Winter 2019

Center for Real Estate Quarterly, Volume 13, Number 1

Portland State University. Center for Real Estate

CENTER FOR REAL ESTATE

QUARTERLY REPORT

Volume 13, Number 1 | Winter 2019

A PUBLICATION OF

Portland State University
Center for Real Estate

AVAILABLE FOR DOWNLOAD AT

pdx.edu/realestate/research_quarterly

A publication of

Portland State University Center for Real Estate
P.O. Box 751-SBA
Portland, Oregon 97207-0751

Publisher

Gerard C.S. Mildner, Ph.D.

Editor

Eric Fruits, Ph.D.

Staff

Melissa Meagher
Chase Bennington
Michael Lowes
Jarrod Howard

Generous financial support provided by

Oregon Association of Realtors
RMLS
Society of Industrial and Office Realtors
TigerStop

CONTENTS

01 //

ECONOMIC & RESIDENTIAL MARKET ANALYSIS

JARROD HOWARD
& ERIC FRUITS
Portland State University

The fourth quarter in Oregon and southwest Washington saw cooling markets with respect to transaction volume, but a favorable market for sellers as prices continue to tick up. In Portland and Vancouver prices continue to be at all-time highs and continue to rise. Portland's neighboring cities appear to be following this trend with home price increases spreading west to Hillsboro and Beaverton as well as south. Portland and Vancouver continue to price people out, causing buyers to look elsewhere for something more affordable with proximity to downtown Portland.

Bend and Redmond continue to be hot areas, but prices have slowed after multiple years of significant increases. With only a moderate decrease in housing prices, Bend continues to face an affordability challenge. As a result, Redmond could be benefiting from a spillover. Prices in Redmond continue to be more favorable and attainable as well as in closer proximity to the expanding Redmond airport. This is likely why we saw transaction volume increase in Redmond by about 50 percent.

With sales prices either steadying or continuing to increase almost everywhere in the state of Oregon and southwest Washington, house sales are slowing. The single-family home supply does not appear to be meeting the necessary demand and forecasts show that gap continuing to widen.

Jarrod Howard ***is a current Master of Real Estate Development candidate through a joint program of Portland State University's School of Business Administration and School of Urban Studies and Planning. He is the 2018 RMLS Student Fellow at PSU's Center for Real Estate.***

Eric Fruits, ***Ph.D. is the editor of the Quarterly Report the Oregon Association of Realtors faculty fellow at Portland State University. He is an adjunct at Portland State University where he teaches course in economics and real estate. Any opinions expressed are those of the authors solely and do not represent the opinions of any other person or entity.***

ECONOMIC FACTORS FACING THE OREGON RESIDENTIAL REAL ESTATE MARKET

Analysis forecasts, over the next five years, Oregon's population will grow at 1.2 percent per year, adding approximately 268,000 residents between 2019 and 2024. The growth rate is slightly lower than in previous years, but substantially higher than projected population growth nationwide.

The number of people working in Oregon is expected to grow slower than population. The Office projects the state will add a little more than 92,000 jobs over the next five years, which amounts to an average annual employment growth rate of a little less than one percent per year. In contrast, U.S. employment is anticipated to grow at an average rate of about 0.4 percent per year. This raises the question: How can Oregon's employment grow at a rate faster than the U.S. as whole, but fail to keep pace with the state's employment growth?

As more Baby Boomers exit the labor force, employment will decline. Despite the stereotype of Oregon as a destination for Millennials and Gen Z, the state's population tends to skew older than the average state. To the extent older residents account for a larger share of in-migration, employment in the state will lag population growth.

Even accounting for age, Oregon is known for having a below average labor force participation rate. The December forecast from the Office notes:

However, the participation rate remains a little lower than expected, when adjusting for the size of the population and the aging demographics. Oregon's participation rate continues to rebound today, which is great news, however any participation gap is still cause for concern. While much of the past decade's patterns can be attributed to the severe nature of the Great Recession, and even the lackluster housing boom itself, some damage is likely permanent.

Personal income is projected to lag the national average into the foreseeable future, according to the Office. In 2019, per capita personal income is about $4,000 lower than the U.S. as a whole. By 2024, the gap is expected to widen to $4,900, or about 7.4 percent lower than U.S. per capita personal income.

These factors—population, employment, and income—play key roles in the demand for housing. The state's economists project that housing starts will ramp up over the next few years, despite a relatively lackluster 2018. The Office forecasts that housing starts will increase by about 5.5 percent each year over the next three years. While demand side factors point to increased pressure to build more housing, supply side factors are likely to dampen the state's economists' optimistic forecast.

Oregon's land use regulations severely constrain the amount of buildable land for residential construction and recent additions to the Portland region's urban growth boundary a not likely to be sufficient to satisfy the increased demand for housing, especially the demand for single-family housing. The 2018 expansion is expected to account for 6,100 new houses and 3,100 apartments, or less than seven percent of the state's projected housing starts over the next five years.

Construction employment may impose a bottleneck in homebuilding. Construction employment has seen big gains since the recession and some builders are complaining of a shortage of construction labor. Facing near full employment in construction, the Office concludes, "construction is expected to add jobs at a slower pace even as the housing rebound continues."

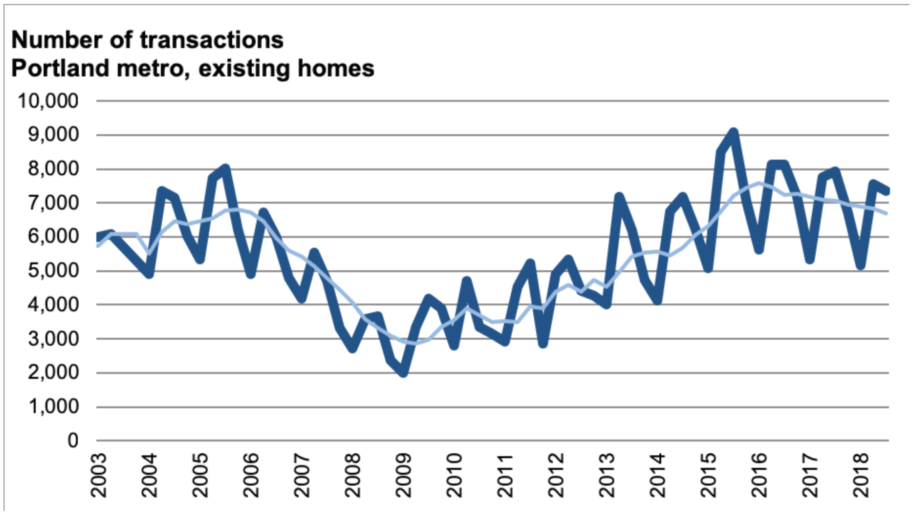
Oregon House Bill 2001, would require every city of more than 10,000 and county of at least 15,000 to allow "middle-housing" of two, three and four-unithomes in residential neighborhoods within their urban growth boundary. By allowing for multi-family development in areas currently zoned for single family, the total number of housing units would likely increase, while the number of single family units would decline, leading to an increase in price for single family residences. In addition, the "option value" of being able to develop an existing single-family property into a multi-family property would likely increase the land value of current single family units that would be subject to HB 2001. (One unintended consequence of HB 2001 may be initiatives to designate more neighborhoods as historic districts as a way to stifle the tear down and redevelopment of existing homes.)

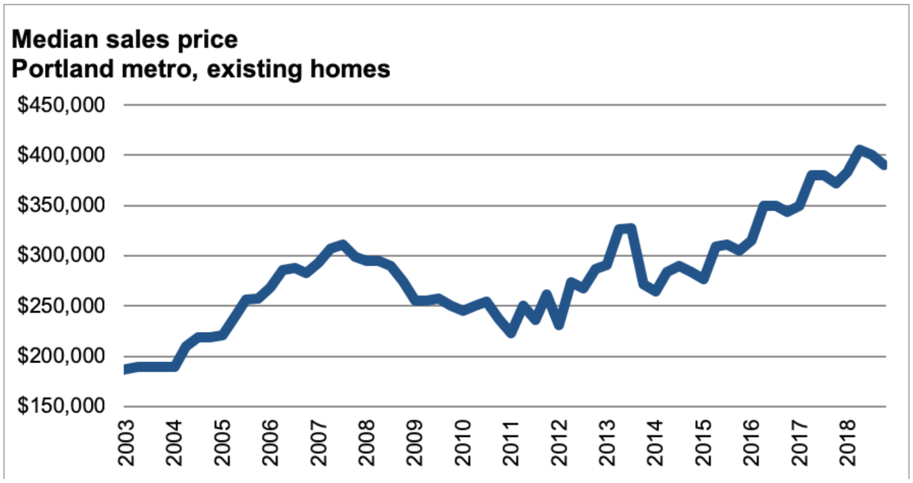
Several property tax reforms are working their way through the legislature; all of them would require voter approval to upend existing property tax limitations written into the state constitution. One of them, Senate Joint Resolution 2, would redefine assessed value (AV) to equal no less than 75 percent of real market value (RMV). The resolution introduces an exemption on the first $25,000 of assessed value. Nevertheless, for many—if not most—homeowners in Oregon, this would result in a property tax increase. For example, Multnomah County presented information to the Senate Committee on Finance and Revenue showing that approximately 90 percent of residential properties in the county would see higher property taxes under SJR 2.

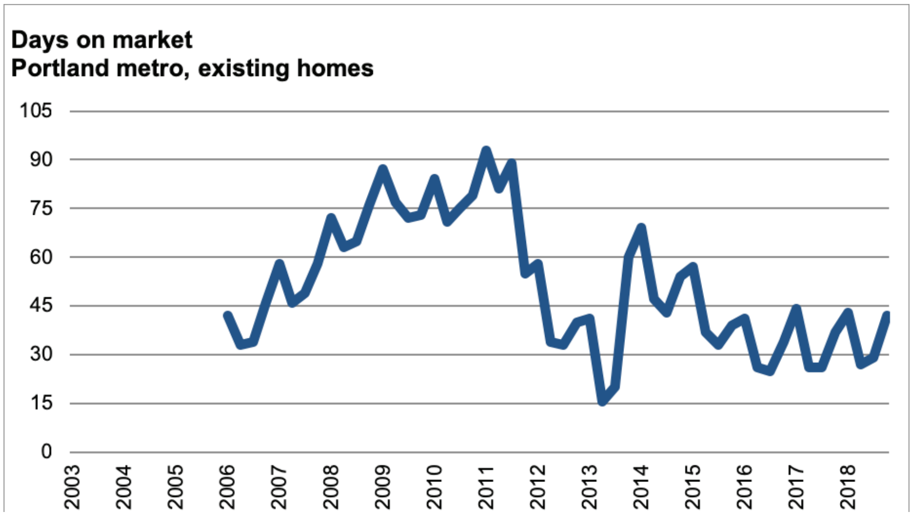
The uncertainties associated with a significant disruption to the current property tax system could disrupt residential property markets as potential buyers and sellers delay transactions until the uncertainties are resolved.

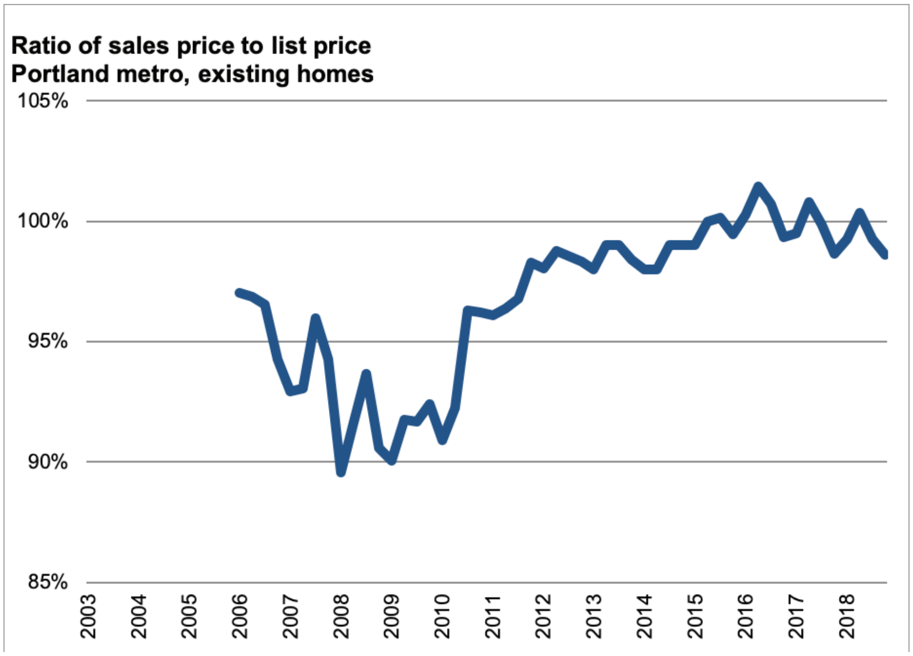
PORTLAND TRANSACTIONS

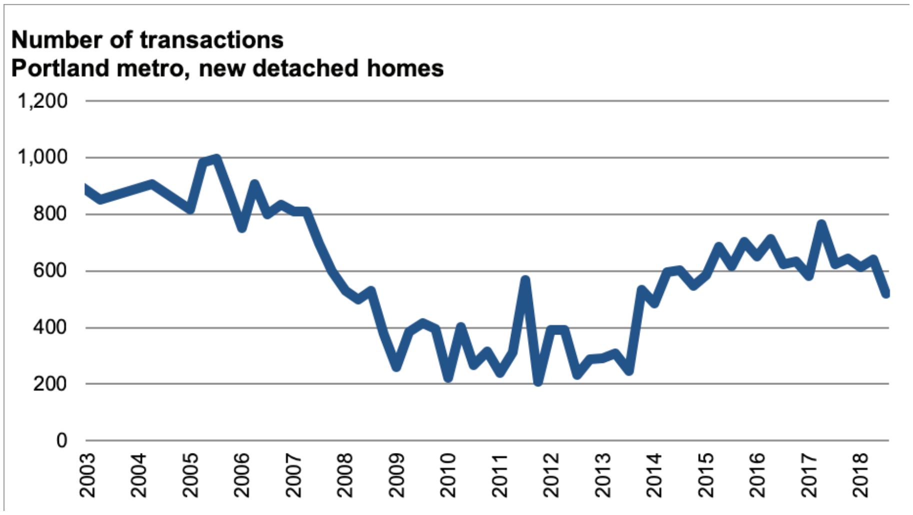
For the third year in a row, existing home sales in the City of Portland have continued trending downward with 1,625 fewer houses sold in the fourth quarter. This is a decrease of over 22 percent from the prior quarter, and 984 fewer houses than the same quarter of last year. In addition, the median sales price increased from the previous year, while the sales price to list price ratio slightly decreased.

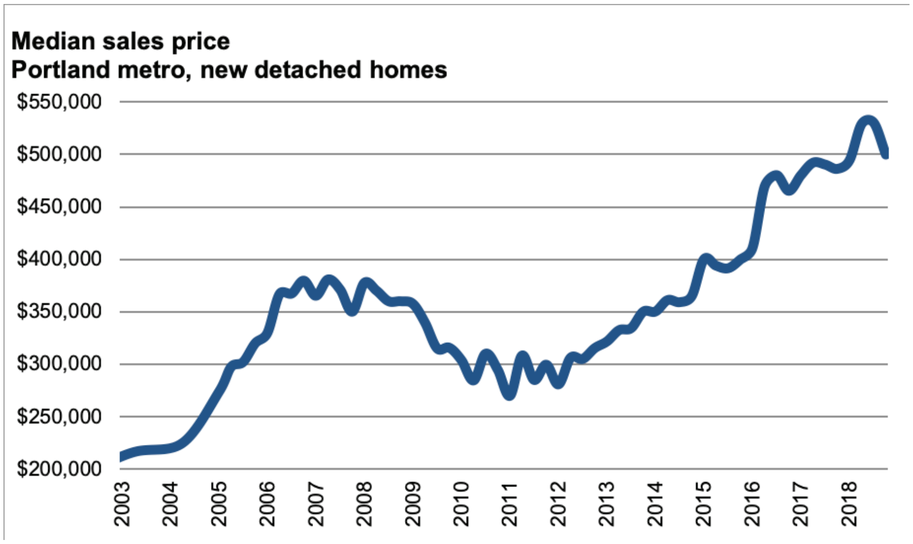







Ratio of sales price to list price
Portland metro, existing homes
105%
100%
95%
90%
85%
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

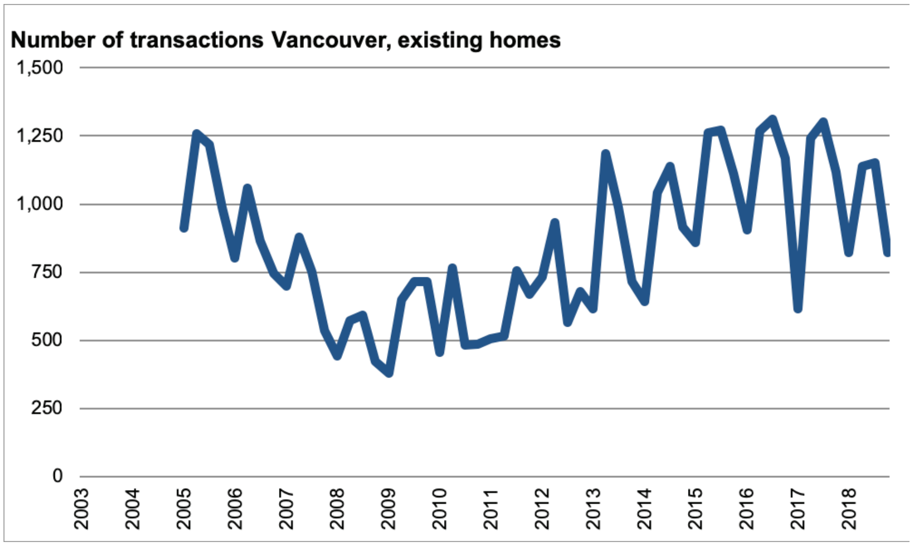

Number of transactions
Portland metro, new detached homes
1,200
1,000
800
600
400
200
0
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

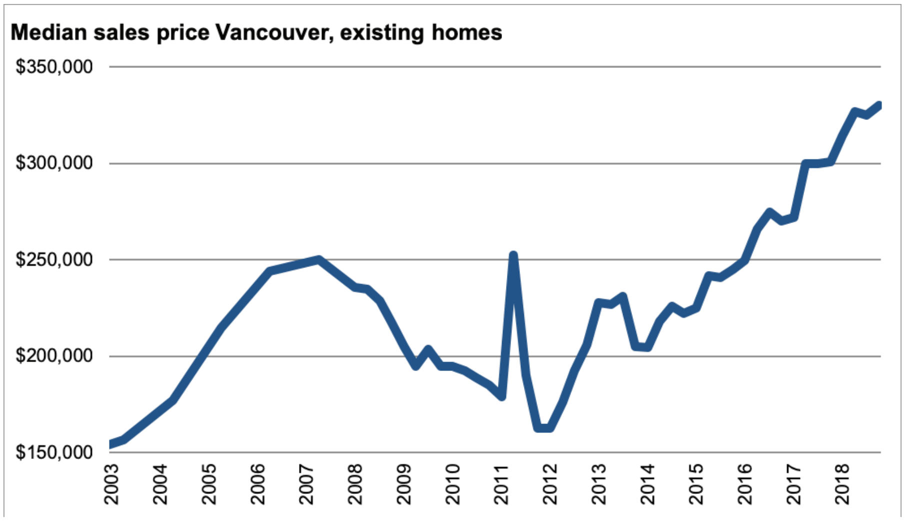

Median sales price
Portland metro, new detached homes
$550,000
$500,000
$450,000
$400,000
$350,000
$300,000
$250,000
$200,000
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

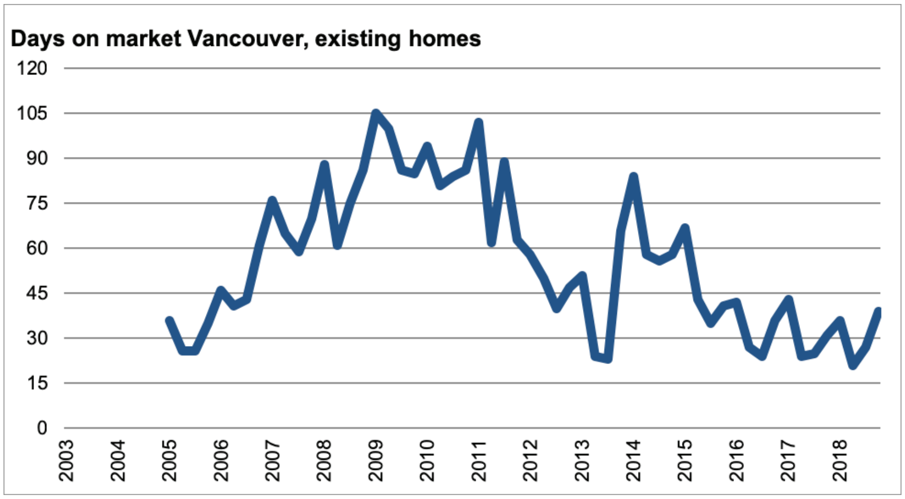
VANCOUVER & CLARK COUNTY

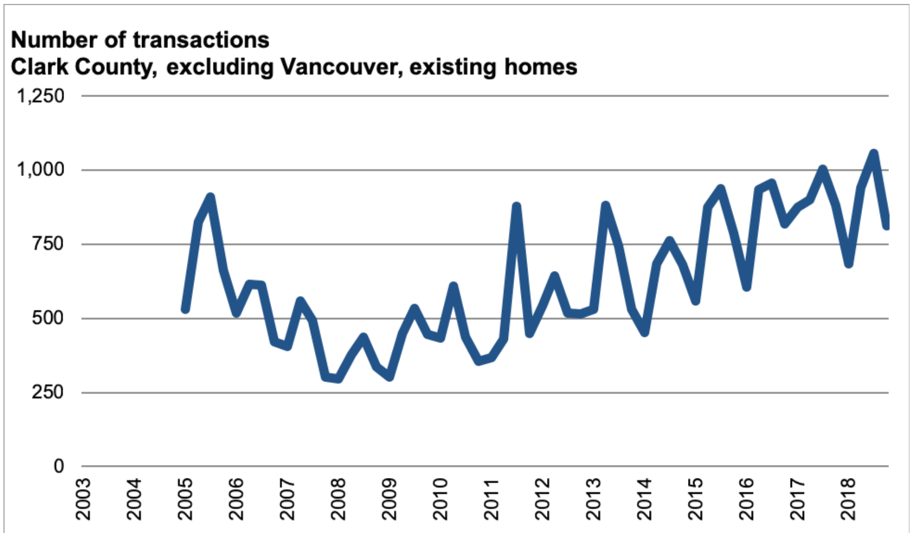
The fourth quarter in Vancouver ended in the fewest number of transactions seen in a fourth quarter since 2013. While the transaction count saw an unusual drop, median sales price continued to increase to $330,000 in the fourth quarter. This is nearly a 10 percent increase from the same quarter last year. The sale-to-list price ratio remained unchanged from the fourth quarter of last year coming in at just over 98.7 percent.

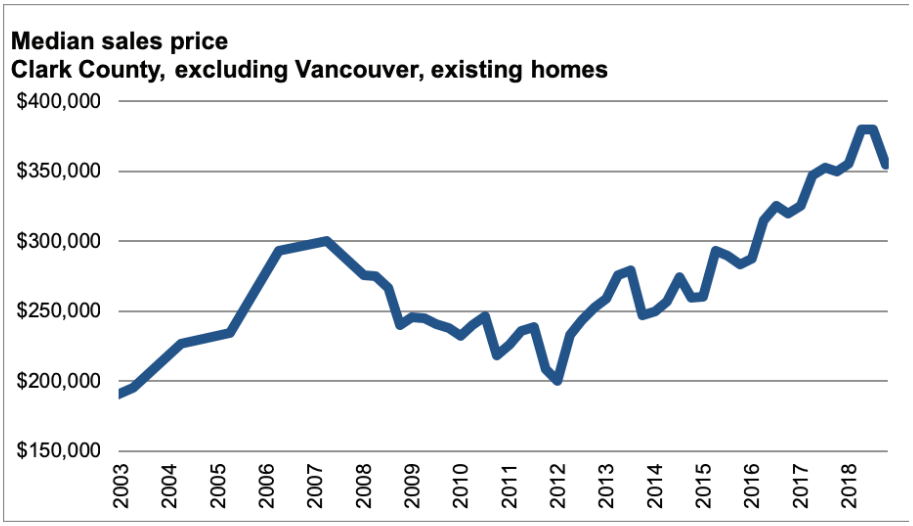
After several years of upward trending, Clark County saw its first decrease siwnce 2010 with 813 transactions, and the highest median sales price for any fourth quarter. Similar to Vancouver, the sales price and listing price ratio steadied from last year at just under 98.3 percent.

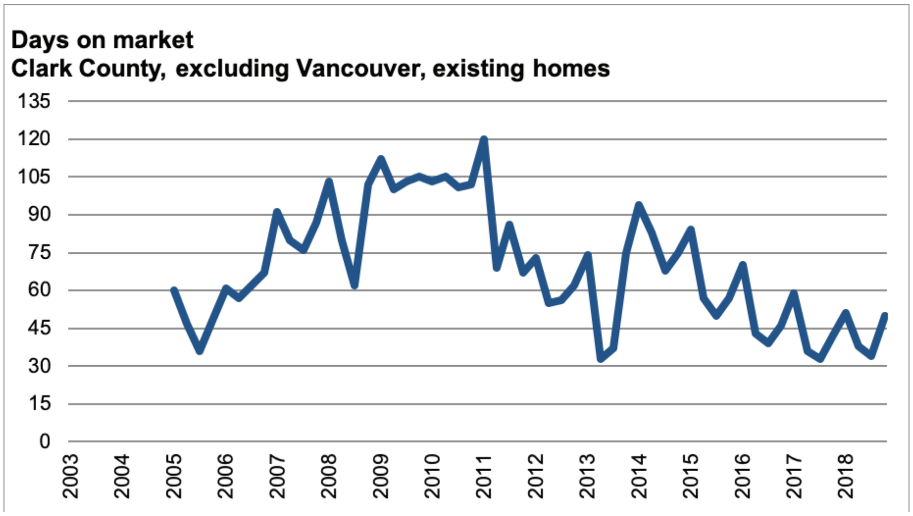







Number of transactions
Clark County, excluding Vancouver, existing homes
1,250
1,000
750
500
250
0
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

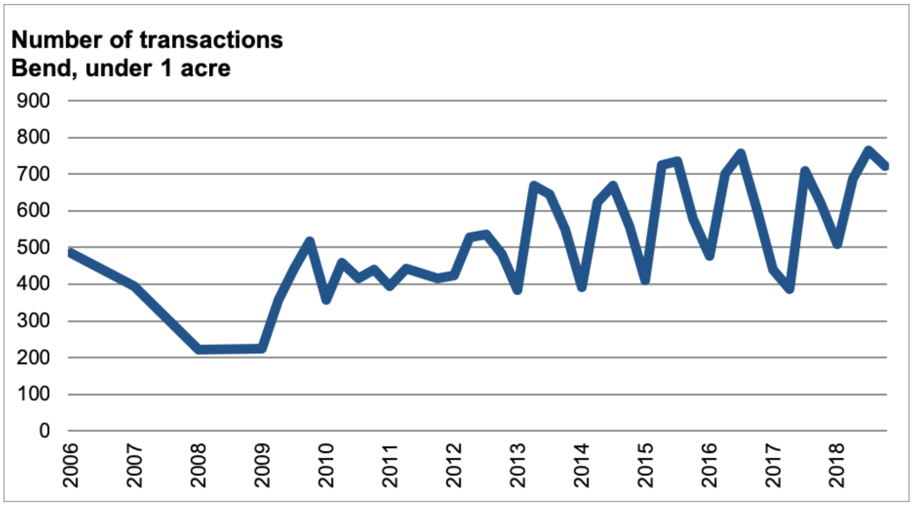

Median sales price
Clark County, excluding Vancouver, existing homes
$400,000
$350,000
$300,000
$250,000
$200,000
$150,000
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

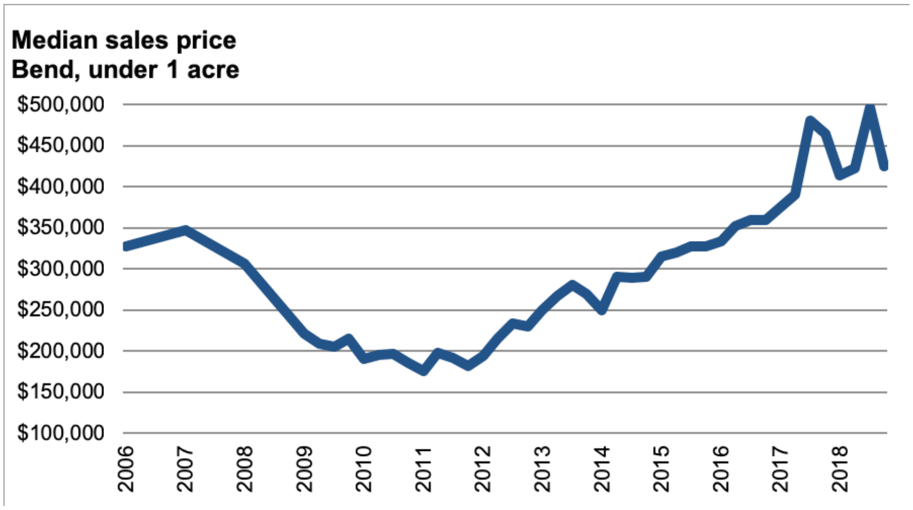

Days on market
Clark County, excluding Vancouver, existing homes
135
120
105
90
75
60
45
30
15
0
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

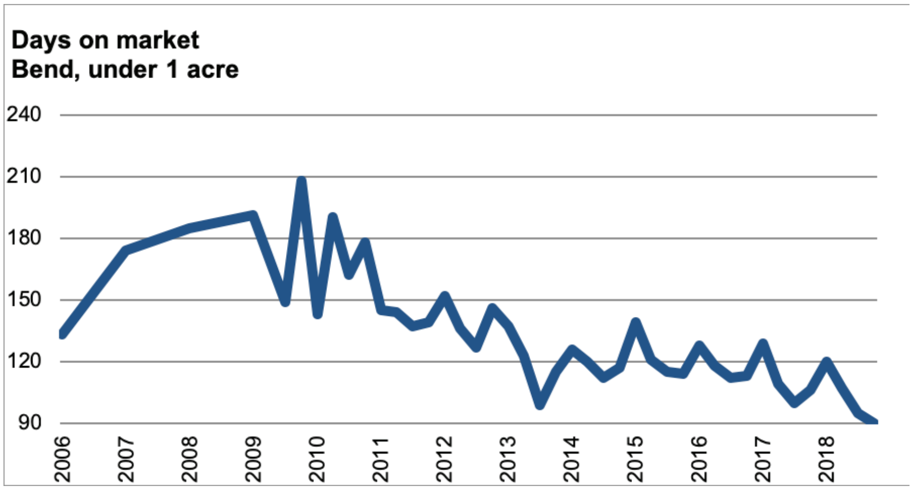
CENTRAL OREGON

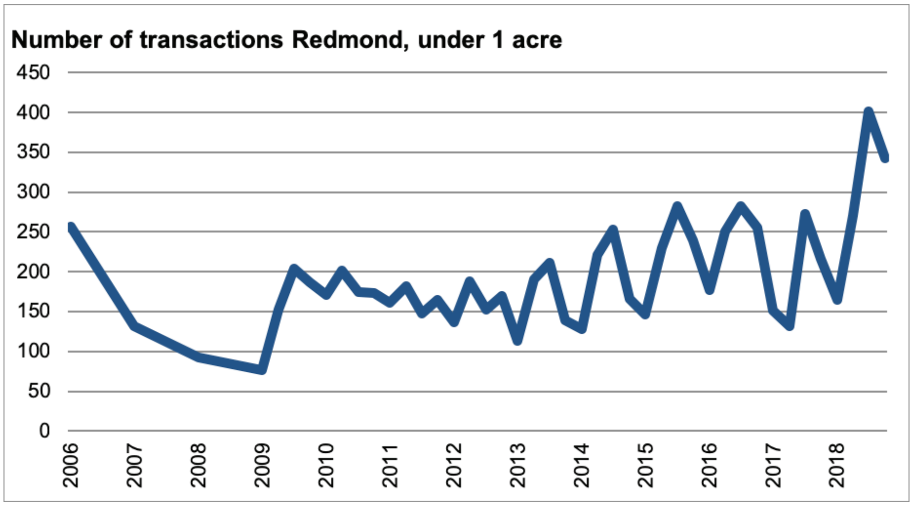
Bend saw an increase in the number of transactions in the fourth quarter with 721 sales in 2018 versus 622 sales in the same quarter of the previous year. Along with the increase in transactions, the median sales price decrease by more than 14 percent from the third quarter and more than 8 percent from the fourth quarter of 2017. This snapped seven consecutive years of increased median home sales prices dating back to 2010. Days on market continues to decrease, coming in at an average of 90 days. This broke the record from the third quarter of 2018 and continues to show houses are staying on the market for a short amount of time.

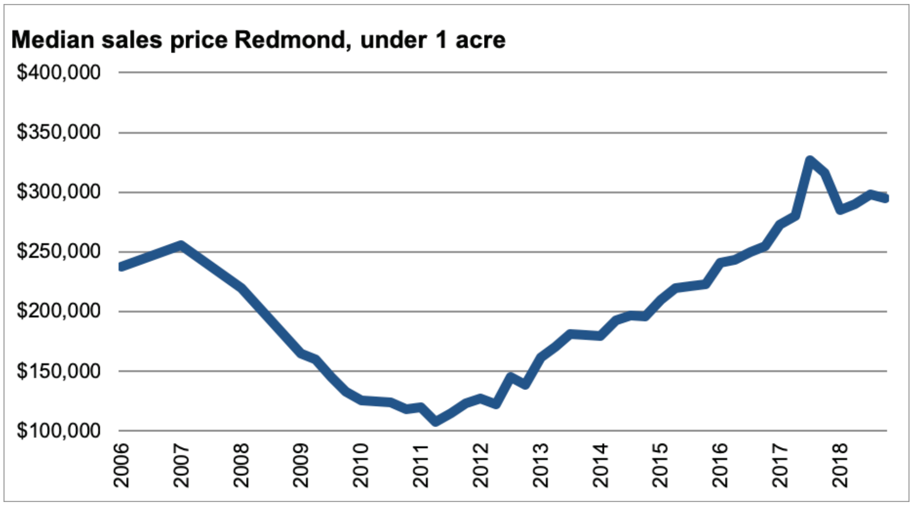
Transactions in Redmond had a 58 percent increase from 2017, amounting to 342 houses sold in the fourth quarter. The median sales price for homes dropped by almost seven percent from the same quarter last year. Average days on market hit a new record low at 92, which is the first time it has been below 100 since this publication began tracking Central Oregon.

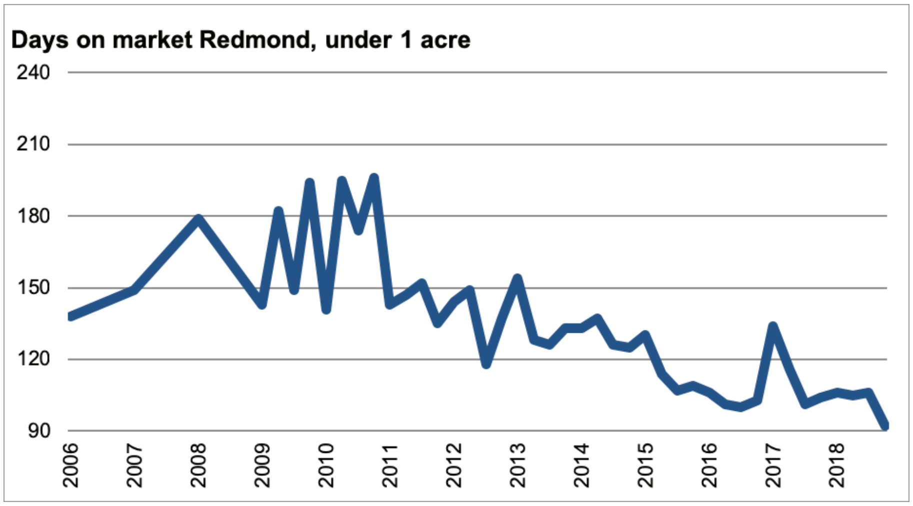






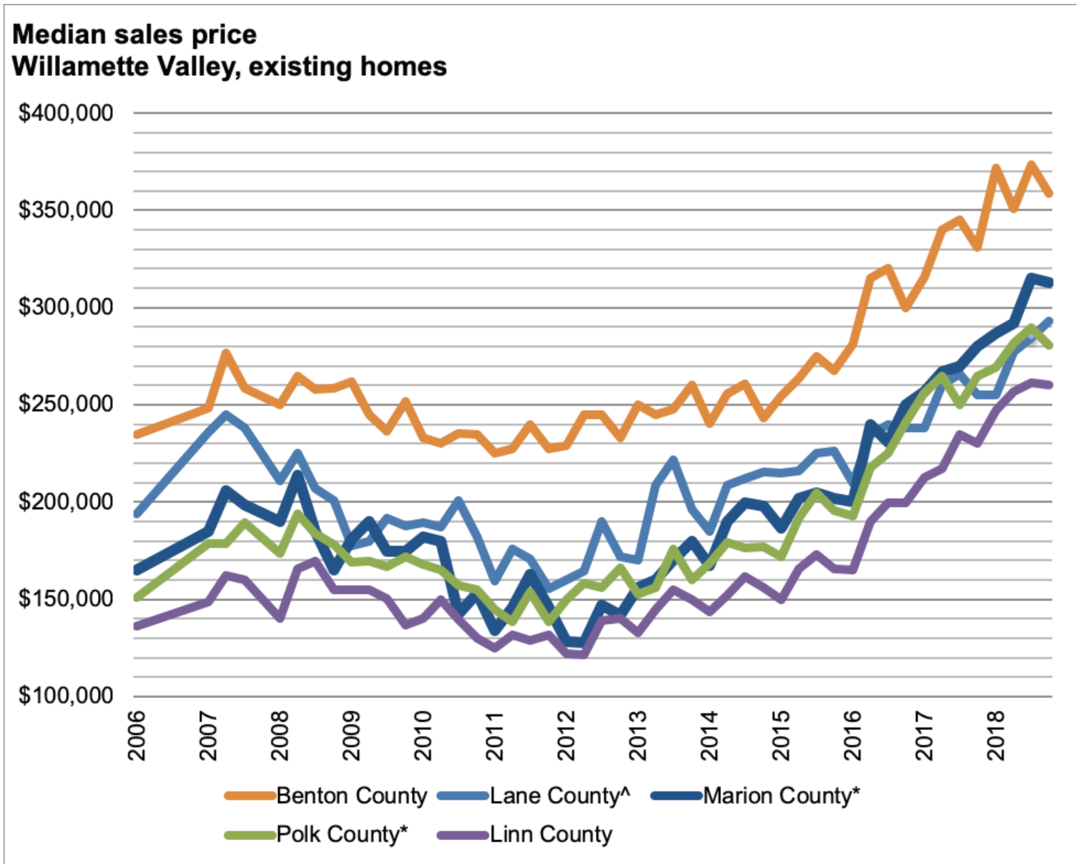

Number of transactions Redmond, under 1 acre
450
400
350
300
250
200
150
100
50
0
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018


Median sales price Redmond, under 1 acre
$400,000
$350,000
$300,000
$250,000
$200,000
$150,000
$100,000
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018


Days on market Redmond, under 1 acre
240
210
180
150
120
90
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

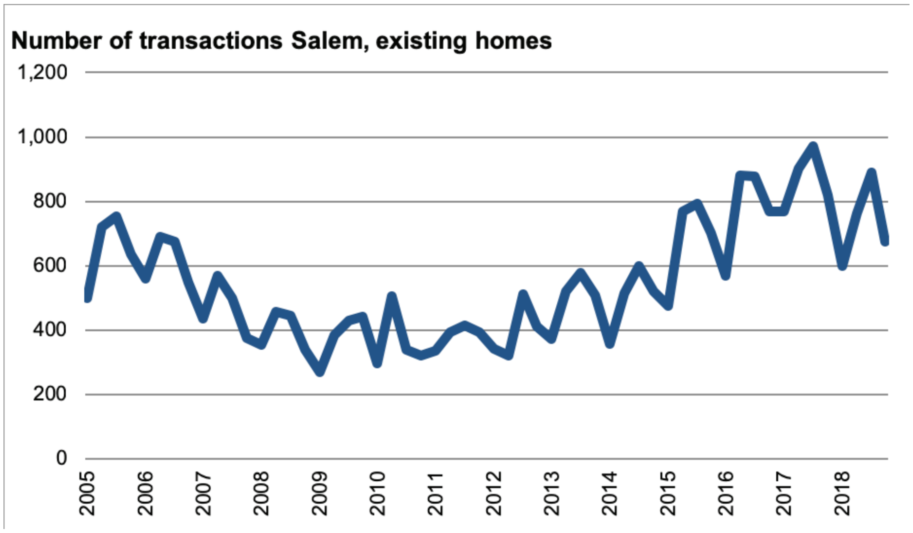
WILLAMETTE VALLEY

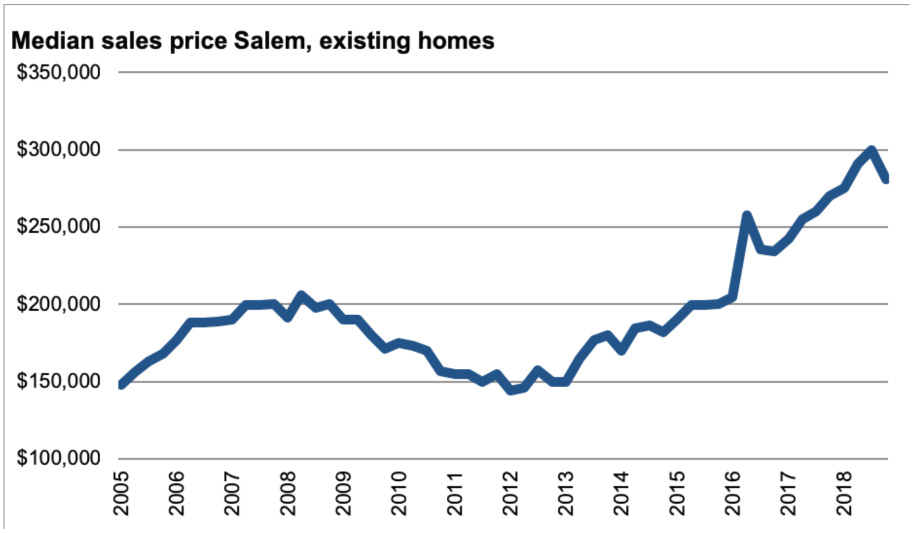
In the Willamette Valley, the fourth quarter of 2018 saw moderate increases in the median sales price from the same quarter of the previous year. Lane County increased the most at almost 15 percent, ending at a median price of $293,000. Linn County saw the second highest percentage increase at just over 13 percent, with a median price of $260,000. Benton County, with a median sales price of $359,000 increased over 8 percent from last year. Marion County had an increase of 11 percent, while Polk County saw the lowest increase in the region with just over 6 percent.

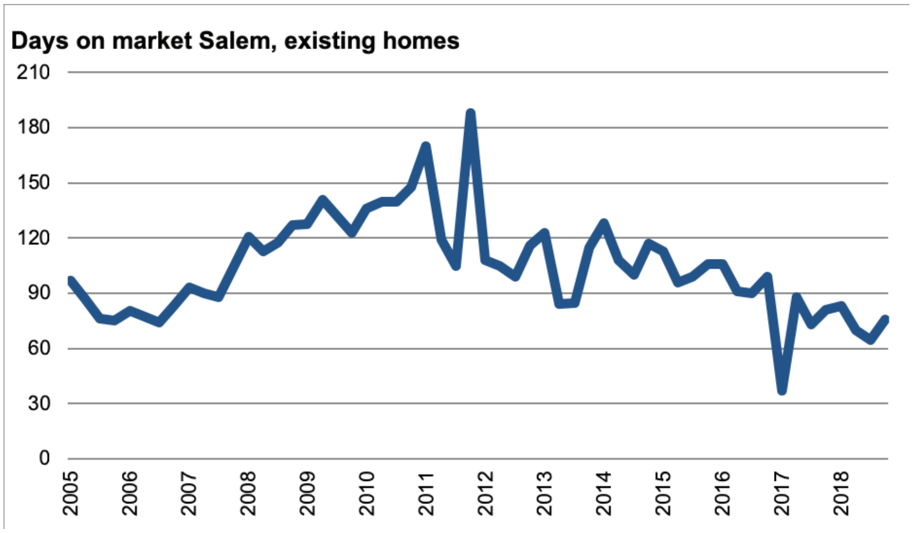


SALEM

Salem continues to look good as median sales price increased and days on market decreased from a year ago. The number of transactions in Salem slowed down from a year ago, but Salem's market is still solid with prices increasing and the average days on market down. Median sales price increased over four percent from the same quarter last year, a $11,000 increase. Transaction count decreased from last quarter by almost 25 percent and by almost 18 percent from the year prior. Average days on market decreased by over six percent from the same quarter last year, with 76 days.

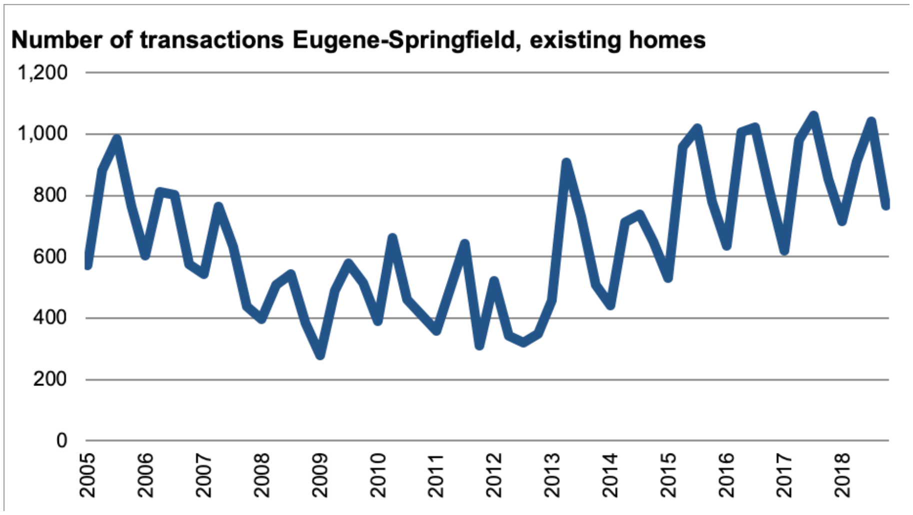


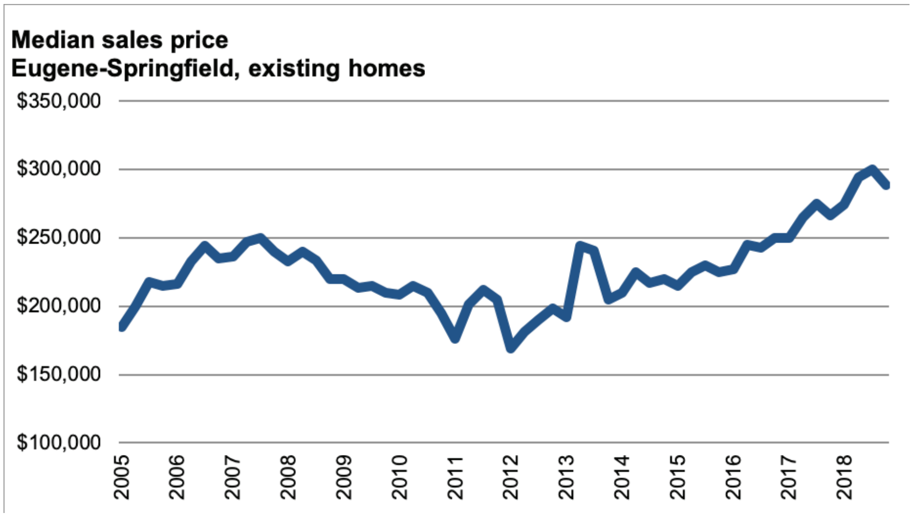


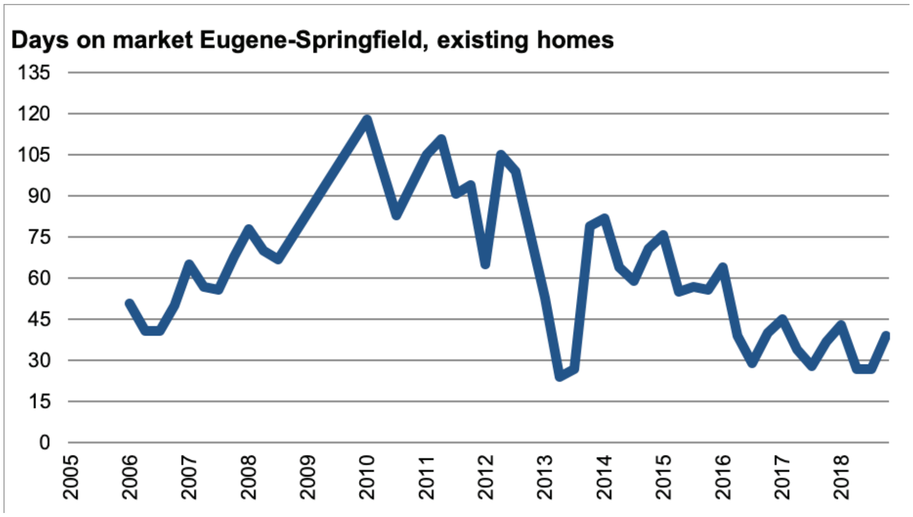


EUGENE-SPRINGFIELD

In the Eugene-Springfield market, the fourth quarter median sales price increased by over eight percent from the same quarter of last year, amounting to $288,250. Along with an increased median sales price, transactions of existing homes sold in the Eugene-Springfield area decreased by over 9 percent from the same quarter of last year with 768 transactions. Days on market as well as the ratio between sales price over list price saw very little change from the previous year.

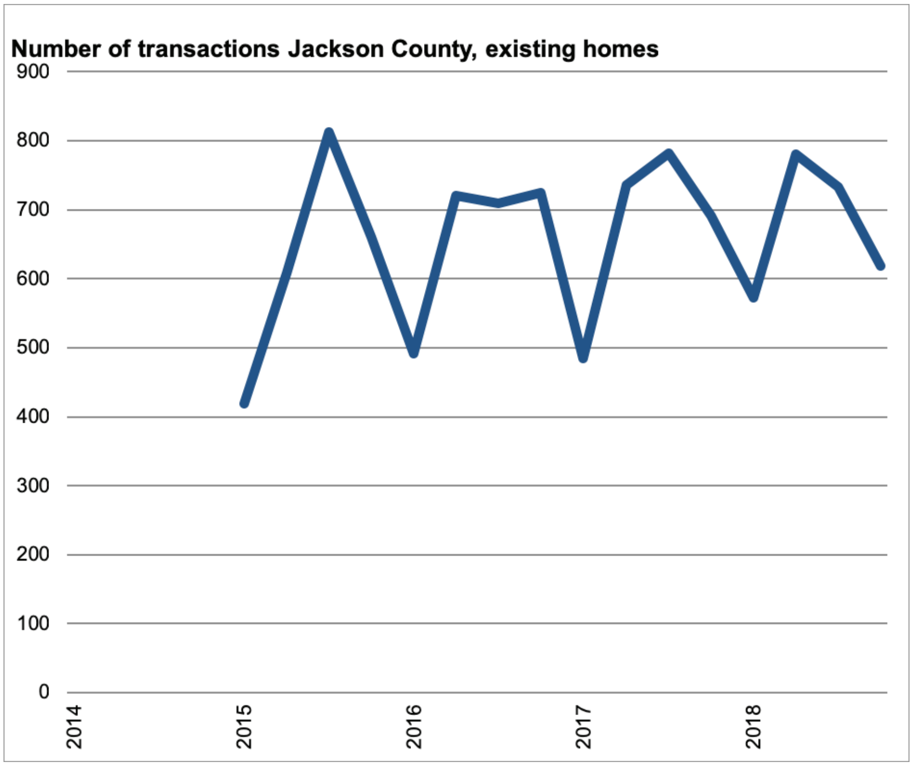


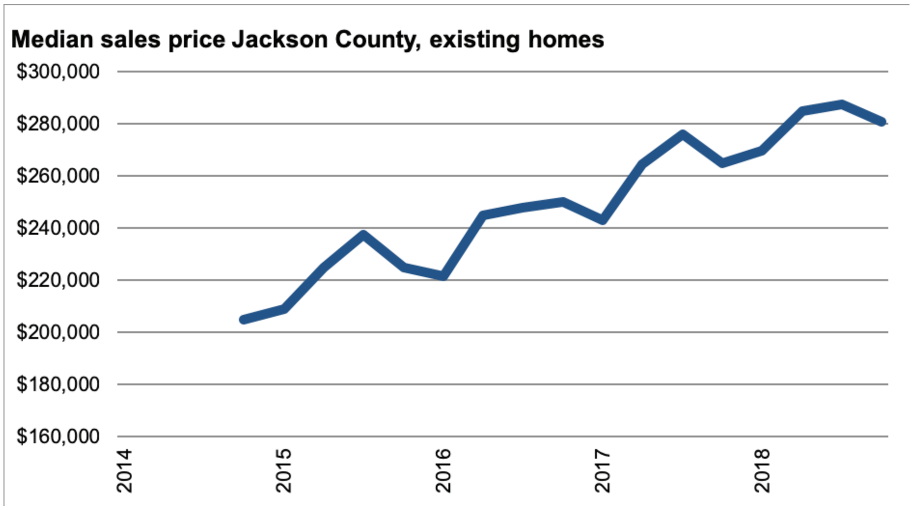


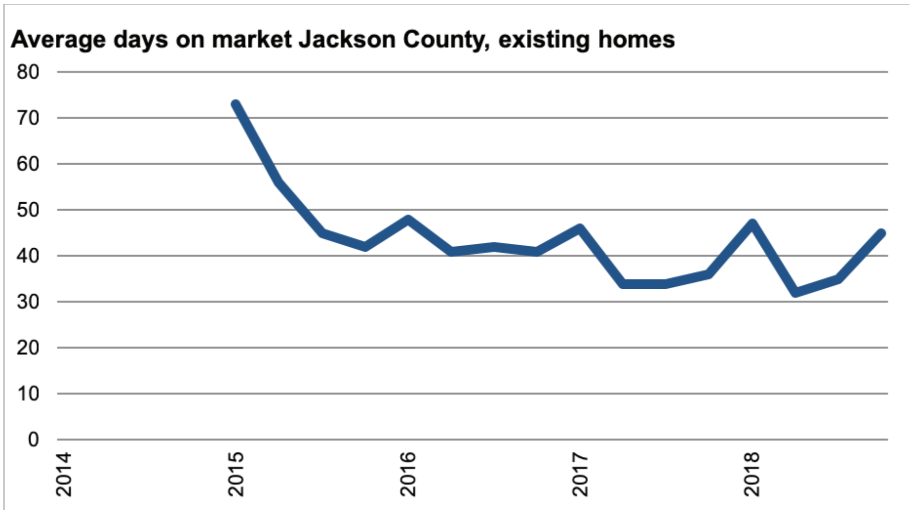


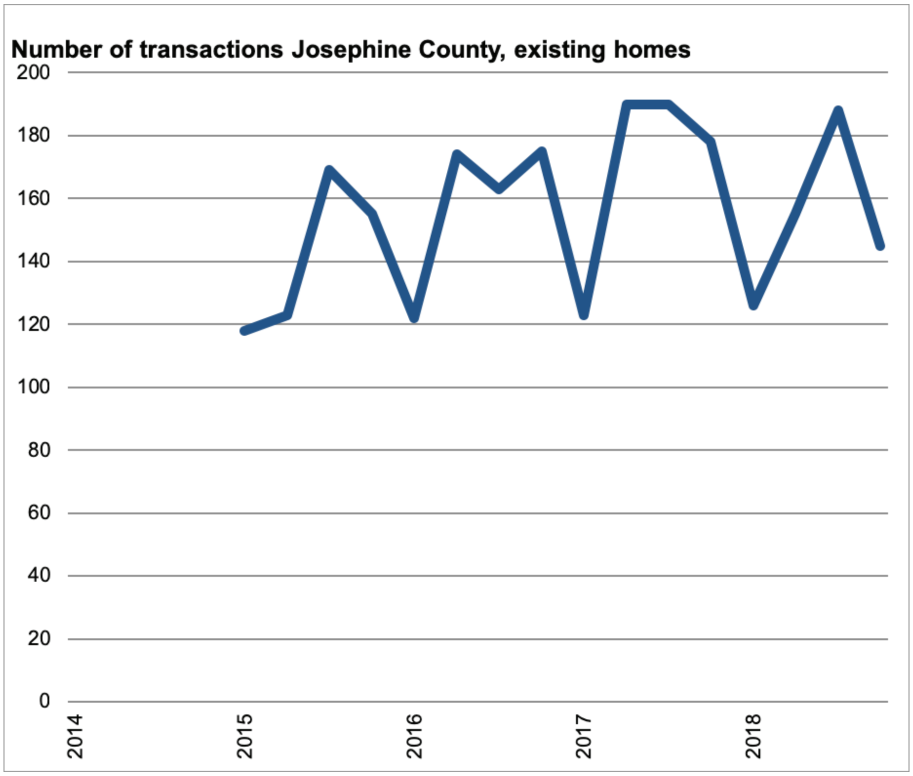
SOUTHERN OREGON

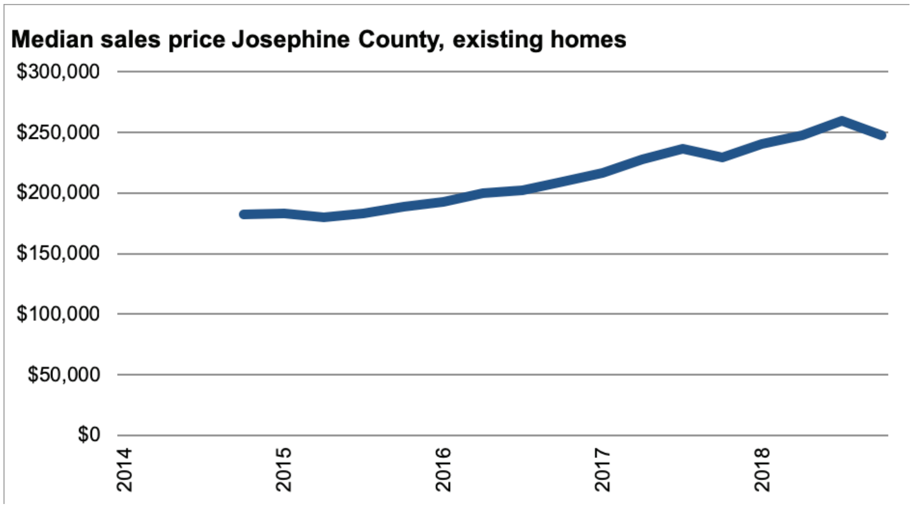
The Jackson County and Josephine County markets moved in tandem in the fourth quarter—median sales price increased, transactions decreased, and days-on-market increased. Jackson County, with a median sales price increase of six percent from the previous year, ended in a median sales price of $281,000. Seventy-three fewer homes were sold this quarter as well as a nine day increase in average days on market. Josephine County ended in a median sales price of $248,000, which is an 18 percent increase from the past year. Transactions decreased by over 18 percent from the last year, while the days on market remained constant.

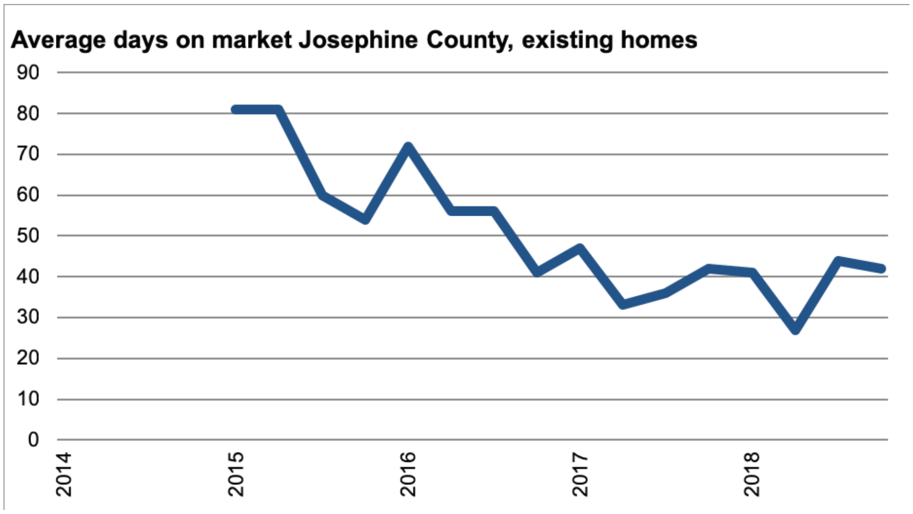







Number of transactions Josephine County, existing homes
200
180
160
140
120
100
80
60
40
20
0
2014
2015
2016
2017
2018


Median sales price Josephine County, existing homes
$300,000
$250,000
$200,000
$150,000
$100,000
$50,000
$0
2014
2015
2016
2017
2018


Average days on market Josephine County, existing homes
90
80
70
60
50
40
30
20
10
0
2014
2015
2016
2017
2018

02 //

PORTLAND MULTI-FAMILY RESIDENTIAL ANALYSIS

CHASE BENNINGTON
Portland State University

The multifamily residential market in the Portland metro area has remained robust through the fourth quarter of 2018, marking a 1.8 percent increase in overall rental growth and the highest volume of multifamily market trades since early 2016, according to Colliers International. While the effects of Portland's inclusionary zoning ordinances of 2016 have likely not yet been fully realized, the delivery of new rental housing has continued to provide sound investment aided by a stable platform of rising market rates and population growth. Rental rates continue to command just above $1.50 per square foot and occupancy is tight at 95 percent throughout 2018, indicating room for further delivery.

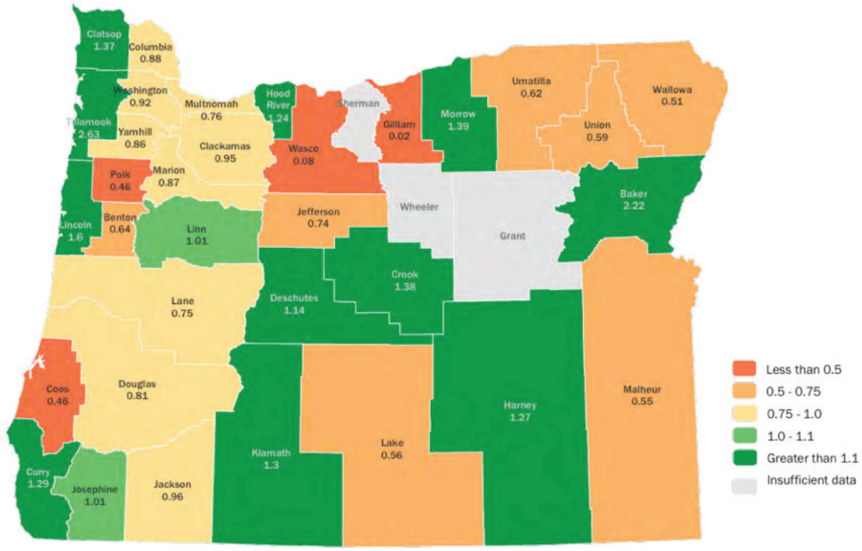
Chase Bennington *is a candidate for the Master's of Real Estate Development degree at Portland State University since the Spring of 2018. He is an Executive Director for the Center for Real Estate's Emerging Leaders club, with an expected graduation date of Summer 2019. Any opinions expressed are those of the author solely and do not represent the opinion of any other person or entity.*

PERMITTING

As the cranes towering over Portland have been indicating for many months, the steady delivery of newly built residential space has continued in the fourth quarter to match the previous 2018 trends at a two percent monthly growth rate. The Census Bureau reports the fourth quarter of 2018 saw approximately 2,400 new building permits issued throughout the Portland metro area for 2,3,4, and 5+ unit multifamily spaces.

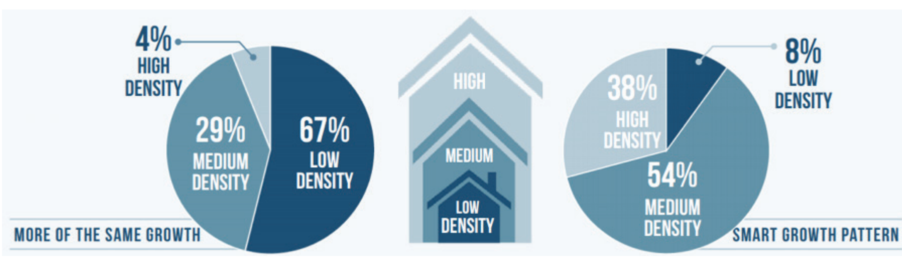
An ongoing shortage of housing in Portland has prompted efforts to boost "smart growth" strategies to supply more units. The Up For Growth National Coalition notes if Portland's current housing development trends continue, 67 percent of new units would be single-family while only 4 percent would come in the form of high-rise, high-density housing. Alternatively, Up For Growth recommends encouraging high-density development to account for 38 percent of the units delivered. Other than shifting development emphasis from single-family homes to higher-density projects, the Up For Growth plan would also nearly double the supply for medium density (low-rise multifamily) units.

Figure 1: Fewer than 1 housing unit produced per household formed since 2000



Source: Up For Growth National Coalition (2019)

Figure 2: Current Housing Trends vs Smart Growth Alternative



Source: Up For Growth National Coalition (2019)

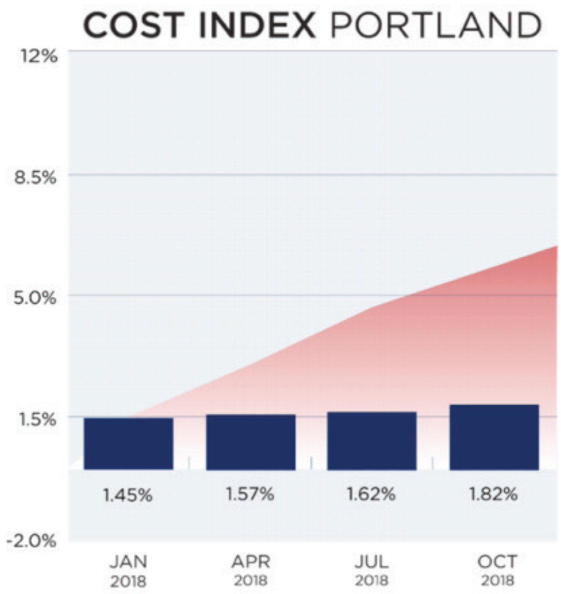
VACANCY, RENTAL RATES, COSTS

As a strengthening labor market and falling unemployment rates increase the rate of family formations, the support for continued rising rental rates for multifamily spaces remains present through the fourth quarter of 2018. Colliers reports steady rental average growth at rates of nearly two percent across all unit sizes, with 1-bedroom units representing the greatest growth at 2.6 percent.

Occupancy across all units has remained at an average of 95 percent despite the continual delivery of new housing. We can expect that the combination of tight occupancy coupled with relatively stable interest rates and slowly rising rental rates are substantial indicators that downtown Portland's housing shortage remains.

Market rates are further expected to rise as a result of rising construction costs. According to fourth quarter data generated by Rider Levett Bucknall, Portland's current multifamily new construction costs range from $160-250 per square foot and reflect a 6.6 percent increase year-to-date, growing at even faster rates than costs in Boston, Los Angeles, New York, Seattle, and Washington, DC. This has been a pervasive trend throughout 2018. Considering the newly-imposed tariffs on some construction material trade and the rising scarcity of skilled labor, it seems reasonable to expect that these expanding construction costs will continue to rise into the foreseeable future.

Figure 3: Construction Cost Growth, Portland 2018



Source: Rider Levett Bucknall (2018)

SALES ACTIVITY

Sales conditions in the 2018 market have remained relatively stable through the end of the year, bolstered by falling unemployment rates, rising population trends and steadily rising rents. Kidder Mathews reports Portland's average multifamily cap rates hovering between 5.6 and 5.2 since mid-2015.

Sales prices per unit have doubled since the post-recession 2009-2013 trends from about $100,000 to over $200,000 in 2017-2018.

The most notable sale of 2018's Portland multifamily properties was that of Indigo at Twelve West, with an average price per unit of nearly three times the market average.

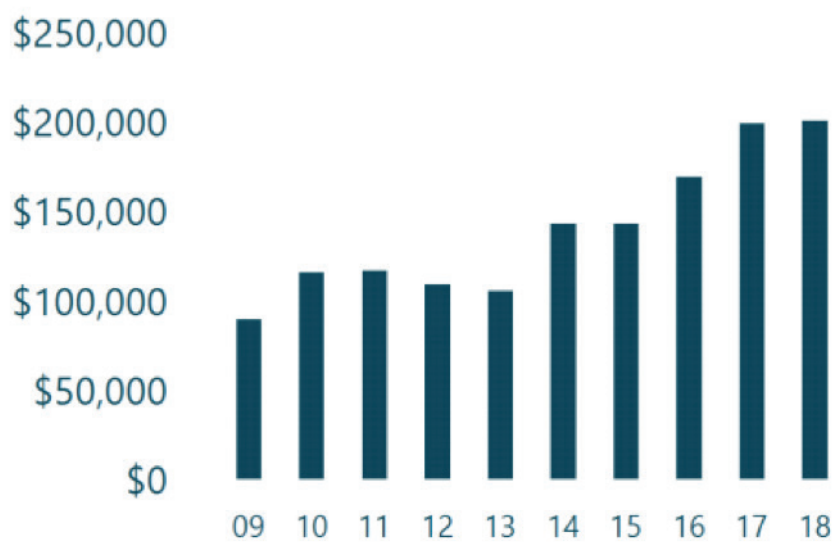
Recent transactions of multifamily property in Portland indicate the presence of a strong investment market. Based on incentives to increase the housing supply along with rising rents and low vacancy rates, we can expect Portland's multifamily economy to continue to grow.

Table 1: Cap Rates by Type, Portland Multifamily Residential

Housing Type	February 2019 Cap Rates
Luxury, New Construction	4.62
Class A	5.14
Class B	5.67
Class C	6.45
Value-Add Purchase	6.34
Average	**5.64**

Source: ALS Nationwide (2019)

Figure 4: Average Sales Price Per Unit 2009-2018



Source: Berkadia (2019)

Table 2: Top Multifamily Sales 2018

NAME	CITY	UNITS	BUILT	DATE SOLD	SALES PRICE	PPU
Indigo @ Twelve West	Portland	273	2009	July	$ 156,057,974	$ 571,640
Thorncroft Farms	Hillsboro	340	1998	January	$ 97,500,000	$ 286,764
Tessera at Orenco	Hillsboro	304	2014	September	$ 85,000,000	$ 279,605
Arbor Creek	Beaverton	440	1984	October	$ 84,300,000	$ 191,590
Sygnii Apartments	Tigard	240	2017	October	$ 75,200,000	$ 313,333

Source: Berkshire Hathaway (2019)

03 //

OFFICE MARKET ANALYSIS

MELISSA MEAGHER
Portland State University

The final quarter of 2018 ended on a positive note. As 2019 begins, the national office market continues to experience rising rents in tech-centered and diverse secondary markets, especially in CBD Class A assets. With more than 50 million square feet of office space expected to deliver this year, the popularity of flexible space continues to grow and dominate leasing activity.

Melissa Meagher *is a Masters 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. While completing her graduate degree Melissa specializes in innovative mixed-use projects, branding, and market analytics. She is the 2018 Society of Industrial and Office Realtors Fellowship recipient and scholar. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.*

Year over year, Portland's office market rent growth has seen an increase of nine percent. However, three substantial office closures as well as the delivery of over a half a million of square feet of new office space in the Central Business District lowered the year-to-date net absorption and pushed the total vacancy rate up to 13.1 percent in the fourth quarter.

High construction costs, competition for tenants as well as increased availability should result in mild rent growth and more tenant concessions. While this may have caused slowing development in the CBD, more bullish development of flex office space in the close-in Eastside continues to dominate the urban core. According to Colliers:

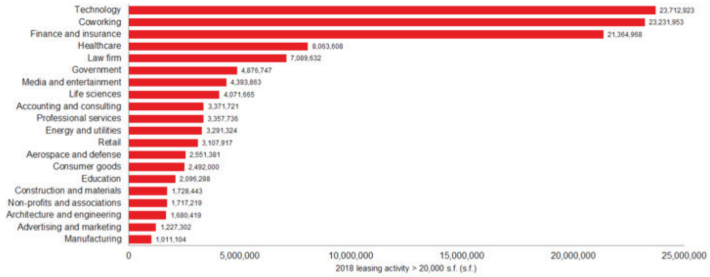
Consistently rising interest rates from the Federal Reserve are intentionally cooling the economy by depressing consumer spending on everything from cars to homes; [however] the Portland MSA's increasingly diverse array of industries, such as apparel, semiconductors, healthcare, education, and technology, will cushion it from any downturn in one of the sectors.

VACANCY

Vacancy rates this quarter saw a large variance across brokerage firms. The Portland office market vacancy rose in the second half of the year to end at 13.1 percent according to JLL, ticking above last quarter's 11.9 percent. Tim Harrison of JLL notes: "Record deliveries put extra pressure on Portland's vacancy rate, which rose 320 basis points year-over-year to 13.1 percent."

Newmark Knight Frank and CBRE's vacancy predictions line up similarly to JLL's while Colliers and Kidder Mathews see a lower vacancy rate at 10.0 percent and 7.5 percent, respectively. CBRE notes, "With tenant's pick of location and space, developments with strong value-add features will continue to stand out among the rest."

Image 1: 2018 Leasing Activity Greater Than 20,000 square feet



Source: JLL

Table 1: Total Vacancy Rates by Brokerage House and Class, Fourth Quarter 2018

Brokerage	Total	CBD	CBD Class A	CBD Class B	CBD Class C	Suburban
Colliers	10.0%	13.2%	12.5%	14.9%	11.6%	-
JLL	13.1%	14.7%	13.2%	17.6%	14.2%	-
Kidder Mathews	7.5%	11.1%	10.7%	10.7%	8.6%	6.1%
Newmark Knight Frank	10.7%	12.1%	-	-	-	-
CBRE	11.8%	12.6%	9.6%	12.4%	22.8%	10.6%

Source: Colliers, JLL, Kidder Mathews, CBRE, and Newmark Knight Frank

RENTAL RATES

Rental rates reached a fifteen-year peak in 2018. According to Jerry Holdner, Director of Research at Kidder Mathews, "The immense amount of deliveries of high-end office space this year was a big driver of the rental increase."

CBRE adds, "The Portland metro market has an unemployment rate of 3.7% with a large push for diversified talent to fill current positions and support future tenants entering the market … this employment growth should spur expansions and aid in filling some of this space over the next few years." The market's average rental rate among brokerage houses ranged from $26.52 to $31.87, while Portland's CBD range was higher, ranging from $31.80 to $36.15.

According to JLL, the close-in Eastside's newest developments are still pushing rents to the highest in the Portland metro area. Harrison notes, "The Close-In Eastside took over as Portland's most expensive submarket, with average rents now $40.00 FSG per square foot." Other suburban submarkets leading the pack are the submarkets of John's Landing and Kruse Way.

ABSORPTION & LEASING

The fourth quarter saw 79,878 square feet of negative net absorption, contrasting the third quarter's 250,903 square feet of positive net absorption. JLL noted:

The CBD bore the brunt of closures in the fourth quarter; with Wells Fargo moving out of most of their space in the Wells Fargo Center and relocating to the Sunset Corridor, The Art Institute closing their school at M financial and Jive's new parent company, Aurea, dissolving the business and shutting down their office at The Reserve.

Year to date, JLL notes of a negative 306,780 square feet in the Portland office market overall, while Newmark Knight Frank reports positive 272,641 square feet year to date.

Some of the most notable lease transactions included Finastra USA's lease of 27,160 square foot of space in the Meier & Frank Building as well as HDR Engineering's new lease in The Congress Center building on Fifth Avenue. The City of Portland will also occupy 14,768 square feet of space in Sixth+Main. With many out of state tenants eyeing new project deliveries, positive absorption should follow.

Table 2: Average Direct Asking Rates ($/sf FSG) by Brokerage House and Class, Fourth Quarter 2018

Brokerage	Market Average	CBD	CBD Class A	CBD Class B	CBD Class C	Suburban
Newmark Knight Frank	$28.76	$32.74	$35.69	$31.12	-	-
Kidder Mathews	$26.52	$31.80	$34.92	$30.12	$25.92	$23.04
Colliers	$27.07	$32.40	$35.78	$30.49	$26.52	-
CBRE	$30.27	$34.20	$38.58	$31.53	$30.48	$25.22
JLL	$31.87	$36.15	$39.32	$34.93	$27.49	-

Source: Colliers, CBRE, Kidder Mathews, JLL, and Newmark Knight Frank

Table 3: Net Absorption (in square feet) by Brokerage House and Market Area, Fourth Quarter 2018 and Year to Date

Brokerage	Q4 Overall	YTD Overall	Q4 CBD	YTD CBD
JLL	(79,878)	(306,780)	(258,206)	(282,530)
Newmark Knight Frank	(209,365)	272,641	(162,123)	(10,644)

Source: JLL & Newmark Knight Frank

Table 4: Notable Lease Transactions, Fourth Quarter 2018

Tenant	Building/Address	Market	Square Feet
HDR Engineering	Congress Center	CBD	39,789
Finastra USA	Meier & Frank	CBD	27,160
Jacobs Engineering (Expansion)	Jacobs Center	CBD	24,523
Unknown	Two Centerpointe	Lake Oswego	24,000
City of Portland	Sixth + Main	CBD	14,768

Source: CBRE & Newmark Knight Frank

SALES TRANSACTIONS

According to Costar, “Total office building sales activity in 2018 was down compared to 2017.” The Director of Research at Kidder Mathews also explains:

Portland remains one of the top locations for domestic buyers on the West Coast and continues to see growing interest from foreign capital. Sales volume in 2018 totaled $1.1 billion in transactions, 8.3% less than 2017’s record-setting volume of $1.2 billion.

Highlight transactions closing the year included the William & Dame’s $76.1 million sale of Tanner Point to CBRE Global Investors, the sale of the Yeon Building to Rockwood Capital LLC as well as Goldman, Sachs & Company’s purchase of the 1631 Thurman building. In a recent press release from Portland Business Journal, Jon Bell notes “The banking giant’s acquisition of the [Thurman] building is part of the continuing trend of institutional investors taking a shine to Portland.” Unico Properties also added The Galleria to its portfolio, which occupies the entire block at 600 Southwest Tenth Avenue. The building has 80,000 square feet of office space on the upper two floors, which Unico Properties plans to convert into creative office space.

Table 5: Notable Sales Transactions, Fourth Quarter 2018

Building/Address	Buyer	Seller	Market	Price	Price/SF
Tanner Point (9 North)	CBRE Global Investors	William & Dame Development	CBD	$76.1 M	$459
The Galleria	Unico Properties	Bill Naito Company	CBD	$64.1 M	$352
The Yeon Building	Rockwood Capital LLC	GAW Capital Partners	CBD	$42.7 M	$336
1631 Building	Goldman, Sachs & Company	Melvin Mark Companies	Northwest	$25.7 M	$382

Source: CBRE & Colliers

DELIVERIES AND CONSTRUCTION

New construction deliveries totaling 466,268 square feet were completed during the final quarter of 2018, contrasting second quarter's 507,932 square feet. In a recent Costar report, total office inventory at the end of the year amounted to 34 million of Class A office space, 68 million of Class B office space, and 33 million of Class-C office space.

After two years of construction, Broadway Tower delivered 177,800 square feet of office space in the final quarter of 2018. Newmark Knight Frank notes, "To date, the tower is 94% occupied with only 10,475 square feet of office space remaining available for lease, as the tower has seen impressive absorption." Flatiron PDX, a smaller innovative development, delivered 24,300 square feet of Class A office space but also reflects similar demand.

In addition, Tanner Point, formerly known as 9North, delivered its Class A office space in the Central Business District and will offer eight floors of office space. Williams & Dame Development bought the vacant property at the corner of Northwest Northrup and 9th Avenue in 2015. Hacker Architects describe the building as "designed for maximum flexibility, to accommodate small tenants as well as multi-floor offices."

Lastly, nearing almost two years of construction, Vancouver's The Murdock delivered and is making positive leasing strides. According to Jacob Pavlik at Colliers, "Vancouver's Waterfront is performing exceptionally well with two existing restaurants (four in the pipeline), 63 apartments ready for occupancy (490 in the pipeline), 40 condos slated to deliver in 2020, 75k SF of office delivered in Q4 (155k SF in the pipeline). All these amenities and are located in the southern portion of Vancouver's central business district providing the much-needed residential and class A office space to satisfy the pent-up demand to revitalize this low-tax suburb of Portland."

Table 6: Notable Development Project Deliveries, Fourth Quarter 2018

Building/Address	Developer/Owner	Market	SF	Delivery Date
Broadway Tower	BPM Senior Living Company	CBD	177,800	Q4 2018
Tanner Point (9 North)	Williams & Dame Development	CBD	202,853	Q4 2018
The Murdock	Gramor Development	Vancouver	77,000	Q4 2018

Source: Colliers and CoStar

Image 2: Tanner Point – Delivered in Fourth Quarter 2018

Source: Hacker Architects

Image 3: The Murdock – Delivered in Fourth Quarter 2018

Source: TheMurdockBuilding.com

Set to deliver in the second quarter of 2019, the industrial office development at 7 SE Stark Street nods to flex space's increasing popularity. According to Works Progress Architecture, the 10-story, 180,000 square foot building situated between the Union Pacific railroad tracks and the Interstate will "allow for open and flexible layouts for creative business to grow within."

It is evident with its dominant leasing activity and development that flex space—and its ability to attract high satisfaction and talent—is here to stay. Abraham Park from the Fred Sands Institute of Real Estate says, "Any design that can create a unique space … is a great concept that the country and economy will continue to need, especially with changing cultural trends and desire for a certain lifestyle for urbanization."

Table 7: Notable Under Construction Projects, 2019 - 2021

Building/Address	Developer	Market	SF	Delivery Date
Nike North Expansion Building B	Gerding Edlen	Westside	1,003,585	Q1 2019
Block 29 Center for Health & Healing	Oregon Health & Science University	Southwest	360,000	Q1 2019
250 Taylor	Third & Taylor Development LLC	CBD	190,825	Q1 2020
The Canvas at Press Blocks	Security Properties + Urban Renaissance Group	Southwest	140,000	Q2 2020
5 MLK Office	Gerding Edlen	Lloyd District	119,570	Q4 2019
District Office	Beam Development	Southeast	90,778	Q2 2019
7 SE Stark	Harsch Investment Properties	Lloyd District	70,000	Q2 2019

Source: CoStar

Image 4: 7 SE Stark Street – Under Construction

Source: Works Progress Architecture

04 //

PORTLAND INDUSTRIAL MARKET ANALYSIS

MICHAEL LOWES
Portland State University

The industrial market in Portland is one of continued strength through the end of 2018. Cushman Wakefield's MarketBeat reports the Portland industrial market saw an all-time low in vacancy rate in the fourth quarter of 2018, dropping to three percent. Much of this can be linked to Portland's Urban Growth Boundary which has limited the amount of available land in the face of increasing demand.

As vacancy has dropped to new lows, rents have reached new highs, sitting at $0.72 per square foot, triple net. Developers have around 2.3 million square feet of industrial projects under construction. Sales of industrial properties are seeing average cap rates of around 5.5 percent to 6 percent.

MICHAEL LOWES *is an Associate Broker at Capital Pacific focusing on retail, office, and industrial investment sales. He is currently a candidate for the Portland State University Masters of Real Estate Development. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.*

VACANCY AND ABSORPTION

Vacancy rates dropped almost one percentage point relative to the previous year. Net absorption has improved by almost 300,000 square feet. The lack of construction in comparison to 2017 can be pointed back to the lack of available land and Portland's strict Urban Growth Boundary. This has also led to a focus of new areas outside of the main I-5 corridor and urban core. Industrial developments have now starting spilling into Canby, Woodburn, and Salem, with access to I-5 being key for site selection.

DELIVERIES AND CONSTRUCTION

Last year saw 3.9 million square feet of new industrial product in Portland, with about 500,000 square feet in the last quarter. The largest new product delivered was the UPS Majestic Westmark Center coming in at 266,160 square feet. With numbers like this, 2018 will be tough to beat on delivery, but with limited vacancies Portland is sure to see the rental rates continue to climb. Portland's industrial market shows no signs of slowing down as the demand increases in the face of limited supply.

INDUSTRIAL OUTLOOK

As the retail real estate market changes, some of these changes will show up in the industrial market. For example, Amazon, a retail industry leader, has continued to grow its industrial footprint. Salem has seen one million square feet of industrial product delivered by Amazon alone, and surely this number will continue to increase.

Portland however, has not made it easy for the expansion of industrial assets. The Urban Growth Boundary is always a hot topic, and the lack of available land to create industrial product will keep the sector growing in the rental category and shrinking the vacancy rates. As this industry continues to grow the Urban Growth Boundary of Portland may need to grow alongside it, if not, then we may be seeing a complete stall in new product since there will be no land to build on.

Q4 2017 v. Q4 2018.

	Q4 17	Q4 18
Overall Vacancy	3.9%	3.0%
Net Absorption	-72k	254k
Under Construction	3.7M	2.3M
Overall Average Asking Rent	$0.71	$0.72

Source: Cushman & Wakefield

NOTABLE TRANSACTIONS

Acquisitions:

Specht Properties, 6433 SE Lake Rd., Clackamas/Milwaukee
992,193 square feet / $48.5M / $48.88 per square foot
QW Properties, Big Eddy Commerce Center, East Columbia/Portland
153,387 square feet / $22.2M / $144.73 per square foot
Dermody, Boyd Coffee, East Columbia/Portland
268,495 square feet / $18.8M / $70 per square foot

Leases:

14300-14340 N. Lombard St. / 151,050SF / Portland
12220 SW Cimino St. / 86,481SF / Tualatin
16800 SE Evelyn St. / 74,235SF / Clackamas/Milwaukee

Source: Cushman & Wakefield

05 //

RETAIL MARKET ANALYSIS

MICHAEL LOWES
Portland State University

“The sky is not falling;the weather is changing” is what Fred Bruning stated at the CAB retail breakfast in early January of this year.Many believe an apocalypse is coming for the retail sector, but Mr. Bruning along with many others in the industry just see it is a shift and a change in focus.

Last yearfor the retail sector ended on a high note.Rental rates ticked upto $19.68 per square foot, a 2.5percentin-creasefrom 2017 according toKidder Mathews.While rental rates increased, vacancy rates decreased to threepercent,a telling sign that the industry is moving in the right direc-tion.Retail space accumulating upwards of 330,00square feetwas delivered in 2018 with over 190,000square feetstill being constructed as we move into 2019.Investors are still purchasing retail assets in full force, with average cap rates at 6.05percentand $216 per square foot.

Michael Lowes ***is an Associate Broker at Capital Pacific focusing on retail, office, and industrial investment sales.He is currently a candidate for the Portland State University Masters of Real Estate Development.Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.***

ABSORPTION

For the sixth straight year retail properties in Portland saw a positive net absorption of more than 800,000 square feetas noted by Kidder Mathews.

Table 1 shows the central business district and I-5 corridor soared in the fourth quarter based off of their net absorption. Shopping centers are leading the way in the product category, driven by the large amount of inventory in the marketplace.

VACANCY

Last year displayed a continued upward trend for the retail market. Vacancy rates continued to drop, by 40 basis points from 2017. Portland wide vacancy rates dropped, except for the Lloyd District. The continued efforts to rebuild Lloyd Center into a place of interest is still moving forward. With the vacancy caused by Sears, the plan is to move forward with a 14-screen Regal Cinemas on the third floor, with retail and office taking the first two floors. This will help fill the box left behind by the struggling retailer.

RENTAL RATES

Rental rates are also moving in the right direction for retail properties. Over the last three years, as seen in Table 1, rental rates have continued to climb at an annual rate of 2.5 percent. Portland's central business district continues to have the highest rental rates, followed by the Northwest area as this area continues to be a sought-after destination for travelers as well as a well to do housing market. Malls and power centers set the pace for product type.

NOTABLE SALES IN THE RETAIL SPACE

Grocery and power centers led the way in highest priced transactions. Per Kellen Kollmorgen's research at Capital Pacific, 2018 topped the previous record set in 2014 for transaction volume in these types of properties with over $745 million in total transactions.

Table 1: Submarket and Property Type Breakdown

Submarket	Total Inventory	Direct Vacancy Rate	Total Vacancy Rate	Total Available Rate	4Q Direct Net Absorption	2018 Total Net Absorption	4Q Leasing Activity	2018 Leasing Activity	Avg Rental Rate
CBD	3,923,892	4.30%	4.40%	6.60%	67,125	76,512	16,628	94,946	$24.36
Lloyd District	5,532,165	2.80%	2.90%	8.80%	(15,536)	(14,930)	0	22,989	$20.40
Northwest	1,759,023	1.70%	1.70%	2.40%	2,958	3,149	6,000	26,092	$23.52
Sunset Corridor / Hillsboro	9,745,942	1.90%	2.10%	3.30%	(2,868)	(4,539)	32,551	112,632	$19.68
I-5 Corridor	11,435,003	3.60%	3.90%	4.70%	61,334	146,411	33,375	127,630	$17.64
Northeast	20,516,662	2.30%	2.30%	3.80%	2,056	156,509	125,492	365,358	$20.04
Southeast	23,321,478	2.60%	2.70%	3.70%	43,433	110,780	121,072	517,569	$17.04
Southwest	14,866,003	2.80%	2.90%	3.80%	(4,436)	137,380	31,477	202,202	$21.24
Clark County / Vancouver	18,950,076	3.80%	3.80%	4.70%	27,507	229,793	94,748	352,431	$20.52
Portland Total	**110,050,244**	**2.90%**	**3.00%**	**4.30%**	**181,573**	**841,065**	**461,343**	**1,821,849**	**$19.68**
Malls	6,386,033	2.10%	2.10%	6.60%	6,904	3,765	18,338	37,579	$25.08
Power Centers	7,936,198	2.60%	2.60%	4.20%	(105,618)	(95,736)	42,523	62,389	$22.92
Shopping Centers	36,733,988	4.70%	4.80%	5.90%	219,623	829,431	250,849	1,005,957	$19.20
Specialty	1,627,999	8.60%	8.60%	9.10%	(1,930)	(75,630)	67,811	74,321	$0.00
General Retail	57,366,026	2.46%	2.78%	3.65%	62,594	179,235	81,822	641,603	$19.50

Source: Kidder Mathews

Table 2: Year Over Year Trends

	2018	2017	2016	Annual % Change
Direct Vacancy Rate	3.00%	3.40%	3.60%	-11.76%
Availability Rate	4.30%	4.10%	4.80%	4.88%
Asking Lease Rate	$19.68	$19.20	$18.12	2.50%
Leased SF	1,821,849	2,236,534	2,358,350	-18.54%
Sold SF	4,338,188	4,285,759	4,230,895	1.22%
Net Absorption	841,065	869,592	867,632	N/A

NOTABLE TRANSACTIONS

Gresham Station / Gresham, OR / Harsch Investment Properties / $64.5M / 7.6% / 341,952 square feet / Anchored by Best Buy and LA Fitness

Oswego Village Center / Lake Oswego, OR / Asana Partners / $33.8M / 4.3% / 102,809 square feet / Anchored by Whole Foods

Sunset Mall / Portland, OR / First Washington Realty / $28.5M / 5.2% / 113,721 / Safeway

Source: Capital Pacific

WHAT TO KEEP AN EYE ON

Sure, Amazon is disrupting the retail market, but to say that it is going to wipe it out is just not the case. Owners and businesses are getting smart and adapting. Big box retailers such as Sears, JC Penney, and Toys R Us have taken extreme hits this year. Now what to do with the big boxes they leave behind or massive vacancies at malls?

Some suggest there is a way to create useful needs from those areas. Things to add entertainment value, and engage mall goers. Others see an inviting way to create a multi-tenant space. All of these will come to the forefront of this coming year as changes in the retail world continue to push forward.

Brick and mortar stores are not going anywhere. The buy online and pick up in store strategy is coming into full swing. Shoppers are able to buy their items online, but head into the store to pick them up—leading to easier returns for the customers, and a chance to take advantage of further sales from products inside the stores for the businesses.

Stores are able to rethink their spaces. Places like Bonobos have seen a change in the way their store is run. Little to no inventory is actually kept at the store, letting them maximize their usage in smaller spaces. Rather, customers come in and try on a size, of possibly a different color, and order from inside the store the actual style they want to be sent to their homes.

These are just a couple strategies that are being used currently, and there are more to come without a doubt. This year will bring a continued shift in the retail world. But, with companies like Amazon trying out brick and mortar locations you can bet that the sector is not going anywhere.