawrence Yun, noted that "limited inventory in Millennials' price range, minimal entry-level condo construction and affordability pressures make buying in the city extremely difficult for most young households" (NAR 2016). In addition, the largest cohort of Baby Boomers will reach retirement age in the next 5-8 years, and should fuel demand for "empty-nester" condos. These trends should impact Portland as well as other major metro areas across the country (Nothaft 2015).

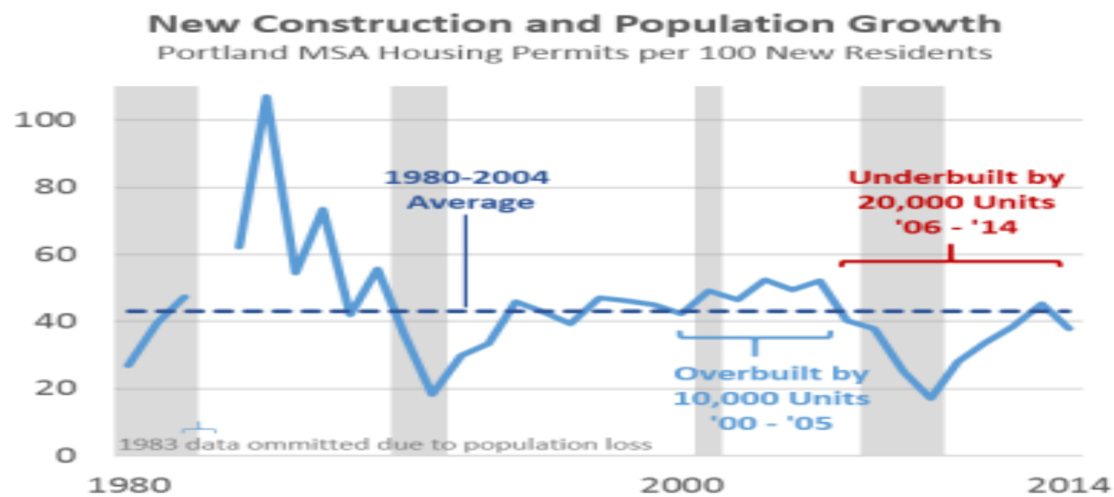
Figure 13: Population by Age Cohort, United States, 2014



Source: CoreLogic, based on data from U.S. Census

In fact, Portland is currently playing "catch-up" in building its housing stock, as the Oregon Office of Economic Analysis estimates that despite overbuilding 10,000 units between 2000 and 2005, the MSA "underbuilt" by 20,000 units between 2006-2014 (taking into account the historical number of housing permits per new residents) (Lehner 2015). This helps to explain the strong price growth seen in condo and single family prices the past few years, as demand is likely out-stripping existing supply – and suggests that new development, especially of lower-priced units, would be successful even in today's market.

Figure 14: Housing Permits per 100 New Residents, Portland MSA, 1980-2014



Source: Oregon Office of Economic Analysis, based on data from U.S. Census, Portland State University, and State of Washington

Second, the main GSEs – Fannie Mae, Freddie Mac, and FHA – have either relaxed, or signaled that they would ease, the stringent regulations imposed on condo units (and condo projects) in the wake of the Great Recession (Dawson 2014; Harney 2016). This should lead to more projects that are "warrantable" – and therefore to more condo units that can get traditional financing, including FHA loans, which are especially important for first-time buyers. This will likely have a ripple effect – as the GSEs increase the number of financeable condo units, more buyers will be able to purchase units, which will help convince banks that they can lend on the construction of new condo projects. With limited new inventory in most markets, the easing of financing should help to stimulate the development of new units.

Third, the wave of legislation in various municipalities across the country that is reining in construction defect lawsuits could spread to other areas – including to Oregon or Portland. As cries for affordable housing in the Portland metro increase in intensity, it is conceivable that lawmakers could help to mitigate the litigation issues that are keeping some developers on the sidelines. Liability issues will also keep many apartment projects from converting to condos as demand ramps up, as many contractors require that owners and developers agree not to convert their projects to condos during the statute of limitations period – providing more of a boost for new condo development (Eyth 2016).

And lastly, in Portland there is discussion currently in the City Council about "middle housing" zoning options for increased density within single family neighborhoods. If adopted in the upcoming Comprehensive Plan, this re-zoning of certain areas of the city could encourage small-scale condo development, in the form of projects of 2-4 units (Redden 2016). Portland has also seen a rise in the development of accessory dwelling units, or ADUs, on single family home lots. These ADUs have typically been used by the homeowner or rented out, but there are a few developers who have turned ADUs (and the home with which they share a lot) into condos, bringing a relatively affordable for-sale option into close-in areas that have seen rapid price growth (Law 2016)

Condo development has indeed come back in certain parts of the country, such as Miami and New York City. Nationally, the condo share of all home sales is approaching pre-recession levels of around 12% (Khater 2014). In Portland and Seattle, the first condo projects are nearly completed, and have had success with pre-sales. It is unlikely that Portland will experience a condo boom like the mid-2000s, but there are many reasons to believe that it and the rest of the country will continue to see a resurgence of condo development as long as strict financial regulations (such as FHA mortgage rules) are eased and frivolous construction defect lawsuits are mitigated. ■

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CROSS LAMINATED TIMBER: THE FUTURE OF MID-RISE CONSTRUCTION

ANDREW CRAMPTON

Portland State University

Cross laminated timber (CLT) is an established construction method that has the potential to revolutionize mid-rise construction in the United States, and revitalize the timber production industry in Oregon. CLT was originally created in Switzerland in the early 1990s. It consists of panels with multiple layers of wood oriented crosswise that are bonded with structural adhesives, and pressed to form a solid, straight, rectangular panel. Finished CLT panels are typically 2 feet to 10 feet wide, with lengths up to 60 feet and thickness up to 20 inches.[1] This allows it to be used for long spans in floors, walls, or roofing.

The prefabricated nature of CLT panels makes it fast and easy to install, generating almost no waste on the job site. CLT panels are prefabricated with pre-cut openings for doors, windows, stairs, service channels, and ducts, and shipped directly from the manufacture where they can quickly and efficiently lifted into place. The panels are shipped with preinstalled lifting straps to effectively utilize

[1] Evans, L. Cross laminated timber: Taking wood buildings to the next level. American Wood Council. MAT240-A – Cross Laminated Timber. 2013.

■ **Andrew Crampton** 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.

just-in-time construction methods and provide substantial savings on construction timelines.

There are more than 500 CLT buildings in Europe. Due to more restrictive building codes and a lack of established production chains, there are only a handful in the United States. The Oregon Forest Resources Institute is aware of six to eight CLT projects under construction or complete in the U.S [2]

The local advancement of CLT research and production has been encouraged by numerous local and national grant programs. Oregon is considered a national leader in CLT research, production, and construction. Oregon BEST and a newly established collaboration between Oregon State University and University of Oregon called the "Center for Advanced Wood Products Manufacturing and Design" are working to support expansion of Oregon's manufacturing capacity to produce CLT. An innovative project from Portland-based LEVER Architecture in the Pearl District, was one of two teams to win a $1.5 million dollar prize at the U.S. Tall Wood Building Prize Competition, a contest sponsored by the U.S. Department of Agriculture, the Softwood Lumber Board and the Binational Softwood Lumber Council.

D.R. Johnson Wood Innovations located in Riddle, OR recently became the first manufacturer in the United States to receive certification from the American Plywood Association (APA) to produce cross-laminated timber. Currently, the maximum panel size that can be produced at their facility is 10 feet × 32 fee × 3, 5,

[2] Andrews, G. Material differences: CLT becomes divisive. *Daily Journal of Commerce.* May 4, 2016.

or 7 feet layers. These extended lengths help to meet longer length construction requirements and increased specification.[3]

As of January, 2015, the State for Oregon Building Codes Divisions approved a statewide alternate method (No. 15-01) that will allow the use of CLT for Type IV, Heavy Timber buildings, a construction type that utilizes larger, exposed wood structural members that have minimum sizes for code required fire-resistive requirements. Currently, Oregon is the only US state to have formally adopted the use of CLT as a Heavy Timber component, however the 2015 IBC code update allowed for submittal of CLT materials as part of the "alternative designs sections of the IBC with allowing local amendments.[4] This will take substantial communication and coordination between regulating governments and project teams.

A 2014 CLT construction feasibility study by Mahlum Architecture, Walsh Construction and Coughlin Porter Lundeen found that CLT construction costs on an 8-story building with a two-story concrete platform would be four percent less than the costs of a 10-story concrete building. The study used a cast-in-place concrete frame structure with post-tensioned concrete floor decks as the base-line cost model. The study also highlighted the need for experienced CLT project engineers, which can a significant potential cost increase. As the Portland market adds CLT engineers, cost saving are expected to surpass the 4 percent baseline estimate.[5]

CLT has the potential to provide a catalyst for mid-rise structures taller than 7-story podium style development, while being more cost effective than high-rise steel construction. The Mahlum study identified that common assumptions for the Seattle market dictate that concrete is too expensive for building only slightly above midrise at heights above 75 feet and lower than around 125 feet. Often, non-high rise lots are built using 5-over-2 construction with 5 stories of light wood frame construction built on top of 2 stories of concrete. This construction method leaves development potential unrealized in high demand areas outside of central city cores that do not have market demand or supportive zoning for high-rise steel construction.

The recent update to the Portland Comprehensive Plan and Zoning Code, coupled with new challenges of impending inclusionary zoning laws and escalating development fees provide a unique opportunity to promote needed mid-rise construction. These large-scale planning code developments should anticipate the potential for allowing and even supporting this development type.

The Portland Planning Bureau is incorporating new mixed-use zones outside the central city core as part of the Comprehensive Plan Update. Although not a likely

[3] Law, S. Grant will help develop Oregon's first cross-laminated timber plant. *Portland Tribune*. October 23, 2014.

[4] State of Oregon, Building Codes Division. No. 15-01: Cross laminated timber provisions. January 15, 2015.

[5] Mahlum, Walsh Construction, and Coughlin Porter Lundeen. CLT feasibility study: A study of alternative construction methods in the Pacific Northwest. May 14, 2014.

substitute to high-rise construction that is prevalent in the City's Central Core, the proposed Urban Center Civic Corridor Mixed Use zones along designated corridors should be adjusted to allow mid-rise construction.

The proposed Mixed Use zones are scheduled for public hearings with City Council late 2016 and ultimate adoption in 2018. The Commercial/Mixed Use 3 (CM3) zone is a large-scale zone intended for sites in high-capacity transit station areas, in town centers, along streetcar alignments, along civic corridors, and in locations close to the Central City. Additionally, the CX Central Commercial and EX Central Employment zones located outside the Central City Plan provide potential for CLT mid-rise construction, and their maximum height are under discussion.

The public amenity of high-quality environments fostered by CLT construction in conjunction with promoting an Oregon-bred industry provides the potential to be incorporated into the density bonus program. Additionally, the limited waste and renewable materials of CLT have sustainability benefits that have public benefit standards that should be incorporated into the FAR Bonus system as part of the Planned Unit Developments allowed in the mixed-use zones.

As proposed, the maximum zone height under a Planned Unit Development on site over 2 acres in size are below. This bonus should be adjusted to allow height bonuses for sites less than 2 acres in size, and the public amenity benefits of CLT could be a factor in considering allowing height bonuses for projects that utilize this construction method.

In order to be eligible for the PUD bonuses, a portion of the development will need to provide affordable housing. Eligible projects can earn up to 100 percent of bonus floor area when 25 percent of floor area in excess of base floor area allowance is housing affordable to households earning less than 80 percent of the area median family income. The soon to be newly implemented inclusionary zoning standards will have a significant impact on project feasibility across all construction types spectrums, and should be considered in conjunction with allowing additional mid-rise construction.

	CM2	**CM3**	**CE**
Base Height Limit (Stories)	45'	65'	45'
PUD Maximum Height Limit	75'	120'	75'
Maximum PUD FAR	4 to 1	5 to 1	4 to 1

The increased popularity of this product stems from a multitude of advantages, such as mass production, prefabrication, customization, rapid construction, and reduced environmental impacts. Additionally, the lighter materials compared to concrete and steel will be advantageous on construction sites located on poor soil quality and lead to dramatic construction cost savings.

CLT has the potential to provide a transformative mid-rise construction type to the Portland market. The burgeoning Oregon market combined with the visual amenity enhancements compared to standard light wood or concrete building materials provide a potential political base to allow increased mid-rise heights along designated corridors and centers outside the downtown core. Portland should study during the Zoning Code updates the possibility of increased 75–120 feet development heights along corridors and locations not suitable to high-rise construction in order to promote this type of development. ■

THE STATE OF THE ECONOMY

Andrew Crampton

Portland State University

Oregon is continuing to experience rapidly rapid growth as job gains and wage increases for Oregon workers are outpacing the national average. The June 2016 State of Oregon Economic and Revenue Forecast projects that the state's economy is quickly approaching full employment. Such a milestone has not occurred in Oregon since 2000. Additionally, underemployment, or those involuntarily working part-time in Oregon is back to pre-recession rates. Given the ongoing economic strength in Oregon, the economic outlook has been raised relative to recent forecasts. Economists working for the state project "full-throttle" rates of growth through the end of 2017. In addition to strong job growth, Oregon average wages are at their highest point since the early 1980s recession, with much of the improvement occurring in the past two to three years.

Oregon's revenue growth has been solid and aligned with expectations; Oregon's expected General Fund revenue sources in 2015-2017 are currently within 0.2 percent of the estimated General Fund revenue forecast projected at the end of the annual legislative session. However, reflecting national trends, corporate tax collections have decreased in recent months.

Corporate tax collections have started to contract in recent months. Nationwide, corporate profits are falling, largely due to rapid appreciation of the U.S. dollar, and struggles among energy firms and other commodity producers. However, the Oregon

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Office of Economic Analysis reports that Oregon corporate tax collections remain large relative to historical norms. Corporate tax revenues are expected to exceed the 2 percent kicker threshold by $10.4 million, generating a kicker amount of $32.3 million.

Due to the better-than-expected economic activity so far in 2016 and the likely limited impact of Brexit, the IMF global growth forecasts for 2016 and 2017 were both marked down by 0.1 percentage points relative to the April 2016 outlook, to 3.1 percent and 3.4 percent, respectively. The outlook worsens for advanced economies (down by 0.1 percentage points in 2016 and 0.2 percentage points in 2017) while it remains broadly unchanged for emerging market and developing economies.

The primary global financial impact from the Brexit vote will be short and medium term uncertainty as politicians have imperceptibly begun the increasingly lengthy and complex withdrawal process. However, the Global Bank Senior figures in both Great Britain and the European Union have both admitted they have only just begun preparing for a protracted negotiation with a timeline that continues to slip further and further out. Negotiations could easily slip so that formal, face-to-face talks on substance do not being until fall 2017 or even early 2018. However, the June 2019 European Parliament elections will be a key milestone for negotiations.

Table 1: Key Economic Indicators, Portland MSA, Oregon, and US Q2 2016

	Q2 2016/ Jun-15	Q1 2016/ Mar 2015	Q4 2015/ Dec 2015
GDP Growth (annualized)			
US	1.2%	0.8%	1.4%
Unemployment Rate			
US	4.90%	5.0%	5.0%
OR	4.80%	4.5%	5.5%
Portland MSA	4.9	4.2%	4.9%
Job Growth Rate (12-mo growth)			
US	1.7%	2.0%	2.0%
OR	3.5%	3.5%	3.2%
Portland MSA	3.1%	3.3%	3.1%
Inflation (12-mo unadjusted)			
US	1.00%	0.9%	0.7%
Interest Rates			
Federal Funds Rate	0.39%	0.4%	0.2%
10-Year Treasury	1.46%	1.9%	2.2%

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

GLOBAL TRENDS

In the United States, first-quarter growth was weaker than expected, triggering a downward revision of 0.2 percentage points to the 2016 IMF growth forecast. High-frequency indicators such as Standard & Poor's Corporation and Economic Cycle Research Institute (ECRI) point to a pick up in the second quarter and for the remainder of the year, consistent with fading headwinds from a strong U.S. dollar and lower energy sector investment.

Productivity growth in most advanced economies remained sluggish, and inflation was below target owing to slack and the effect of past declines in commodity prices. Indicators of real activity were somewhat stronger than expected in China, reflecting policy stimulus, as well as in Brazil and Russia, with some tentative signs of moderation in Brazil's deep downturn and stabilization in Russia following the rebound in oil prices.

The impact of Brexit is projected to be relatively limited for the United States, as lower long-term interest rates and a more gradual path of monetary policy normalization are expected to broadly offset larger corporate spreads, a stronger U.S. dollar, and some decline in confidence

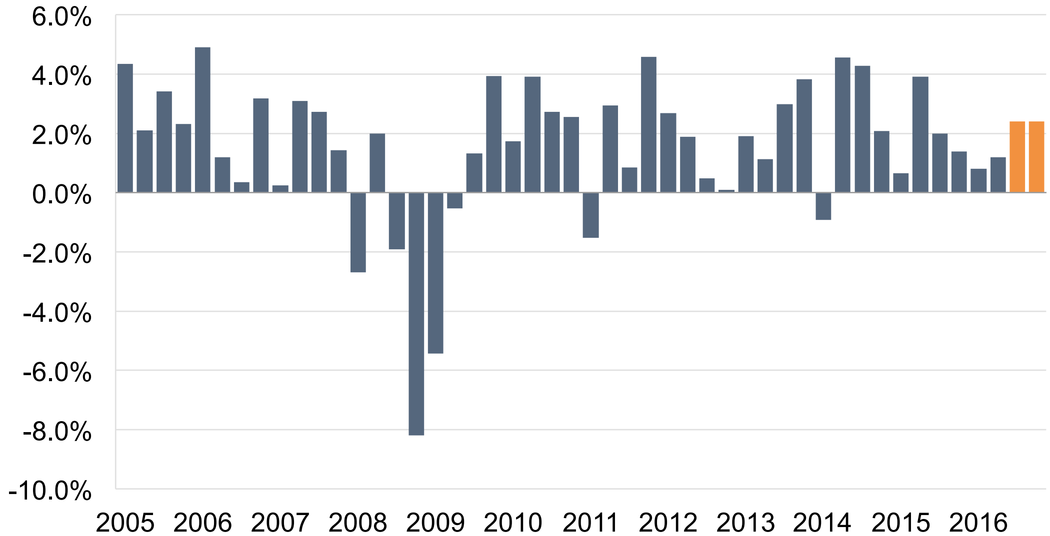
While global industrial activity and trade have been lackluster amid China's rebalancing and generally weak investment in commodity exporters, recent months have seen some pick-up due to stronger infrastructure investment in China and higher oil prices. This was projected in the IMF April World Economic Outlook forecast, in which upwardly revised forecasts of growth in China over the next two years. In China, the near-term outlook has improved due to recent policy support. Benchmark lending rates were cut five times in 2015, fiscal policy turned expansionary in the second half of the year, infrastructure spending picked up, and credit growth accelerated.

The Wall Street Journal recession odds forecast for July is at the highest point post-recession, with a 21 percent chance of an US recession within 12 months, up from a 15 percent projection in December 2015. Before Britain voted to leave the European Union last week, the majority of traders believed the Fed would raise interest rates at least once in 2016, according to Bloomberg data. Since Brexit, though, those odds have plummeted to almost zero. In fact, according to traders, the probability of a rate cut is now larger than a rate increase.

GDP/OUTPUT

Real gross domestic product increased at an annual rate of 1.2 percent in the second quarter of 2016, according to the advance estimate released by the Bureau of Economic Analysis. In the first quarter, the revised GDP figure was 0.8 percent. In previously published estimates, first-quarter GDP was estimated at 1.1 percent. The 0.3-percentage point downward revision to the percent change in first-quarter real GDP primarily reflected downward revisions to residential fixed investment, to private inventory investment, and to exports that were partly offset by upward revisions to nonresidential fixed investment, to PCE, to state and local government spending, to imports, and to federal government spending.

Figure 1: Gross Domestic Product, United States, Annualized Percent Change, 2005–2016 Q2



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

Overall, the Portland economy is strong, with a couple concerning data points that could impact future growth. The Portland job growth rate over the last 12 months of 2.8 percent is noticeably faster than the 1.7 percent for the United States. This growth rate is on par with many other western metro regions, such as Seattle, San Francisco and Denver.

Despite positive economic growth, two warning flags have appeared in the local data recently. First, manufacturing employment has stopped growing, while all other major industries continue to show impressive growth. State economists have also flagged a lack of job growth in the past 12 months for "Employment Services," also known as "staffing services" or "temporary help." This industry tends to be a leading indicator for the larger economy and is very sensitive to changes in the business cycle. However, with a 4.4 percent unemployment rate, it is possible that both industries have just stalled after so many years of strong growth.

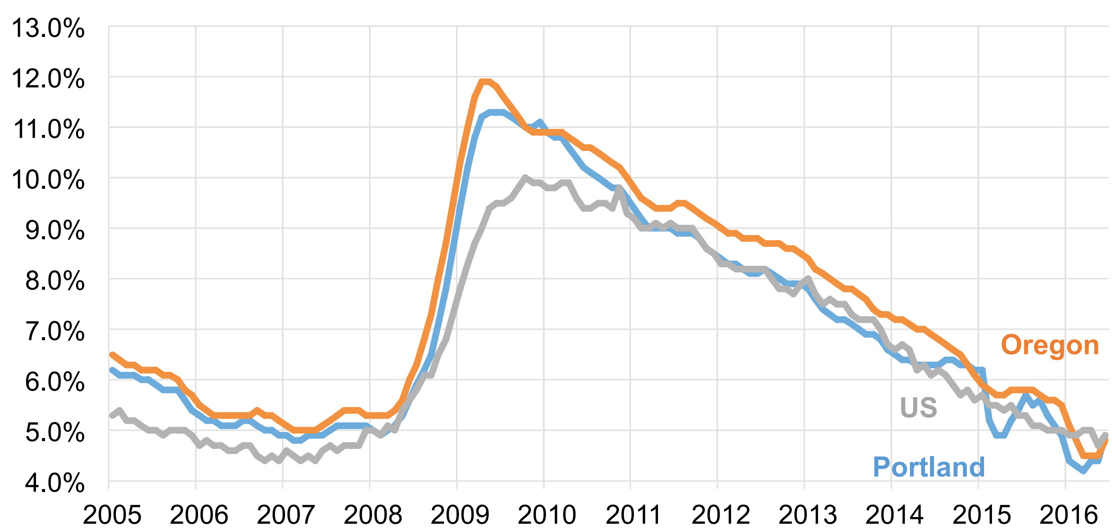
EMPLOYMENT

The Bureau of Labor Statistics (BLS) reported that total U.S. nonfarm employment increased by 287,000 in June and 442,000 for the quarter. This compares with growth of 228,000 in June 2015 and 752,000 for the first quarter of 2015. National unemployment figures remained steady at 4.9 percent, matching lows not seen since April 2008. The unemployment rate increased by 0.2 percentage point to 4.9 percent in June, and the number of unemployed persons increased by 347,000 to 7.8 million. These increases largely offset declines in May and brought both measures back in line with levels that had prevailed from August 2015 to April.

The unemployment rate for both Oregon and the Portland Metropolitan Statistical Area (MSA) increased to 4.8 percent and 4.9 percent respectively after historic first quarter lows primarily due to tightening manufacturing employment from the slumping US dollar, decreased corporate profits, and technology sector layoffs due to corporate restructuring. Despite these losses, state economists classify the state employment picture as "full-throttle," and have dampened their projections of a recession occurring in the next year.

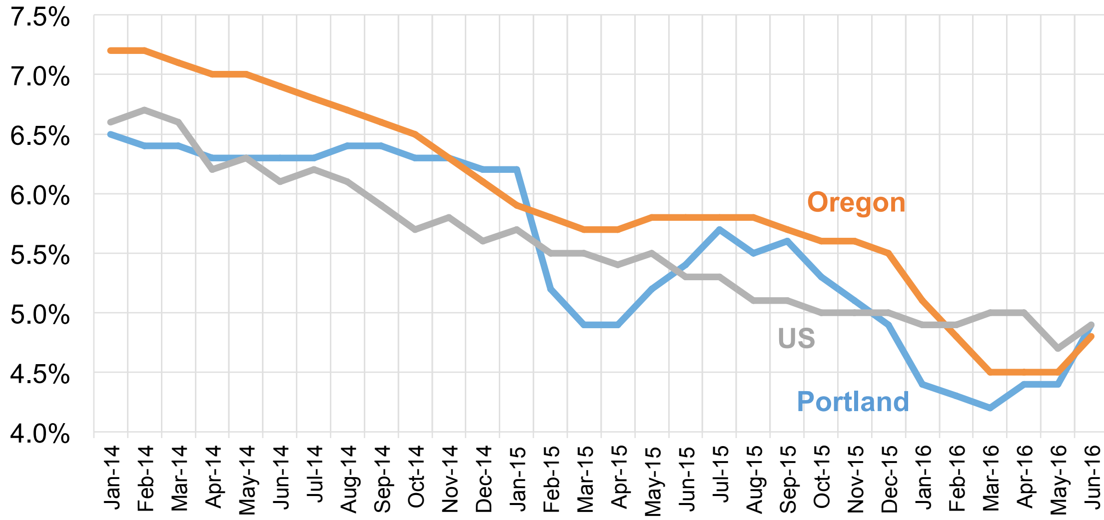
In positive news, construction is a strong growth market with one in seven new state jobs occurring in that industry. Construction added over 5,000 new jobs, with 8.9 percent growth rate. In the Portland market, construction jobs are fueled by rapid multi family building and recently escalating single family building with a projected year end output of 8,4042 single family units and 6,056 multi-family units.

Figure 2A: Unemployment Rate, Portland MSA, Oregon and United States, 2005-2016 Q2



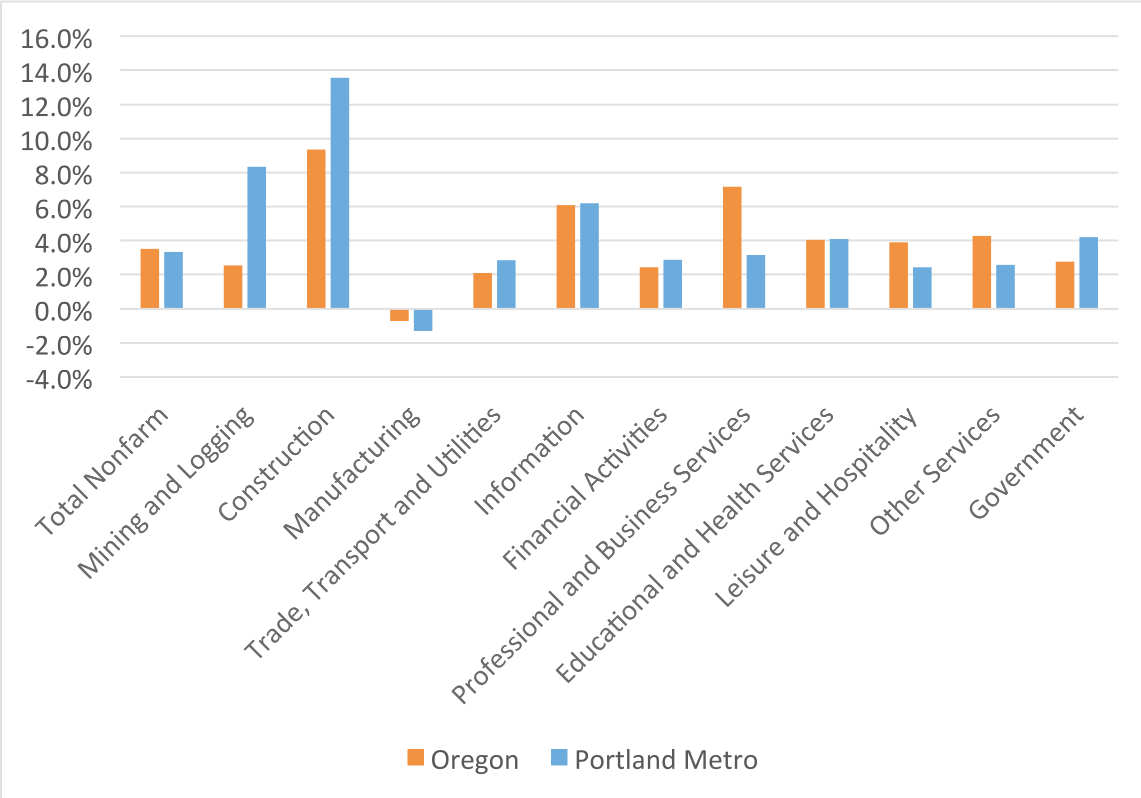
Source: Bureau of Labor Statistics

Figure 2B: Unemployment Rate, Portland MSA, Oregon and United States, Jan 2014-June 2016



Source: Bureau of Labor Statistics

Figure 3: Employment Growth Rate by Sector, Portland MSA and Oregon, 12 Months to June 2016



Source: Oregon Employment Department

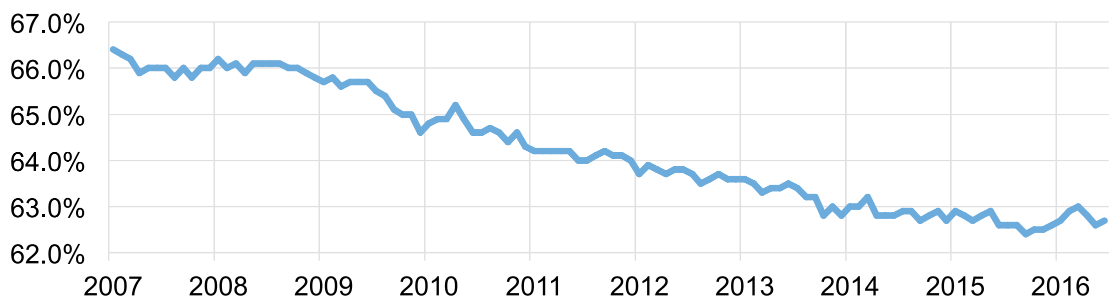
The job gains in 2015 and so far in 2016 are the best in the past two decades. Over the past two years the state has added 5,000 jobs every month, which translates into 3.5 percent growth on an annual basis. Such gains are stronger than the peak of the housing boom last decade. Only the mid-1990s boom saw comparable gains. At that time, employment gains were similar, nearly 5,000 per month, however growth rates were higher due to the smaller population and employment base.

Strong job gains have helped lead to relatively wage gains. According to Oregon's Office of Economic Analysis, "wages in Oregon are increasing at near double-digit rates, which is better than during the mid-2000s expansion but still below the 1990s gains. Average wages per worker are currently increasing 3-4 percent per year, which is faster than inflation of 1-2 percent per year. While national wage trends have just begun to accelerate in the past six to nine months, Oregon's have been strong for a couple years now."

Wage growth has been strong in the Portland MSA as well, and according to the Oregon Employment Department the metro area's hourly wage of over $19 is 14th highest among the 50 largest U.S. metro areas and 11 percent higher than the national average. As noted here the past few quarters, in the Portland MSA much of the growth in average wages has been driven by high-paying jobs, especially those in the software sector in Multnomah County.

Job growth in Oregon and Portland is expected to continue, driven by projected population growth and in-migration trends. However, the rate of growth is expected to moderate over the next two years. The Oregon Office of Economic Analysis expects job growth of 2.7 percent in 2016 and 2.6 percent in 2017, representing a slight downward revision from their prior forecast. This would translate to nearly 50,000 new jobs per year in the state over the next two years.

Figure 6: Labor Force Participation Rate, United States, 2007-2016 Q2



Source: Bureau of Labor Statistics

INFLATION

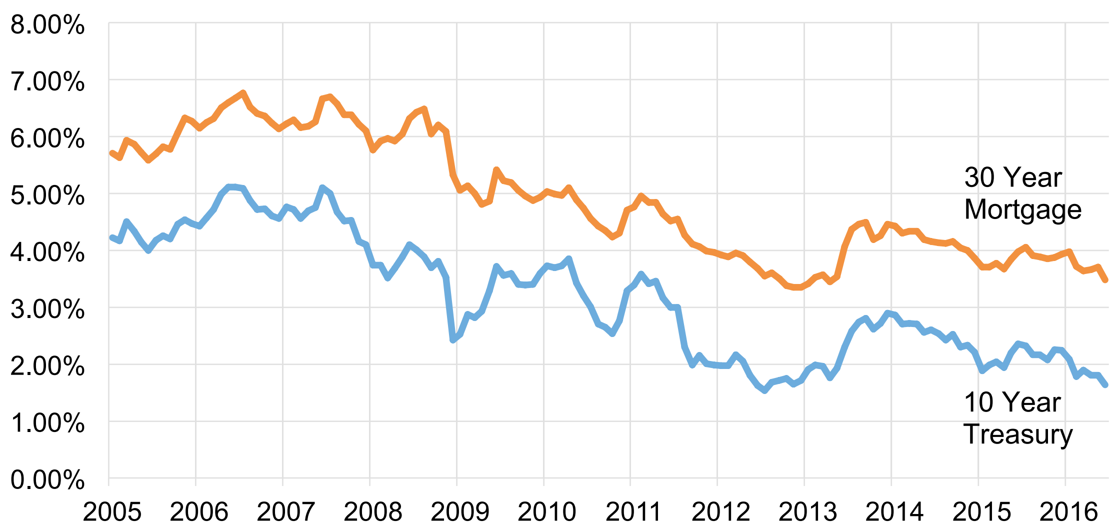
The Consumer Price Index for All Urban Consumers (CPI-U) increased 0.2 percent in June on a seasonally adjusted basis, the U.S. Bureau of Labor Statistics. Over the last 12 months, the all items index rose 1.0 percent before seasonal adjustment. For the second consecutive month, increases in the indexes for energy and all items less food and energy more than offset a decline in the food index to result in the seasonally adjusted all items increase. The food index fell 0.1 percent, with the food at home index declining 0.3 percent. The energy index rose 1.3 percent, due mainly to a 3.3-percent increase in the gasoline index; the indexes for natural gas and electricity declined. The Wall Street Journal's Economic Forecasting Survey projects that the unadjusted 12-month CPI will increase by 1.8 percent in December 2016 and 2.2 percent in June 2017.

INTEREST RATES

Given the strong unemployment data, the Federal Reserve opted to maintain the fed funds target rate in a range of 0.25 percent to 0.50 percent at its June meeting. Brexit induced global uncertainty also factored into the Fed's decision, said Chair Janet Yellen. While the median forecast of Fed policymakers remained at two additional rate hikes in 2016, the number of officials who see just a single move rose to six from one since the previous poll in March. The 10-year Treasury and the 30-year mortgage rate both declined to 1.46 percent and 0.39 percent.

In China, stocks finished flat as investors gauged the pace of the country's economic growth. Returns for the April data disappointed investors following encouraging readings during the first quarter. Concerns resurfaced over how much stimulus the government would provide to sustain growth and the amount of debt on corporate balance sheets.

Figure 7: Treasury and Mortgage Rates, United States, 2005-2016 Q2



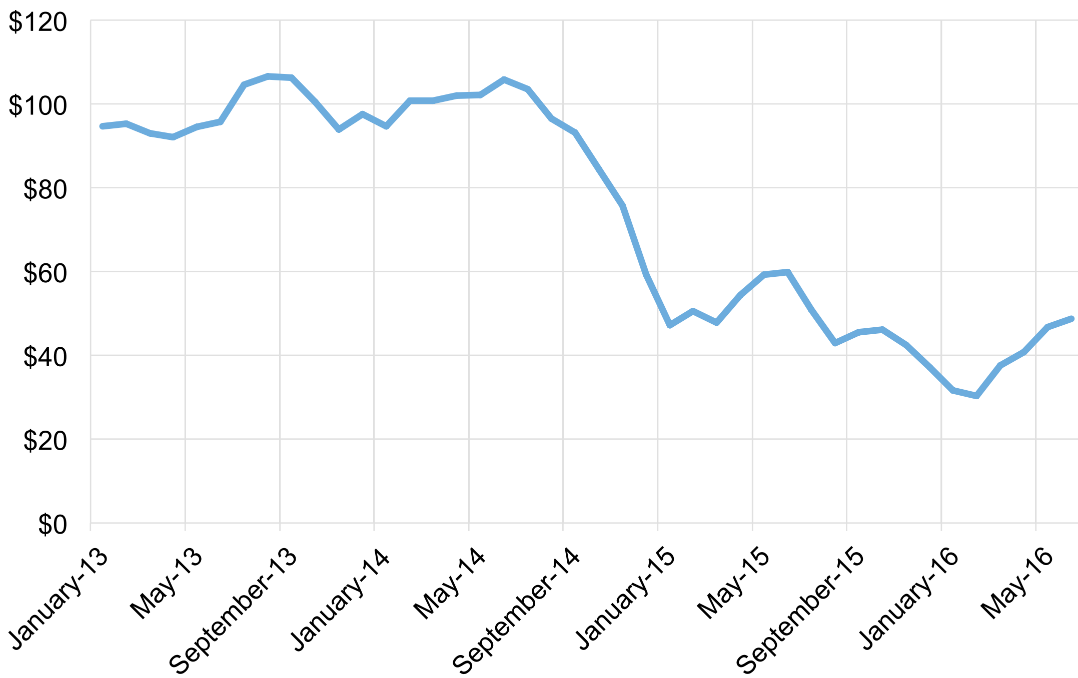
Source: Federal Reserve

CAPITAL MARKETS

Markets are dealing with political uncertainty from the fallout from Brexit but are assisted by prospects of a strengthening U.S. economy. Downside risks to global growth point to a U.S. Federal Reserve on hold. The U.S. economy grew far less than expected in the second quarter with inventories falling for the first time since 2011, but a surge in consumer spending pointed to underlying strength. Global stocks rose modestly in a volatile quarter marked by heightened concerns about threats to worldwide economic growth. Stocks initially dropped sharply after the June 23rd Brexit vote, but a strong bounce-back rally erased most of the losses. Rising oil prices fueled gains in the energy sector while consumer discretionary stocks declined. High-grade bonds, the U.S. dollar and gold rallied. The broad Standard & Poor's 500 Composite Index rose 2 percent; the Dow Jones Industrial Average also advanced 2 percent and the Nasdaq composite was flat. The quarter was characterized capital flight to established, safe sectors in light of global uncertainty. The telecommunication services and utilities sectors rose 7 percent, while consumer staples gained 5 percent. Information technology and consumer discretionary were the only sectors to post declines, losing 4 percent and 1 percent, respectively.

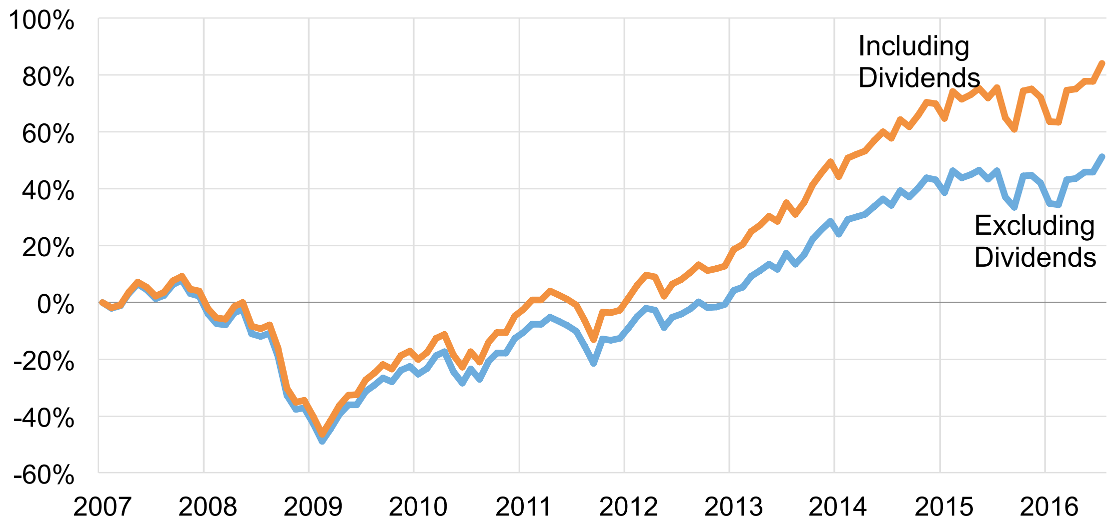
Declines in excess oil supply due to a slowdown in non-OPEC production and supply disruptions in Nigeria and Canada have helped recently increase oil prices and resulted in easing oil exporters' sovereign bond spreads from February-March highs. $48.76 in June, $46.71 in May and $40.75 in April. This could possible help the struggling oil production market in the United States.

Figure 8: Oil Price per Barrel (WTI Spot), 2013–2016 Q2



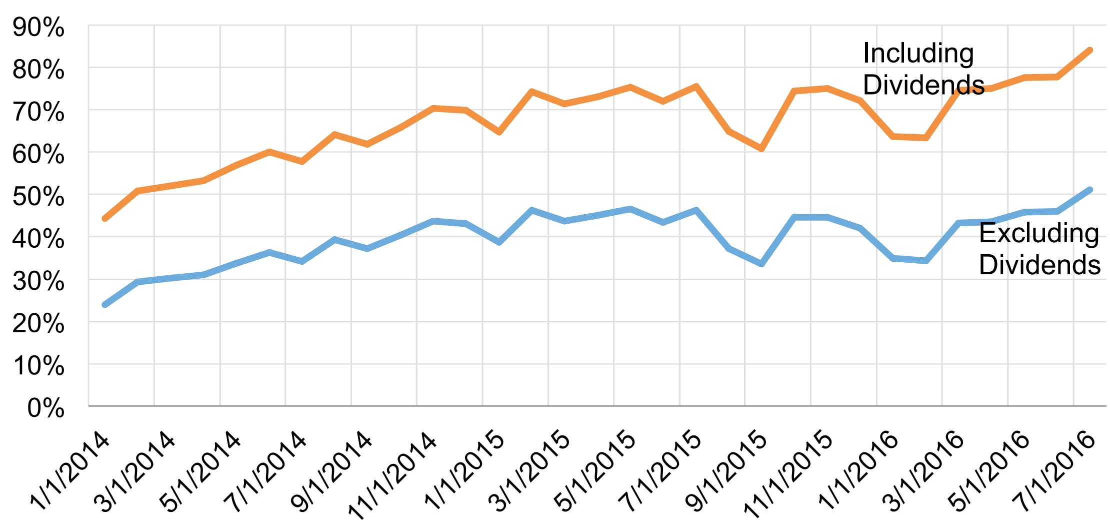
Source: US Energy Information Administration

Figure 9A: Standard & Poor's 500 Index, 2007–2016 Q2



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

Figure 9B: Standard & Poor's 500 Index, Jan 2014–July 2016



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

LOOKING AHEAD

Oregon and Portland's economies continued a strong economic performance in the second quarter with strong employment growth, however the dependence on manufacturing employment, which showed signs of slowing employment growth in the last quarter is concerning and could impact future growth projections.

As the U.S. economy enters the 84th month of expansion, including the longest string on monthly job gains on record, the outlook remains positive. The ongoing job gains and wage growth are pulling workers back into the economy and measures of slack, or underutilization, continue to improve. The U.S. economy is finally nearing full employment. ■

RESIDENTIAL MARKET ANALYSIS

ALEX JOYCE

RMLS Student Fellow
Master of Real Estate Development Candidate

Single family trends in the second quarter of 2016 were strong across the state. The active summer home buying season reversed trends compared to last quarter in every market analyzed here. Home prices were up in every market, and in many markets the increase was substantial even compared to last year.

Transaction volume jumped substantially compared to last quarter in every metro area, reflecting the seasonal uptick in activity. In most areas, transactions also increased compared to the same quarter last year indicating a continued long term expansion. However, the number of transactions in Portland and Bend declined compared to the same quarter last year. Vancouver's transactions were flat compared to last year. This could be due to a combination of factors, such as limited supply compared to demand or, related, historically high home prices.

Permits for new single family homes were down 14 percent statewide compared to last quarter with wide variation across the state. Portland's permit activity heavily influenced the state figures. Portland declined compared to last quarter, Bend was flat, while Eugene saw more than double the permits this quarter compared to both last quarter and the same quarter last year. Compared to the

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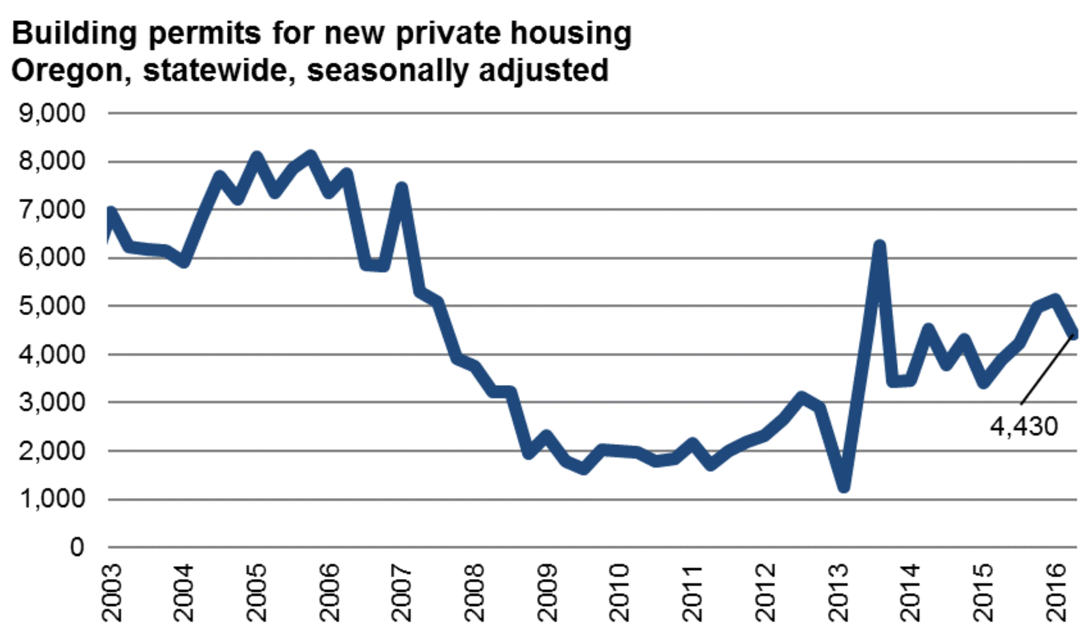
same quarter last year, permit activity is up nearly 30 percent, and up most substantially in markets outside of Portland.

National Association of Realtors shows existing home sales continuing to rise in most metros across the country. The national existing median single family home price is $240,700 in the second quarter – a 4.9 percent increase from the same quarter last year. Job growth, low mortgage rates and limited inventory are cited as reasons for the escalating home prices.

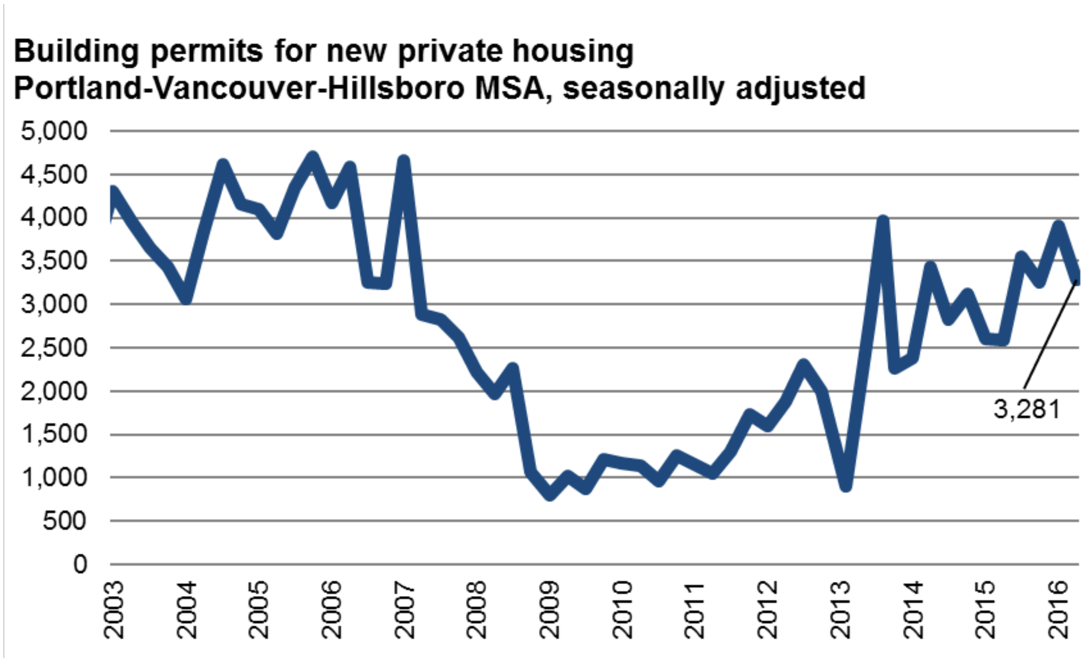
NAR's chief economist, Lawrence Yun, says, "Steadily improving local job markets and mortgage rates teetering close to all-time lows brought buyers out in force in many large and middle-tier cities." "However, with homebuilding activity still failing to keep up with demand and not enough current homeowners putting their home up for sale, prices continued their strong ascent – and in many markets at a rate well above income growth."

LOCAL PERMITTING

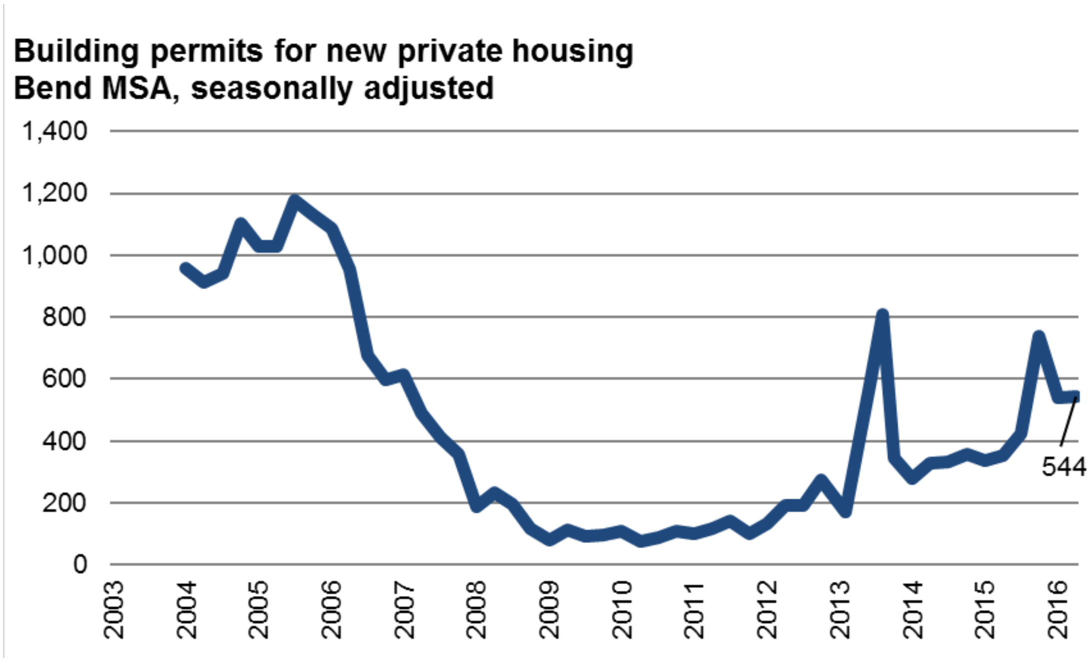
In the second quarter of 2016, 4,430 building permits for new private housing units were issued in total across Oregon. This is 14 percent fewer permits than were issued in the prior quarter but nearly 30 percent more than were issued in the first quarter of 2015.



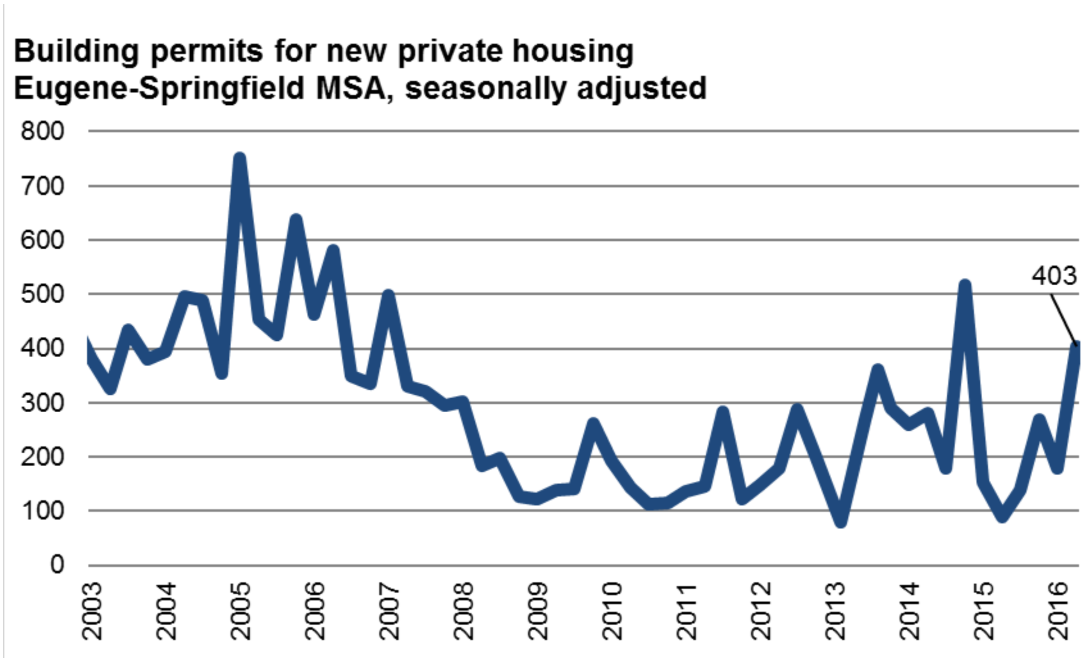
3,281 permits for new private housing units were issued in the Portland-Vancouver-Hillsboro Metropolitan Statistical Area (MSA) in the second quarter. This represents an 16 percent decrease in permits compared to the first quarter, but a 26 percent increase in year-over-year permitting. Over half of decrease in statewide permits compared to last quarter are due to the decrease in Portland permits. Permitting across the rest of the state was mixed.



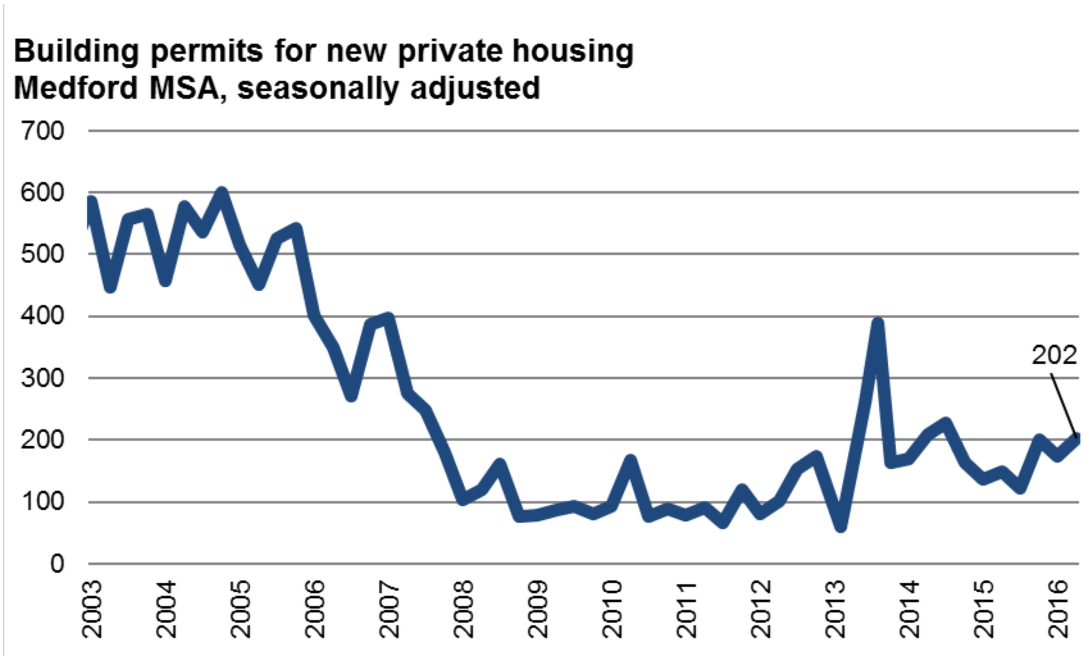
Bend MSA permitting remained flat compared to last quarter, rising from 541 to only 544 this quarter. Year-over-year increases remained high this quarter as they were last quarter, with a 62 percent increase compared to the the same quarter last year.



The Eugene-Springfield MSA's second quarter permitting jumped substantially compared to the single quarter slump last quarter. This continues the rise in new permits that began a year ago. Permitting for new private housing units totaled 403, which represents a 124 percent increase from last quarter and a 163 percent increase over the same period a year ago.



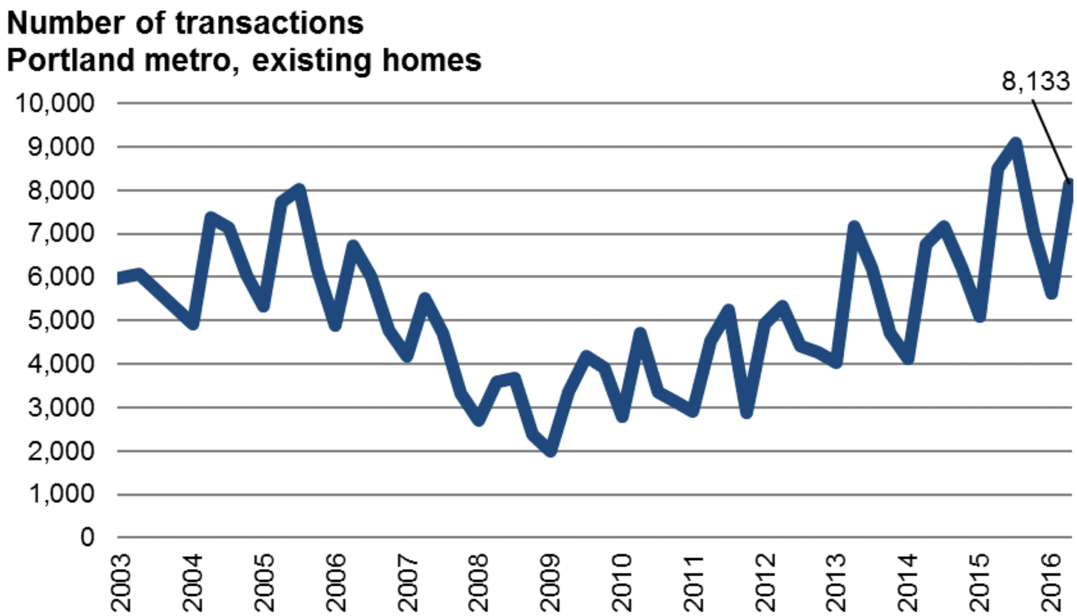
New permits in Medford MSA increased this quarter moderately, increasing 17 percent. Similar to other markets, the increased number of permits this quarter represents a substantial uptick from the same quarter last year – an increase of 47 percent.

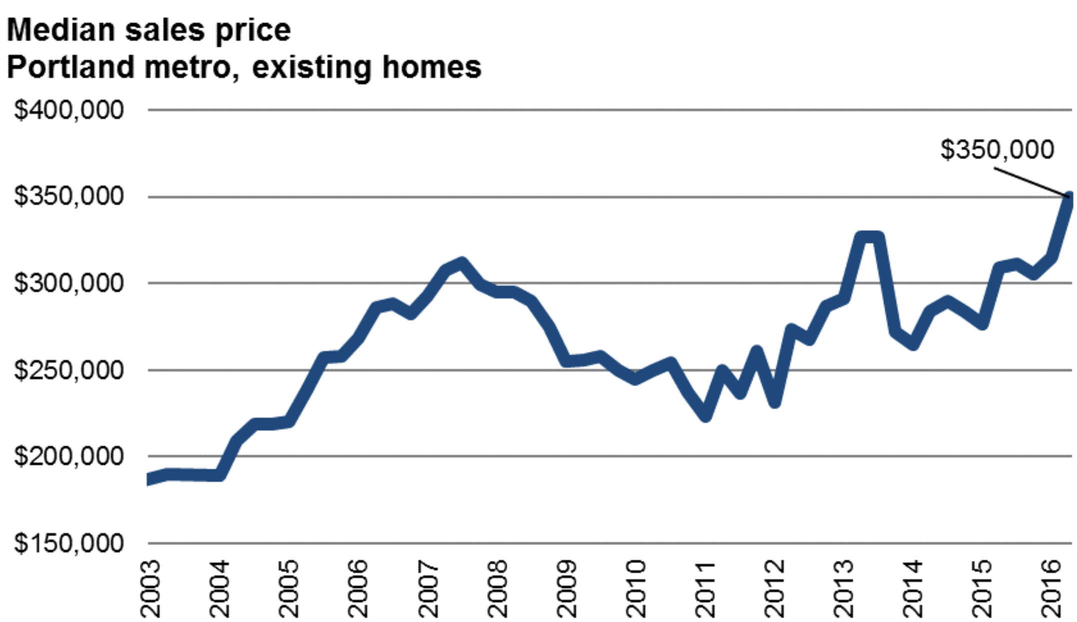


PORTLAND TRANSACTIONS

The second quarter saw seasonal increases in transactions and a substantial uptick in median sales prices in the Portland market. The number of transactions were 4 percent fewer than the same quarter last year. But the median sales price for existing homes increased 11 percent compared to last quarter and 13 percent compared to the same quarter last year. Compared to last quarter when the median price for existing homes was $315,000, this quarter the median price is $350,000.

The seasonal uptick in home buying drove down the average days on market for existing homes 36 percent from 41 to 26 compared to last quarter. This represents nearly 30 percent fewer average days on market compared to the same quarter last year. Final sales prices in the second quarter continued to be above list price, rising from 100.27 percent of list last quarter to 101.46 percent of list this quarter.


Number of transactions
Portland metro, existing homes
8,133
10,000
9,000
8,000
7,000
6,000
5,000
4,000
3,000
2,000
1,000
0
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016


Median sales price
Portland metro, existing homes
$400,000
$350,000
$350,000
$300,000
$250,000
$200,000
$150,000
2003
2004
2005
2006
2007
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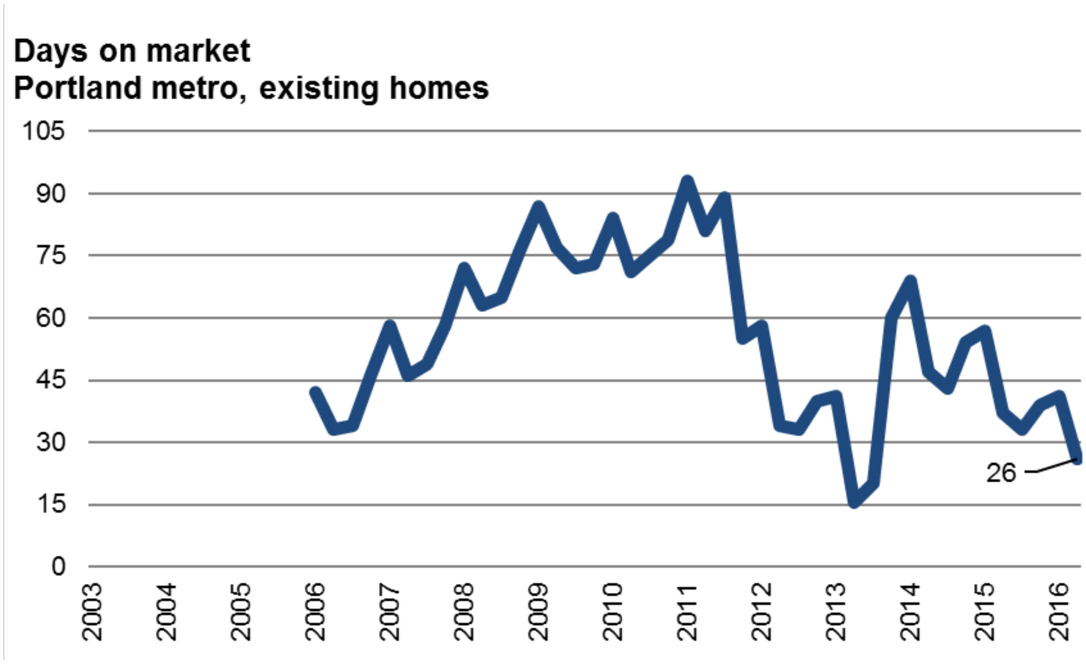
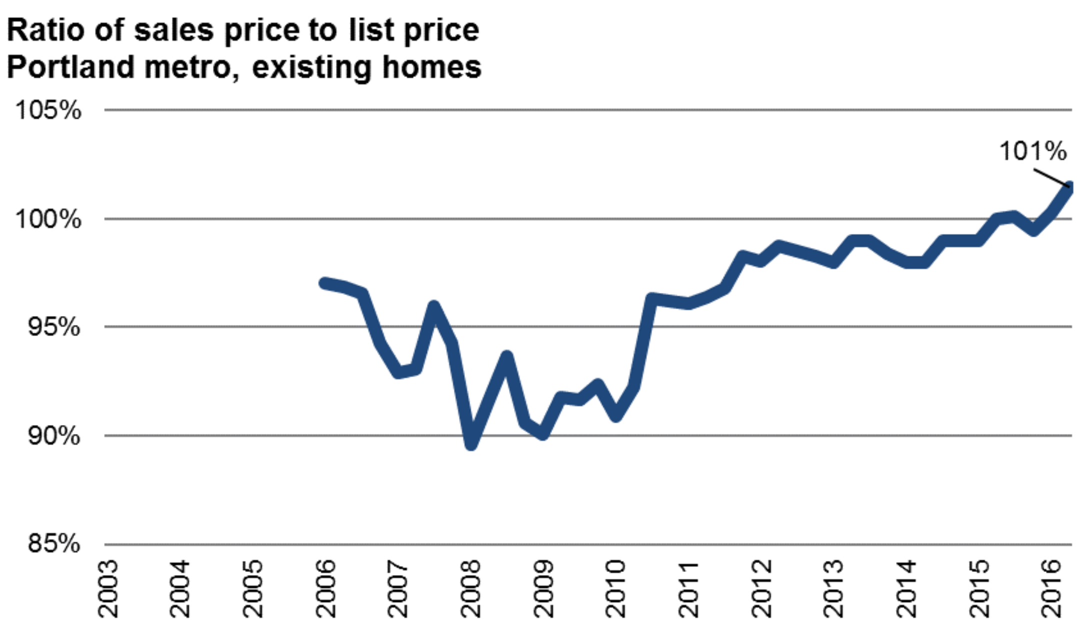
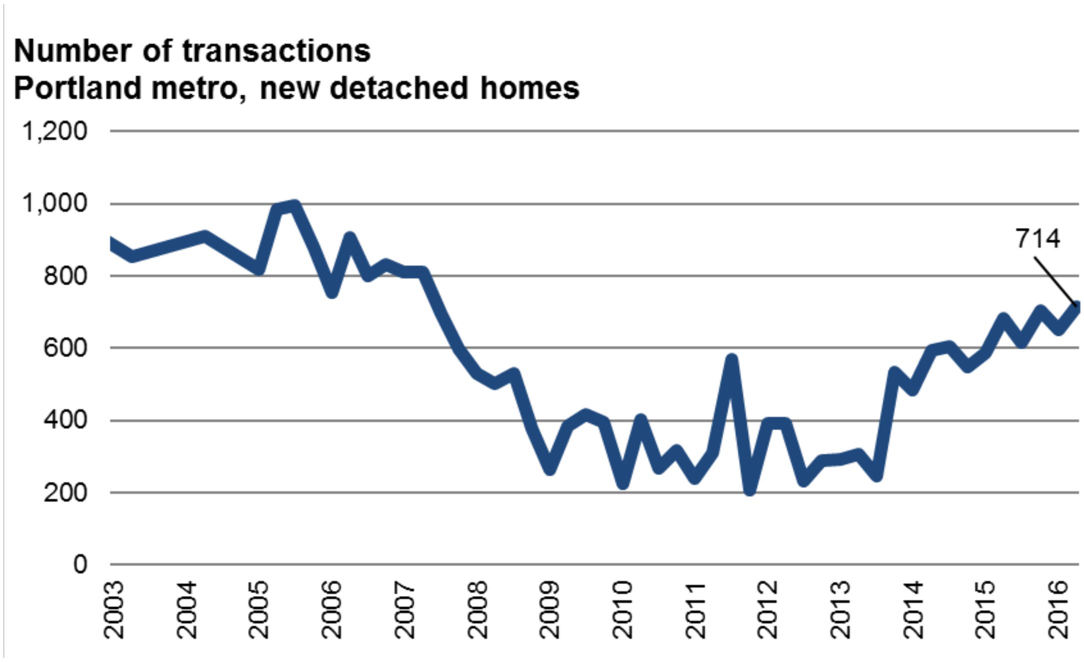
2012
2013
2014
2015
2016

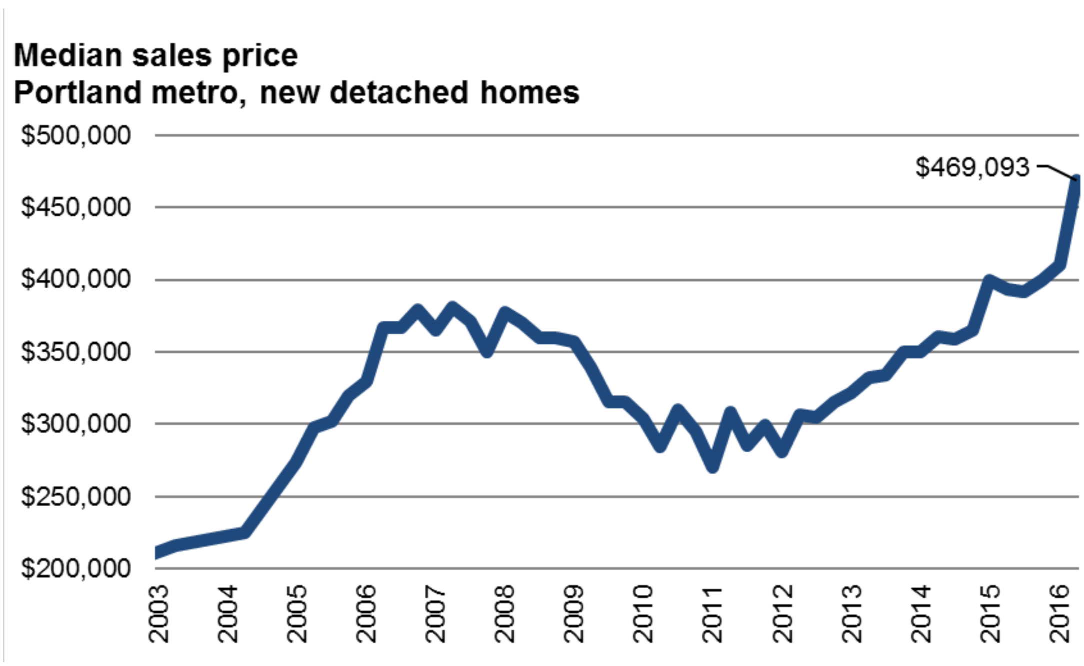




In the sale of new homes, the number of transactions saw over a 9 percent uptick compared to last quarter and a 4 percent increase compared to the same quarter last year. This runs counter to the declining year-over-year transaction count for existing homes in Portland.

New home median sales price saw an even more substantial increase than sales price for existing homes. Last quarter, the median sales price for new homes was $410,500 compared to $469,093 this quarter – an increase of 19 percent. Compared to the same quarter last year, new home prices have increased over $75,000 or 19 percent.

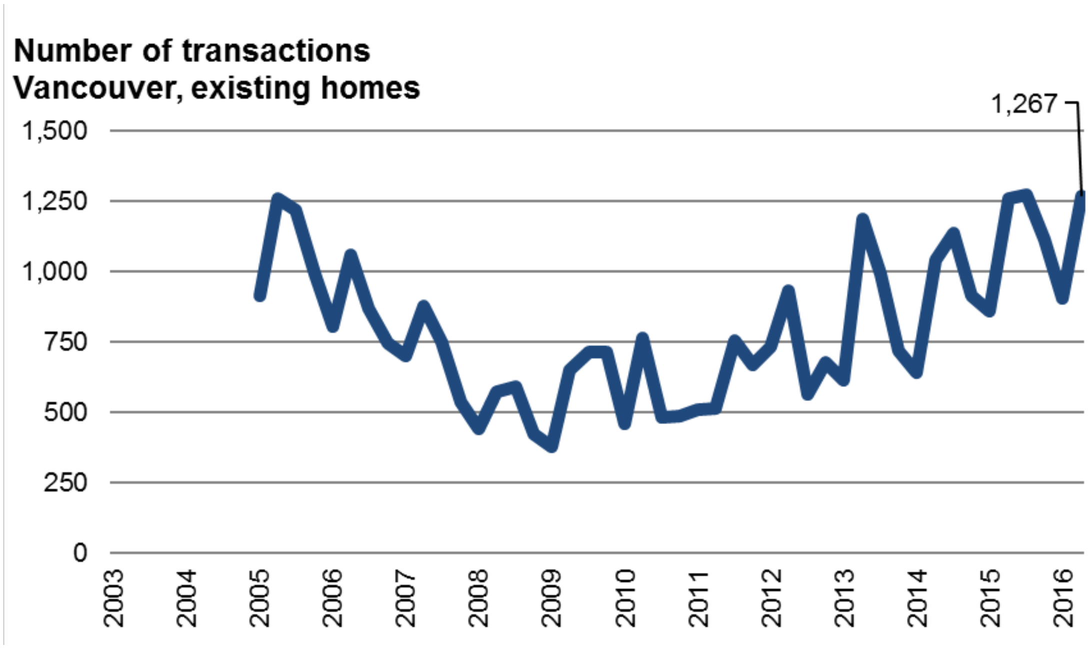


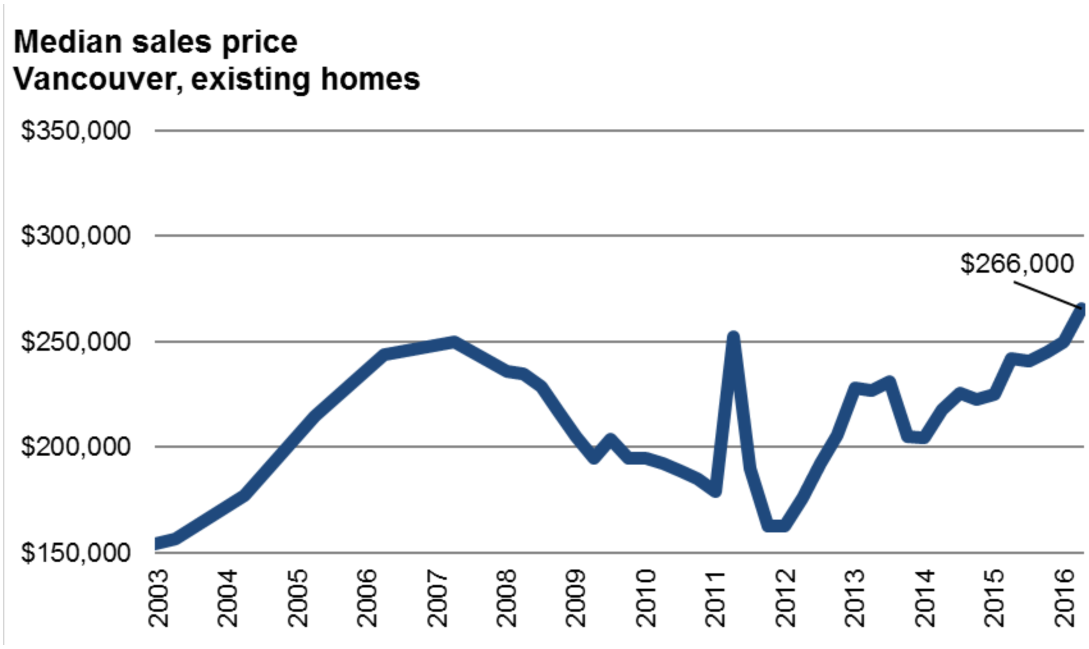


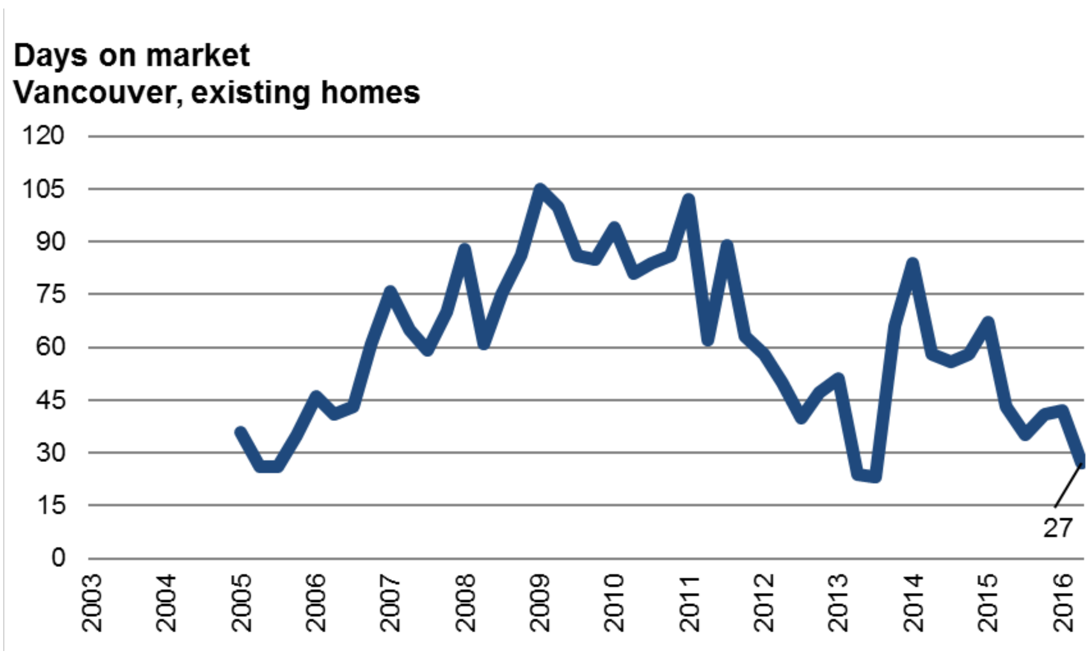
VANCOUVER AND CLARK COUNTY TRANSACTIONS

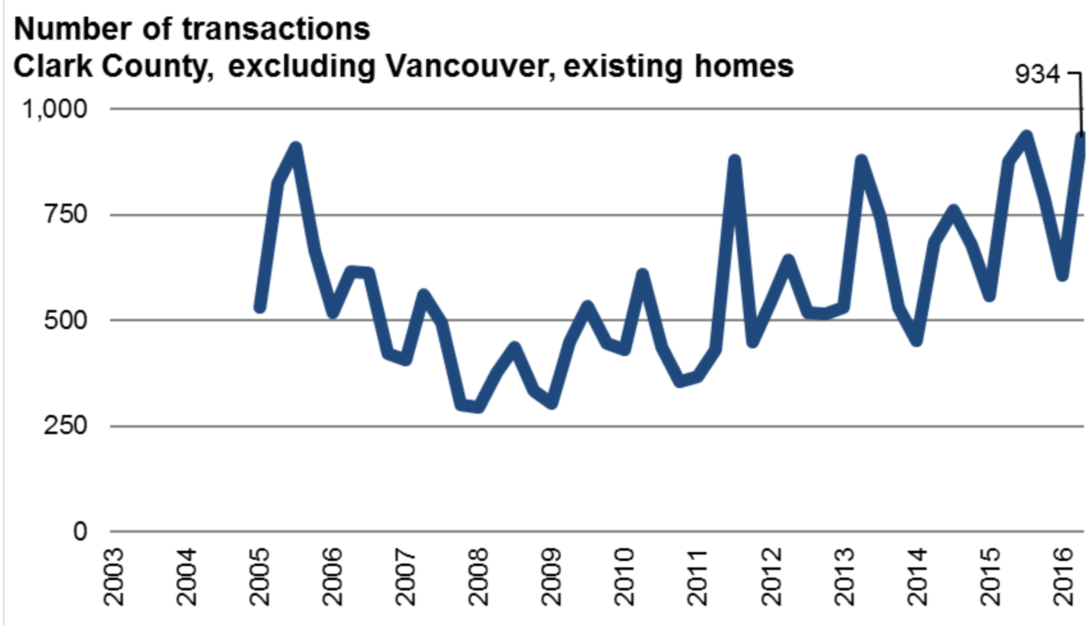
Vancouver and Clark County both also experienced a substantial, seasonal uptick in home sales compared to last quarter. Vancouver experienced a 40 percent increase in transactions of existing homes compared to last quarter – a similar change to Portland. While Portland experienced a slight decline in year over year transactions, Vancouver's transactions were flat compared to the same quarter last year. Clark County transactions were 54 percent higher compared to last quarter and nearly 7 percent higher compared to a year ago.

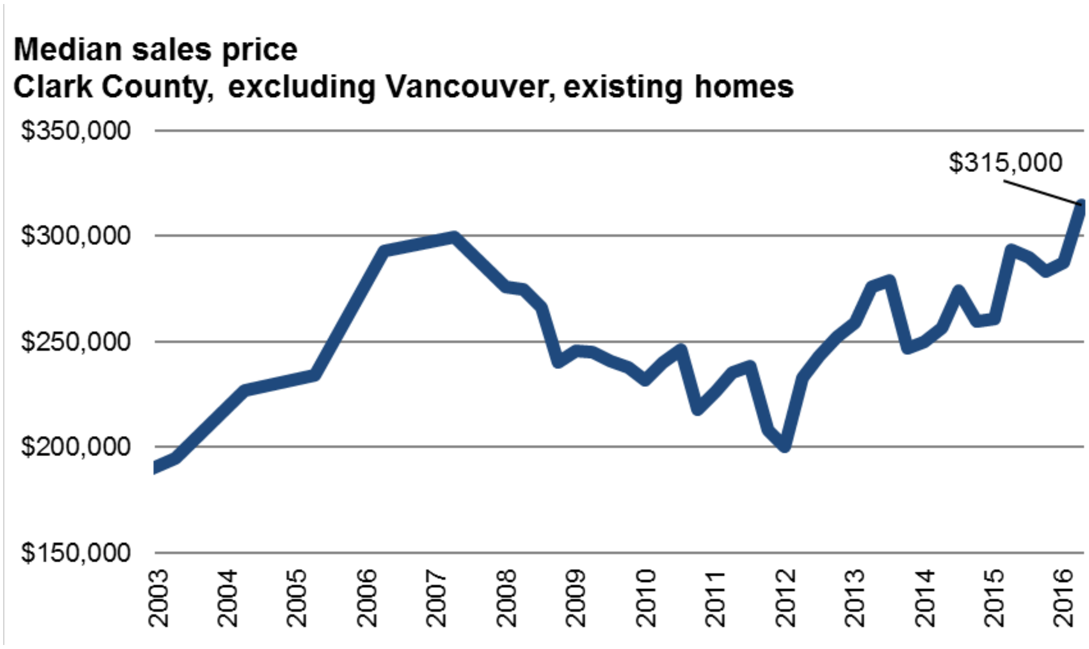
Average days on market dropped substantially for both Vancouver and Clark County, a reflection of increased summer sales activity but also a substantial reduction compared to the same quarter last year. The average days on market for Vancouver declined nearly 36 percent compared to last quarter and 37 percent compared to the same quarter last year. Clark County saw a 38 percent decline in average days on market compared to last quarter and a 24 percent decline compared to the same quarter a year ago.

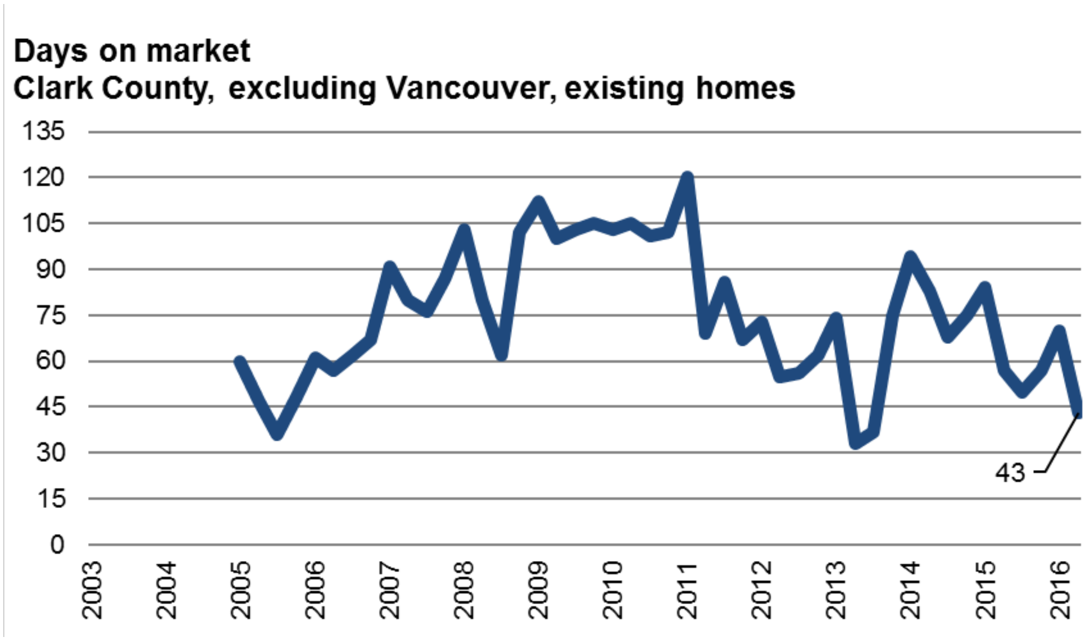



Median sales price
Vancouver, existing homes
$350,000
$300,000
$250,000
$200,000
$150,000
$266,000
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016


Days on market
Vancouver, existing homes
120
105
90
75
60
45
30
15
0
27
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016


Number of transactions
Clark County, excluding Vancouver, existing homes
934
1,000
750
500
250
0
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016


Median sales price
Clark County, excluding Vancouver, existing homes
$350,000
$315,000
$300,000
$250,000
$200,000
$150,000
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016



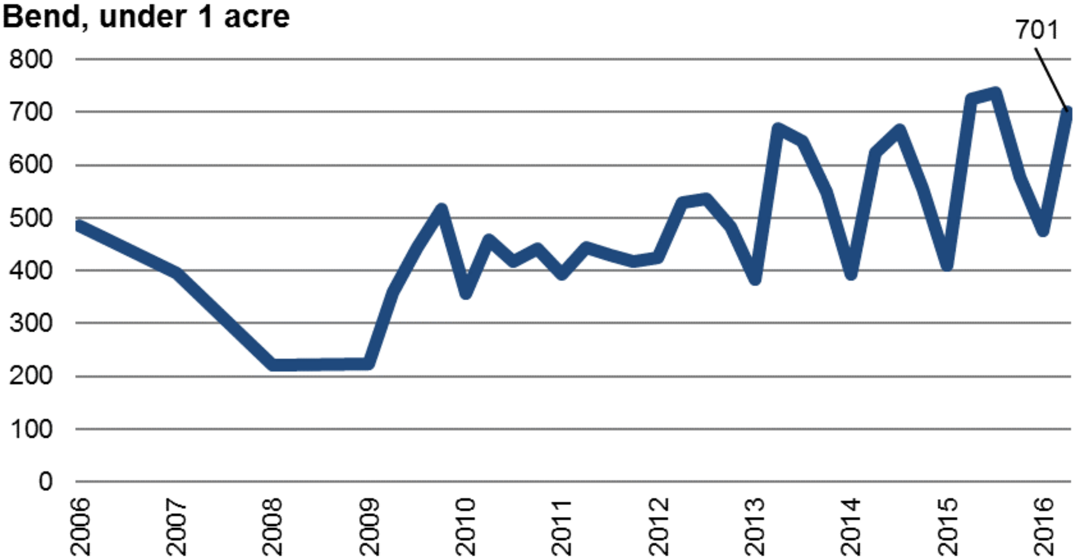
CENTRAL OREGON TRANSACTIONS

Transactions in Central Oregon followed the statewide trend of substantial increases compared to last quarter. Bend saw a 47 percent increase compared to last quarter, but similar to Portland, saw a 3 percent decline compared to the same quarter last year. Redmond experienced a 41 percent increase in transactions compared to last quarter and nearly a 9 percent increase compared to the same quarter last year.

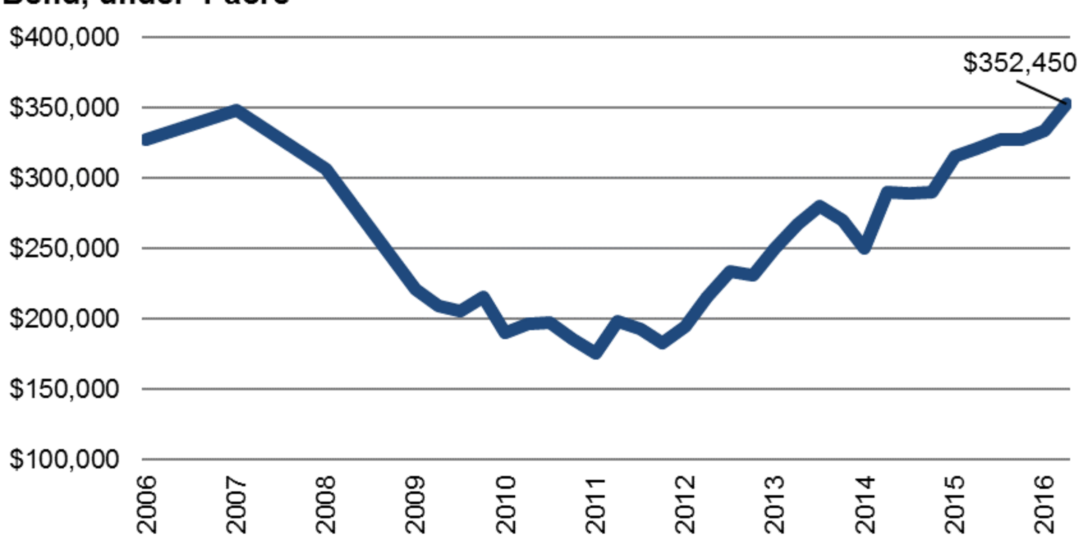
Median home prices in Central Oregon continued the steady, year-over-year increases. Bend experienced nearly a 6 percent increase in median sales price compared to last quarter, and nearly a 10 percent increase compared to the same quarter last year. Redmond saw a slight 1 percent uptick in home prices compared to last quarter, but that still represents a nearly 11 percent increase compared to the same quarter last year.

Average days on market fell as expected during the active season, but also fell compared to last year. Bend's average days on market dropped 10 days from 128 last quarter to 118 this quarter, a near 8 percent decline. Compared to the same quarter last year, this represents a 2.5 percent decline. Redmond saw nearly a 5 percent reduction in average days on market compared to last quarter, which represents over an 11 percent decline compared to last year.

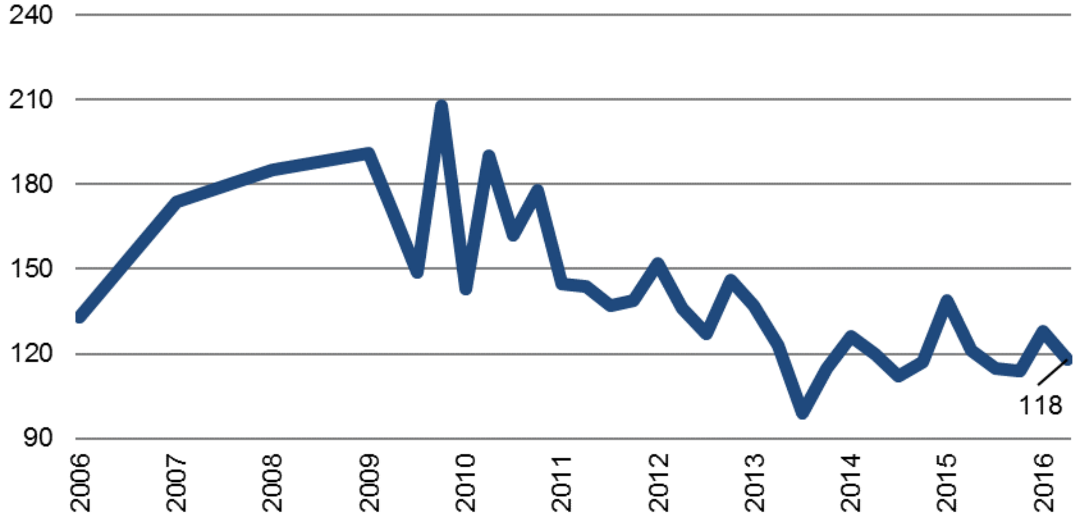
Number of transactions
Bend, under 1 acre



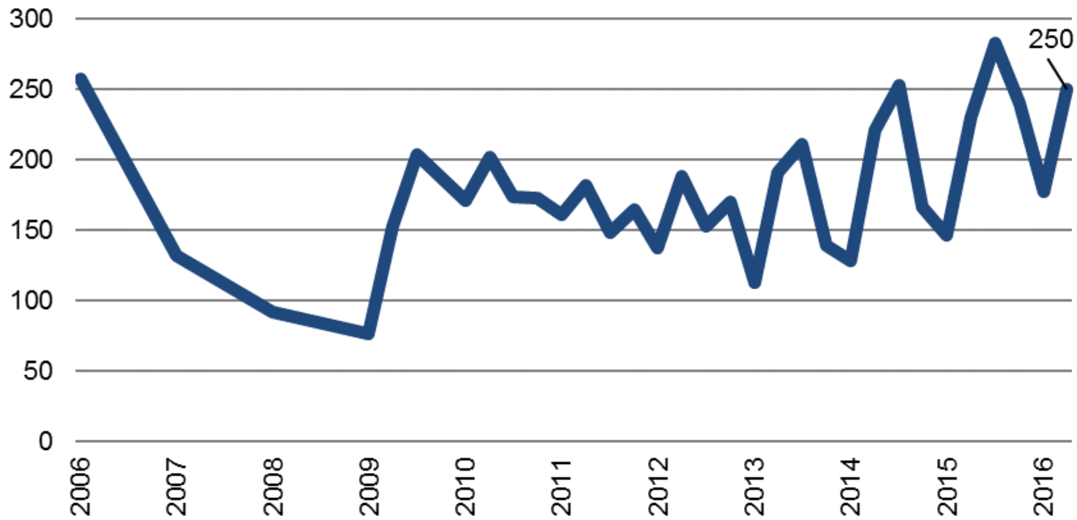
Median sales price
Bend, under 1 acre

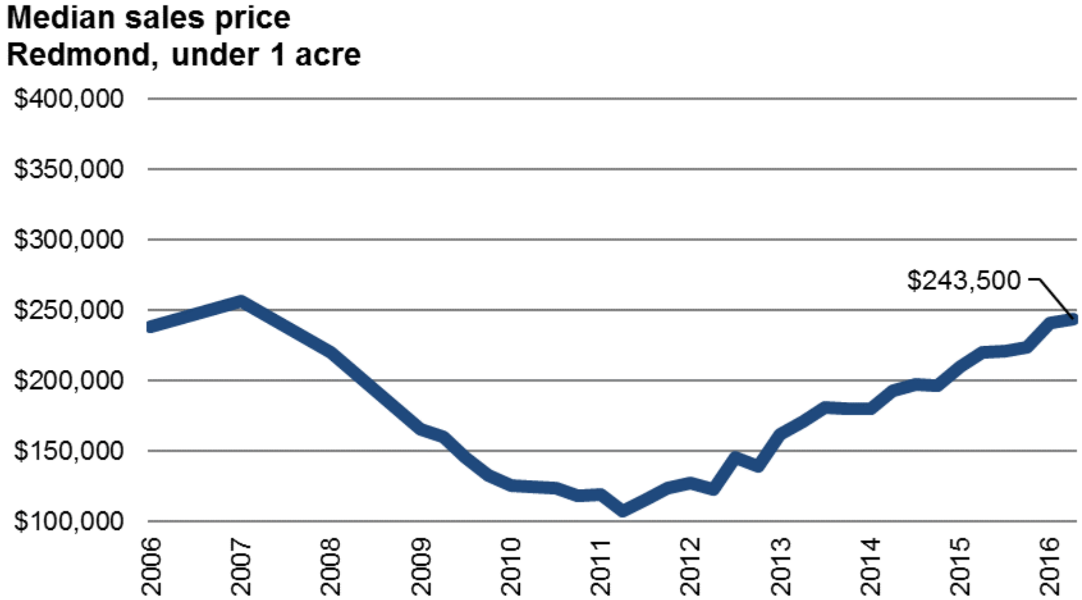


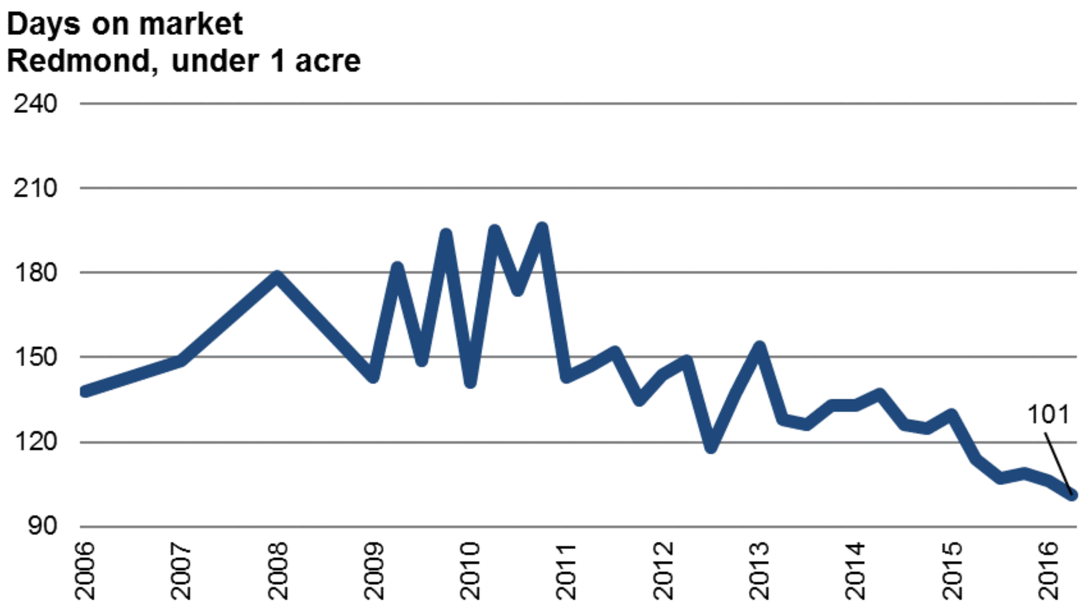
Days on market
Bend, under 1 acre

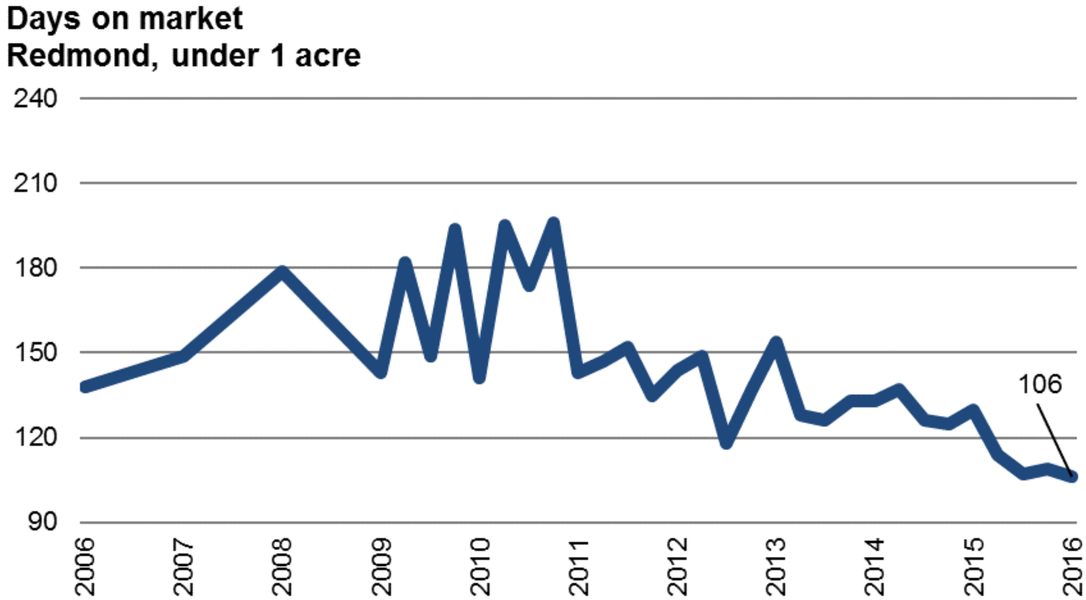


Number of transactions
Redmond, under 1 acre




Median sales price
Redmond, under 1 acre
$400,000
$350,000
$300,000
$250,000
$200,000
$150,000
$100,000
$243,500
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016

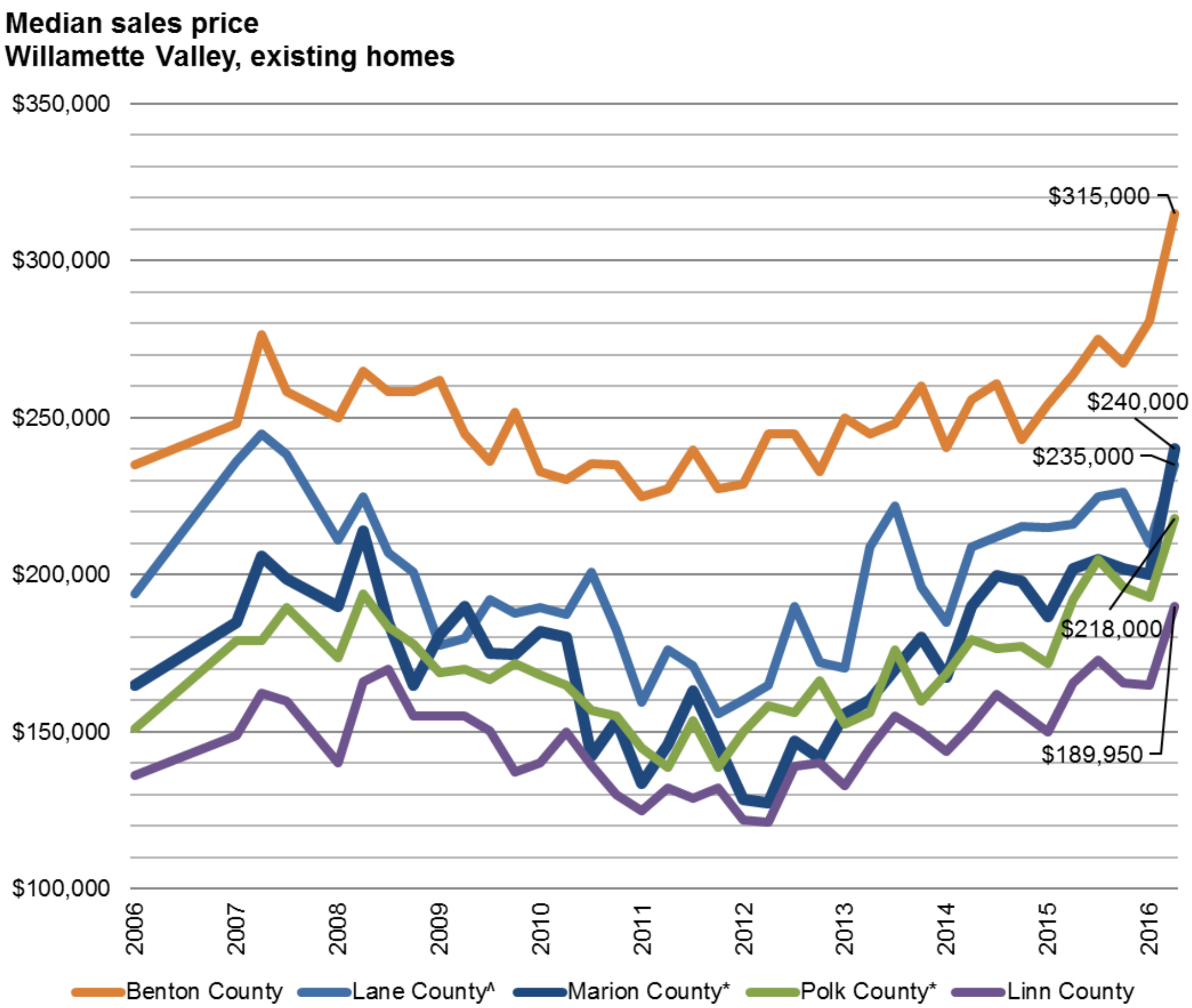

Days on market
Redmond, under 1 acre
240
210
180
150
120
90
101
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016



WILLAMETTE VALLEY TRANSACTIONS

The substantial uptick in median sale prices seen across the state this quarter was also evident in counties across the Willamette Valley. Aside from Lane County, all Willamette Valley Counties saw double digit increases in median sales prices.

- Benton County: $315,000 median price, a 12 percent increase from the prior quarter and a 19 percent increase year-over-year
- Lane County (excluding Eugene): $235,000 median price, a 12 percent increase from the prior quarter and a 9 percent increase year-over-year
- Marion County (excluding Salem): $240,000 median price, a 20 percent increase from the prior quarter and a 19 percent increase year-over-year
- Polk County (excluding Salem): $218,000 median price, a 13 percent increase from the prior quarter and a 13 percent increase year-over-year
- Linn County: $189,950 median price, a 15 percent increase from the prior quarter and a 14.6 percent increase year-over-year



^Excluding Eugene *Excluding Salem

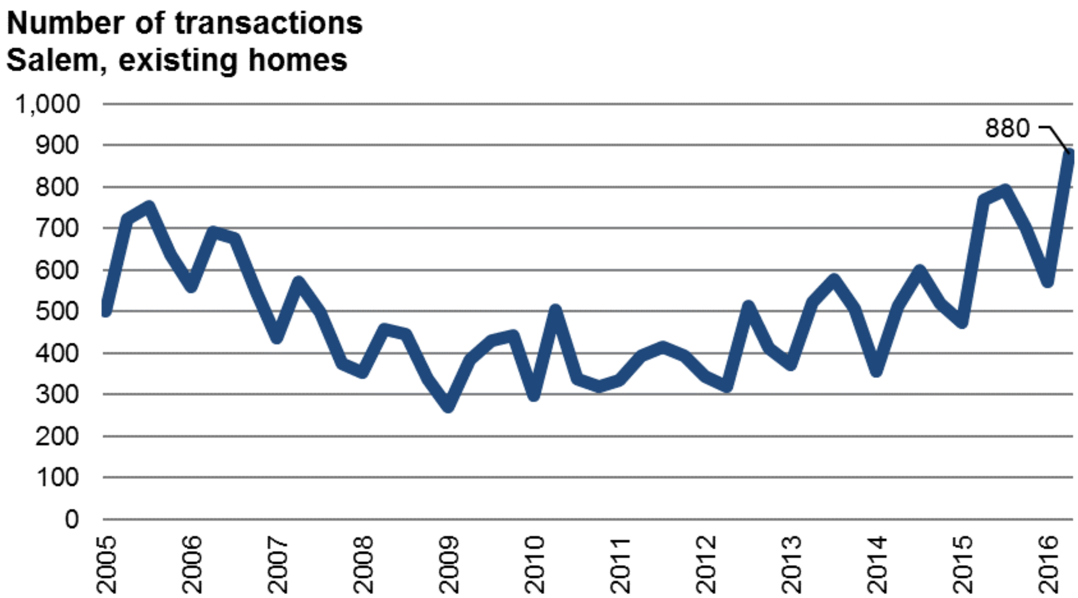
SALEM TRANSACTIONS

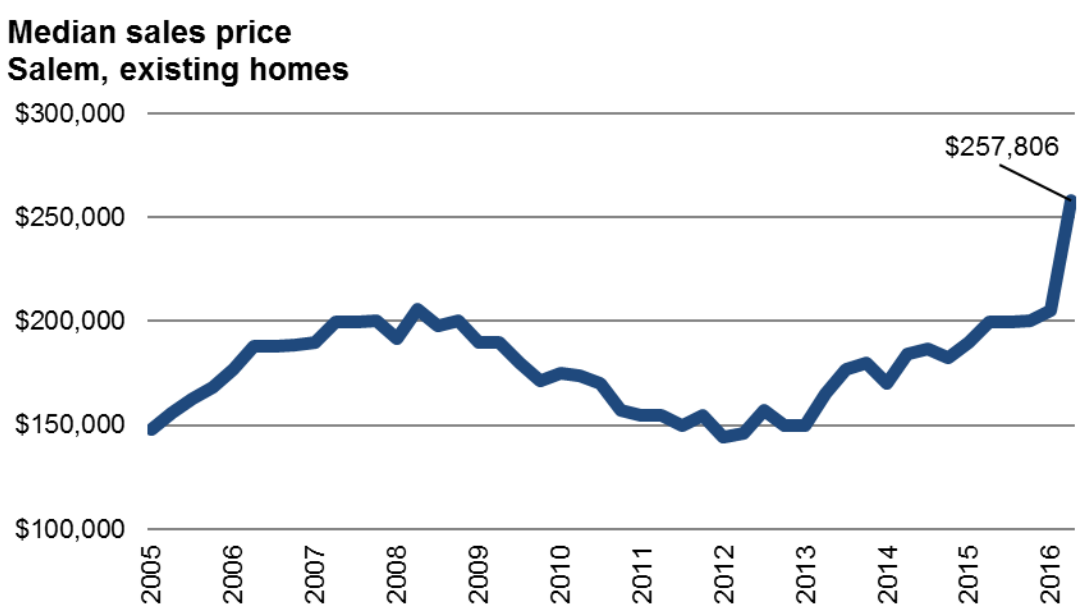
Transaction volume in Salem also experienced a robust seasonal expansion of 54 percent, and a healthy expansion of over 14 percent compared to last year – unlike the slight declines in year over year transactions in Portland and Bend.

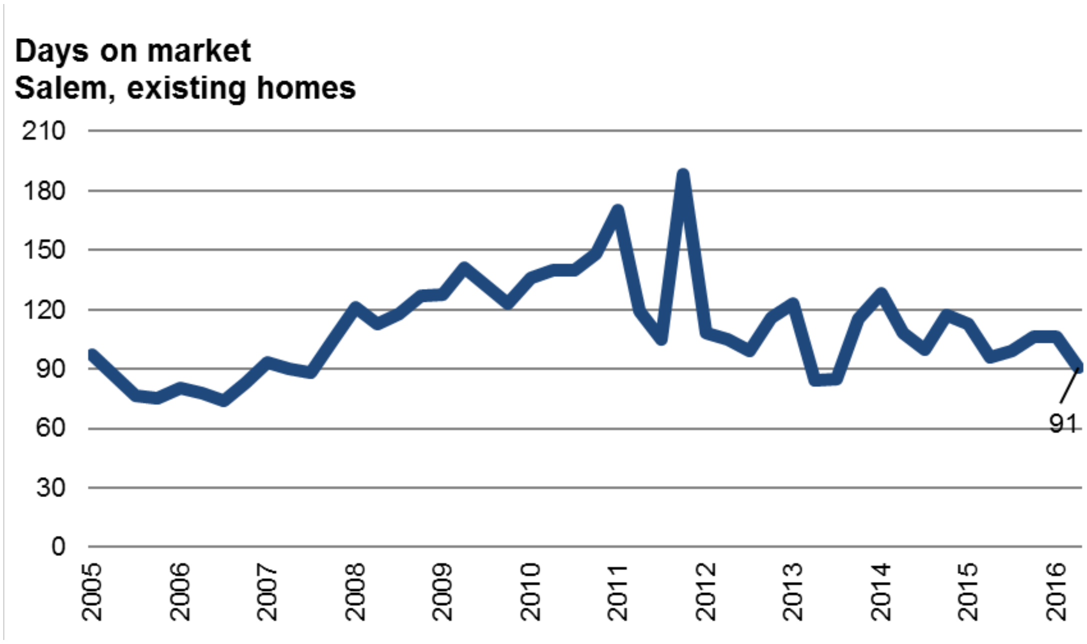
Median sales prices also experienced the substantial increases seen across the state. Median home prices last quarter were $205,000, while this quarter prices reached $257,806 – an increase of nearly 26 percent. Compared to the same quarter last year, this price change represents a 29 percent increase.

Average days on market also declined both compared to last quarter and a year ago. Compared to last quarter, average days on market declined 15 days, or

14 percent, from 106 to 91. This represents a 5 percent decline from the same quarter last year.





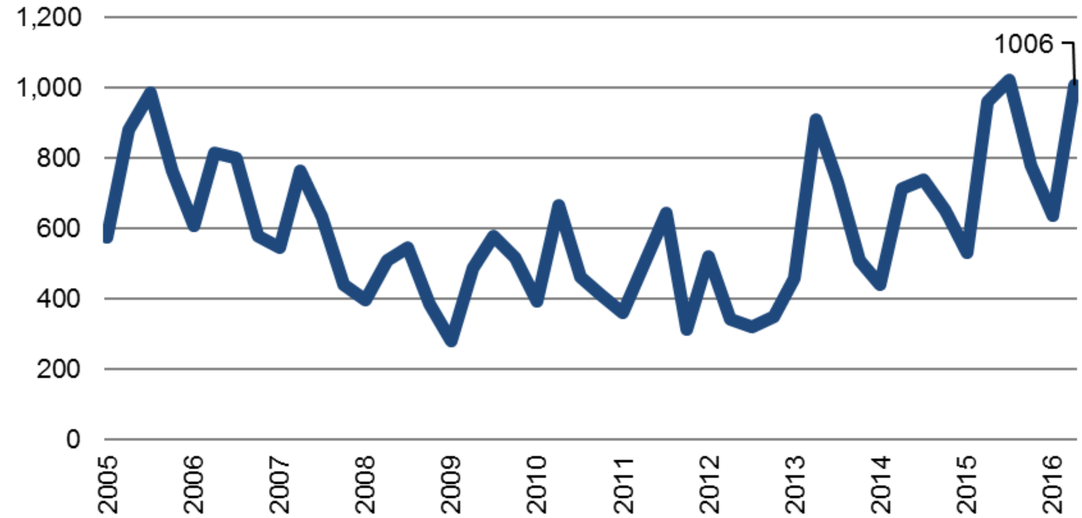


EUGENE–SPRINGFIELD TRANSACTIONS

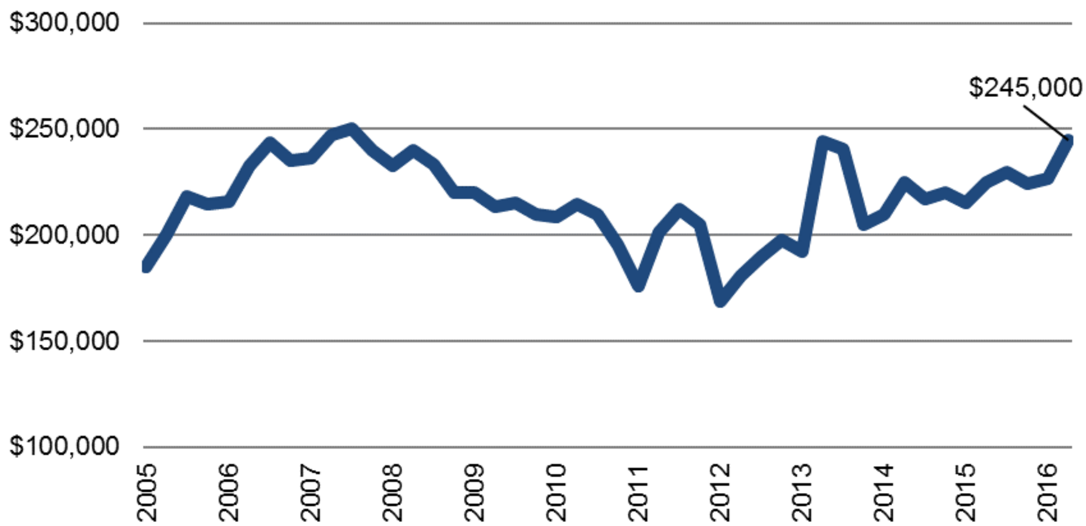
Like many other areas of the state this quarter, Eugene-Springfield experienced a substantial increase in sales volumes and reduction in average days on market, as well as a steady increase in home prices. Transaction counts jumped 58 percent compared to last quarter, which represented a 5 percent increase from the same quarter last year.

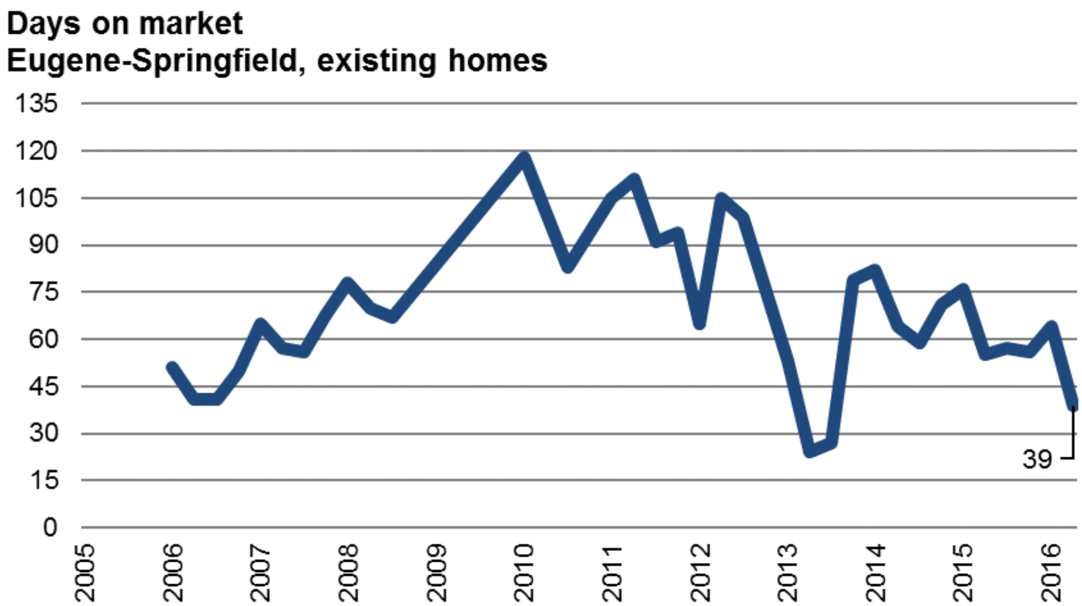
Sales prices expanded from $227,000 last quarter to $245,000 this quarter, an increase of 8 percent. The increase compared to the same quarter last year is 9 percent. Average days on market declined a full 25 days this quarter compared to last, from 64 to 39 days on average. This represents a 39 percent drop compared to last quarter and 29 percent compared to the same quarter last year.

Number of transactions
Eugene-Springfield, existing homes



Median sales price
Eugene-Springfield, existing homes



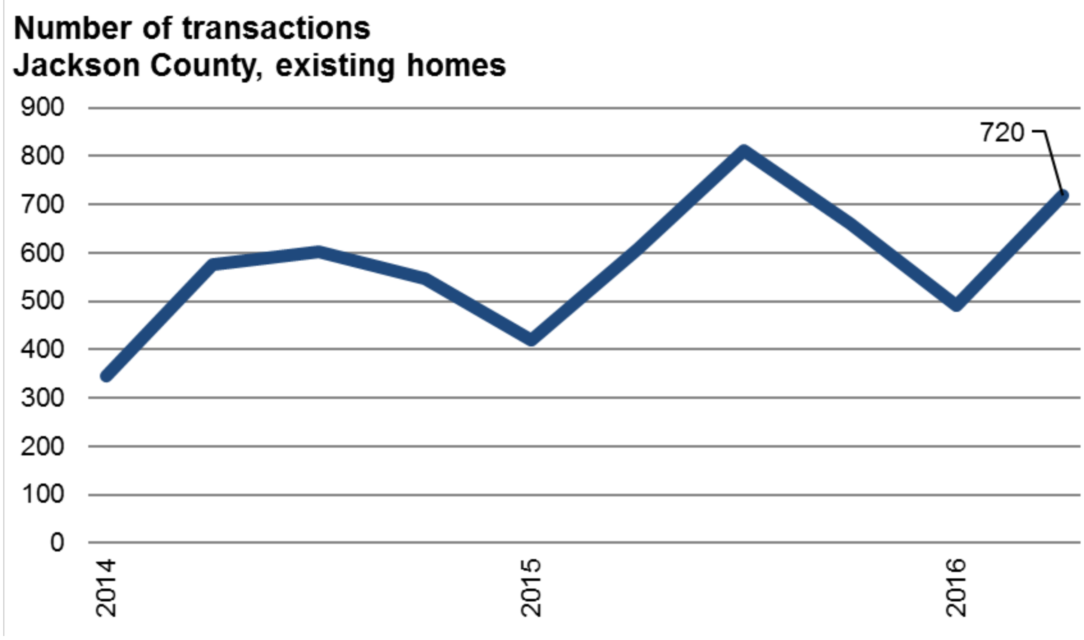


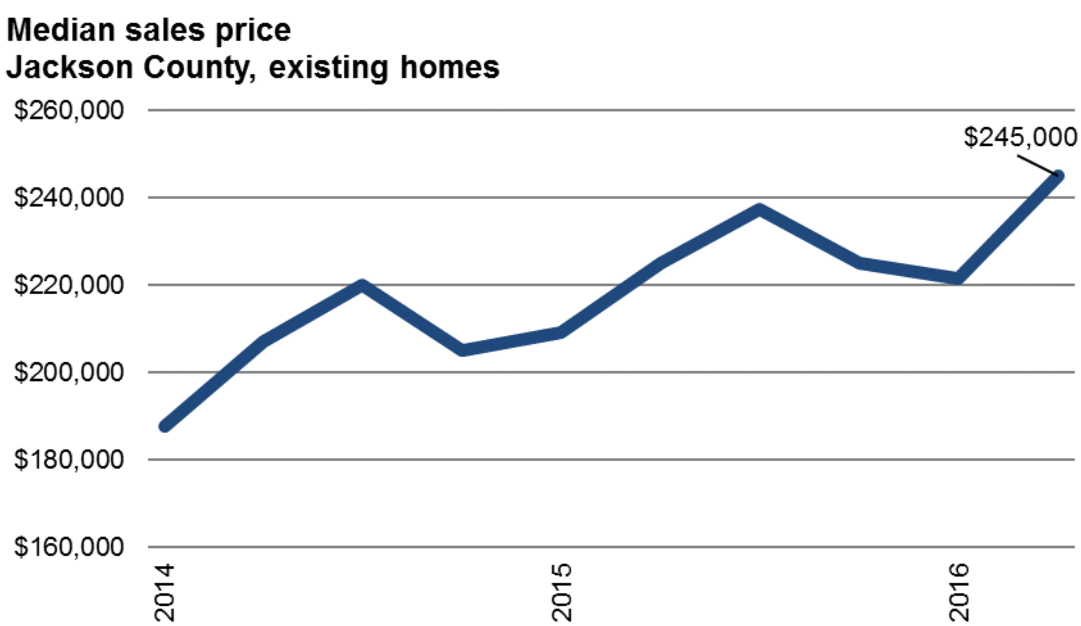
SOUTHERN OREGON TRANSACTIONS

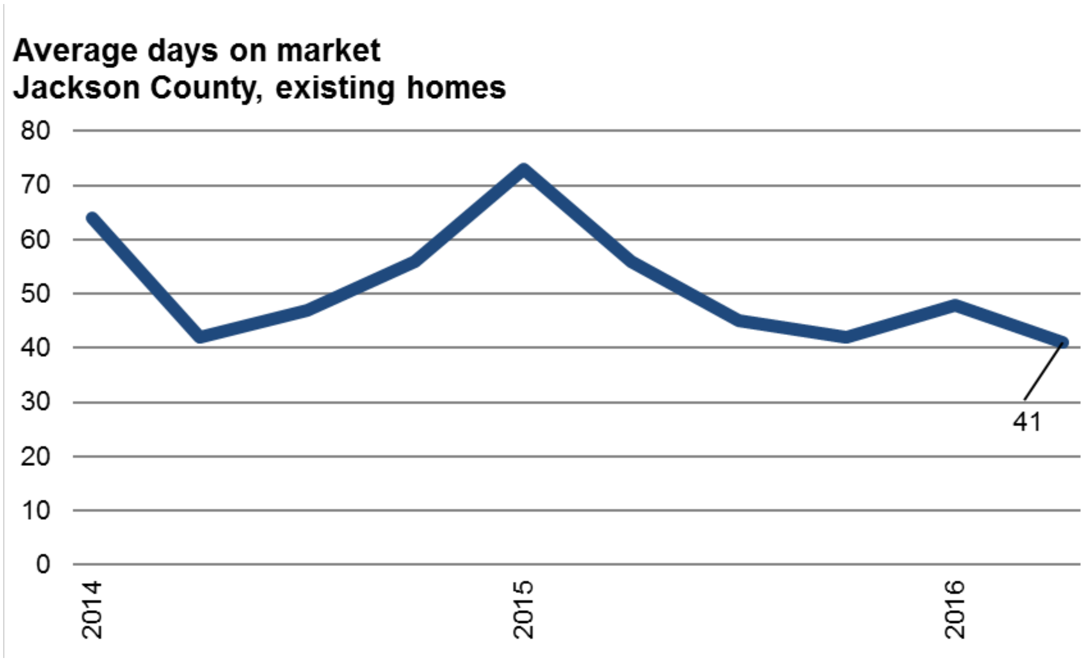
Trends in Southern Oregon tracked with trends across the state: a seasonal uptick in transaction activity compared to last quarter and increased activity compared to the same quarter last year. Median home prices increased both compared to last quarter and the same quarter last year. And average days on market decline compared to last quarter, but particularly compared to the same quarter last year.

Data for southern Oregon is provided in rolling three-month groupings, and the most recent dataset available for this region covers the April 1 – June 30, 2016 time period.

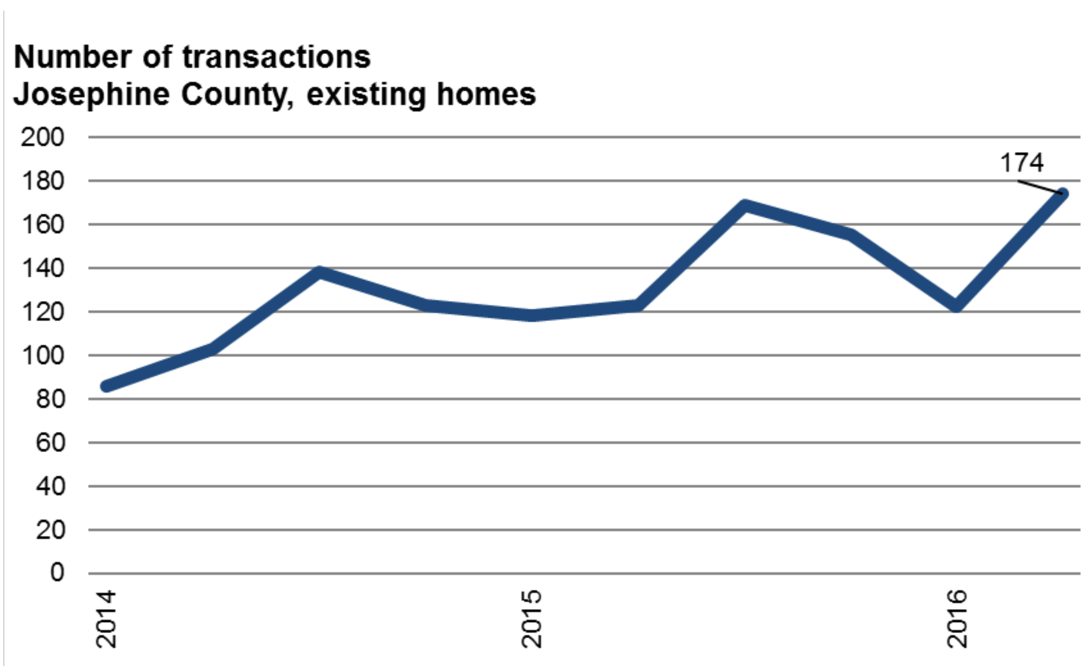
The following figures display the data for Jackson County.

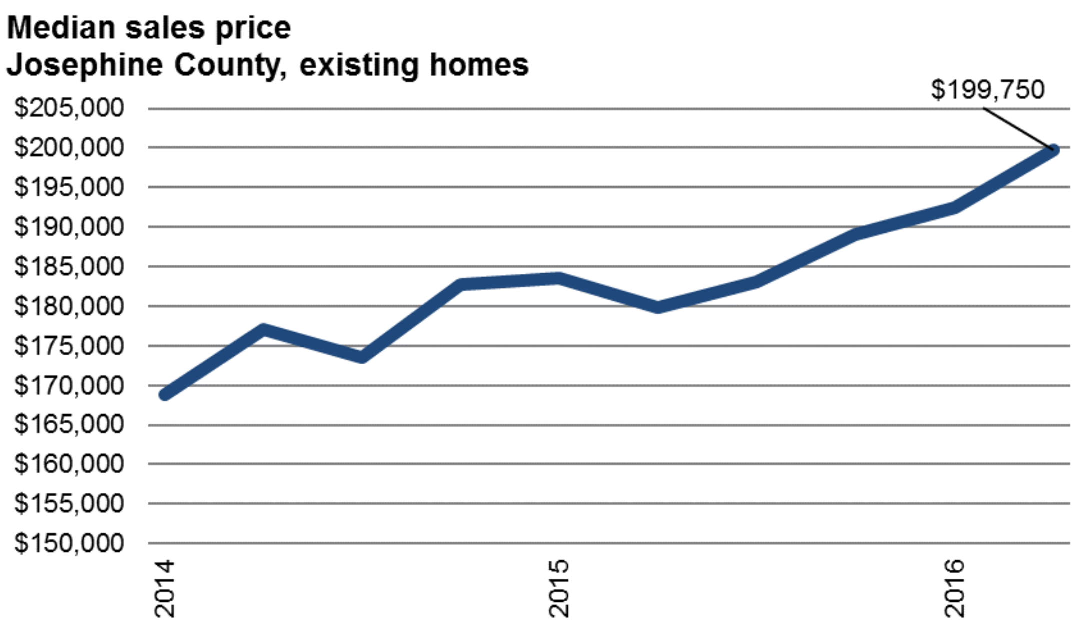

Number of transactions
Jackson County, existing homes
900
800
700
600
500
400
300
200
100
0
720
2014
2015
2016

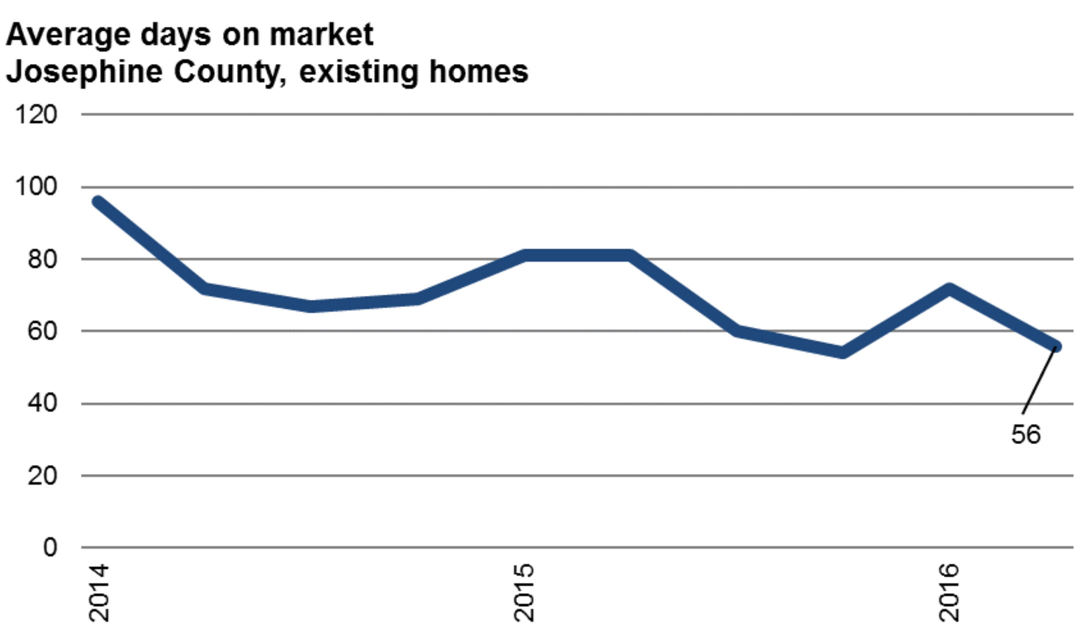

Median sales price
Jackson County, existing homes
$260,000
$240,000
$220,000
$200,000
$180,000
$160,000
$245,000
2014
2015
2016



The following figures display the data for Josephine County.




Median sales price
Josephine County, existing homes
$199,750
$205,000
$200,000
$195,000
$190,000
$185,000
$180,000
$175,000
$170,000
$165,000
$160,000
$155,000
$150,000
2014
2015
2016


Average days on market
Josephine County, existing homes
120
100
80
60
40
20
0
56
2014
2015
2016

MULTIFAMILY MARKET ANALYSIS

Marc Strabic

Portland State University

So as we roll through the summer here in the Northwest, now is a good time to take stock of the multi-family market, the progress made so far in 2016, and to begin forming some predictive thoughts for year-end and early 2017 expectations. **The big picture** in national rent rate averages continue to show moderation in annual effective rent growth in a majority of markets, a trend that started in the fourth quarter of 2015. The AXIOMetrics second quarter report pegs the national effective rent growth percentage for this quarter at 3.7 percent, a 43 basis-point decrease from the first quarter. It also represents a 134 basis-point drop from a year ago. This quarter's percentage also breaks a streak of 19 straight months of 4.0 percent or higher annualized effective rent growth.

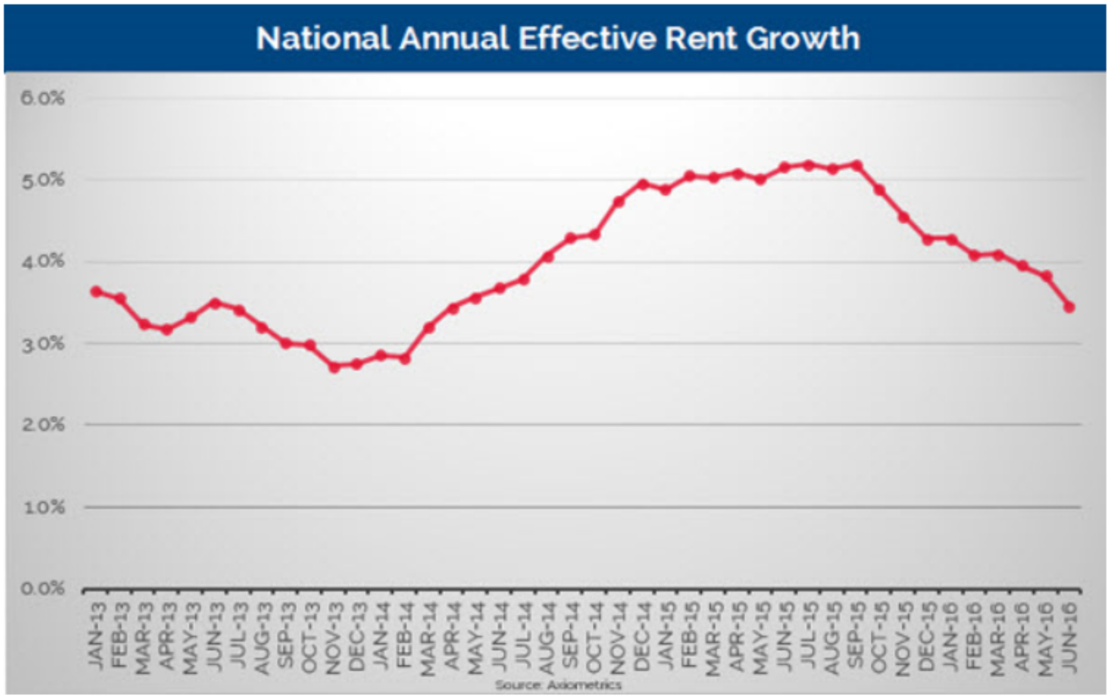
Historically, we are still well above the national average, but it is becoming clearer that we may have reached a peak in this current apartment cycle for rent growth. Nationally, indicators are pointing to year-end rent growth totals in the 3 percent to 4 percent range for most markets—maybe less in cooler markets, likely higher in the hottest markets. What is not so clear yet is if we have reached a peak in cap rate compression, at least not for the Portland MSA.

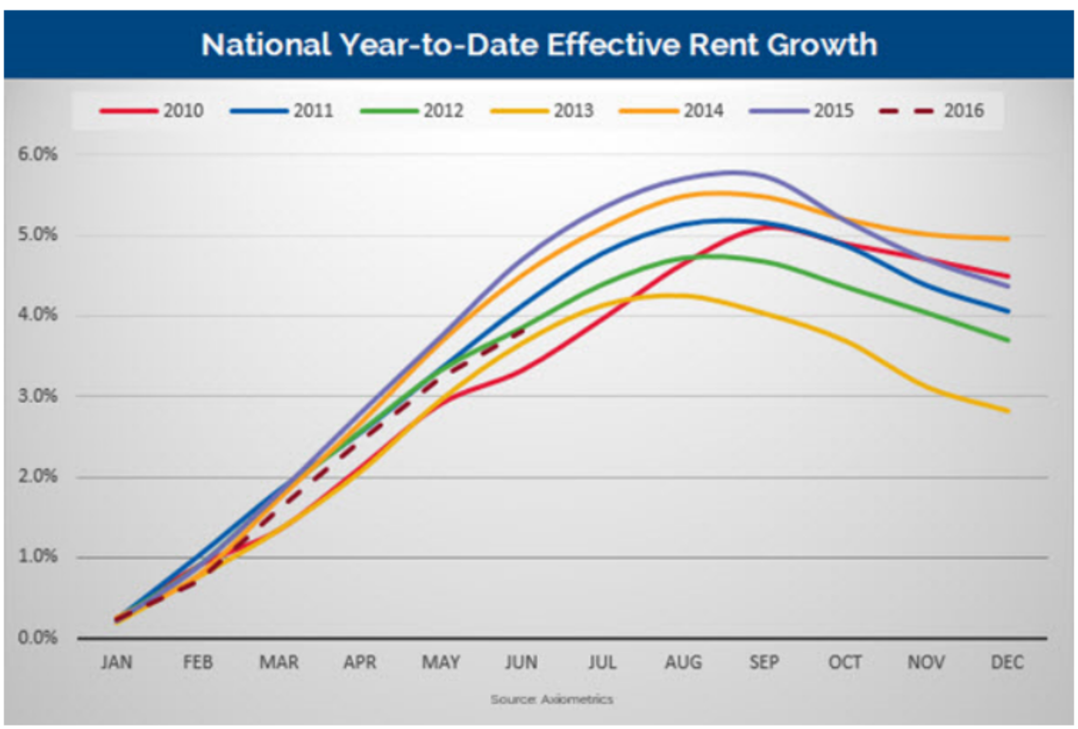
■ **Marc Strabic** is a current Master of Real Estate Development candidate through a joint program of Portland State University's School of Business Administration and School of Urban Studies and Planning, as well as a commercial broker with HSM Pacific Realty. He is the 2016 Multi-Family Graduate Student Fellow at PSU's Center for Real Estate. Any errors or omissions are the author's responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.

In Portland, rent growth, rental rate growth and occupancy figures mirror national trends, albeit at more robust levels. AXIOMetrics' Top 50 U.S. Markets for annual effective rent growth for the second quarter shows Portland ranked #15 at 5.1 percent. We remain committed to our earlier assessment last quarter that we will not see major shifts in the multi-family market this year, but like the national figures, Portland continues to soften in annualized rent growth for the second quarter. When looking at year-to-year changes in the rent growth rate, Portland is cooling quite rapidly, but it is important to keep in mind historical trends and recent performance in multi-family markets. As we have stated in previous reports, annualized effective rent growth rates of 9 percent to 13 percent, annualized, are quite unsustainable. So while seeing rates in the 5 percent range may cause one to pause, Portland will outperform most markets nationally and perform above its historical averages throughout 2016. On the sales front, decreasing rent growth has yet to impact cap rates, as year-over-year quarterly cap rates continue to compress; it remains to be seen if this continues through 2016.

THE NATIONAL PICTURE IN MULTIFAMILY

Nationally, **effective rent growth** is decreasing in most U.S. markets. Occupancy is also decreasing. As with the previous quarter, rent growth and occupancy rates remain well above their historic national averages, but with three quarters of decreasing performance, it is safe to say we are beginning to see a reversion to the mean in most national markets. AXIOMetrics notes that rent growth has slowed to 3.7 percent.


National Annual Effective Rent Growth
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
JAN-13
FEB-13
MAR-13
APR-13
MAY-13
JUN-13
JUL-13
AUG-13
SEP-13
OCT-13
NOV-13
DEC-13
JAN-14
FEB-14
MAR-14
APR-14
MAY-14
JUN-14
JUL-14
AUG-14
SEP-14
OCT-14
NOV-14
DEC-14
JAN-15
FEB-15
MAR-15
APR-15
MAY-15
JUN-15
JUL-15
AUG-15
SEP-15
OCT-15
NOV-15
DEC-15
JAN-16
FEB-16
MAR-16
APR-16
MAY-16
JUN-16
Source: Axiometrics

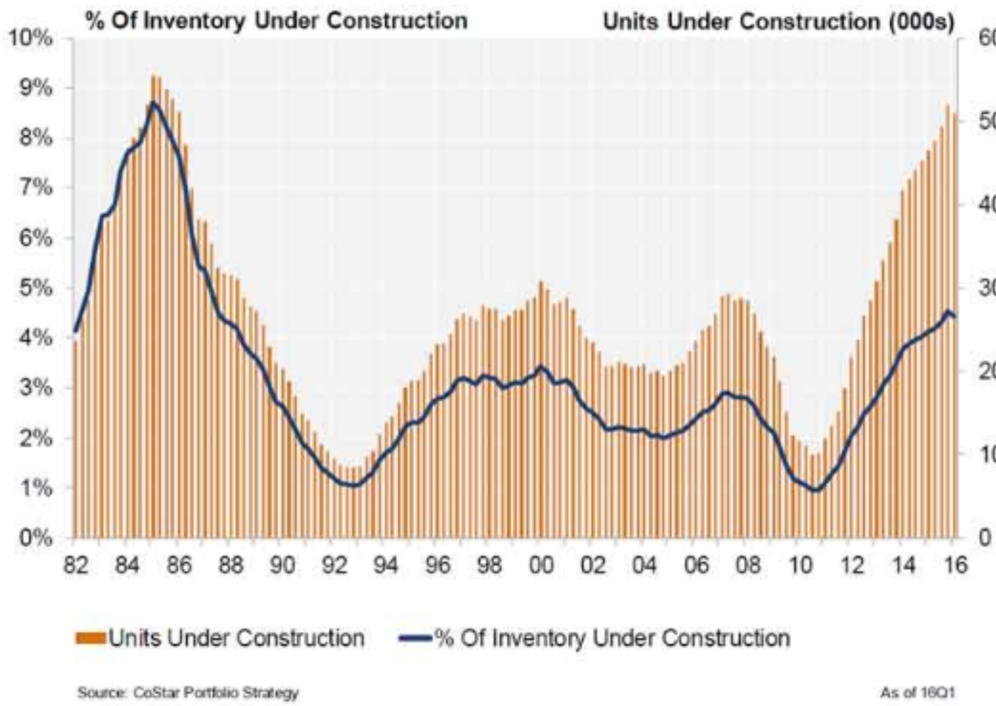

National Year-to-Date Effective Rent Growth
2010
2011
2012
2013
2014
2015
2016
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
JAN
FEB
MAR
APR
MAY
JUN
JUL
AUG
SEP
OCT
NOV
DEC
Source: Axiometrics

Year-over-year performance is clearly pointing to softening markets. The above chart highlights a post-recession trend that will further deflate growth averages: annualized softening in the later months of the year. As we can see, this trend of year-end softening has consistently played out since 2010, and 2016 is on track to repeat this trend. With an expected softening to occur in the fourth quarter, we anticipate year-end performance to be at or near 3-3.5 percent for most markets, numbers still above the historical average of 2.2 percent But not so fast on that forecasted demise of this current boom in multi-family—many markets are still performing well above their 2010-2015 averages as noted in the chart below.

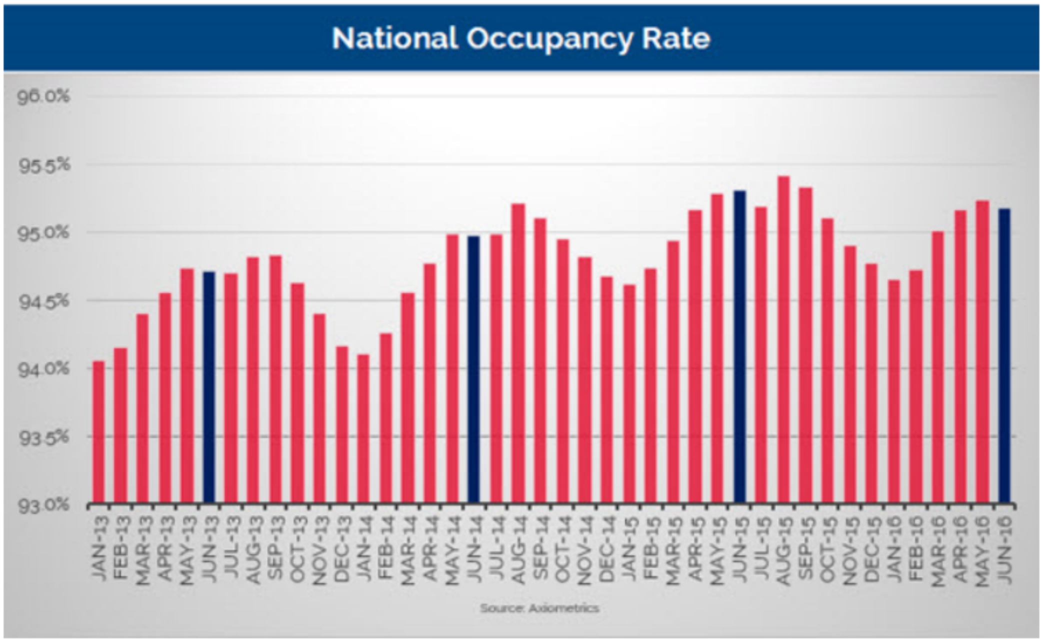
Market	June 2016 YTD Rent Growth	2010-2015 Average YTD Rent Growth	June 2016 Annual Effective Rent Growth	June 2016 Annual Effective Rent Growth Rank*
Seattle	9.6%	6.4%	7.9%	2
Sacramento	9.2%	5.0%	10.9%	1
Raleigh	6.2%	4.4%	4.2%	21
Portland	6.1%	7.3%	5.1%	15
Charleston	6.0%	4.4%	5.0%	16
Chicago	5.9%	3.8%	2.8%	36
Denver	5.9%	7.3%	3.5%	28

*Among Axiometrics top 50 metros
Source: Axiometrics

Why? A big part of falling effective rent growth and occupancy rates is due to **construction starts**. Many consider 2016 to be a peak year in multi-family construction with a level of starts not seen since the 1980s. In the top 54 U.S. markets: CoStar predicts 240,000 new units delivered in 2016; another 220,000 in 2017. If these figures holds true, they will represent the fourth consecutive year of 200,000 (or more) units delivered per year, a first since the 1980s. Yet unlike the 1980s, these new units represent a smaller percentage of the overall market. The current four-year growth period represents approximately 4 percent of the overall multi-family stock; in the 1980s it represented over 9 percent. So, we do anticipate some softening of rents in many markets as more supply comes on line, but we will remain above our historical trends in rent growth, even with truly aggressive construction starts. The chart below represents new construction totals for all markets, not just the Top 54.



Occupancy rates provide an effective way to evaluate the overall health of the market. According to AXIOMetrics, the national average in occupancy rates for 1Q2016 was 94.8 percent. The national rate for 2Q2016 is 95.2 percent. While this technically represents a quarterly increase, as one can tell from the chart below, the normalized annual trends in occupancy almost always decrease through the winter months. A better representation of decreasing occupancy rates can be seen in year-over-year numbers. Last year's occupancy percentage was 10 basis-points higher than the current quarterly figure. The year-over-year numbers specifically for June show a 13 basis-point drop from 2015. While immediate trends show some weakness, overall national occupancy numbers are quite healthy. The year-over-year totals, ending in the second quarter of 2016, for the past 3 years are as follows:



Regarding national economic trends, the overall numbers continue to improve ever so slightly on a quarterly basis: U.S. Bureau of Labor Statistics, seasonally adjusted unemployment through June of 2016, is 4.9 percent, down from 5.0 percent in March. Do note that unemployment is up 0.2 percentage points from May. The U.S. economy added 272,000 jobs in June, again above the average about 222,000 jobs per month for the proceeding 12 month cycle. **On a metro basis**, jobless rates were lower in June than a year earlier in 285 of the 387 metropolitan areas, higher in 75, and unchanged in 27. Nonfarm payroll employment was up in 329 metropolitan areas over the year, down in 47, and unchanged in 11.

In summary, national apartment rent growth is now slightly lower than 4 percent and it snaps a streak of seven continuous quarters (19 consecutive months) at or above 4 percent. While this points toward a softening market, the previous streak was a 20-year record, so perspective is important. The national average for rents increased to $1,277, representing a slight increase from the first quarter, which averaged $1,248. The takeaway for the second quarter: softening is occurring in apartment fundamentals nationally, but do not mistake the downturn in growth rates to indicate that a major shift in market fundamentals is underway. Many markets are still well above their historical averages and the national totals themselves remain above historical averages.

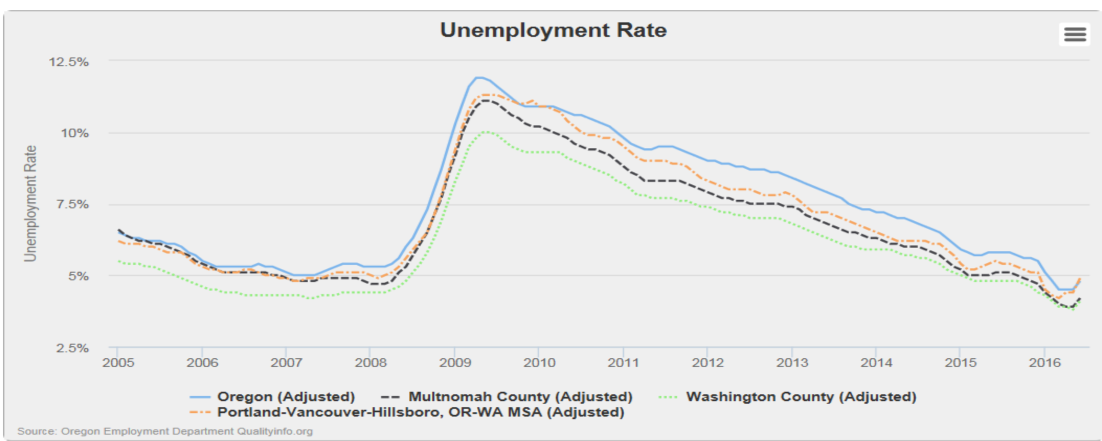
PORTLAND APARTMENT MARKET OVERVIEW

In the second quarter of 2016, the multifamily market in the Portland-Vancouver-Hillsboro Metropolitan Statistical Area (MSA) is showing that new construction is starting to meet demand, a welcome sign for many renters in the market. Colliers International is reporting a 96.50 percent vacancy factor for the MSA, which is roughly the same as in the first quarter. In their May market update, CBRE states a vacancy factor equal to our first quarter report, or 96.48 percent. Zillow shows a Portland City rental average of $1,871 per month and a $1,780 per month averge for the overall MSA. Colliers, which tracked over 200,000 indivdual units, shows a average monthly rent of $1,151.00.

AXIOMetrics measured the Portland-Vancouver-Hillsboro MSA's annual effective rent growth for June 2016 at 5.1 percent; year-to-date rent growth is 6.1 percent. This ends Portland's run in the Top 10 markets for annualaized effective rent growth; Portland is now ranked #15 nationally. As with national data, this change is reflected in new supply, not weaking demand.

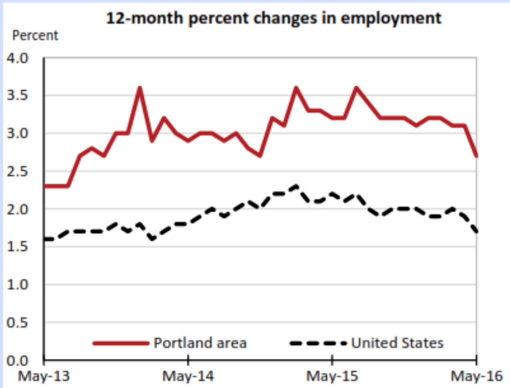
Oregon's economy is still adding jobs. Oregon's Employment Department shows a current unemployment rate of 4.5 percent and 4.2 percent for the Portland MSA. A recent ecomomic forecast by Oregon State economists sees strong job growth through the end of 2017:

> Robust job growth continues in Oregon. Since the beginning of 2013, Oregon job growth has picked up from around 1.5 to 2.0 percent to more than 3.0 percent today. The outlook calls for this growth to persist for another year and a half before longer-run demographic trends weigh on growth. While consistent with the general character of recent forecasts, this marks an upward revision to the employment outlook. Previously our office expected the deceleration in job growth to happen in early to mid-2017. Now, our office expects this to occur at the end of 2017. Wages and incomes remain relatively unchanged to previous outlooks.



On the **economic front in Portland**, the U.S. Bureau of Labor Statitics show a Portland MSA unemployment rate of 5.1 percent at the end of June 2016, a slight increase from our last report (4.9 percent). State statitics show a seasonally adjusted rate of 4.9 percent, but with a year-over year increase of .5 percent. The information, financial and construction sectors lead the local economy in job growth, all typically well paying jobs.

Over-the-year changes in employment on nonfarm payrolls and employment by major industry sector



Source: U.S. BLS, Current Employment Statistics.

Portland area employment (numbers in thousands)	May 2016	Change from May 2015 to May 2016	
		Number	Percent
Total nonfarm	1,140.6	30.4	2.7
Mining and logging	1.2	0.0	0.0
Construction	57.8	2.8	5.1
Manufacturing	121.7	0.0	0.0
Trade, transportation, and utilities	209.5	4.4	2.1
Information	26.1	2.1	8.8
Financial activities	68.8	2.8	4.2
Professional and business services	174.4	4.5	2.6
Education and health services	166.0	5.2	3.2
Leisure and hospitality	116.6	3.1	2.7
Other services	40.3	1.3	3.3
Government	158.2	4.2	2.7

Source: U.S. BLS, Current Employment Statistics.

TRANSACTIONS

Listed below is a table of significant mutifamily transactions, courtesy of Colliers International, that have occurred in the Portland area for the second quarter of 2016.

PROJECT	CITY	SALE DATE	SALES PRICE	# UNITS	PRICE/UNIT	PRICE/SF	CAP RATE
Breckenridge Apartment Homes	Portland	5/17/2016	$81,500,000	357	$228,291	$301.58	5.50
Cook Street Apartments	Portland	5/12/2016	$69,000,000	206	$334,951	$302.89	
Townfair Apartments	Gresham	5/9/2016	$31,000,000	265	$116,981	$139.71	5.75
The Preserve	Oregon City	6/13/2016	$21,500,000	135	$159,259	$181.80	
Boulder Gardens	Clackamas	5/12/2016	$18,000,000	157	$114,650	$156.52	4.63
The Crossings	Clackamas	6/10/2016	$13,452,500	96	$140,130	$153.07	
Hogan Woods	Gresham	6/3/2016	$11,100,000	100	$111,000	$116.84	5.50
Royal Green Apartments	Gresham	5/31/2016	$10,500,000	90	$116,667	$119.75	5.61
King Street Lofts	Portland	5/13/2016	$8,300,000	36	$230,556	$385.83	5.00
Castlewood Arms	Beaverton	4/28/2016	$7,950,000	72	$110,417	$129.58	

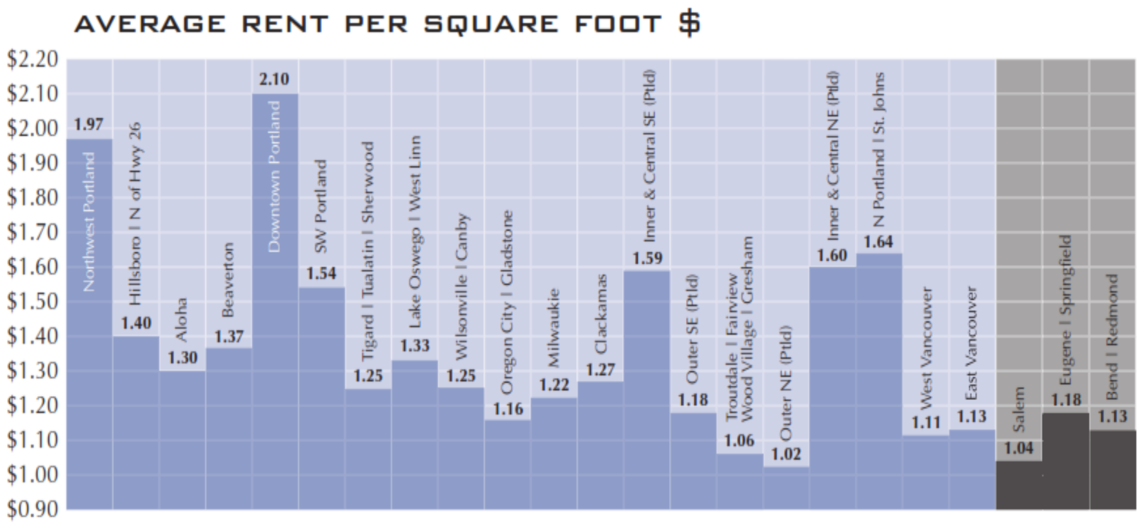
Measuring these sales, we show an average sales price of $27,230,250 with an average unit price of $166,290 and price/SF of $198.76. The total value of these transactions exceeds $275 million; the total number of units equals 1,514.

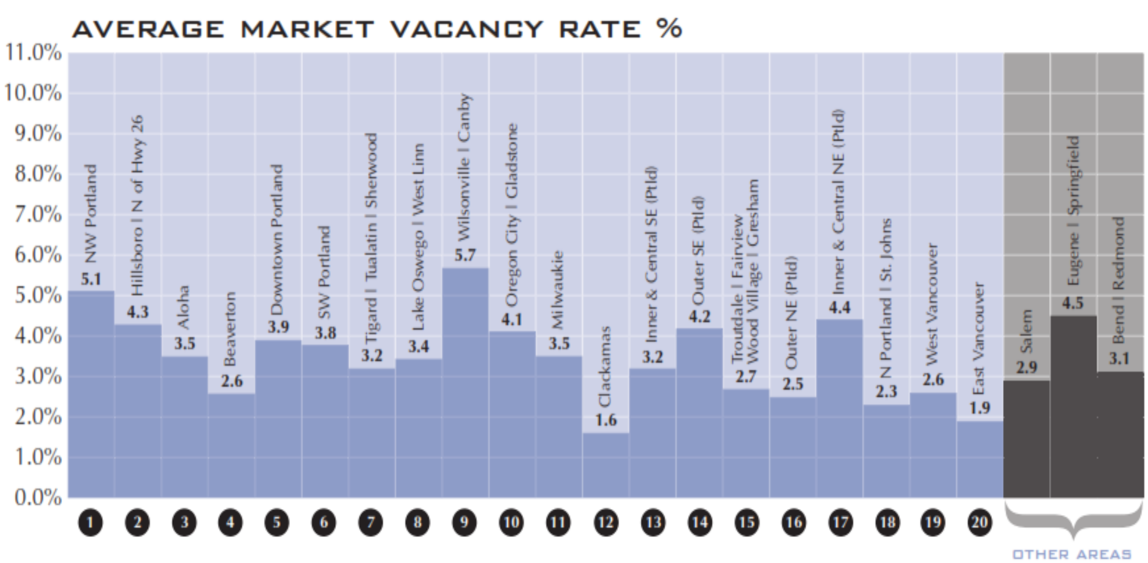
Sperry Van Ness/Bluestone & Hockley's year-to-date totals of sales transactions (all product types sales over 450K) show 136 sales equating to $939,570,545 in sales volume, this represents a 3.5 percent decrease in total sales transactions and 8.4 percent decrease in overall sales volume. Their report shows an average price/SF of $157.62, and year-over-year increase of 5.5 percent. They show an average cap rate of 5.62 percent, representing a compression of 2.4 percent from this point in 2015.

EFFECTIVE RENTS

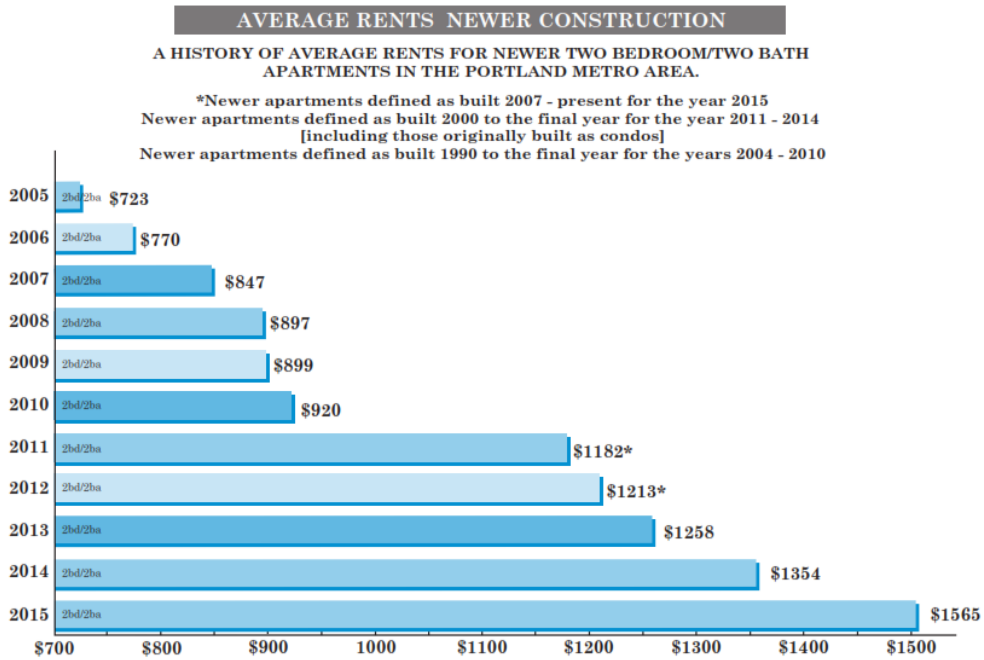
Below are representations of average rents per square foot and average vacancy rates for the Portland MSA submarkets, as compiled by Multifamily NW in its most recently published survey. Both charts are from their Bi-Annual Report/Spring 2016.

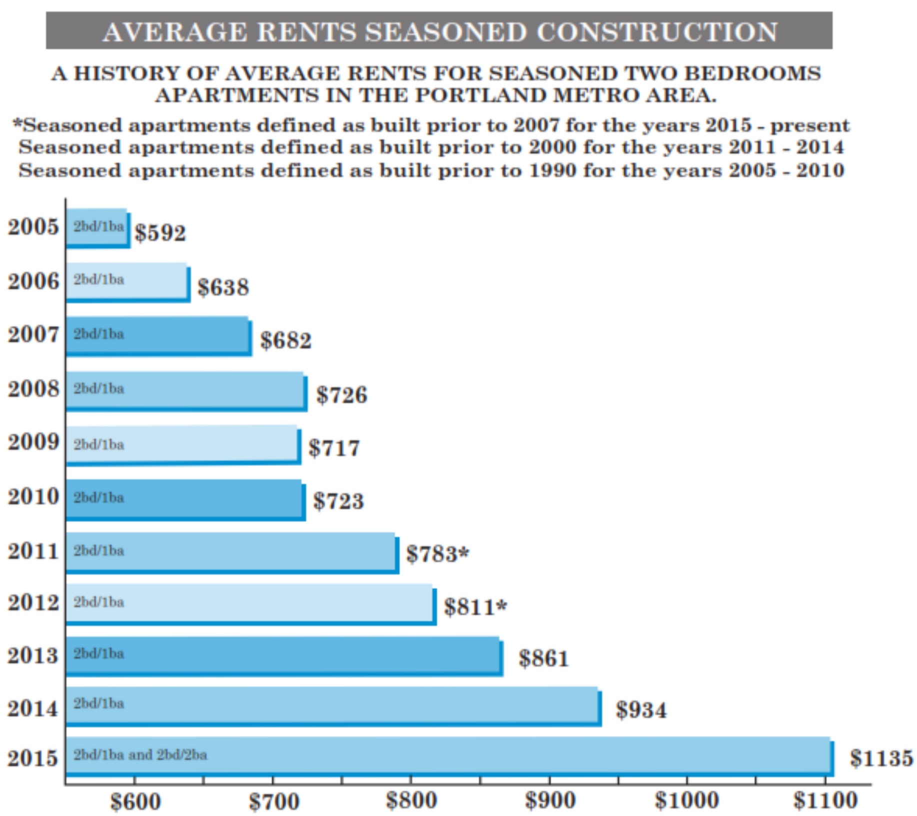
Submarket Spring 2016:





Below is a chart of area rents, courtesy of Norris & Stevens, for newer contruction and exisiting construction, in the Portland MSA.





PERMITS & CONSTRUCTION

The following information pertains to building permit issuances for the second quarter of 2016/year-end totals for projects **with five or more private housing units only**, as tracked by the U.S. Census Bureau.

Year-to-date totals show the Portland-Vancouver MSA issued 95 building permits for structures of five units or more, equaling 3,813 units. Second-quarter and year-to-date permit totals (including Clark Co.) for the five areas surveyed are:

Area	2Q Total Permits	2Q Total # of Units
City of Portland	17	753
Multnomah County	18	777
Clackamas County	11	151
Washington County	13	86
Clark County, WA	13	180

Area	YTD Permits	YTD # ofUnits
City of Portland	33	1,659
Multnomah County	34	1,683
Clackamas County	15	386
Washington County	27	1,482
Clark County, WA	19	262

NEW CONSTRUCTION

The following totals and samples are courtesy of the spring 2016 Barry Apartment Construction Report.

Total Units Proposed and Under Construction

Area	Proposed	Under Construction	Total
North Portland	1,878	462	2,340
Close in East Portland	4,850	2,154	7,004
Close in West Portland	5,225	3,542	8,767
Suburban West	3,750	1,364	5,114
Suburban East	1,325	242	1,567
Suburban South	1,067	899	1,966
Clark County	3,488	498	3,986
Total	21,583	9,161	30,744

Total Projects Proposed and Under Construction

Area	Proposed	Under Construction	Total
North Portland	49	12	61
Close in East Portland	81	36	117
Close in West Portland	58	26	84
Suburban West	20	7	27
Suburban East	26	9	35
Suburban South	9	6	15
Clark County	33	9	42
Total	276	105	381

Sampling of Proposed Projects

Name	Address	City	Units	Complete	Notes
North Portland					
N. Harbor Apts	N Harbor Way & N. Anchor	Portland	264	proposed	3-5 story podium
Interstate Bowling Site	6049 Interstate	Portland	180	proposed	4-story mixed use
Mississippi	3403 N Mississippi	Portland	175	proposed	Mixed use development
Close-in Eastside					
Oregon Square	800 NE Oregon	Portland	1,030	proposed	4 high rise towers
Lloyd Movie Apts	1510 NE Multnomah	Portland	980	proposed	multiple buildings
Burnside Bridgehead	139 SE MLK	Portland	343	proposed	12 story construction
NE 20th Apts	518 NE 20th	Portland	230	proposed	5-6 story construction
Close-in Westside					
PSU Apts	325 SW Harrison	Portland	424	proposed	15 stories with grocer
Conway Apts	1621 NW 21st	Portland	370	proposed	Mixed use development
BRIDGE Housing	2095 SW River Pkwy	Portland	365	proposed	5 story construction
Glisan Tower	1430 NW Glisan	Portland	273	proposed	14-story development
Suburban Westside					
Holly Site	Barnes & Cedar Hills	Portland	600	proposed	mid-rise construction
Johnson Creek, 2 sites	Barnes & Cedar Hills	Portland	1025	proposed	mid-rise construction
Sunset Hills	6400 SW Canyon Rd/	Portland	267	proposed	garden style construction
Orenco Woods	22180 NW Burch	Hillsboro	252	proposed	54 acre site
Suburban Eastside					
Wood Village Apts	NE 223rd & Glisan	Wood Village	168	proposed	
Gateway Apts	887 NE 102nd	Portland	160	proposed	Mixed use development
Suburban South					
Eagle Landing	10220 SE Causey	Happy Valley	400	proposed	Planned residential development
Beavercreek Apts	19896 Beavercreek	Oregon City	180	proposed	Live work units included
Clark County					
Brush Prairie Apts	11911 NE 119th	Brush Prairie	332	proposed	garden style construction
Waterfront	1000 Columbia St	Vancouver	150	proposed	
192nd Apts	192nd & 20th	Vancouver	292	proposed	four buildings

OFFICE MARKET ANALYSIS

MELISSA BEH

Portland State University

Oregon's economy has remained strong and steady throughout 2016 with an average 3.0 percent year-on-year growth, which was accompanied by a robust job market—Oregon currently employees 1.83 million people. Jones Lang LaSalle points to Education and Health Services as the leader in job market growth with an average of 6,520 jobs year-to-year thus far. Over the next few years, economic and employment growth in Oregon is expected to be higher than average with non-farm employment growth projected to be 3.5 percent in 2016 and 3.0 percent in 2017.

Oregon's healthy second quarter economy and job market keeps office development growing and active.

- ✧ **JLL** emphasized Oregon's continued economic growth from 2016's first quarter, highlighting job growth and vigorous metro area construction. Deliveries in the metro area in 2016 thus far have equaled 571,605 square feet of office space with 1.37 million square feet currently being built or renovated. Fifty-five percent of buildings under construction are pre-leased. Much of the new construction is focused in the CBD and urban core of Portland.

- ✧ **Colliers** focused on the cost of doing business in the Portland metro area. "Moody's Analytics reports cost of doing business in the metro area has increased, from 91 percent of the U.S. baseline in Q1 to 96 percent in Q2."

■ **Melissa Beh** 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.

Wage growth and high rental rates for office and industrial space are major factors. Potential zoning and inclusionary housing changes, along with the possibility of construction excise and business receipts taxes, is worrying to both business owners and investors.

- **CBRE** highlighted the extremely low overall market vacancy rate that fell below 10 percent, landing at 9.97 percent, a phenomenon that has not occurred since 2001 according to their records. This rate is especially impressive considering inventory increased by 42 percent in the first half of 2016. CBRE reports a net positive absorption of 444,593 square feet in the Portland office market – the highest since the first quarter of 2013.

VACANCY

CBRE's data show vacancy holding below ten percent, a rate that hasn't been seen since the first quarter of 2001. Downtown vacancy decreased to 8.2 percent from 8.7 percent, while the Lloyd district fell to an astounding low of 2.9 percent vacancy rate. The suburban market vacancy rate officially fell below 12 percent and landed at 12.3 percent. JLL reported total vacancy at 8.8, a slightly higher rate than the 8.3 percent reported in the first quarter.

Table 1: Total Vacancy Rates by Brokerage and Class, Second Quarter 2016

Brokerage	Total	CBD	CBD Class A	CBD Class B	CBD Class C	Suburban
CBRE	9.97%	8.2%	8.7%	7.9%	8.7%	----
Colliers	8.7%	10.0%	10.5%	9.6%	9.3%	8.3%
JLL	8.8%	7.9%	9.0%	9.2%	7.1%	9.7%

Source: JLL; CBRE; Colliers International

Table 2: Portland Vacancy Rate by Market area and Submarket, First Quarter 2016

Location	Q2	Change from Q1
Portland CBD	7.9%	-1.3%
Lloyd District	5.2%	-1.4%
Portland Central City	**7.6%**	**-1.3%**
Clackamas / Milwaukie Totals	8.5%	-1.0%
Airport Way/Columbia Corridor	7.1%	-0.3%
Close In Eastside	4.9%	-0.7%
Outer Eastside	9.5%	2.7%
Portland Eastside Suburbs	**6.9%**	**0.3%**
217 Corridor / Beaverton	13.5%	0.4%
I-5 South Corridor	13.8%	-0.4%
Kruse Way	10.8%	-3.2%
Northwest	3.8%	-0.1%
Sunset Corridor	10.5%	-2.7%
SW Close In	7.1%	-0.3%
Portland Westside	**10.9%**	**-01.1%**
Cascade Park/Camas	6.0%	0.3%
CBD/West Vancouver	9.3%	0.5%
Hazel Dell / Salmon Creek	6.9%	-0.9%
Orchards/Outer Clark	11.1%	0.6%
St. John's Central Vancouver	24.9%	-0.1%
Vancouver Mall	3.9%	1.8%
Vancouver Suburbs	**8.8%**	**0.5%**
Portland Metro	8.8%	**-0.9%**

Source: JLL

RENTAL RATES

JLL reported and overall rent percentage change of 10.4 percent. In the Lloyd District, office rental rates between Class A and Class B spaces are narrowing. Currently Class A rental rates are at $30.74 and Class B are at $28.79. This narrowing is occurring because there is a shortage of Class A creative space in the area which is pushing tenants towards new and renovated Class B and C creative office space. CBRE reported CBD asking rates are up 6 percent year-over-year and suburban asking rates, for the fifth continuous quarter, are up, currently at 4.3 percent year-over-year.

Table 3: Average Quoted Rates ($/SF FSG) by Brokerage and Class, First Quarter 2016

Brokerage	Average	CBD	Suburban	CBD Class A	CBD Class B	CBD Class C
CBRE	$25.00	$28.90	$21.85	$31.04	$26.81	$25.15
Colliers	$23.89	$28.89	--	$31.28	$28.48	$23.00
JLL	$25.70	$29.88	--	$27.95	$23.98	$23.23

Source: CBRE, Colliers International, JLL

Table 4: Portland Average Direct Asking Rent ($/p.s.f.) Ranked by Market Area and Submarket, Second Quarter 2016

Location	Q2	Change from Q1
Portland CBD	$30.28	$0.42
Lloyd District	$25.95	($0.30)
Portland Central City	$29.96	$0.36
Clackamas / Milwaukie Totals	$21.35	$0.02
Airport Way/Columbia Corridor	$19.78	$0.19
Close In Eastside	$25.44	($0.15)
Outer Eastside	$19.83	$1.51
Portland Eastside Suburbs	$21.59	$0.61
217 Corridor / Beaverton	$21.25	($0.17)
I-5 South Corridor	$22.26	$0.42
Kruse Way	$28.94	$0.13
Northwest	$33.98	($1.19)
Sunset Corridor	$20.60	$0.04
SW Close In	$19.29	$0.86
Portland Westside	$23.61	$0.47
Cascade Park/Camas	$19.77	$0.12
CBD/West Vancouver	$20.63	$0.38
Hazel Dell / Salmon Creek	$21.46	$0.48
Orchards/Outer Clark	$19.74	$0.34
St. John's Central Vancouver	$19.89	($0.01)
Vancouver Mall	$18.26	$0.57
Vancouver Suburbs	$19.99	$0.12
Portland Metro	$25.12	$0.53

Source: JLL

ABSORPTION AND LEASING

CBRE reported all three downtown submarkets ended the second quarter with positive net absorptions (CBD, Northwest, and Lloyd District). The data also shows that Portland suburban markets have maintained a 12-month rolling net absorption above 500,000 for the last six quarters. Q2 ended with the highest absorption thus far at 791,441 square feet. JLL reported the net absorption for Q2 lines up with annual demand projections of 750,000 square feet in 2016 – this amount, once reached, will be the first time supply will exceed demand in six years.

Table 5: Net Absorption (square feet) by Brokerage and Area, Second Quarter 2016

Brokerage	Overall	CBD	Suburban
CBRE	444,593	198,439	213,768
Colliers	539,374	213,976	----
JLL	188,4881	152,470	----

Source: JLL; CBRE; Colliers International

Table 6: Notable Lease Transactions, Second Quarter 2016

Tenant	Building/Address	Market	Square Feet
Elemental Technologies	1320 Broadway	CBD	101,400
Consumer Cellular, Inc.	Tigard Corporate Center	217 Corridor/Beaverton	82,140
KPFF	US Bancorp	CBD	47,788
D+H USA Corporation	1320 Broadway	CBD	45,617
Under Armour	Under Armour	SW Close In	38,698
Energy Trust of Oregon	Lincoln Building	CBD	34,161
Design Within Reach	Stagecraft Building	CBD	28,000
KeyBanc Capital Markets	US Bancorp	CBD	27,714
Centrl Office	Block 75	Close In Eastside	23,00
Kaiser Permanente	Montgomery Park	Northwest	22,114
Cardno, Inc.	Willamette Oaks	SW Close In	20,998
M.J. Murdock Charitable Trust	The Waterfront – Block 6	CBD/West Vancouver	18,000
Digital Trends	US Bancorp Tower & Plaza	CBD	17,869
Moovel North America	The Overland	CBD	17,176
Confidential	Block 300	CBD	17,151
DiscoverOrg	Bank of America Bldg	CBD/West Vancouver	15,975
Neighborhood Health Center	Providence Tanasbourne Health Center	Sunset Corridor	14,979

Source: JLL; CBRE

SALES TRANSACTIONS

Colliers International data show $375 million in transactions in the second quarter. JLL reported a total of over $500 million within the first half of 2016 with both urban and suburban areas showing strong assets.

Table 7: Notable Sales Transactions, Second Quarter 2016

Building Address	Submarket	Price	Price/SF	SF
Commonwealth Building	CBD	$69,000,000	$316	218,499
Evergreen Corporate Center	Sunset Corridor	$45,5000,000	$171	266,000
South Center I-IV	I-5 Corridor	$44,250,000	$129	342,316
Tanasbourne Commerce Center	Sunset Corridor	$31,100,000	$169	183, 907
Hanna Andersson Building	Lloyd District	$31,031,486	$259	119,948
Oswego Pointe I	Lake Oswego/West Linn	$3,920,000	$290.28	13,504
14300 SE First Street	Cascade Park	$3,500,000	$192.67	18,165

Source: JLL; Colliers International

DELIVERIES AND CONSTRUCTION

Two notable deliveries during Q2 were Park Avenue West and Pearl West, but even with such large spaces demand is still higher than supply – a trend that does not seem to be slowing as of yet. JLL reports 50 percent of active construction is happening within the CBD. JLL data show Portland tenants are bigger than in recent history. In 2007 the average size leased space for office tenants was 6,500 square feet, now that number is more than 9,000 square feet. The number of signed leases for 20,000 square feet or more has grown 66 percent in the last five years. JLL anticipates this trend will carry on and is currently tracking 3.85 million square feet of demand. Much of this growth comes from the technology sector (currently at 25 percent) that makes up the largest portion of tenants in need of office space.

Class A creative office space is in high demand in city as well as the suburbs. CRBE highlighted the demand for quality office space in both the downtown and metro markets. Over 46 percent of the market's negative absorption in Q2 was from Class B buildings. Tenants are looking to upgrade, particularly in the CBD, Northwest, Close In Eastside, and Lloyd District.

Construction costs are rising and building timelines are getting longer, a fact developers need to be aware of. Developers are also using new and renovated projects to attract Class A tenants by offering more and more high-end amenities. Though rental rates are rising, new construction is allowing more price-conscience tenants to grab up non-renovated Class B and C spaces.

Table 8: Portland Office Market Construction and Deliveries by Submarket, Second Quarter 2016

Location	Deliveries	% of Total Deliveries	Under Construction	% of Total Construction
Portland CBD	**441,109**	**77%**	686,903	50%
Lloyd District	28,563	5%	181,594	13%
Portland Central City	469,672	82%	868,497	63%
Clackamas / Milwaukie Totals	--	--	16,720	--
Airport Way/Columbia Corridor	--	--	--	--
Close In Eastside	72,000	12.5%	112,785	8%
Outer Eastside	--	--	--	--
Portland Eastside Suburbs	72,000	12.5%	129,505	9%
217 Corridor / Beaverton	--	--	--	--
I-5 South Corridor	--	--	--	--
Kruse Way	--	--	--	--
Northwest	29,933	5.2%	56,000	4%
Sunset Corridor	--	--	--	--
SW Close In	--	--	110,120	8%
Portland Westside	29,933	5.2%	166,120	12%
Cascade Park/Camas	--	--	206,000	15%
CBD/West Vancouver	--	--	--	--
Hazel Dell / Salmon Creek	--	--	--	--
Orchards/Outer Clark	--	--	--	--
St. John's Central Vancouver	--	--	--	--
Vancouver Mall	--	--	--	--
Vancouver Suburbs	--	--	206,000	15%
Portland Metro	571,605	100%	1,370,122	100%

Source: JLL

INDUSTRIAL MARKET ANALYSIS

ANDREW CRAMPTON

Portland State University

The Portland area's industrial market continued a strong second quarter, with robust demand for increasingly limited available industrial space pushing vacancy rates to historically all-time lows. Colliers reports vacancy rates of 4.3 percent, a decrease of 20 basis points from the first quarter. The combination of large institutional investors, strong employment growth and increasing population growth are fueling a pipeline of an expected 4 million square feet of projects proposed and under construction, according to Colliers. Major projects include a 303,360 square foot building under construction in the Hillsboro Brookwood Business Park, with speculation that Amazon is the end-user, according to Capacity Commercial Group.

VACANCY AND RENTS

Metropolitan Portland's industrial vacancy continues to reach new lows in the second quarter of 2016, with CBRE reporting a drop from 4.0 percent to 3.6 percent. Colliers reports a region-wide vacancy rate of 4.3 percent, a decrease from the 2015 third quarter vacancy rate of 4.9 percent. Portland's eastside submarket showed the greatest improvement in vacancy this quarter, with the Southeast experiencing a 68 basis point improvement quarter-over-quarter while the Northeast dropped 50 basis points. Both submarkets are now below three percent vacancy.

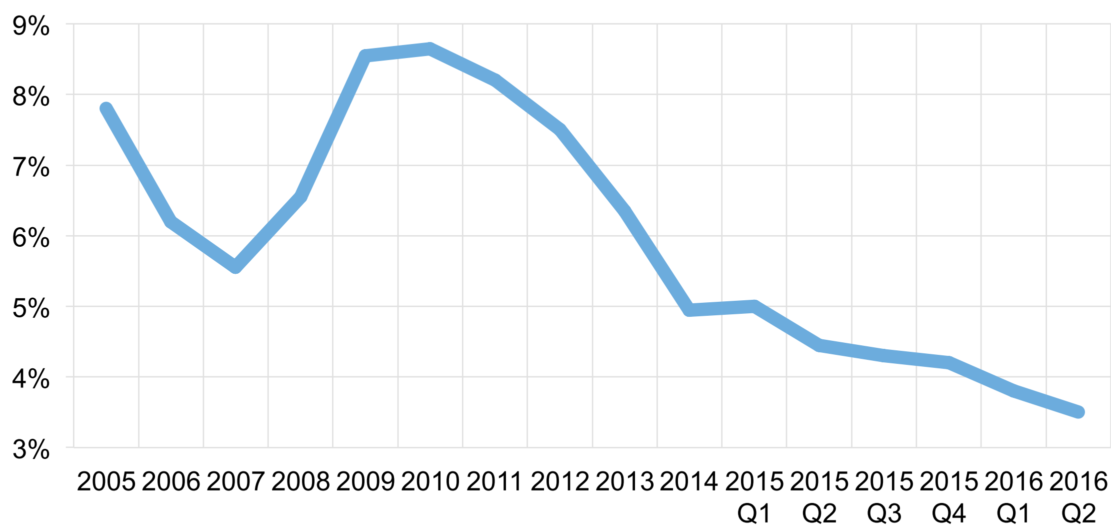
■ **Andrew Crampton** is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.

Table 1: Portland Metro Industrial Quarterly Report Survey Q2 2016

	Colliers	JLL	CBRE	Mathews	Q2 2016
Vacancy					
- Distribution/Warehouse	4.30%	3.40%	4.00%	4.20%	3.98%
- Flex	8.30%	8.60%	-	-	8.45%
- Weighted Average	4.66%	3.89%	4.00%	4.20%	**4.19%**
Manufacturing		4.7%			
Rents *					
- Distribution/Warehouse	$0.52	$0.56	$0.43	$0.53	$0.51
- Flex	$0.97	$0.96	$1.05	-	$0.99
- Weighted Average	$0.56	$0.60	$0.49	$0.53	**$0.54**

Portland's industrial market fundamentals remain strong at the mid-year point. CBRE reports that overall vacancy fell below 4 percent and is now just 7 points from reaching 3.5 percent. As vacancy continues to contract, relocation options for mid-sized and larger tenants becomes more difficult, and more renewals-in-place with smaller tenants becoming displaced if room for expansion is necessary. The total sales volume from the second quarter was nearly $229 million, according to Kidder Matthews. The average sale price per square foot was $98. With nearly 3 million square feet under construction and broker sentiments that most of it will be leased prior to delivery, the market may see up to 5 million square feet delivered per year.

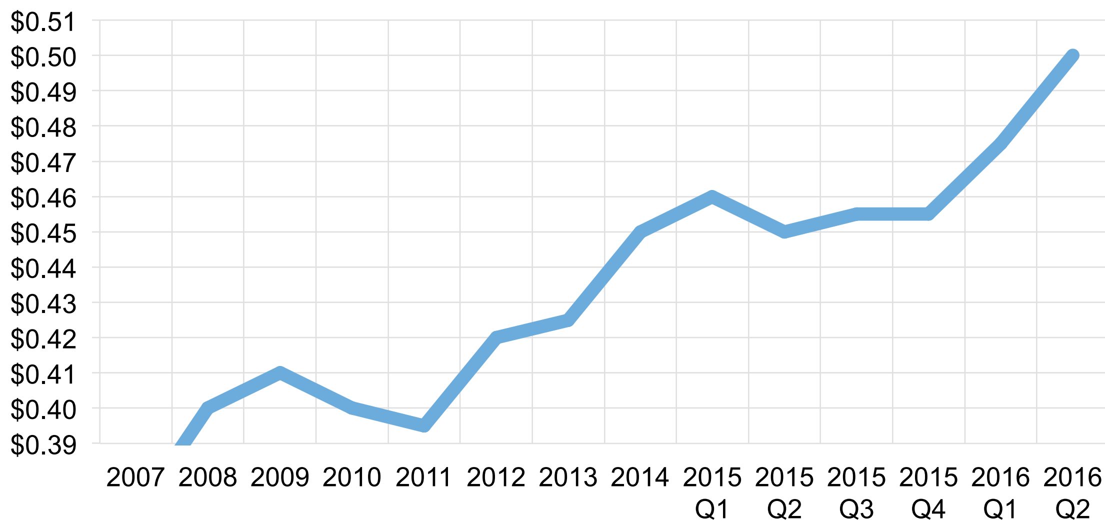
Figure 1: Portland Metro Distribution/Warehouse Vacancy Rate, 2007–2016 Q2



Sources: Average of Quarterly Reports from CBRE, JLL, Colliers

Strong demand also pushed up asking rental rates to record high levels in the second quarter. Asking rates in distribution/warehouse space is priced at $0.43 triple-net with newer, well-located asking up to $0.50 per square foot. The surcharge for office space is now at an average of $0.85 per square foot, according to CBRE. Distribution/warehouse transactions are between $0.38 to $0.40 per square foot for older warehouse space, and up to $0.42 to $0.45 per square foot in Portland's newer facilities. Asking rates for flex spaces continue increasing to an average high of $1.05. JLL reports that the Portland Industrial market has experienced a 12 month increase of 12 percent to $0.56 per square foot, with new product typically leased before occupancy.

Figure 2: Portland Metro Distribution/Warehouse Asking Rents, 2007–2016 Q2



Sources: Average of Quarterly Reports from CBRE, JLL, Colliers

ABSORPTION AND DELIVERIES

CBRE reported positive net absorption of over 671,376 square feet in the second quarter and 1,244,480 net absorption YTD. Of the leases signed above 10,000 square feet in the second quarter, 91 percent were from companies that were either stable or growing. Large users continue a shift in Portland's industrial market towards national and multinational corporations. Portland saw an increase in large users in 2015 with 25 leases signed for spaces over 100,00 square feet averaging more than 315,00 square feet, up 66 percent from the previous year. This trend is continuing in 2016, with the average year to date lease size of the top 5 leases at 171,208 square feet, anchored by the 235,200 square foot PDX Logistics Center transaction. The large spike in 2015 top 5 lease size was fueled by the 600,000 square foot Subaru Distribution Center at the Port of Portland's Gresham Vista Business Park.

Integra Realty Resources estimates a change in value over the next 12 months to increase 0.1 percent to 1.9 percent for flex industrial and 2 percent to 3.9 percent for industrial. Construction square footage is projected to deliver 2,500,000 in the next 12 months and annual absorption of 250,000 square feet of flex industrial and 1,000,000 of industrial.

Table 3: Average Square Footage of Yearly Top 5 Leases

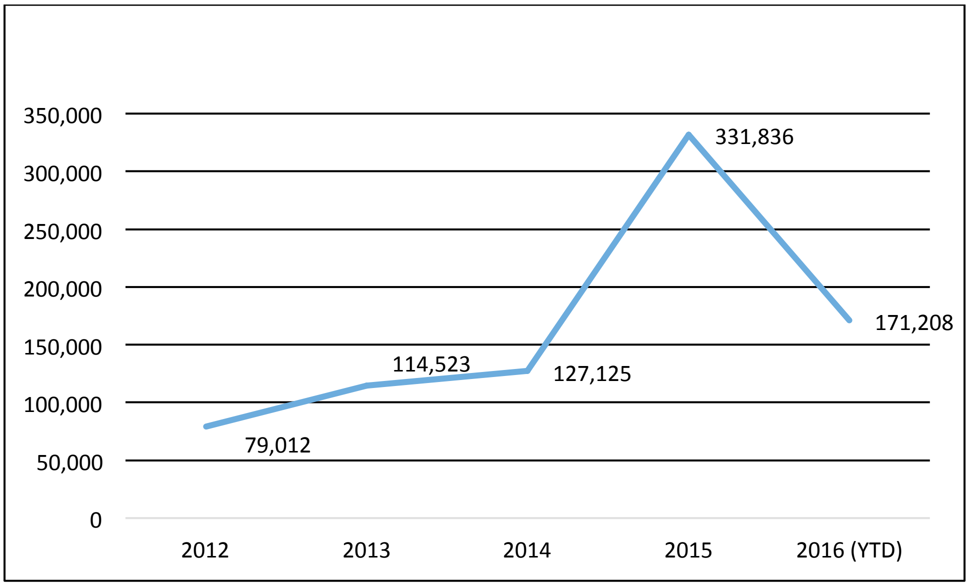


Table 2: Portland Metro Industrial Net Absorption Last 4 Quarters (Excluding Intel)

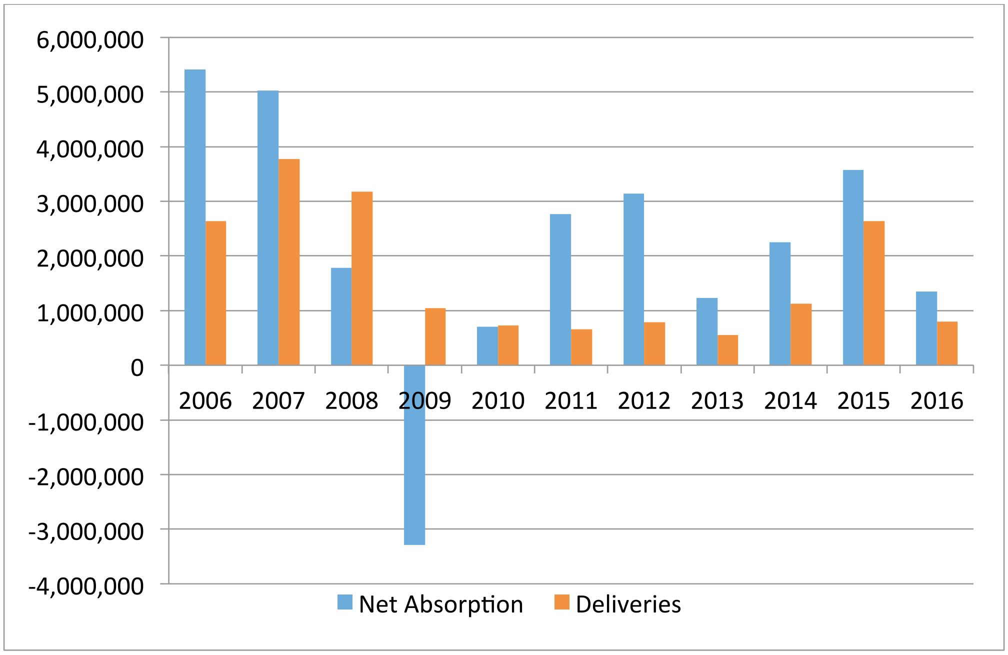
JLL Deliveries and Absorptions

	Distribution/Warehouse	Flex	Total
Q3 2015	1,759,619	156,810	1,916,429
Q4 2015	1,908,179	1,237,599	3,145,778
Q1 2016	573,104	5,696	578,800
Q2 2016	671,376	97,354	768,730
Total Last 4 Quarters	4,912,278	1,497,459	6,409,737

Source: JLL

Despite this long-term trend towards large institutional corporate owners, the recent completion of major projects including the PDX Logistics Center and Gresham Vista Business Park could lead to a second cycle of speculative investment in smaller speculative projects. JLL reports that projects ranging in size from 25,000 square feet to 75,000 square feet currently account for 30 percent of the speculative development currently underway, which will address a much needed market gap for mid-sized users.

Figure 3: Portland Metro Industrial Net Absorption & Deliveries, 2005–2016 YTD (Excluding Intel)



Sources: 2006-2016 Colliers Quarterly Reports and 2016 JLL Quarter 2 Report

Industrial Demand

JLL is currently tracking 4.1 million square feet of industrial demand. The demand is primarily being driven by large users, with the average size requirement being 115,000 square feet and 1.7 million square feet required from tenants seeking spaces in excess of 200,000 square feet. Over 44 percent of these users are in the logistics and distribution sector, with 84 percent looking for space in the NE Columbia Corridor. As Portland's population continues to surge, the expansion of delivery and freight service centers will follow suit, keeping the demand for warehouse and distribution space strong.

INVESTMENT ACTIVITY

JLL reports that 2016 has seen over $142 million in sales so far, with the sale of PDX Logistics Phase I for $44.6 million and a cap rate of 5.7 percent being the largest this year

According to CBRE, the overall price per square foot increased in the quarter from $103.10 to $110.62. While all classes of industrial building sales continue toward pre-recession levels, investment sales are nearly level with owner/user product at $105.12 per square foot.

Table 4: Notable Portland Metro Industrial Lease Transactions Q2 2016

Notable Lease Transaction Q2 2016

Address	Location	Size (s.f.)
UPS	Portland	235,200
Bay Valley Foods (Renewal)	Portland	150,000
Cummins	Portland	120,000
AOSOM	Wilsonville	105,361
Kellogg's	Portland	95,576

Sources: CBRE and JLL

LOOKING AHEAD

Portland is running out of prime undeveloped industrial land. The recent purchase of 47.5 acres of the former Colwood golf course for the new 789,837-square-foot U.S. Postal Service's mail distribution center has taken prime industrial development land out of the market. Developers, who may have waited for a build-to-suit tenant in previous cycles, are showing signs or a willingness to move forward on a speculative basis to capture demand in the market. The employment data captured this increased activity as the construction sector was the second best performing industrial sector for the third month in a row, adding 2,800 year-on-year jobs in May.

With the market's fundamentals likely to remain strong over the next four quarters, demand for limited supply is also set to drive industrial sales prices even higher, pushing capitalization rates to even lower levels. Most analysts expect speculative developments to continue, and some predict that future projects are likely to be smaller in overall size than those currently under development, with many targeting small- and mid-sized tenants. ■

RETAIL MARKET ANALYSIS

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While big brand name store closures have been on the rise in the U.S. since January (Ralph Lauren and Uniqlo being the most recent to announce closures), overall shopping center vacancies are down compared to recent quarters. Although national rental rates have increased, the current vacancy rate is at a low 7.6 percent (down from 7.8 percent in the first quarter). Consumer spending was the main cause of this quarters' growth and both investment and inventories fell for the first time since 2011.

Cushman & Wakefield note that while the full effects of Brexit are still unknown, the U.S. economy is one of the strongest in the world and will unlikely be greatly felt by the long-term effects of Brexit. The two main markets Brexit could impact are tourism and luxury retail. With the pound at a 30 year low UK travelers may cancel their U.S. summer travel plans, but the strength of the dollar could encourage more travel and spending from Americans. Retail brands looking to expand to the UK will likely find themselves in a challenging economy that could also negatively impact efforts to expand to the rest of Europe.

A major factor in the national growth last quarter came from the restaurant industry and Portland is no exception. In August of 2016 the Washington Post named Portland the number one "food city" in the U.S. With projects such as the Pine Street Market opening and the anticipated James Beard Public Market coming in 2018 this national ranking is not a surprise. With that said, according to the website, Eater (pdxeater.com), 34 restaurants have closed in Portland just this year.

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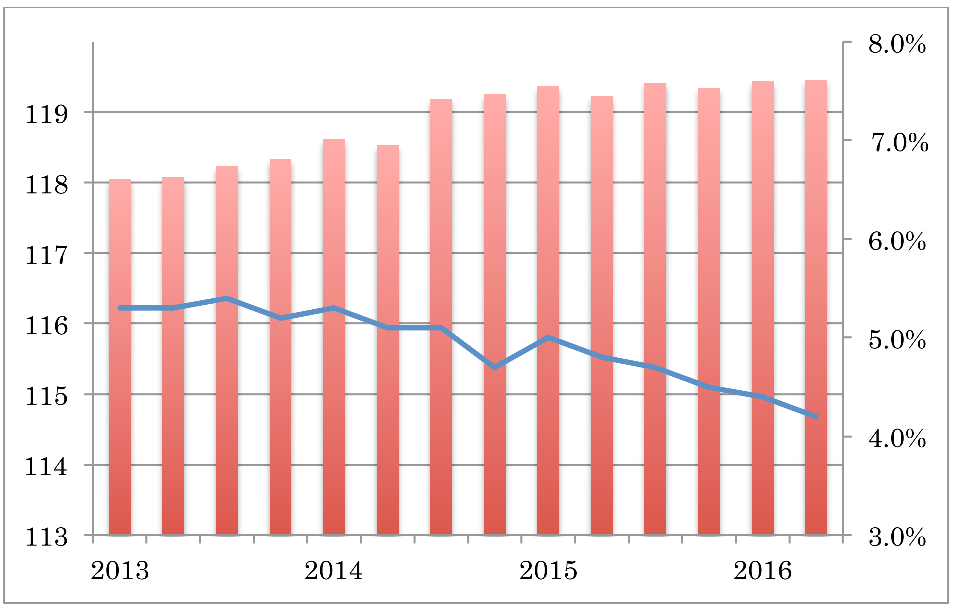
Part of this is due to the extreme growth Portland is experiencing driving rising retail rent prices.

VACANCY

Costar reported that Portland vacancy rates continued to show a steady decline, an overall market trend seen during the last four quarters, with the direct vacancy rate ending at 4.2 percent for the second quarter. (Compared to 4.3 in the second quarter and the national rate of 7.6 percent.)

Figure 1: Portland Retail Market Net Rentable Area (square feet in millions) and Vacancy (%) by Quarter, 2013-2016



Source: Kidder Mathews and CoStar

Costar data showed an overall vacancy rate of 4.2 percent with all submarkets at the five percent level or below, with the exception of Clark County. The Northwest is notable with the lowest rate of 2.6 percent.

Table 1: Portland Retail Market Vacancy by Submarket, Second Quarter 2016

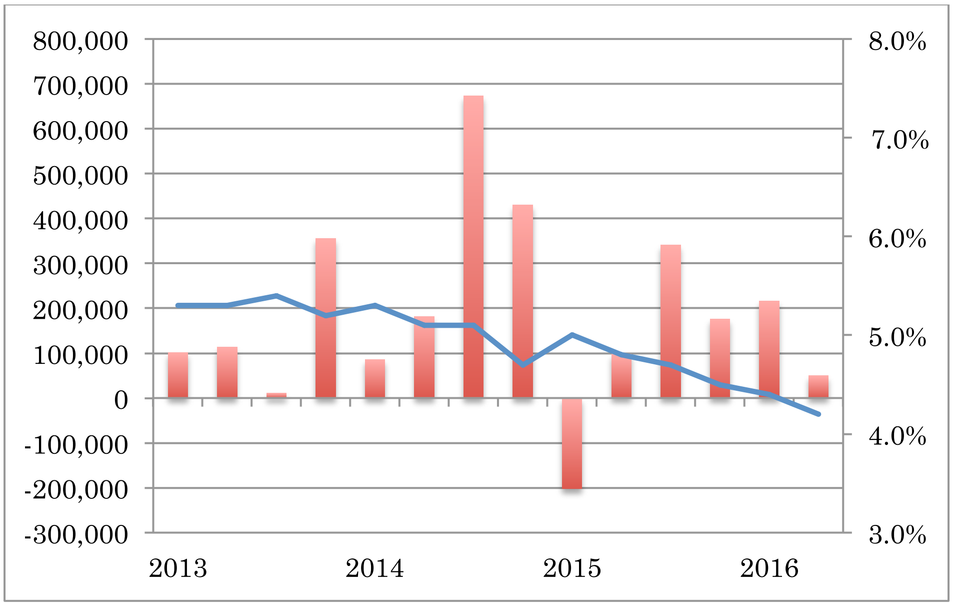
Submarket	Vacancy (%)
CBD	4.0%
Clark County	5.9%
I-5 Corridor	5.0%
Lloyd District	4.9%
Northeast	3.5%
Northwest	2.6%
Southeast	4.0%
Southwest	3.5%
Westside	3.4%
Total	**4.2%**

Source: CoStar

ABSORPTION AND LEASING

Costar reports a net absorption of 49,616 square feet in the second quarter. This number represents a basically flat net absorption, but specialty centers and malls were some of the most prominent leasers.

Figure 2: Net Absorption Rate (square feet) and Vacancy (%) by Quarter, 2013-2016



Source: Kidders Matthew and CoStar

Table 2: Portland Retail Market Absorption by Submarket, Year-to-date 2016

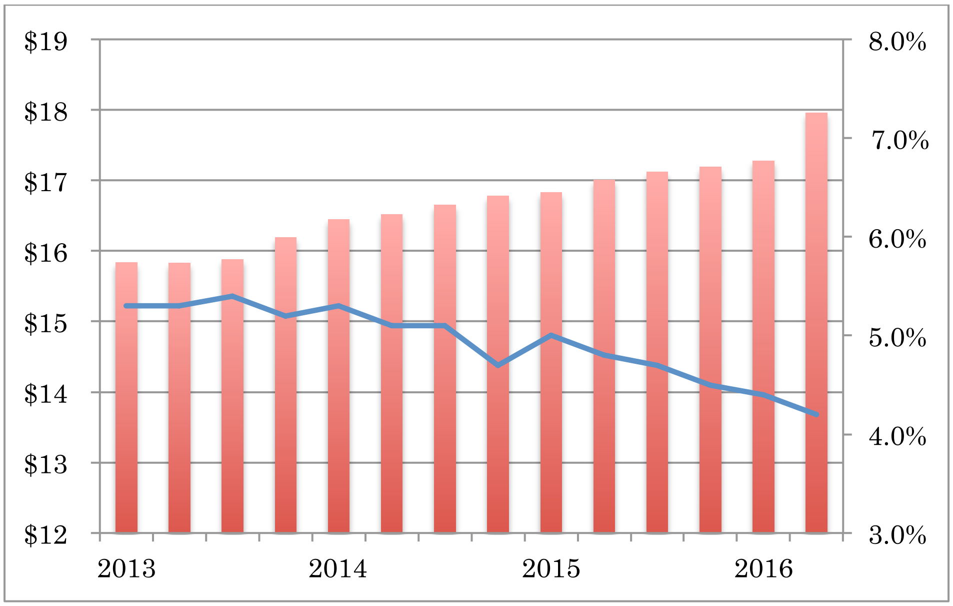
Submarket	YTD Absorption	Absorption as a % of YTD RBA
CBD	15,320	0.08
Clark County	84,474	0.07%
I-5 Corridor	(20,525)	1.1%
Lloyd District	(14,525)	(2.3%)
Northeast	71,966	0.6%
Northwest	17,966	6.7%
Southeast	(26,224)	0.6%
Southwest	16,978	0.5%
Westside	76,367	(0.3%)
Total	**221,278**	**0.7%**

Source: CoStar

RENTAL RATES

Costar reports that rents continued to trend up, ending at $17.96 per square foot NNN per year. This is 2.2 percent increase from the previous quarter.

Figure 3: Portland Retail Market Average Quoted Rates ($/SF/Yr/NNN) and Vacancy (%) by Quarter, 2013-2016

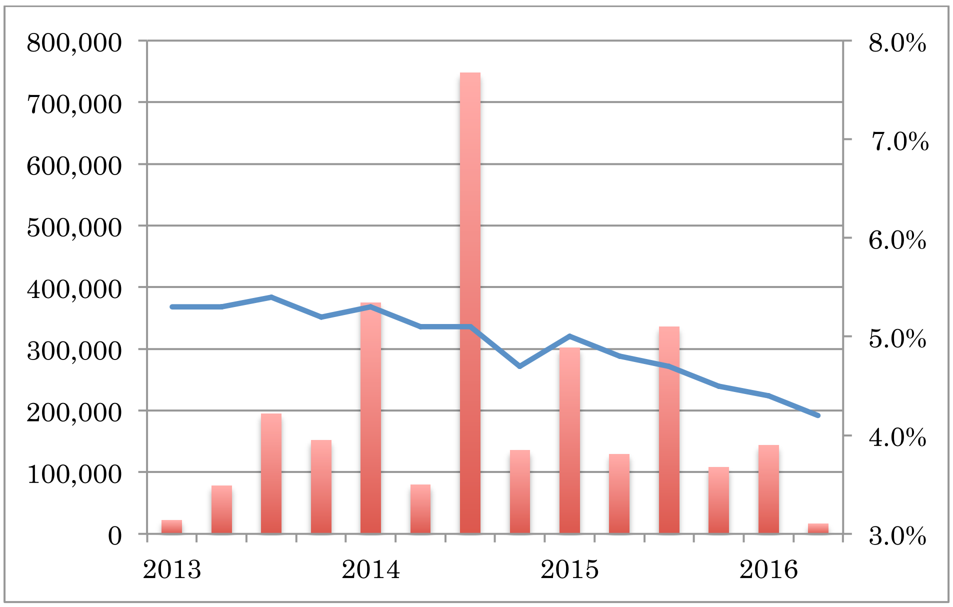


Source: Kidders Matthew and CoStar

DELIVERIES AND CONSTRUCTION

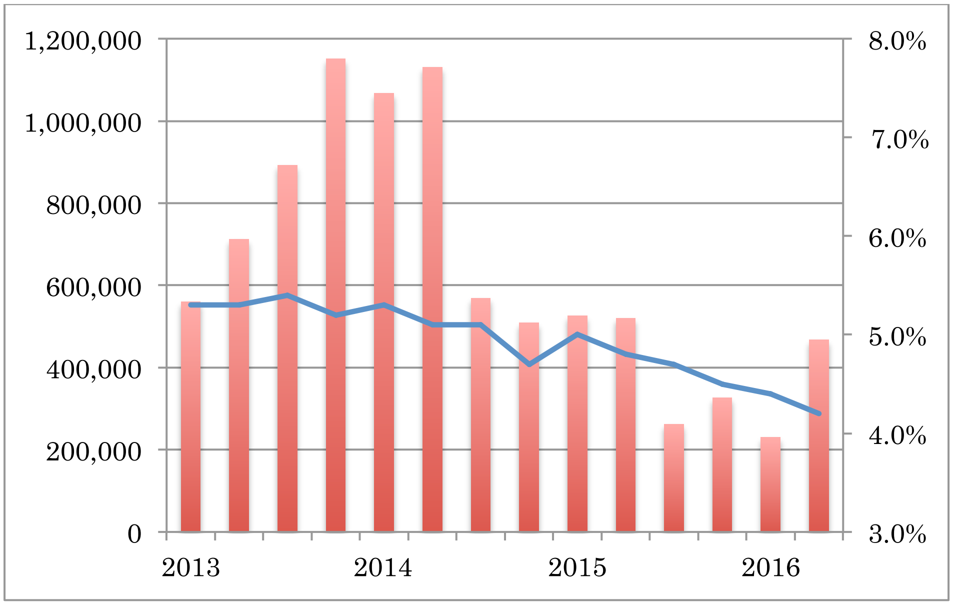
CoStar reported a total of three buildings delivered for a total of 16,163 square feet for the quarter. There are a total of 18 projects under construction, for a total of 467,380 square feet, 87.2 percent of the total square footage is already pre-leased. Some notable projects include Parkway Village at Sherwood – The Old Spaghetti Factory and 1511 NE 92nd Ave.

Figure 4: Portland Retail Market Deliveries (square feet) and Vacancy (%), 2013-2016



Source: Kidder Mathews and CoStar

Figure 5: Portland Retail Market Construction (square feet) and Vacancy (%), 2013-2016



Source: Kidder Mathews and CoStar

SALES

Table 3: Notable Investment Transactions, Second Quarter 2016

Property	City	Sale Price	Square Feet	Price/SF
Evergreen Marketplace	Washougal	$43.0	184,612	$232.92
Andresen Marketplace	Vancouver	$43.0	184,612	$232.92

*These two buildings were part of the same sale with a cap rate of 6.70% cap rate.

Source: CoStar