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ECONOMIC OVERVIEW

Economic Analysis

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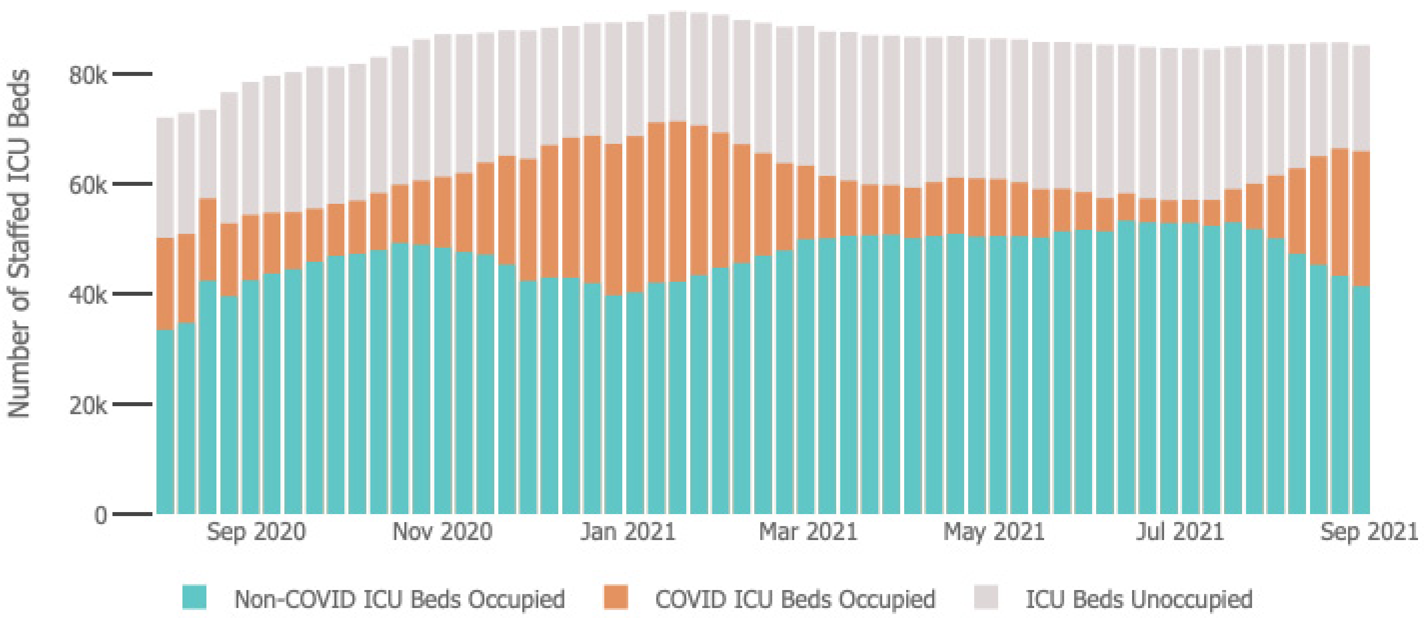
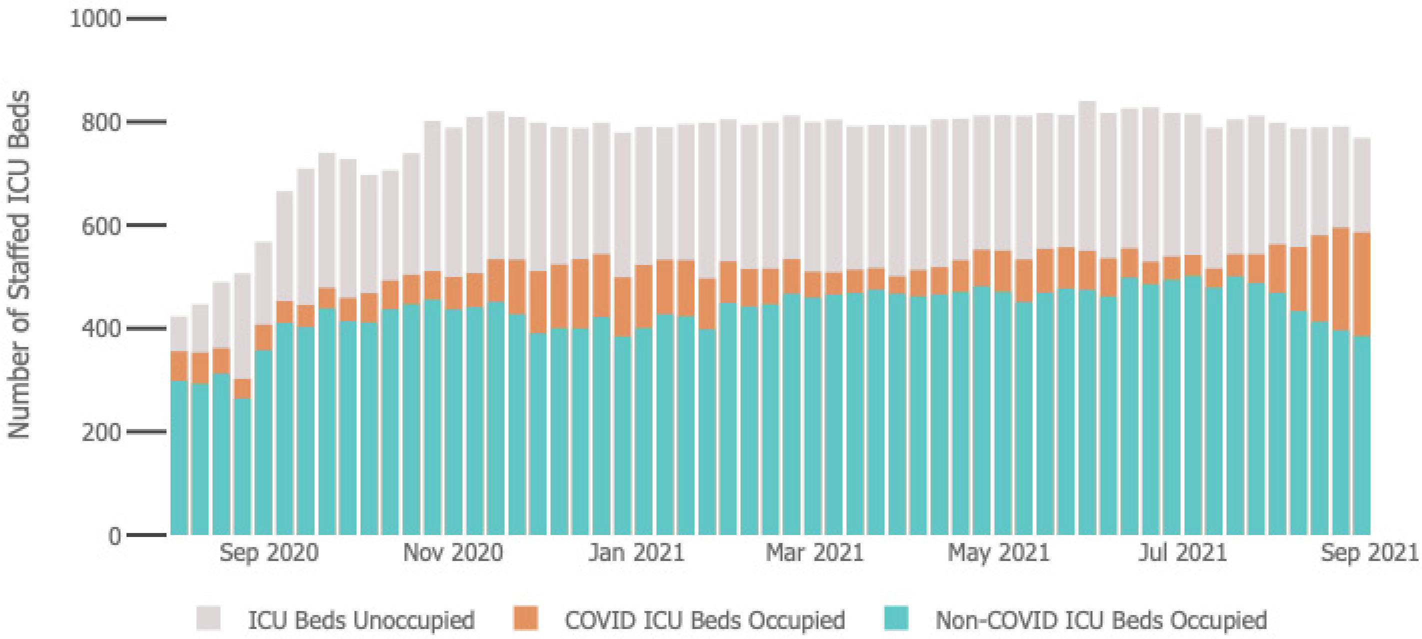
Following an optimistic spring and early summer and rising vaccination rates, the emergence of the Delta variant has pushed back plans for reopening many sectors of the economy. Economic growth was robust through the summer as COVID-related restrictions were lifted, assisted by record levels of federal stimulus. The level of vaccine resistance appears to be persistent, and we may have to rely upon immunity associated with COVID infections to increase community immunity to necessary levels. The current surge in COVID-related admissions will likely stress hospital systems nationwide, with many areas already close to or beyond capacity. In the state of Oregon, we are currently seeing COVID patients overwhelm hospital systems in areas such as southern Oregon.

ICU CAPACITY AND COVID-19 IMPACTS, UNITED STATES



(US Department of Health and Human Services)

ICU CAPACITY AND COVID-19 IMPACTS, STATE OF OREGON

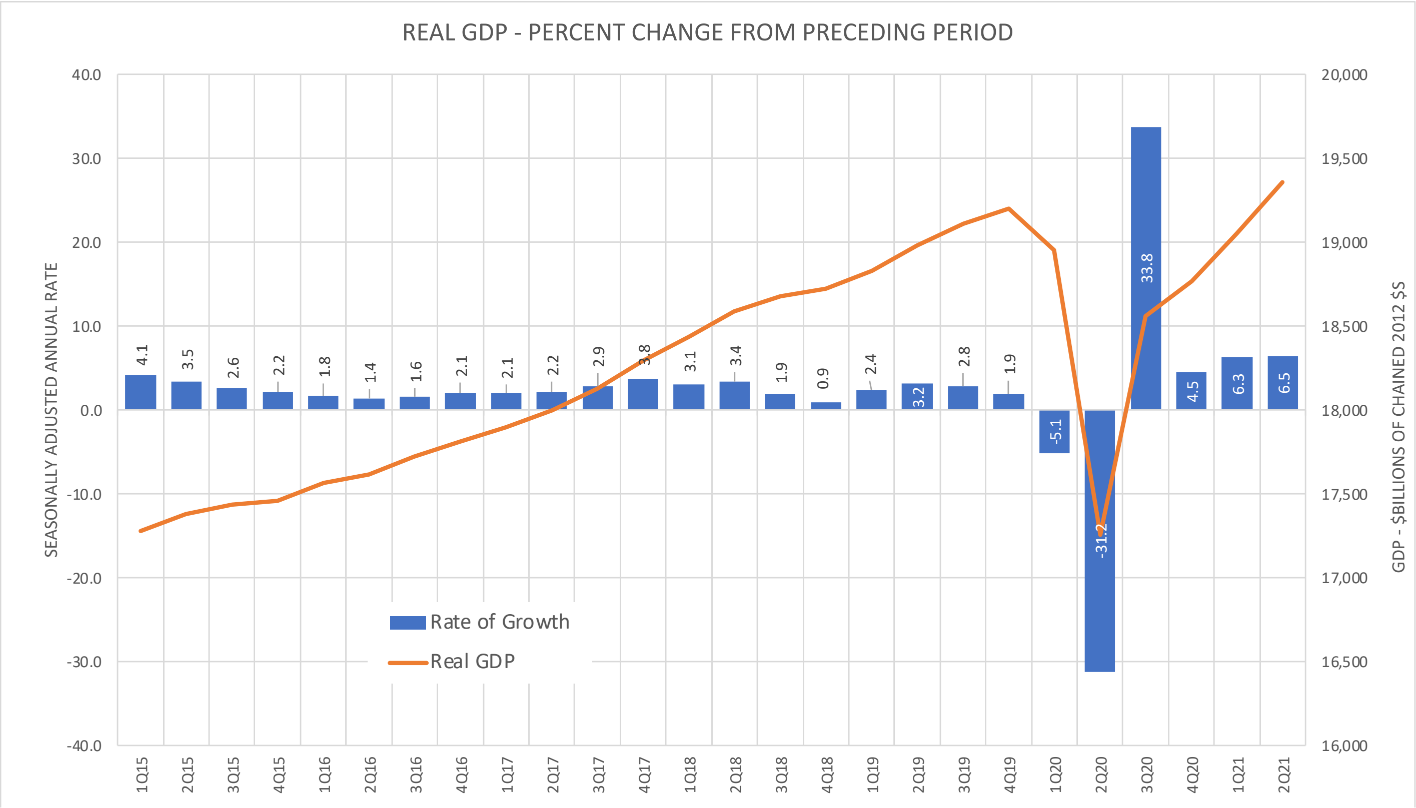


(US Department of Health and Human Services)

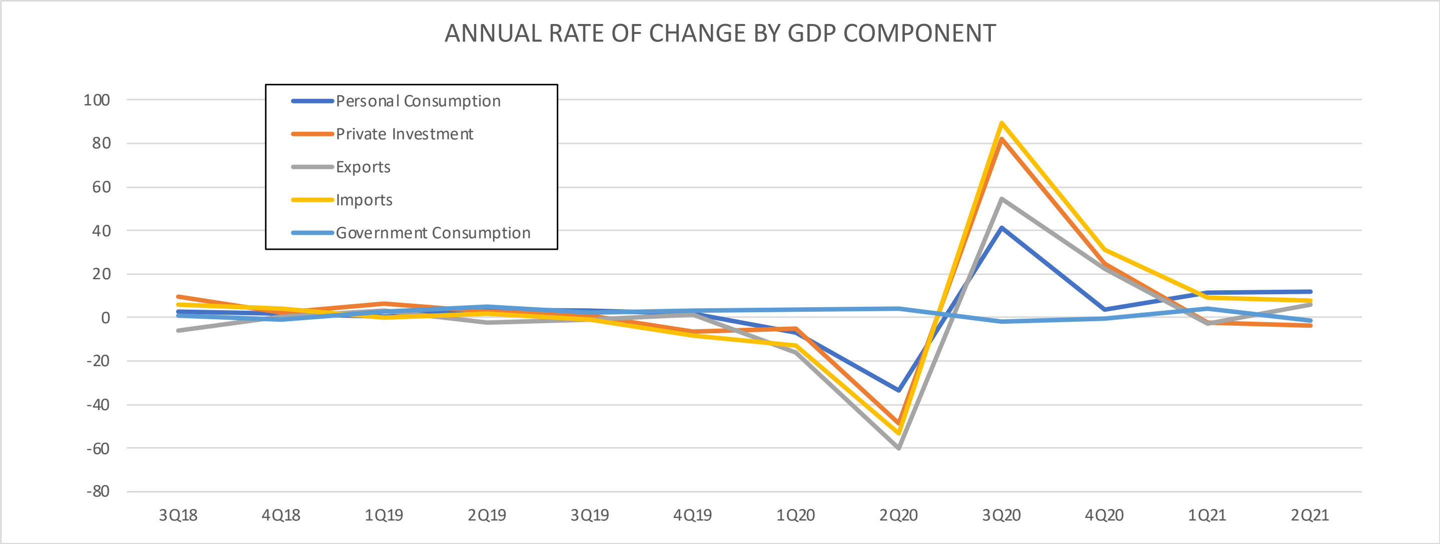
While we remain hopeful that there is an eventual end to the pandemic, recent usage patterns and preferences associated with the pandemic may be persistent. The associated uncertainty will have a substantive short-term impact on investor interest in certain asset classes and locations.

At a national level, the economy continued to expand at a robust rate through the second quarter, with overall GDP estimates now above pre-pandemic levels. The economy remains below the long-term growth trend. Personal Consumption continues to remain strong, and exports have risen rapidly in the last few quarters, but Private Investments and Government Consumption have been trending downwards. The exceptional level of fiscal stimulus to consumers during the pandemic will likely drive personal consumption for a few more quarters.

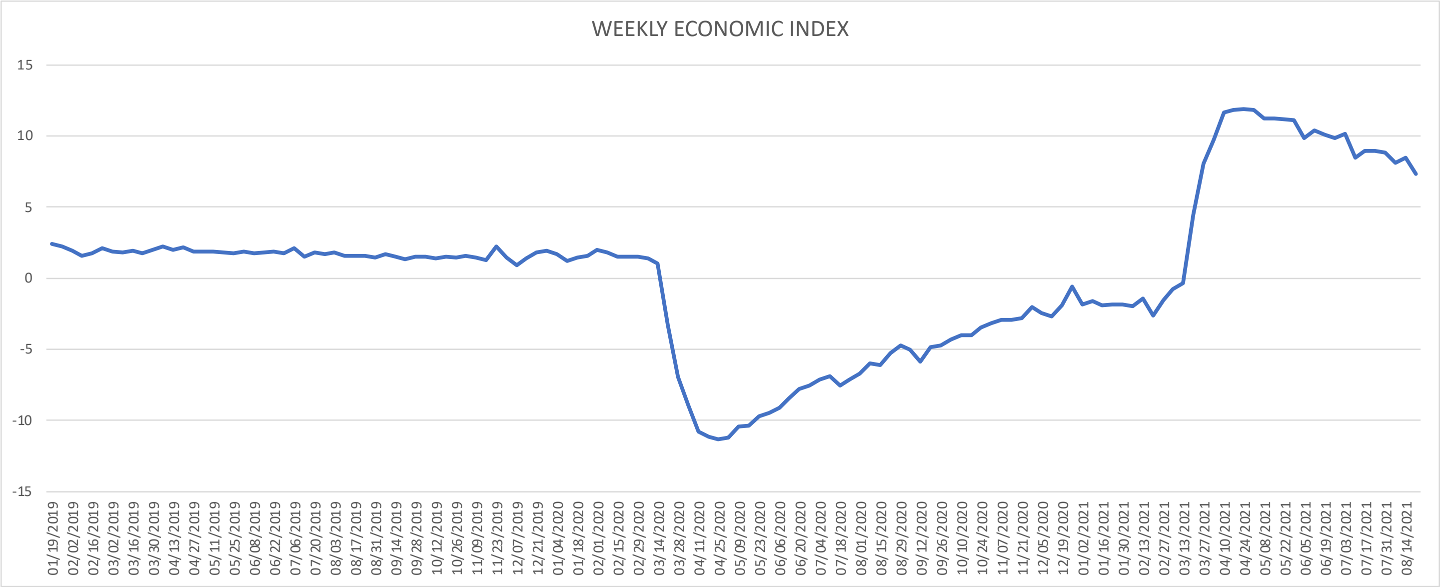
To get more current information on economic performance we can look at more frequently updated indices such as the Weekly Economic Index (WEI). The WEI is an index of ten daily and weekly indicators of real economic activity, scaled to align with the four-quarter GDP growth rate. It represents the common component of series covering consumer behavior, the labor market, and production. The index shows a declining pattern since May 2021, which is attributable to decreases in rail traffic, tax withholding, and fuel sales, and an increase in initial unemployment insurance claims (relative to the same time last year), which more than offset an increase in electricity output (relative to the same time last year). Because the WEI measures changes over a 52-week period, the large positive reading also reflects the sharp deterioration in economic conditions during the same time last year.



(US Bureau of Economic Analysis)

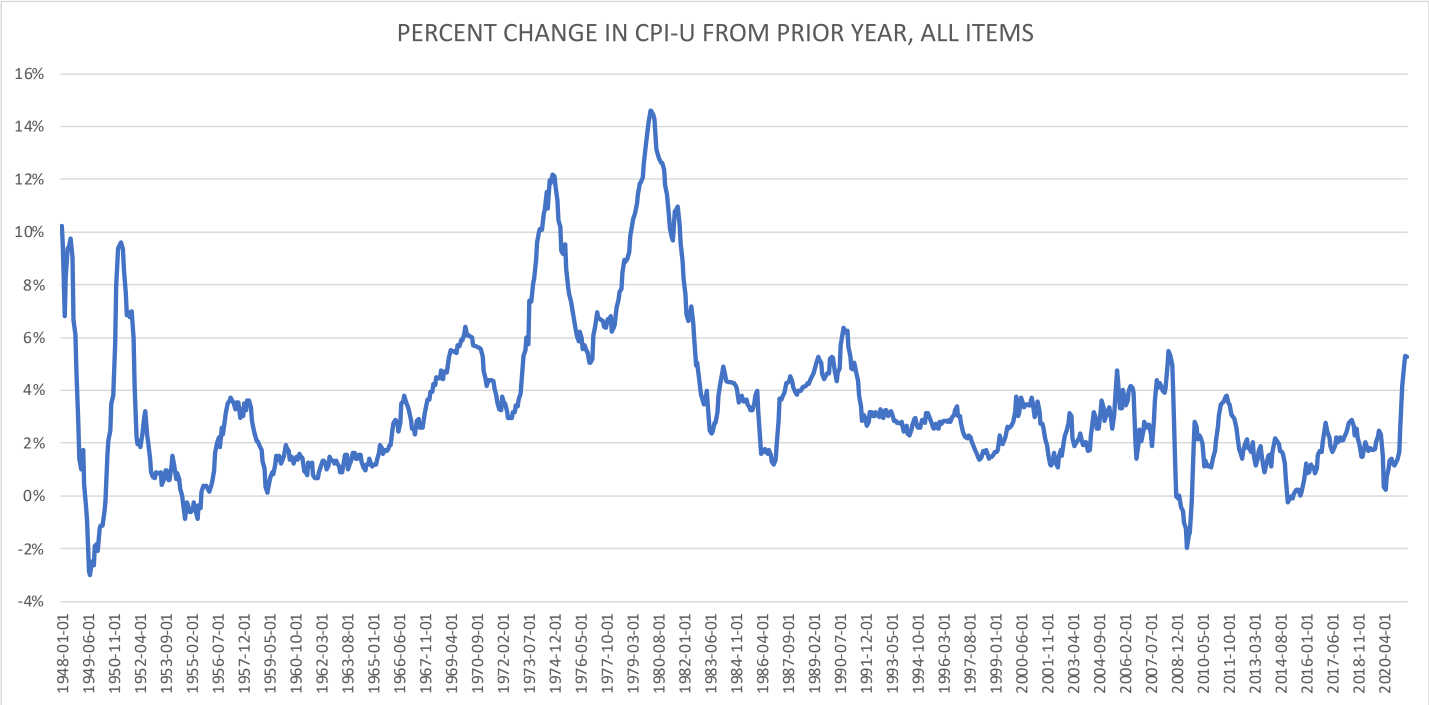


(US Bureau of Economic Analysis)



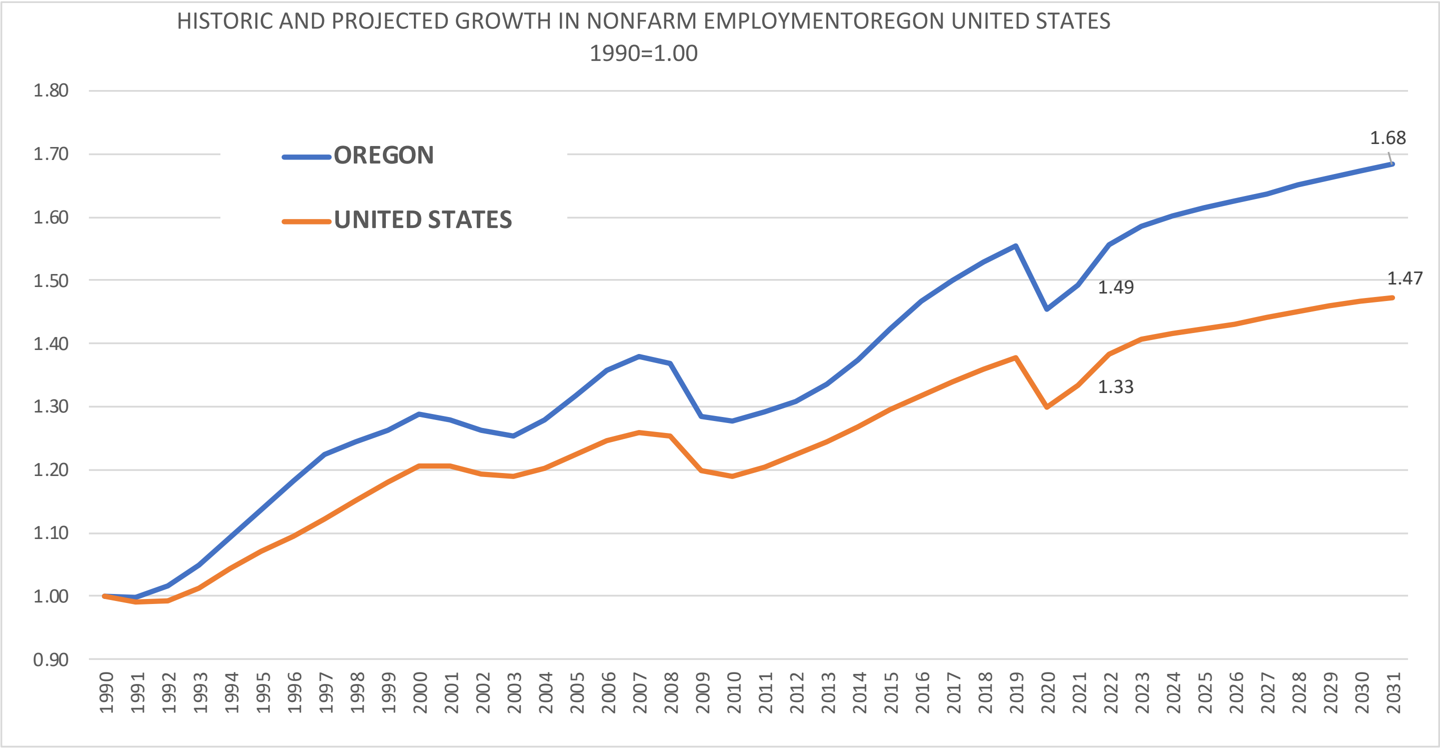
(Lewis, Daniel J., Mertens, Karel, and Stock, James H., Weekly Economic Index, https://www.newyorkfed.org/research/policy/weekly-economic-index.)

An area of recent concern is the potential for inflation, which has not been a significant factor in the market for over twenty years. In response to concerns, several Federal Reserve officials have indicated a need to cut back on central bank bond buying. Low interest rates have been capitalized into land and property values, and any significant shift in interest and/or capitalization rates would substantively impact the real estate markets. In addition, as demonstrated by the sharp run up in construction materials cost in the last year, inflationary impacts can very directly impact the ability of the market to deliver product profitably.

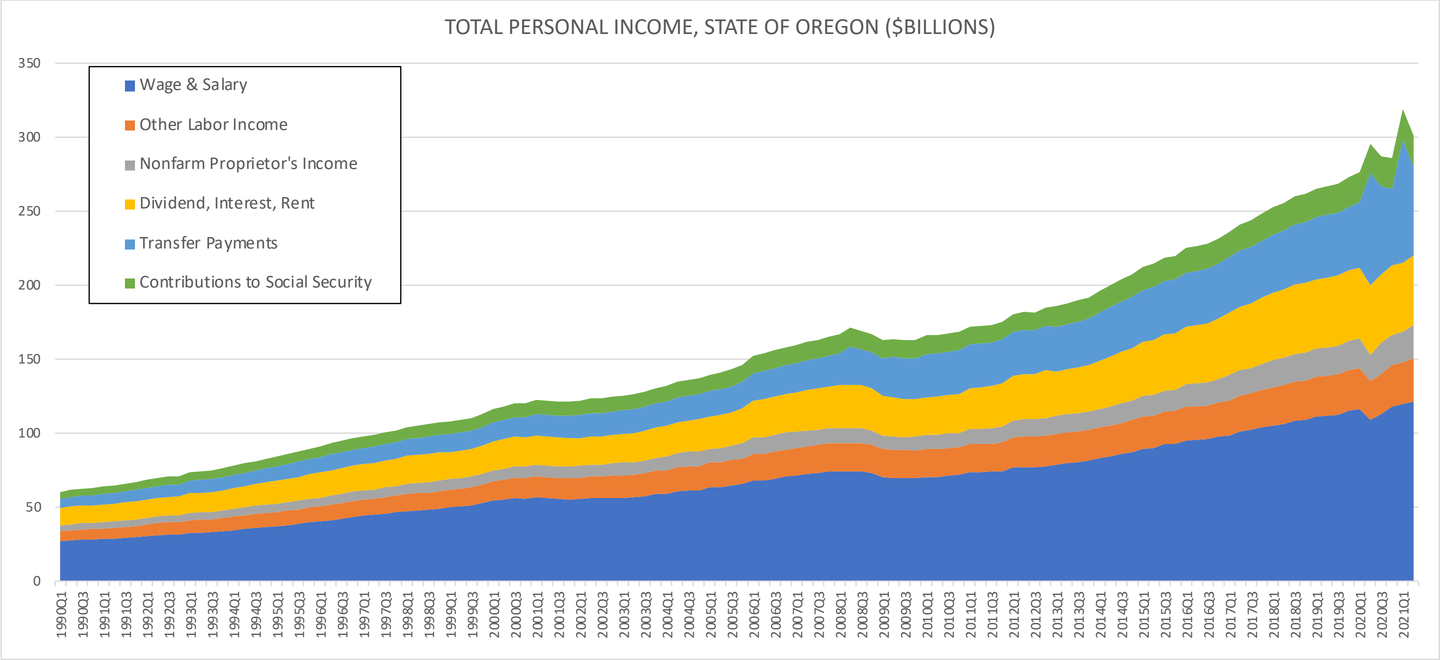


(US Bureau of Economic Analysis)

The state of Oregon has outperformed the national average in terms of employment growth for decades and is expected to continue that pattern through 2031 in the state's most recent forecasts. Income levels in the state of Oregon have risen sharply during the pandemic, with reductions in wages and earnings more than offset by sharp increases in transfer payments. While the transfer payments reflect a one-time influx, the impact is likely to be extended as personal balance sheets are improved which will fuel elevated personal consumption.

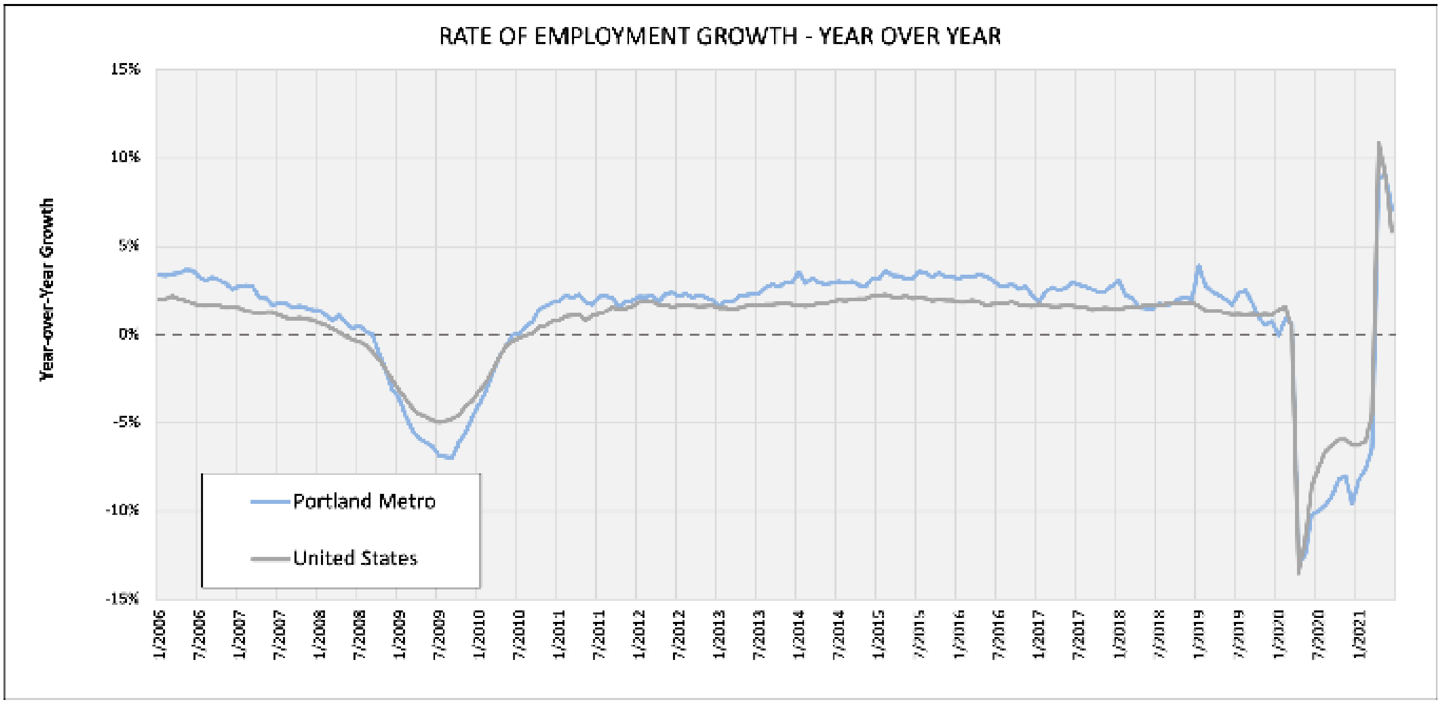


(State of Oregon Economist's Office)

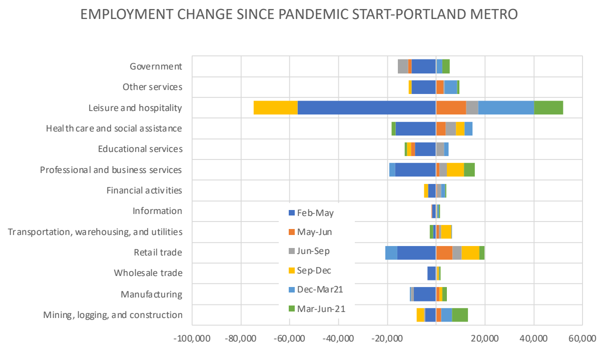


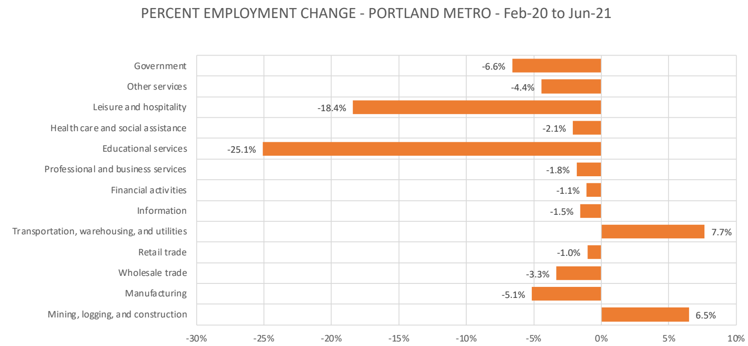
(State of Oregon Economist's Office)

The rate of employment growth in the Portland metropolitan area has largely followed the national average in the last year. Despite recent growth, only the transportation, warehousing, and utilities sector and construction sectors have employment levels above the pre-recession levels. The leisure and hospitality sector remains 25.1% below February 2020 levels, while government and manufacturing also remain well below pre-recession levels.



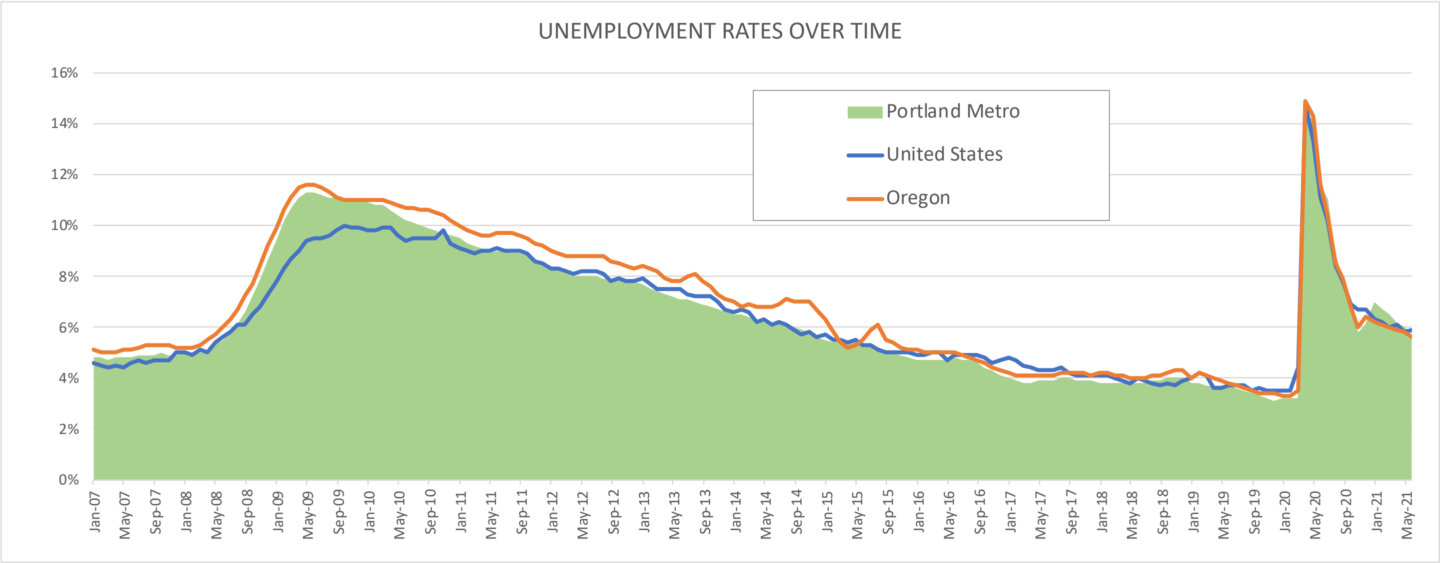
(State of Oregon Employment Department)





(State of Oregon Employment Department)

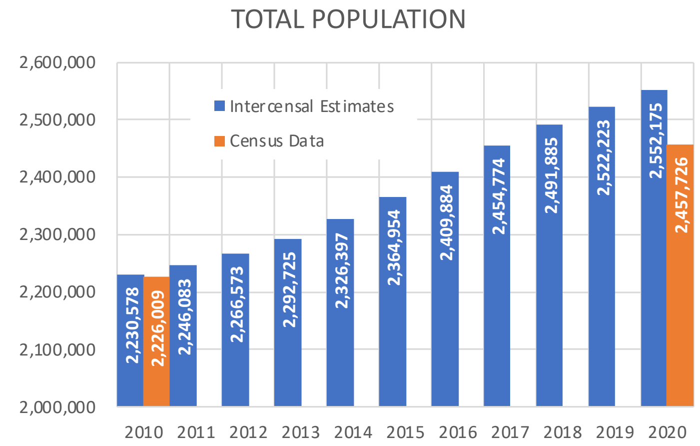
The unemployment rate in the Portland metro area has tracked with the national and statewide rate and was estimated at 5.7% in June 2021. While steadily improving, the rate remains well above the pre-pandemic level. The rate is likely a bit understated due to short-term reductions in the labor force participation rate. If school openings go forward as planned it should increase the ability to work outside of the home for significant portions of the labor force.

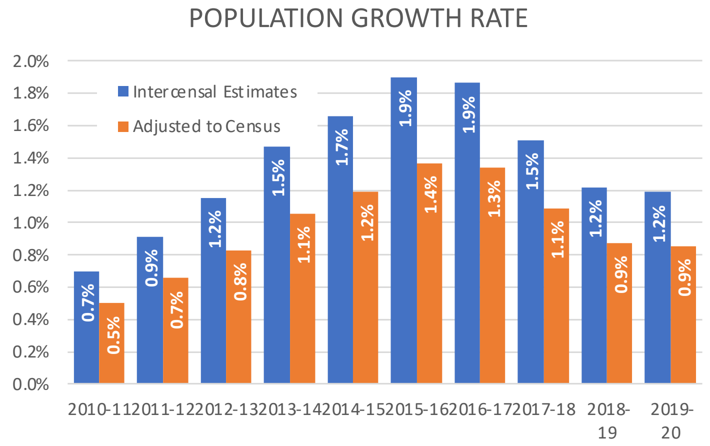


(State of Oregon Employment Department)

2020 CENSUS

The US Census Bureau recently released preliminary numbers from the 2020 Census. Every decade this release requires a recalibration of intercensal estimates, which tend to become increasingly unreliable as we get further from the census. The 2020 census indicated a population level of just over 2.51 million in the Portland metropolitan area (April 2020), roughly 40,000 below the intercensal estimate (July 2020). This would indicate that population growth in the metro area was only 88% of what was estimated in the intercensal numbers. If we assume that the shape of growth is correct in the intercensal estimates, we can adjust interim estimates to fit the curve to fit the new endpoint.





(Population Research Center and US Census Bureau)

The state of Oregon's intercensal estimates are 30,000 greater than the 2020 census numbers for 2020. It should be noted that the time period of these estimates is somewhat different, as the census reflects April number while the intercensal estimate reflects July numbers. The average annual growth rate for Oregon was 1.0% from 2010 through 2020. Reconciling the census numbers with the intercensal estimates yields higher than expected population growth in jurisdictions such as Bend and Salem, with lower-than-expected growth in Portland during this period.

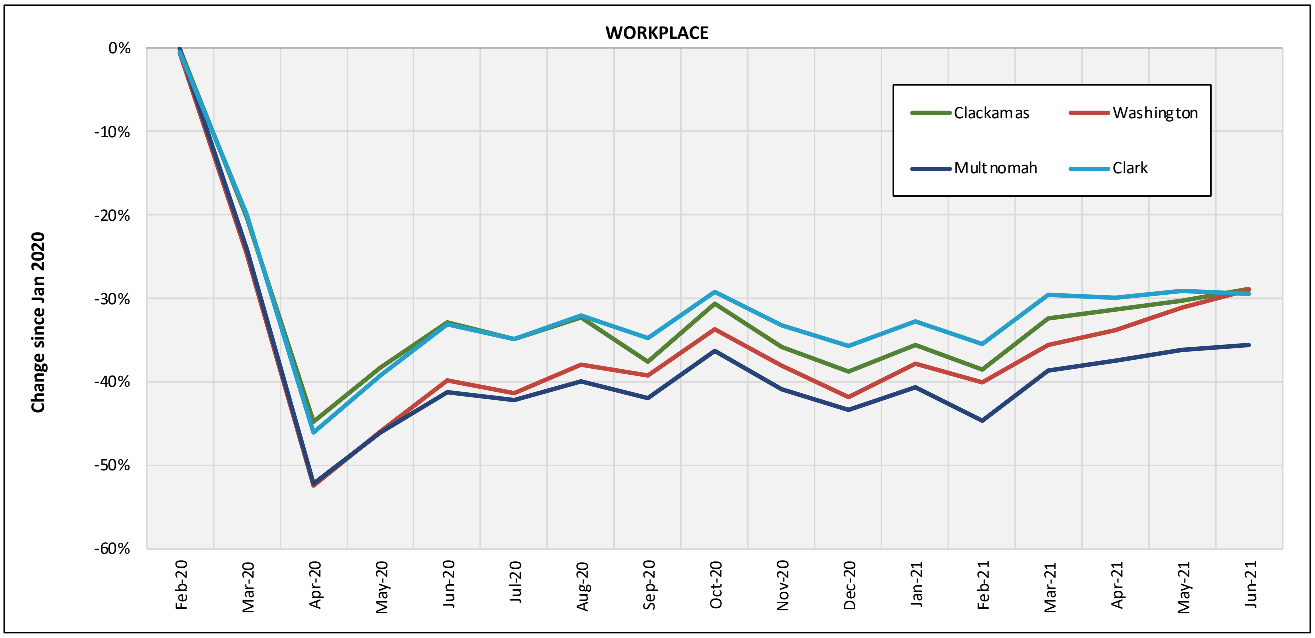
	Intercensal 1-Jul-20	Census 1-Apr-20	Avg. Rates 2010-20		
			Differential	Intercensal	Census
OREGON	4,268,055	4,237,256	-30,799	1.1%	1.0%
Bend	92,840	99,178	6,388	1.9%	2.6%
Portland	664,675	652,503	-12,172	1.3%	1.1%
Salem	168,970	175,535	6,565	0.9%	1.3%
Hillsboro	104,670	106,447	1,777	1.3%	1.5%

(Population Research Center and US Census Bureau)

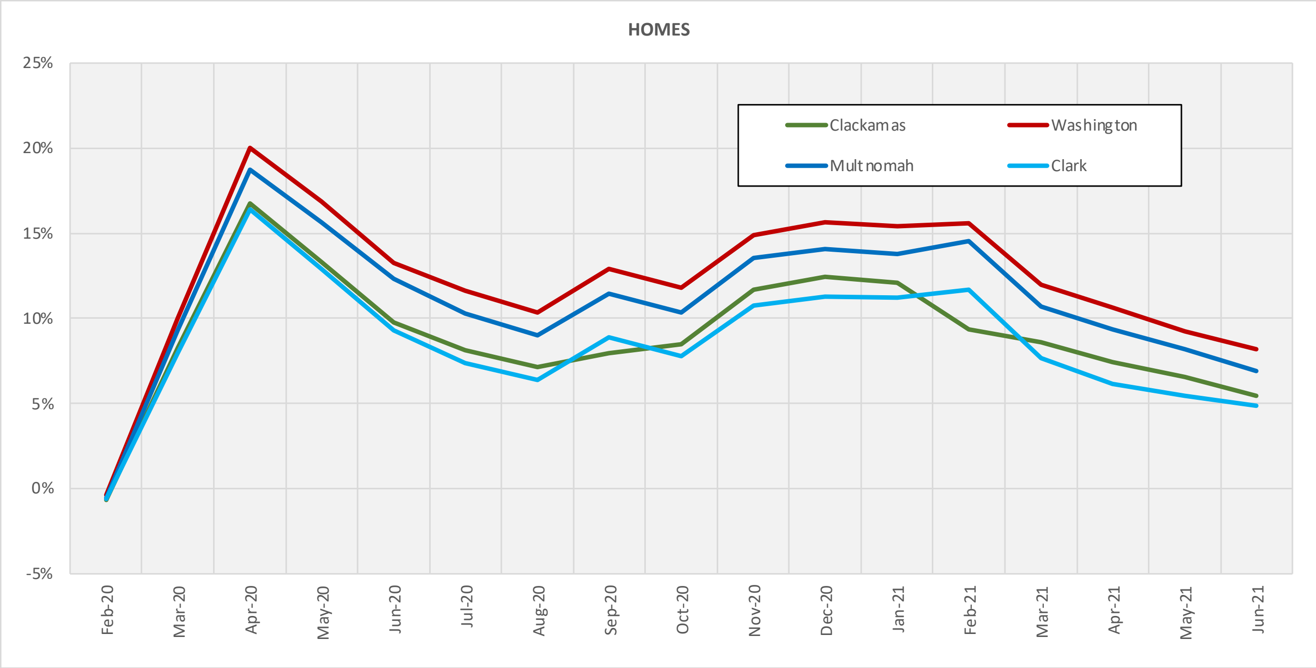
MOBILITY

Smart phone data provides revealing insights into changing mobility patterns during COVID, and gives some indications of where we are in the recovery. The data indicates areas and services that people avoid, while also indicating the activity level and vitality of urban areas. Google provides this data on the county level. The following data compares the aggregate amount of time spent in different locations to the January 2020 median (pre-pandemic condition). The data does not show year-over-year changes, and thus does not distinguish between seasonal changes.

Google's data show a steep decline in time spent at workplaces and an increase in the time spent at home in March and April last year. Multnomah County saw the biggest impact, while the suburban counties saw a lower level of impact. Most counties have seen only modest improvement over the past year. For Oregon as a whole, workplace activity remains 27% below pre-COVID levels. Part of this is due to a loss of jobs. Applying these rates to current employment indicates that 24% of those who worked at a workplace pre-COVID now work remotely.

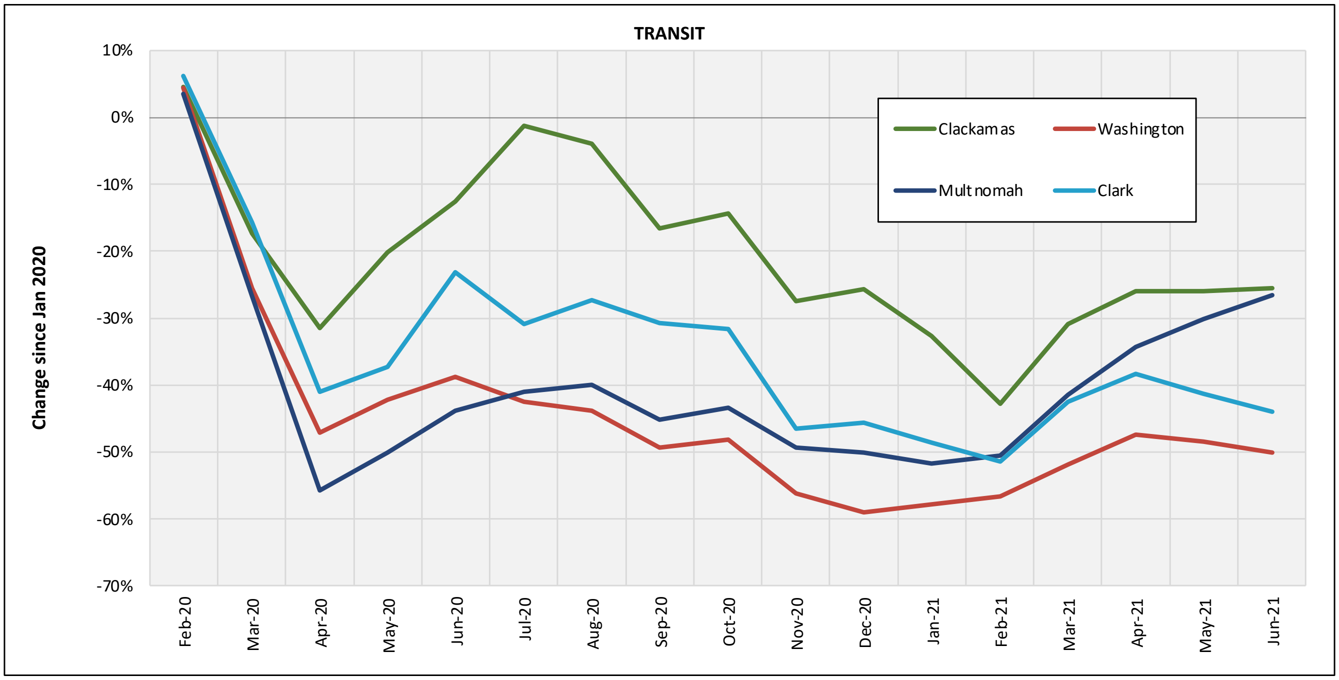


(Google)



(Google)

The use of transit reached a bottom in Multnomah County in April last year, while Washington County did not reach the bottom until December. The counties are currently 27% and 50% below the January 2020 level, while Jackson and Deschutes counties are only 2% below. Visits to parks are highly seasonal, and very limited in January. However, most counties had less visits to parks in March 2021 than in February 2020. Park visits in June this year are only slightly higher than in June last year.



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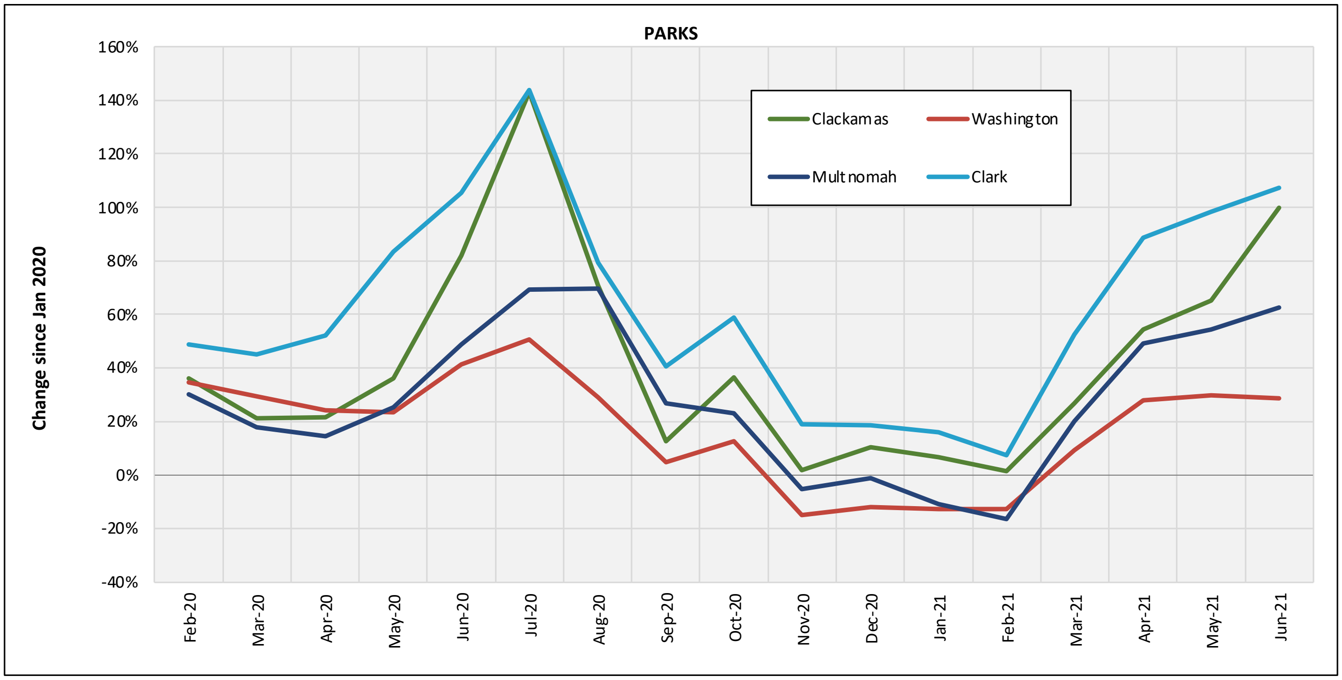
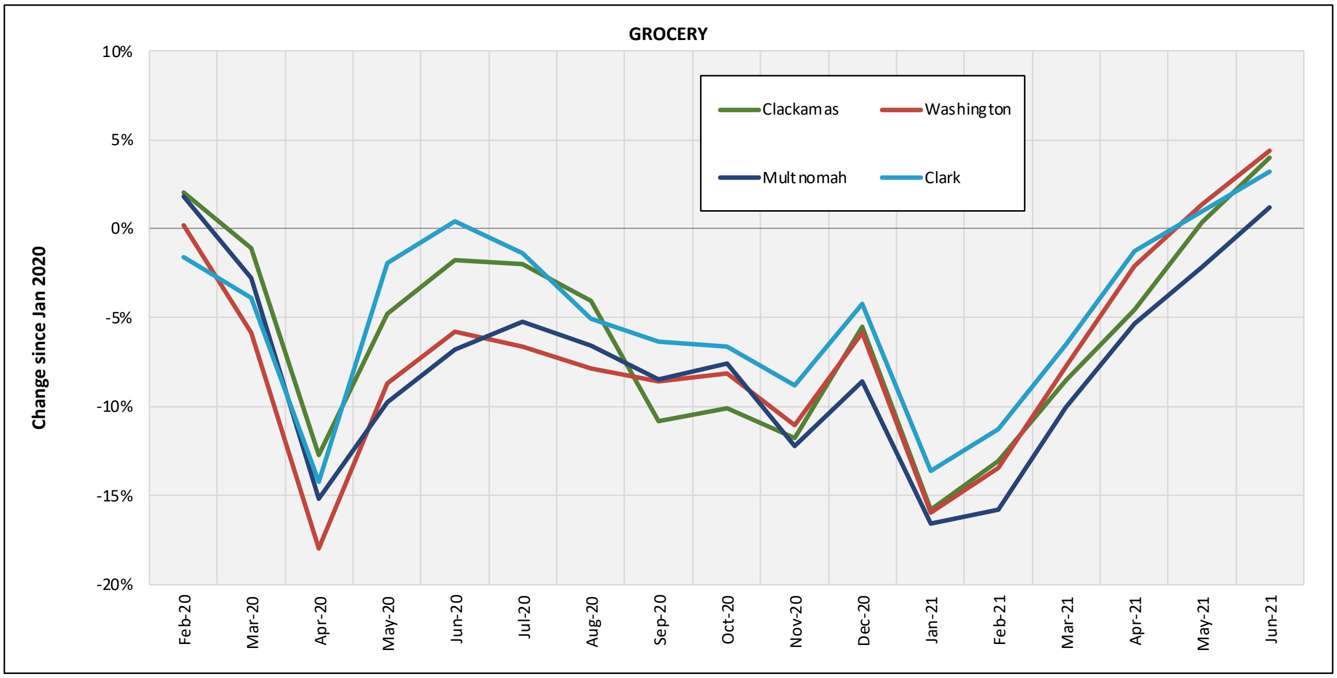


(Google)

Visits to grocery stores initially dropped 8% to 18% early in the pandemic. Store visits in June this year were higher than just before COVID. Multnomah County was the hardest hit due to a decline in lunch visits. Other forms of retail that represent fewer necessary goods saw steeper initial declines and remain below pre-COVID levels. Multnomah County has again taken the biggest hit, with current activity levels 18% below January 2020. As retail traffic would normally increase in Multnomah County during the summer, this suggests that the county, and Portland in particular, still has a way to go to recover its pre-COVID urban vitality.



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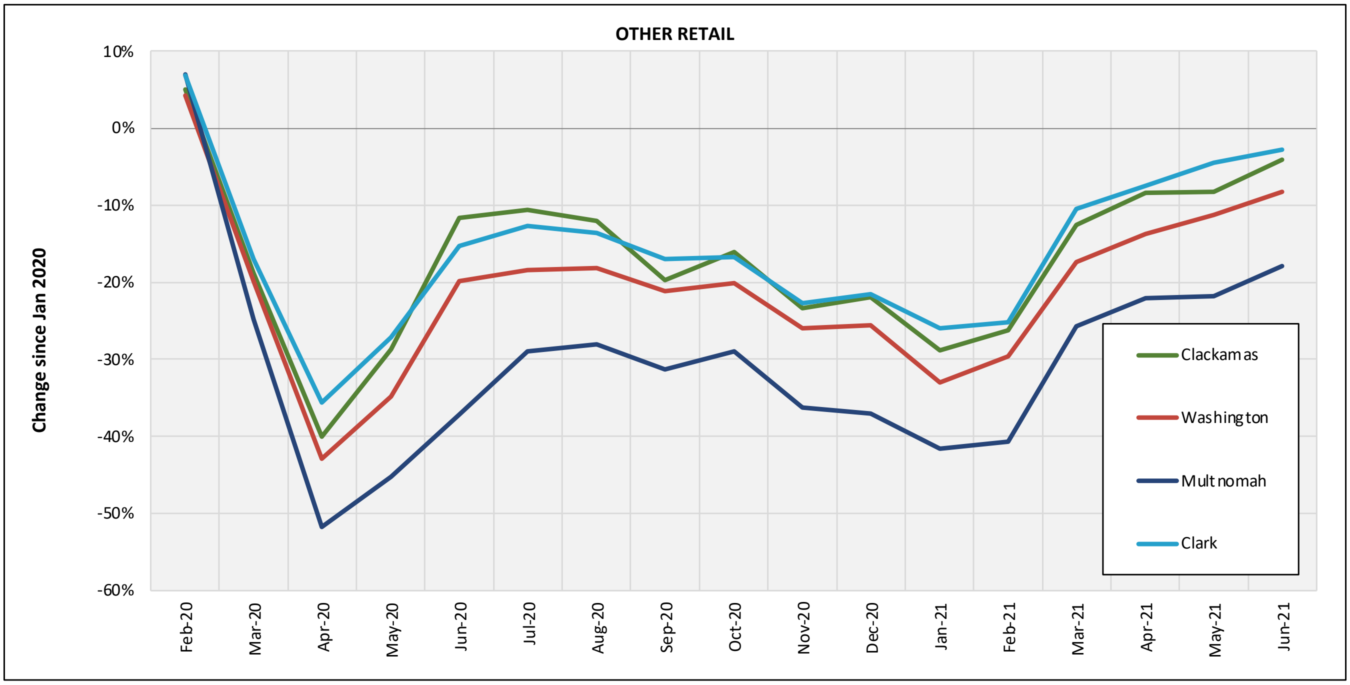
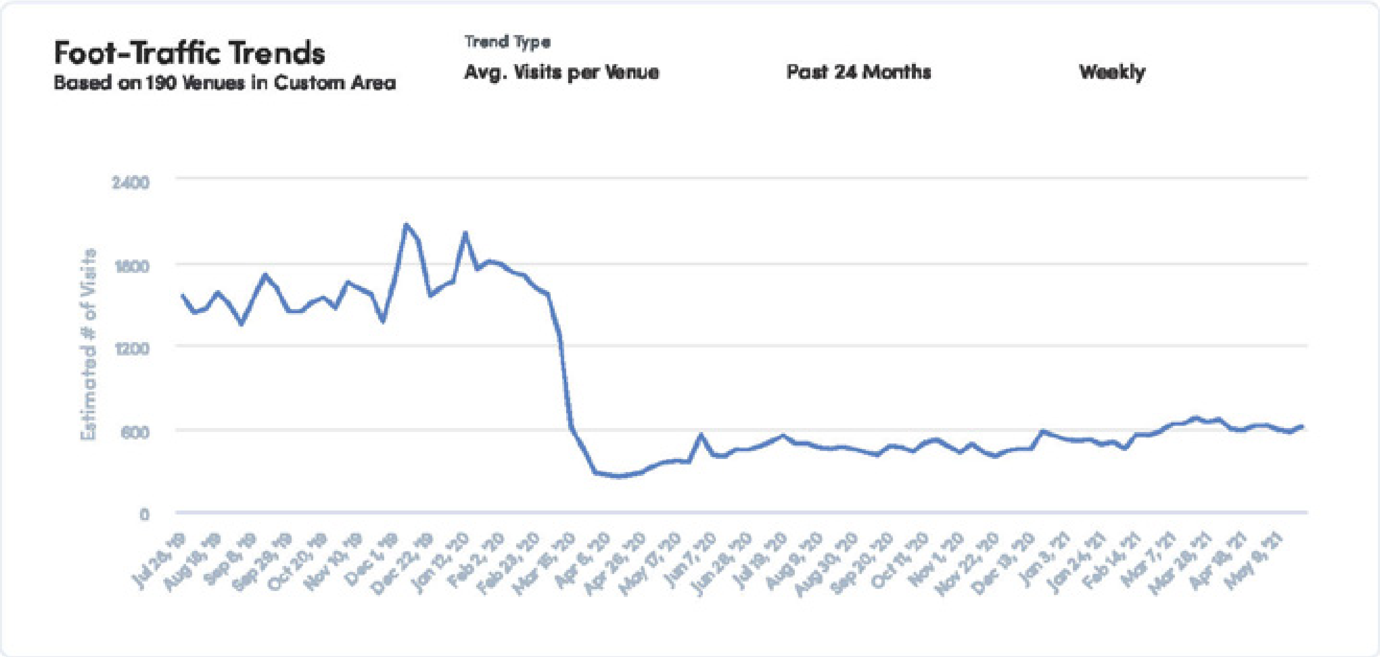


(Google)

If we look at downtown Portland (inside the I-405 loop), the shift in observed foot traffic has been significant, with little improvement since the pandemic started. Foot traffic information collected from cell phones indicate a drop in traffic of two thirds during the pandemic, with very limited growth. A combination of ongoing protest damage, increased levels of homelessness, and most importantly, the sharp reduction in daytime population as firms keep employees at home, have all contributed to an environment that is highly challenging to downtown retailers. While it was expected that major firms would start returning to their office in September, the Delta variant has put those plans on hold for now.

CHANGE IN FOOT TRAFFIC OVER TIME, PORTLAND CBD – WEST OF RIVER AND EAST OF I-405 LOOP



(Alphamap)

02

NAIOP DEVELOPMENT

Suburbs, Edge Cities and Santa Fe: A Conversation with Joel Garreau

Gerard C.S. Mildner
Trey Barrineau
Portland State University

Gerard C.S. Mildner is an associate professor of real estate finance and academic director at the Portland State University Center for Real Estate in Portland, Oregon. Trey Barrineau is the managing editor of publications for NAIOP.

[Note: This article is adapted from the Fall, 2021 issue of NAIOP Development magazine.]

The status of the suburb has become a weathervane of American culture, criticized for its homogeneity and environmental impact, yet loved for its affordability and convenience. Joel Garreau's modern classic "*Edge City: Life on the New Frontie*r" (1991), explored the biggest revolution in how the world builds cities, focusing on giant suburban office nodes and the development that grew up around them.

"Edge cities are typically freeway-hugging agglomerations of regional malls, business parks, hotels and the occasional rental apartment complex," wrote Christopher B. Leinberger of George Washington University in the Summer 2018 issue of NAIOP Development magazine. "They are dependent on cars and trucks as their primary or only transportation option. And they are where the vast majority of economic growth and substantial real estate development occurred in the late 20th century U.S."

Development magazine recently sat down with Garreau to discuss the future of cities – edge and otherwise – on the 30th anniversary of his groundbreaking book. The conversation has been edited for clarity and length.

Development: Could you talk about the origins of your first book, "The Nine Nations of North America," and how that led to "Edge City"?

Garreau: Back in the late 1970s, I was the national editor at the Washington Post, responsible for all the reporters outside Washington, D.C. The conventional wisdom at that time was that the American built environment had turned homogenous and bland. It was all the same airports, all the same interstates, nothing was different. But when my reporters were out there trying to get a handle on the continent, we discovered that was not true at all.

There is no way that South Texas is anything like Maine. There is no way that Seattle is like Miami. Anyway, we ended up drawing on cocktail napkins to show boundaries that were real. We used this originally as a news prediction device. That resulted in the book called "The Nine Nations of North America." Ten years later, I had another one of these moments. I ended up living in Fauquier County, Virginia, which is about an hour west of Washington, in the foothills of the Blue Ridge Mountains.

I drove back and forth every day and started seeing office towers erupt along my commute, including in Tysons Corner. I thought, "What? This is not suburbia!" Anyway, it led to another epiphany. I decided to get to the bottom of this because I had been taught in school that sprawl was bad. As a reporter, I needed to discover who is responsible for this and expose them, because that's what Washington Post reporters do, right?

I started investigating, and one of the many things I discovered was that developers cared about what they did. They carried pictures of these buildings around in their wallets like they were children. They took them out and they showed them to me, and they felt passionate about their work. All they were doing was giving the American people what they demonstrably showed they wanted by that most reliable of measures – their willingness to pay for it.

So, I said, "OK, well, wait a minute. Why did they think they were just giving Americans what they wanted? What is it about Americans that made them think that this is right? Anyway, one thing led to another, and that was the origin of my second book, "Edge City."

I discovered that Americans put an extraordinary value on individuality. They want to be able to live where they want, shop where they want and work where they want, all in unlimited combination. And if you have those things, what you end up with is nodes at the intersection of transportation corridors.

I went to Coldwell Banker to confirm my hunch. In the late 1980s, it took four of their offices two weeks to generate these numbers. That's when I discovered that, for example, Tysons Corner, Virginia, was the largest urban core between Washington and Atlanta, even back then, as measured by white collar jobs, using 250 square feet office space per worker as a surrogate for that. The book identified 123 places in the U.S. that had all the functions that a major city had always had through history, and yet looked nothing like old downtowns. There were almost three times as many Edge Cities as there were downtowns of comparable size. These were not suburbs. They were their own "urbs". Few had ever talked about these places as such.

Development: Some downtowns rebounded since your book came out and many Edge Cities are struggling to stay competitive. For example, Tysons, the archetypal Edge City, is now adding housing, sidewalks and commuter rail. What's next?

Garreau: What's replacing Edge Cities and old downtowns is this new form of urbanity that's as revolutionary now as Edge Cities were when they first started back in the '70s and '80s. They are so revolutionary that they're dividing Edge Cities and the downtowns into the places that will survive and the places that will die. They're going to have to compete with these new places. The major thing is that these areas encourage novel experiences and interaction in places far smaller and more charming and scenic than we're used to seeing in anything so sophisticated. And they're not suburbs. They're typically far from major metros. If you can't compete with that, you're in trouble as urban center.

This is the biggest revolution in how we build cities since Edge Cities. It's these places that are a lot like Santa Fe, New Mexico, and they're erupting globally. They're very different from the old-fashioned cities. Their big draw is that technology has allowed them to become urbane without the burdens of being urban.

Profile of Santa Fe, New Mexico	
Population, 2019	84, 683
Population Change, 2010-19	4.7%
Percent Hispanic	55.2%
Percent White alone, not Hispanic	40.0%
Median Home Price, 2015-2019	$280,000
Median Gross Rent, 2015-2019	$1,080
Bachelor's Degree, Age 25+	41.7%
Median Household Income	$57,972
Population Per Square Mile	1,477.8
Mean Travel Time to Work, Age 16+ (minutes)	19.3

Source: US Census Bureau

This is the opposite of suburbanization. This is not sprawl, this is aggregation – people coming together – and dispersion away from industrial-age places to human-scaled places. It's people coming together, but to their ideal places. As everything digital accelerates, these places are excelling at the one thing that you can't digitize –face to face contact– that's becoming more and more rare and valuable. We've discovered during the pandemic how stir-crazy you can get. Face-to-face is important. It's critical to building trust, to falling in love, and to having fun.

Santa Fe is the classic example of this phenomenon because it's urbane. It has amazing world-class opera, charming architecture, distinguished restaurants – and great places to buy used boots, of all things! Quirky bookstores, mountains and diversity. And with a population of only about 85,000 people.

Development: What's driving this?

Garreau: Cities throughout human history have been shaped by the state-of-the-art technology at that time. If the state-of-the-art in transportation is shoe leather and donkeys, what you get is Jerusalem at the time of Jesus. Sixteen centuries later, the state of the art becomes horse-drawn wagons and ocean-going sail. All of a sudden you get cities like Amsterdam, or Boston, because they're based on horse-drawn wagons and sail, and they operate in entirely different ways. Then railroads produced cities like Chicago. And later, the automobile results in places with multiple cores, like Los Angeles.

Then along came the jet passenger plane. I will give you an example. In 1955, what was the southwestern-most major league baseball team in the United States?

Development: St. Louis?

Garreau: Very good. What happened is that you just simply couldn't maintain a major league schedule if your team is located any farther southwest than St. Louis if you were moving the players by train. But jets changed all that. They allowed the eruption of world-class metros in places that would not before have been practical – Dallas, Denver, Houston, Atlanta, Phoenix, Sydney, Beijing and so many others.

So, Edge Cities were a combination of the automobile and the jet plane, plus the corporate computer. Then, shortly after "Edge City" came out, the big boom was in the internet, which only a few people knew about when I wrote in 1991. The New York Times didn't have more than a dozen references to it, if that. If they ever talked about the internet, it was about the bizarre way that scientists were talking to each other. That was the internet in 1991.

Now, the internet is spurring these "Edge City 2.0's," places like Santa Fe, where people can get weapons-grade sushi delivered to them overnight and make six-digit incomes while being surrounded by interesting people and trout streams. But not just any remote place. People value natural beauty with remarkable face-to-face. You can see this in commercial real estate right now. Malls are dying and office buildings are being converted into apartments. We really haven't seen an old-fashioned Edge City like Tysons built from scratch in 30 years, and it's because these Edge Cities are being replaced.

You could see this taking off just over a decade ago. Wenatchee, Washington was the fastest appreciating real estate metro 15 years ago. It was just booming. I thought I knew this continent pretty well, but I had to look up where Wenatchee, Washington is. It turns out that Wenatchee is three hours east of Seattle, on the dry side of the Cascades, which explains a lot. So, Seattle's full of people with great jobs, and Amazon, Microsoft, and the Gates Foundation, and all that. Yet it rains all the time.

Then, I discovered that Wenatchee has over 200 days of sunshine a year, and great skiing, and that it's only three hours away. It was beautiful, enchanting and great for face-to-face, so folks would go there for the weekend. It's an old story, but at the end of a marvelous vacation, people will turn to each other and say, "Why are we leaving?"

When you see them arriving on Thursday and returning on Tuesday, that's the revolution. At that point, they're spending more time living and working in Wenatchee than they are in Microsoft's Edge City in Redmond. That's the revolution. To be clear, does this mean that we're now lone eagles? That we're abandoning cities? No. Humans are social animals. Solitary confinement is an extreme punishment, and humans love face-to-face. That's the whole point of these new places that are similar in feel to Santa Fe.

Development: Is the supply of these places infinite? What do you see as the main constraints? An airport?

Garreau: That's a really good question. I'm debating this, as I was back in the late '80s with the original Edge City concept, trying to figure out what the laws are. What are the rules? Yes, airports. That was my first guess that the limiting factor was an airport. But I'm finding they'll puddle-jump surprising distances if they love the place enough. Consider South Jordan, Utah. It's between the 10,000-foot-tall Oquirrh Mountains and the 12,000-foot-tall Wasatch range. It's as if people are wanting something new, something beyond the patterns that had come before. That's why these placing are thriving.

Folks like concentrated, walkable real places that have evolved naturally. But they don't want to live like pioneers. Think Monticello with broadband. These new places look nothing like sprawl. As I say, it means urbane, well beyond what we have ever thought of as urban. So, weekend getaways that look and function like Sante Fe are becoming the new places people and economies are moving.

Now, that doesn't necessarily mean that Edge Cities and downtowns die. Again, face-to-face interaction is the critical element for any urban agglomeration, and lots of Edge Cities can pass the test, like Reston, Virginia, for example. That's a good place for face-to-face interaction. The point is, all these new places are the new competition. They're occurring far beyond what we currently think of as a major metro. The premiums for these places is that they are not like Tysons.

The 15 Fastest-Growing Large Cities Between July 1, 2017, and July 1, 2018, With Populations of 50,000 or More on July 1, 2017			
Rank	Name	Percent increase	2018 total population
1	Buckeye, Arizona	8.5	74,370
2	New Braunfels, Texas	7.2	84,612
3	Apex, North Carolina	6.8	53,852
4	Frisco, Texas	6.1	188,170
5	Meridian, Idaho	6.1	106,804
6	McKinney, Texas	5.4	191,645
7	Georgetown, Texas	5.2	74,180
8	Rowlett, Texas	5.1	66,285
9	St. Cloud, Florida	5.0	54,115
10	Ankeny, Iowa	4.6	65,284
11	Dublin, California	4.5	63,445
12	South Jordan, Utah	4.4	74,149
13	Midland. Texas	4.4	142,344
14	Castle Rock, Colorado	4.3	64,827
15	Round Rock, Texas	4.3	128,739

Source: US Census

Development: So the number of these places in the United States could be in the 50s or 100s? Have you settled on a definition of size or scope?

Garreau: So, with "Edge City" I had a metric – office space as a surrogate for white collar jobs. So, I got all that great data from the real estate industry and I divide by square foot per worker, and voila, that's how many white-collar jobs that were there. You can debate whether 250 was the right number of square feet per job, especially as they moved to the cube farms. But it was the best available data.

Now, to do this now with these places, I suspect the most reliable surrogate would be to watch for the most explosive growth in tiny markets. That's what tipped me off to Wenatchee. It was a fast-growing metro. Once the census had to recognize Wenatchee as a metro, the city would appear on the real estate industry's list.

In any case, you do the best you can with the data you have. You should look at the list of fastest-growing metros, fastest-appreciating metros, and what pops up are these places. The top 10 or top 20 just pop out as the "new Santa Fe's." Then go check them out.

The 15 Fastest-Appreciating Small Size Cities Between 2000-2010 With Populations Less than 150,000 in 2020			
Rank	Name	Percent increase	Median Home Price, 2020
1	Lehigh Acres, Florida	148.8%	$183,509
2	Rialto, California	124.2%	$384,574
3	Victorville, California	123.3%	$269,579
4	Vallejo, California	121.2%	$438,032
5	Mesquite, Texas	110.8%	$191,440
6	Lowell, Massachusetts	110.7%	$314,488
7	Warren, Michigan	110.1%	$148,016
8	Antioch, California	108.0%	$480,233
9	Sparks, Nevada	106.8%	$363,894
10	Daly City, California	106.0%	$1,071,308
11	Santa Clara, California	105.7%	$1,235,305
12	Inglewood, California	105.4%	$604,388
13	Miami Gardens, Florida	105.1%	$277,628
14	San Mateo, California	100.7%	$1,425,572
15	Fairfield, California	96.6%	$475,589

Source: US Census Bureau, American Community Survey, and ConstructionCoverage.com

Tysons, Virginia, is often considered the quintessential Edge City. Other prominent examples include Century City in Los Angeles; King of Prussia, Pennsylvania; and the Research Triangle Park near Raleigh, North Carolina.

WHAT MAKES A PLACE AN EDGE CITY?

Here's how Joel Garreau defined an edge city in his influential book, published 30 years ago:

An Edge City:

- "Has five million square feet or more of leasable office space — the workplace of the Information Age."
- "Has 600,000 square feet or more of leasable retail space. That is the equivalent of a fair-sized mall."
- "Has more jobs than bedrooms. When the workday starts, people head toward this place, not away from it."
- "Is perceived by the population as one place. It is a regional end destination for mixed use — not a starting point — that 'has it all,' from jobs, to shopping, to entertainment."
- "Was nothing like 'city' as recently as 30 years ago. Then, it was just bedrooms, if not cow pastures. This incarnation is brand new."

ABOUT JOEL GARREAU

Joel Garreau is a former reporter and editor at The Washington Post. He has been a fellow at The New America Foundation in Washington, D.C., an affiliate of The Institute for Science, Innovation and Society at Oxford, a Science Journalism Laureate at Purdue University, and a member of Global Business Network. He has also served as a fellow at Cambridge University, the University of California at Berkeley and George Mason University. He is currently the Professor of Culture, Values and Emerging Technologies, Emeritus, at Arizona State University.

03

COMMERCIAL MARKET

Office Market Analysis

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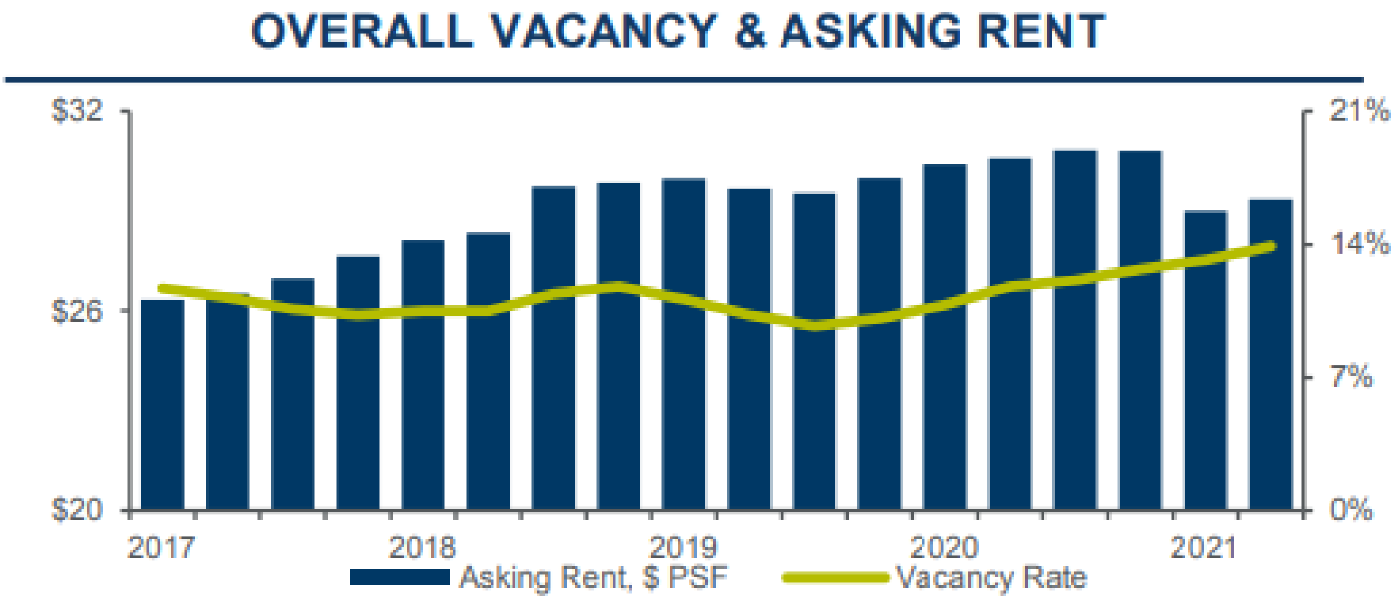
EMPLOYMENT OVERVIEW

With the lifting of most COVID restrictions on June 30, the Portland economy has begun to revive across multiple sectors, albeit at a slow rate with many headwinds still remaining. The unemployment rate in Portland was estimated at 5.6% during May 2021, comfortably below the national average of 5.9%, and far from the high of 13.2% at the height of the COVID pandemic in April 2020. Total non-farm employment currently stands at 1,115,900 and, while an improvement over the dismal second quarter 2020 results, the current second quarter 2021 total is 89,700 below peak first quarter 2020. Many of these losses are in the entertainment and hospitality sectors which were devastated by COVID shutdowns, but a substantial sum also is from the closing of offices and the expiration and vacating of office leases coinciding with the rise of work-at-home employee arrangements such as Zoom calls.

Two factors going forward seem to give some slight hope to the overall Portland employment market are the return of foot traffic to the downtown Portland business core and the reopening of in-person learning within the Portland Public School system. All metrics of downtown Portland foot traffic which collapsed more than 80% in the second quarter of 2020 appear positive and slightly improving in the second quarter of 2021 but far below pre-pandemic rates. Parking meter transactions are up 53% year over year but still 45% below February 2020. Trips downtown via TriMet were down 73% year over year and crossings of the Morrison Bridge were also down 33%. Recent attempts to reopen the downtown business core for office workers and tourists appear ineffective, at least at the present time. This is likely attributable to the lingering effects of the pandemic, which include public perceptions of dangerous conditions in the area, rampant homeless populations, rising street crime, and other negative quality-of-life issues. The reopening of Portland Public Schools for in-person learning will allow parents burdened with childcare issues during COVID shutdowns to return to office work, which could facilitate an increase in traffic to the downtown core.

OFFICE MARKET RATES

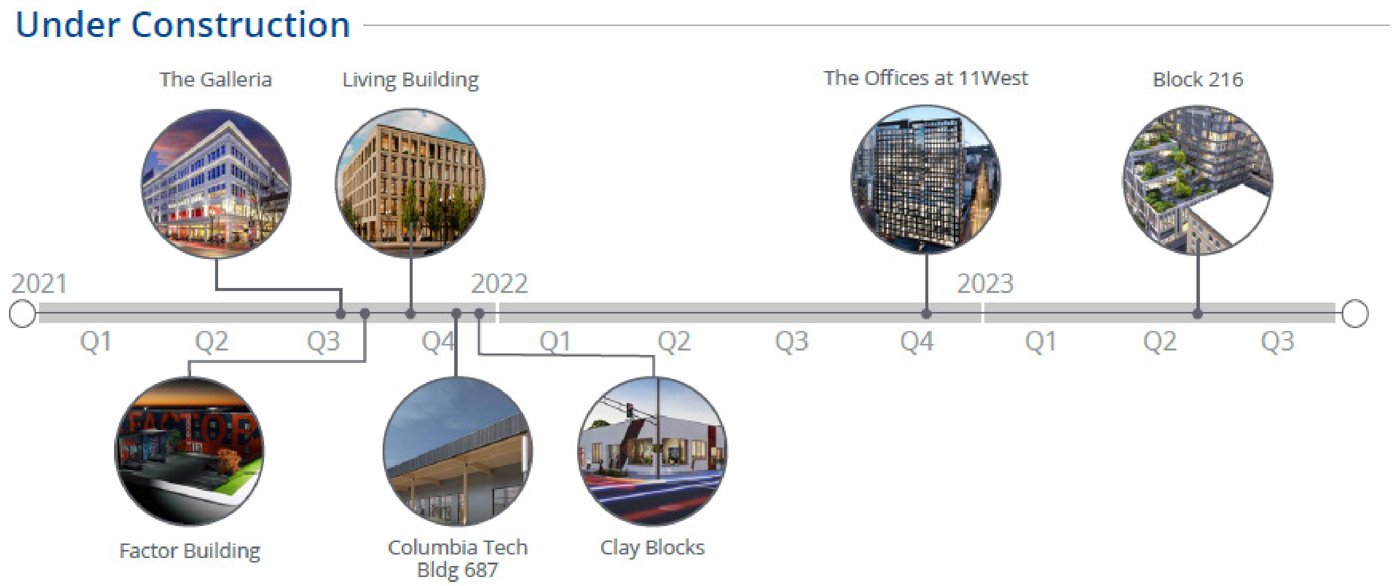
Direct office vacancy rates across all commercial areas of Portland stand at 10.5% at the end of the second quarter of 2021, reflecting a whopping 40% decline in occupancy year over year. Asking lease rates remained stable from the first quarter at $28.02/SF for office properties overall and $32.19 for Class A office. All figures clearly show that office leasing has not returned to pre-pandemic levels. While there are quarter-over-quarter rental rate increases for office properties in the suburbs around Portland, rental rates and leasing activity remains weak in the Portland Central Business District ("CBD") where extensive landlord concessions are necessary to execute new leases or renewals.



Source: Cushman & Wakefield

Overall office property vacancy in the CBD has increased to 20% in the second quarter of 2021, a rise from 15.4% during the same period in 2020. Current inventory stands at 73,130 square feet, a slight decline from 73,600 square feet in the first quarter of 2021. There is 80,000 square feet of new supply, up from 40,000 square feet in the first quarter, suggesting developers are continuing to add new office space despite historically flat demand. Another 1,409,000 square feet is currently under construction, a modest rise from 1,340,000 in the first quarter of 2021, once again showing further future supply despite no significant indicators of rising demand. As predicted, net absorption was a negative 17,000 square feet in the second quarter of 2021, but this reflects an improvement from a negative 886,000 square feet in the first quarter, explained mostly by the required notice given for leases during the height of the pandemic in the second quarter of 2020.

Construction rates have been steady between 1.0 million and 1.6 million of new space in Portland since 2017 and this trend shows no sign of abating. With more than 1.7 million square feet of negative absorption across the city with half in the CBD alone, there is plenty of space available for professional firms, technology companies, and government agencies which still are leasing space, albeit at not as rapid a pace as just two years ago. Nine new leases for more than 25,000 square feet were signed in the second quarter of 2021. But while the demand for space is still strong in places, there is much vacant existing and soon-to-arrive new space available. Rents will remain stagnant for some time with landlords in fierce competition for tenants with major concessions more the rule than the exception.



Source: Colliers

PORTLAND SUBLEASING MARKET

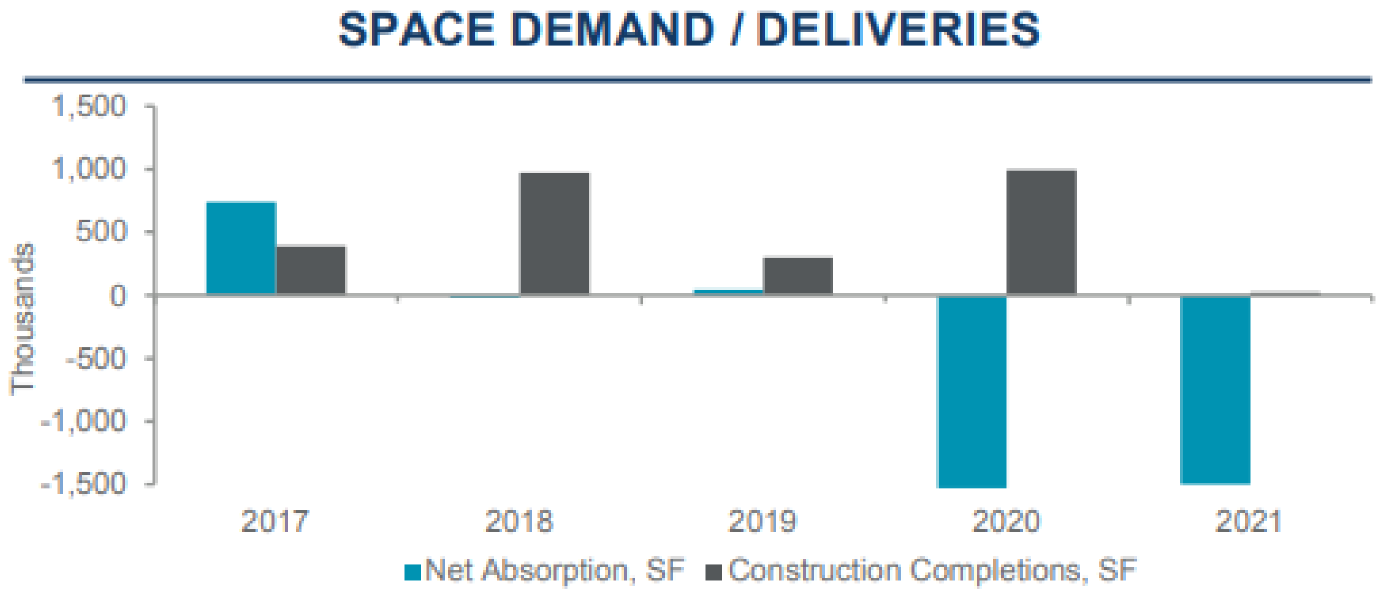
Subleasing activity for Class A office space spiked strongly higher during the first two quarters of 2020 at the height of the COVID shutdowns as tenants attempted to generate income for space left vacant due to temporary and permanent business closures. This trend manifested itself across all sectors of Portland real estate including retail and hospitality but was expressly profound as new leasing demand for office space collapsed. According to statistics reported by CBRE, Portland subleasing activity in the first quarter of 2020 jumped

36% year-over-year, similar to what the brokerage firm has seen in other nearby markets such as Seattle, San Francisco, and San Jose. CBRE estimates during the second quarter of 2021 there were 667,000 square feet of Class A for sublease in Portland.

Despite these high numbers there are some glimmers of good news. Subleasing activity in Portland was substantially higher during the last two other most recent economic recessions; during the 2001 NASDAQ bubble crash and the 2008 Great Recession, which adds some perspective to the depth of the current problems. In the fourth quarter of 2001 more than 1.2 million square feet of Class A was being shopped for sublease in Portland. In the fourth quarter of 2009 more than one million square feet was available for sublease, a staggering 50% increase from just one-half million square feet in the previous quarter. In strict quantitative terms, the current Class A office leasing problems are less than half in size of recent leasing crashes or just 7% of the total Class A supply currently available.

While subleasing availability has increased, much of the space being offered by tenants represents just a fraction of their entire leaseholds. In other words, tenants are not completely vacating offices or closing shop in Portland but merely scaling back the amount of space they occupy on a temporary basis. CBRE reports thirty-three office subleases comprising 255,000 square feet were executed in Portland during the second quarter of 2021, but the average sublease size was just 7,729 square feet with much of this demand being absorbed by tenants in adjoining offices simply expanding their footprints at the expense of their neighbors.

In addition, much of the sublease activity is simply from firms executing permanent leases for larger spaces, taking advantage of low rental rates offered during the pandemic. For example, Ampere Computing signed a lease for 40,000 square feet at the Tanner Point building on Northwest Ninth Avenue and immediately made available for sublease its current 19,000 square feet office at the Field Office on Northwest Front Avenue.



Source: Cushman & Wakefield

Despite gloomy headlines about companies closing their offices and permanently shuttering their operations, all signs from the sublease market in Portland suggest companies are sticking with their leases and merely waiting out the return of normal in-person operations post COVID. Still, there is no denying current sublease volume is historically high, albeit not as extreme as observed during recent real estate crashes. Still, subleasing volume is a forward-looking economic indicator of possible future primary leasing troubles since sublease activity has historically preceded the permanent closing of many firms and their offices in Portland. For example, The Riveter put 10,600 square feet of its total leasehold in Southeast Portland up for sublease in the spring of 2021 only to announce in June its location would permanently close. This said, the sublease numbers overall show the current Class A leasing market is far from the worst performing in recent history with many indications the depth of primary leasing volume collapse has been already reached.

RESOURCES

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2. Colliers
https://www.colliers.com/en/research/portland/2021-q2-portland-metro-office-market-report

3. JLL
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04

COMMERCIAL MARKET ANALYSIS

Industrial Market Analysis

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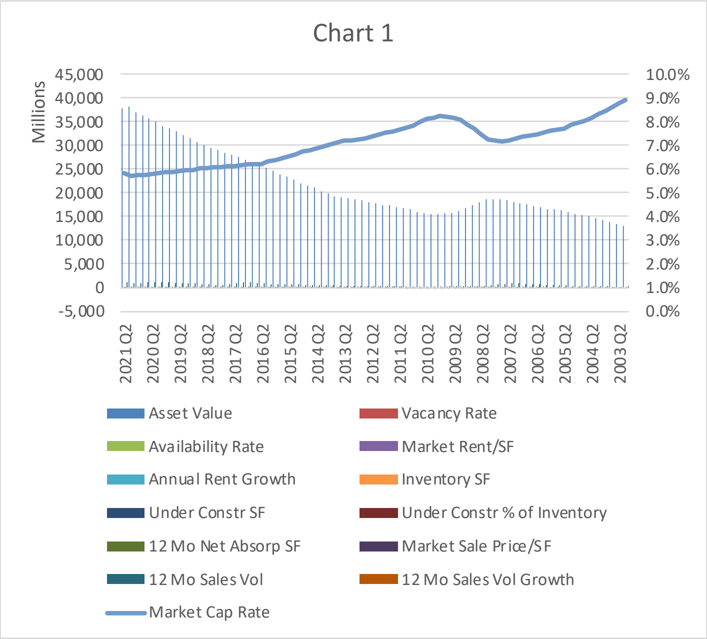
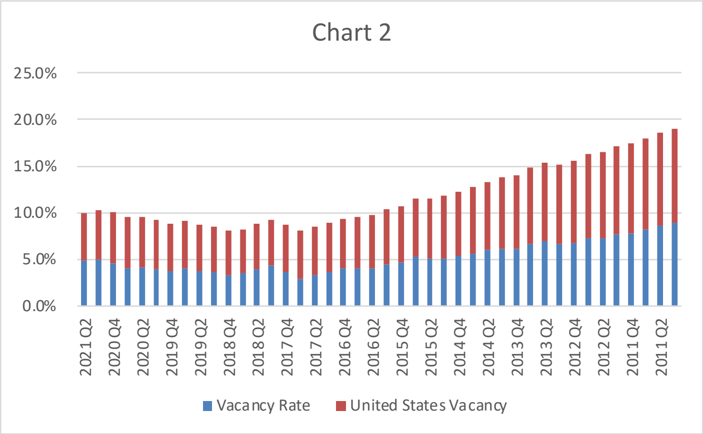




INTRO

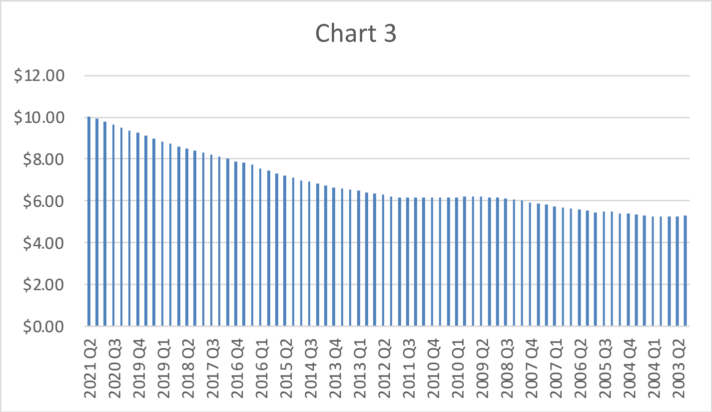
At this stage, the U.S. government has widely distributed vaccines, and most of the country has lifted COVID-19 restrictions. In-person activities are resuming, albeit with caution and consideration of the risks involving variant transmissions. The industrial market segment was a bright spot during the pandemic.

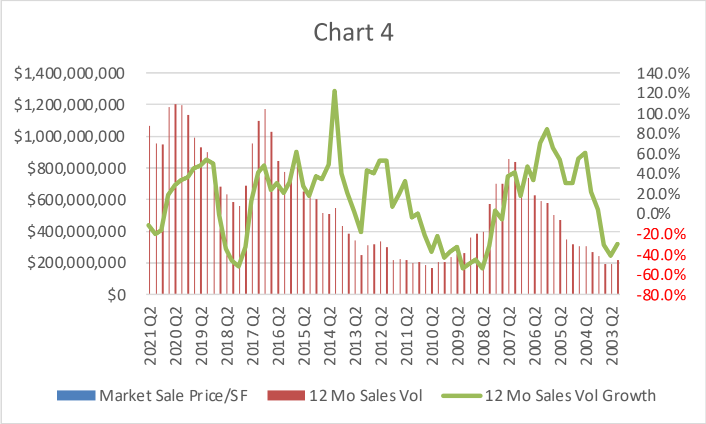
Before the pandemic, Portland's industrial market had performed very well. The pandemic increased the demand for industrial real estate. COVID-19 forced governments to impose lockdowns which shifted demand and forced in-person retailers to shut their doors. Consumers went to e-commerce and packaged delivery in an unprecedented way. Before the lockdowns, e-commerce had shown steady growth, and the global pandemic accelerated the trend and demonstrated its resilience. Industrial was one of the most robust real estate markets over the past year. As our daily lives proceed toward a reopening, there is uncertainty about the permanence and adjustments we will make to our daily lives. The following is a summary of trends impacting the industrial market.

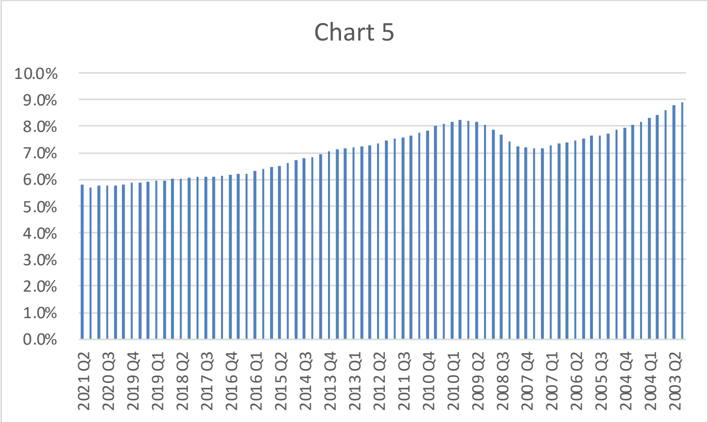
Nationally, logistics and parcel delivery had the most activity in the past year. Many businesses saw their online sales increase, while other companies have increased their online presence. New participants in e-commerce increased 21% year over year (JLL), and e-commerce as a whole had year over year growth of 44.5% in the second quarter of 2021 (CBRE). This increase is driving growth in the wholesale, warehouse, logistics, and delivery services sectors. Although the rate of e-commerce growth peaked in 2020 during the pandemic, most analysts forecast growth to continue, although not as robust.

Supply chain disruptions are another factor that may influence the expansion of industrial space. Trade wars, tariffs, and the pandemic have caused widespread halts, delays, and excessive cost increases for materials. As the world reopened, the demand for materials and goods resumed, and many industries, such as construction, have seen supply shortages. External factors exposed the vulnerabilities of global supply chains and forced companies to reassess their capabilities.

Some companies will look to restore aspects of their manufacturing process or source input materials from domestic manufacturers. Other companies will increase







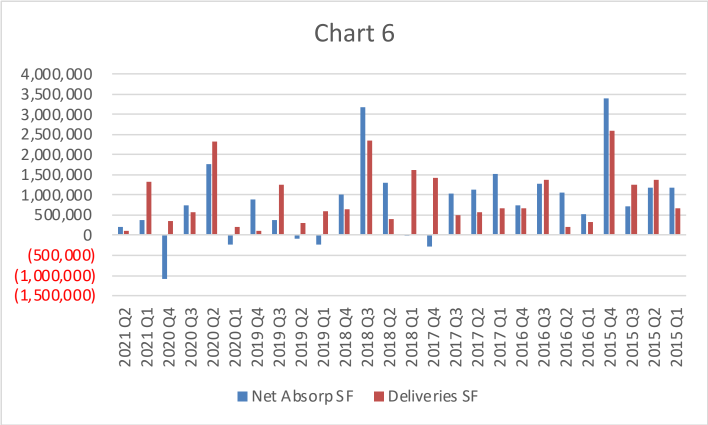
their space for inventory control purposes to hedge against future supply chain disruptions.

LOCAL

Over the past decade, Portland's industrial real estate sector was trending in a very positive direction. In the second quarter of 2021 there have been low vacancy rates, rising rents, higher sales prices, and compressing cap rates. Portland's growing metropolitan region and sound fundamentals continue to draw investment to the region. Often considered a second-tier market, private buyers still account for most trades in Portland's industrial market. However, the growth of the area has caught the attention of institutional capital. Large-scale properties have lifted the region's sales volume. Institutional buyers now make up 30% of total acquisitions, which has doubled over five years. In the second quarter of 2021, however, institutional sales volume declined from the previous quarters, with the primary explanation being a lack of large-scale investment opportunities. With demand present, developers will be wise to watch the next round of urban growth boundary (UGB) expansion applications.

Large-scale projects are seeing a trend toward higher construction requirements. Automation, especially in fulfillment centers, can require infrastructure for heavy systems of high tech machinery. Robotics can also utilize more height in buildings. At the DJC Oregon builders breakfast roundtable, Perlo Construction noted a trend in the higher structural requirements in industrial construction.

The cannabis industry has become a sector vying for industrial space. Oregon has seen tremendous year to year growth in the cannabis industry. In 2020, Oregon recorded a record-breaking $1.1 billion, up from the previous year's $795 million in sales. Wholesalers, growers, manufacturers, and grow equipment suppliers are amongst those seeking industrial space. One of the Portland area's most significant industrial transactions in the past year was a long-term lease for 378,000 square feet in the Blue Lake Corporate Park for Hawthorne Hydroponics, a cannabis grow supplier company. Cannabis remains illegal at the federal level, which imposes some limitations on the industry's growth. For example, access to banking services and the reluctance of traditional institutions to participate in cannabis businesses cause major finance hurdles for cannabis



businesses. The ban on interstate commerce is another limiting factor. After the 2020 election, there are now 37 states who have legalized cannabis for at least some purposes. Earlier this year, Congress passed the SAFE Banking Act on a 321-101 vote, which would allow banks to serve cannabis businesses in legalized states. Although the bill is not likely to survive the Senate, the congressional support and new state legalizations indicate a change in national sentiment.

SUPPLY

Industrial vacancy rates in the region have trended downward over the past decade. The Portland industrial sector ended the second quarter of 2021 with a healthy 4.9% vacancy rate, just below Portland's ten-year historical average and below the national average. There were just 119,720 square feet in new deliveries during the quarter. Net absorption for the area was 101,193 square feet.

Land constraints remain a big challenge for new supply in the Portland metro area. Flat developable parcels with good access to major highway and freeway corridors are most in-demand, but few lots are readily developable. As a result, speculative development construction has leveled off in the Portland metro area despite strong demand. Developers continue to look beyond the Portland metro area, especially for large-scale fulfillment centers where transportation access is readily available. One of the year's biggest headlines was Amazon's $27 million land purchase from Specht Development in Woodburn, Oregon. Amazon plans to build a headline-grabbing, five-story 3.84 million square foot fulfillment center by 2023.

RENTS

Rents have continued the upward trend of the last decade. Average market rents during the second quarter hit $10/square foot for the first time in market history. Final mile spaces near large populations remain in high demand. With limited space expected to come onto the market, competition for space is expected to grow.

Leasing activity improved in the second quarter of 2021. Kidder Mathews reported a 37.5% annual increase in leasing activity, bringing the second quarter total to 2.59 million square feet. The growth in leasing activity is an encouraging sign for the economy. Market reports from

		Trend
Vacancy	4.9%	Same
Rent/SF	$10.00	Up
Sales/SF	$152	Up
Cap Rate	5.8%	Up
Net Absorption	206,968	

the various brokerage houses have forecasted vacancy rates to remain low and demonstrate the competitive and robust demand for industrial space. The pipeline of construction is heavily owner-occupied or built to suit. 72.7% is pre-leased. Limited new supply is expected to hold down vacancy rates and put upward pressure on rents.

SALES AND CAPITAL MARKETS

Sales volume has continued to set records in Portland's industrial segment. In 2019, industrial sales volume reached approximately $1.8 billion, an all-time high. Although the uncertainty of the pandemic disrupted 2020, there were still over $1 billion in sales. Sales volume for the second quarter of 2021 was approximately $270 million. Market sale price/square foot had steady growth, hitting $153/sf in the second quarter. Cap rates have compressed to 5.78%, dropping approximately 40 basis points since 2016 and 200 basis points since 2011.

05

COMMERCIAL MARKET ANALYSIS

Retail Market Analysis

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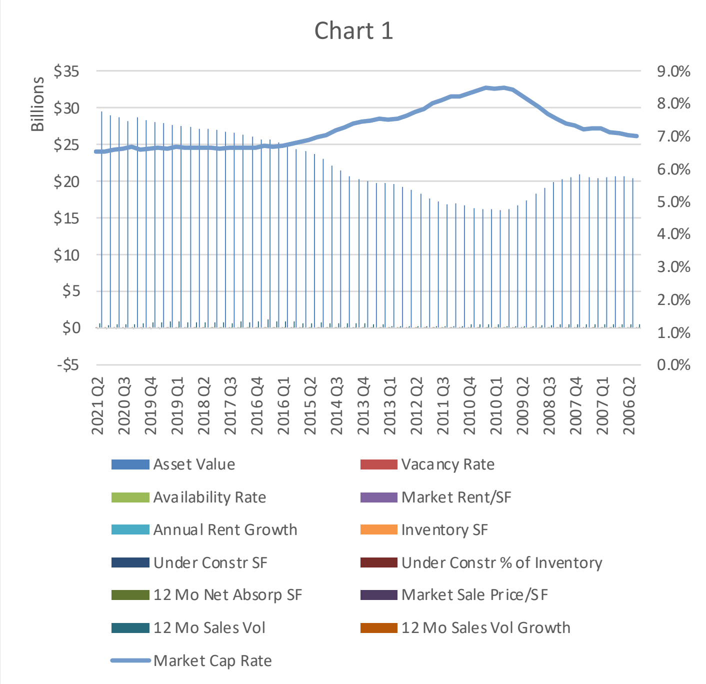
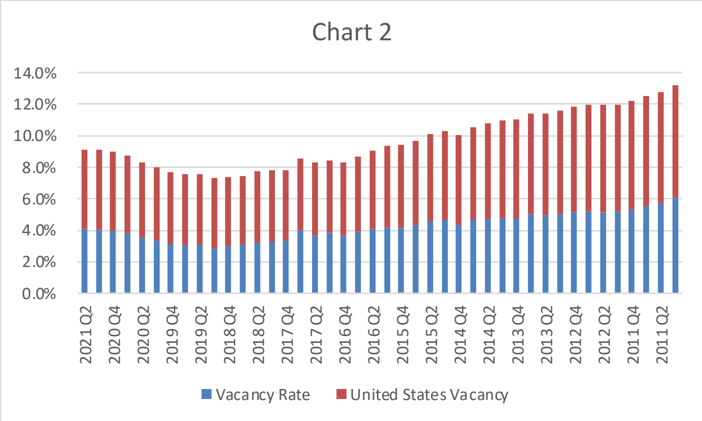
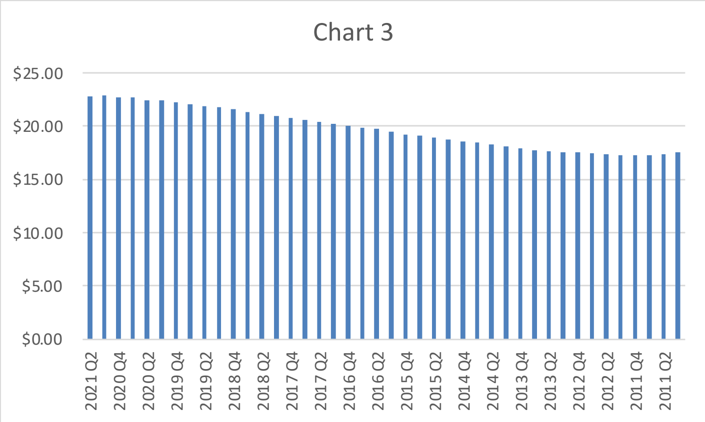






RETAIL

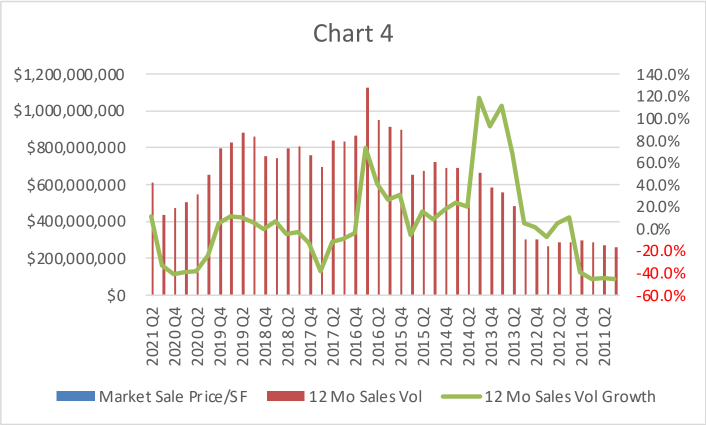
In general, retail has suffered throughout the pandemic. Shutdowns and restrictions halted in-person activities and hit leisure and hospitality the hardest. Other segments of the retail sector were forced to pivot or close shop. There has been an increase in businesses adopting some form of e-commerce, accelerating long-term trends.

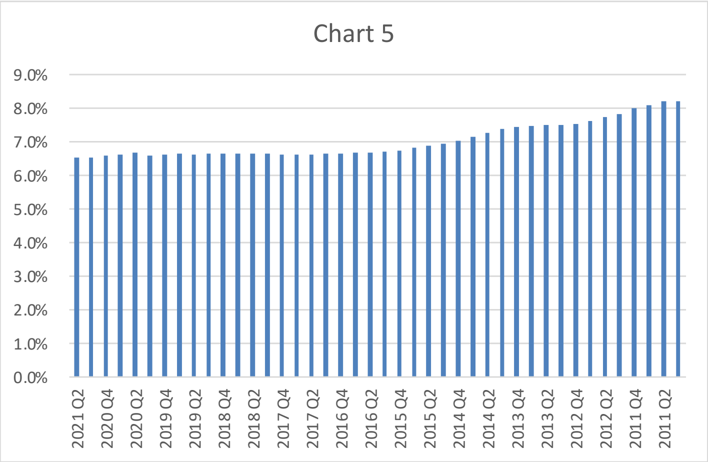
The government widely distributed COVID-19 vaccines during the second quarter, and governors lifted most restrictions. Thanks to a robust federal stimulus policy response, total incomes are higher than pre-pandemic levels. At the beginning of 2021, pent-up demand and consumers flushed full of cash were fueling a turnaround in the retail sector. However, despite the reopening, retail sales have stalled in the second quarter. Some of this could be attributed to supply chain disruptions, price surges, and worker shortages, but another lingering factor is the rise in COVID-19 infections due to the Delta variant. Businesses who have adapted their practices to delivering goods, whether online, quick-service, or hybrid store distribution, are better suited to survive the uncertainty. Leisure, hospitality, and other in-person retail will be intently monitoring the situation.

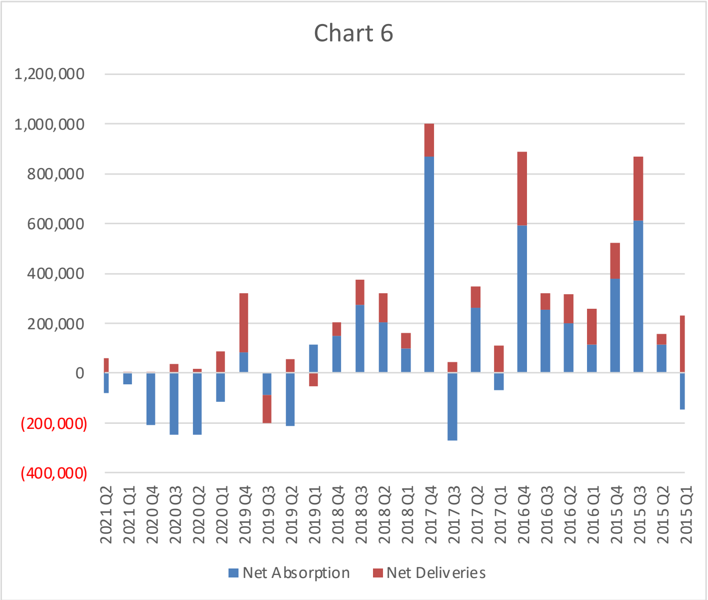
PORTLAND METRO

Oregon lifted its COVID-19 restrictions allowing in-person activity to resume on June 30th, 2021. Retail leasing activity is up for the fourth consecutive quarter, with over 500,000 square feet of space leased by the end of the second quarter. As retail activity regains strength, the geographic distribution of leasing trends are something to watch. Even before the pandemic, retail growth activity was occurring away from central business districts. Household and population growth in peripheral areas have created attractive areas to capture consumer spending. There is currently 718,933 square feet under construction in the greater Portland metro area, of which around 585,000 square feet is occurring in suburban submarkets (CoStar).

Retail in the central business district took a significant hit during the pandemic. Daytime populations in these areas plummeted as the virus forced employers to have their workers work from home. The reopening has begun, but it remains up in the air how employers will proceed with work location requirements for their employees. The emergence of the Delta variant







has delayed the reopening as well. Without daytime populations returning to pre-pandemic levels, downtown will remain a problematic investment. In the NAIOP webinar, *Where is The Portland Commercial Real Estate Market Going Post-Pandemic?* local panelists echoed the sentiment that this may represent a golden opportunity to reshape the suburbs and peripheral neighborhoods into inspiring places.

ABSORPTION

Net absorption was negative for the sixth consecutive quarter. The second quarter ended at negative -76,609 square feet, which relative to 2020 is an improvement. The minimal new deliveries and increase in lease rates have helped lower the negative absorption rate.

VACANCY

Vacancy rates ended at 4.1% in the second quarter, rising slightly from the previous quarter's 4.0%. Portland's relatively low volume of new supply has helped keep vacancy rates low and approximately 100 basis points below the national average. Compared to Portland's historical performance, vacancy rates are trending upward. In the first quarter of 2019, retail vacancy rates hit a ten-year low of 2.9%, but since then, the first quarters of 2020 and 2021 had vacancy rates at 3.3% and 4%, respectively.

Strip centers had the highest vacancy rate of all retail types at 6.5%, followed by neighborhood centers at 6.1%. Both categories typically report the highest vacancies in the Portland Market. Power centers and neighborhood centers have had the sharpest vacancy rate increases over the past year. Higher vacancy rates are expected considering the pandemic, and the reopening will be an interesting test for retailers.

RENTS

Average rents began to recover in the second half of 2020, but in 2021 rent gains were starting to level off. Average rents were $22.81/square foot in the second quarter, a slight decrease from last quarter's $22.86 rate. Analysts are projecting minimal rent growth over the next few quarters as concerns over Delta variant raise uncertainty for the sector overall.

		Trend
Vacancy	4.1%	Up
Rent/SF	$22.81	Down
Sales/SF	$236	Same
Cap Rate	6.5%	Same
Net Absorption	(78,109)	

SALES

Overall investment activity in retail has trailed all other categories of real estate. Long-term e-commerce trends remain a concern for investors and the pandemic has undoubtedly added an element of skepticism. Sales volume in 2020 was the lowest since 2012. Nonetheless, the second quarter of 2021 was the best quarter since early 2019.

One area that continues to spark interest for investors is grocery store anchored centers. In the first quarter of 2020, three Safeways were sold to private investors in three separate transactions. In the third quarter of 2020, an Albertsons in Lake Oswego sold at a 5% cap rate. A Walgreens in Sandy, Oregon sold at a 6.3% cap rate in 2020 as well. One of the notable deals in the second quarter of 2021 was the $487 million sale of a 28-property portfolio of Fred Meyer grocery stores across Oregon, Washington, Idaho, and Alaska. The buyer was Florida-based Benderson Development which has a national portfolio of over 120 grocery-anchored centers. The second quarter of 2021 had the most sales volume since the first quarter of 2019, and grocery store sales accounted for approximately half of that volume.

06

HOUSING MARKET

Multi-Family Residential Report

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Portland Metro area in this report is defined as Vancouver, Beaverton, Gresham, Hillsboro, Milwaukie, Lake Oswego, Oregon City, Fairview, Wood Village, Troutdale, Tualatin, Tigard, West Linn, Battle Ground, Camas and Washougal.

INTRO

The Portland metro multi-family market has shown a robust recovery over the past six months. Vacancies are forecasted to decline over the next three years, returning to 2013- 2016 levels. Multi-family year over year rents are forecasted to increase around 4.0% to 9.0% over the next three years. The number of units under construction has dropped from a high of around 13,000 in 2018 to 4,800 for 2021, with future development levels uncertain. Portland's metro population growth is forecasted to increase and return to 2012-2013 levels in the coming years.

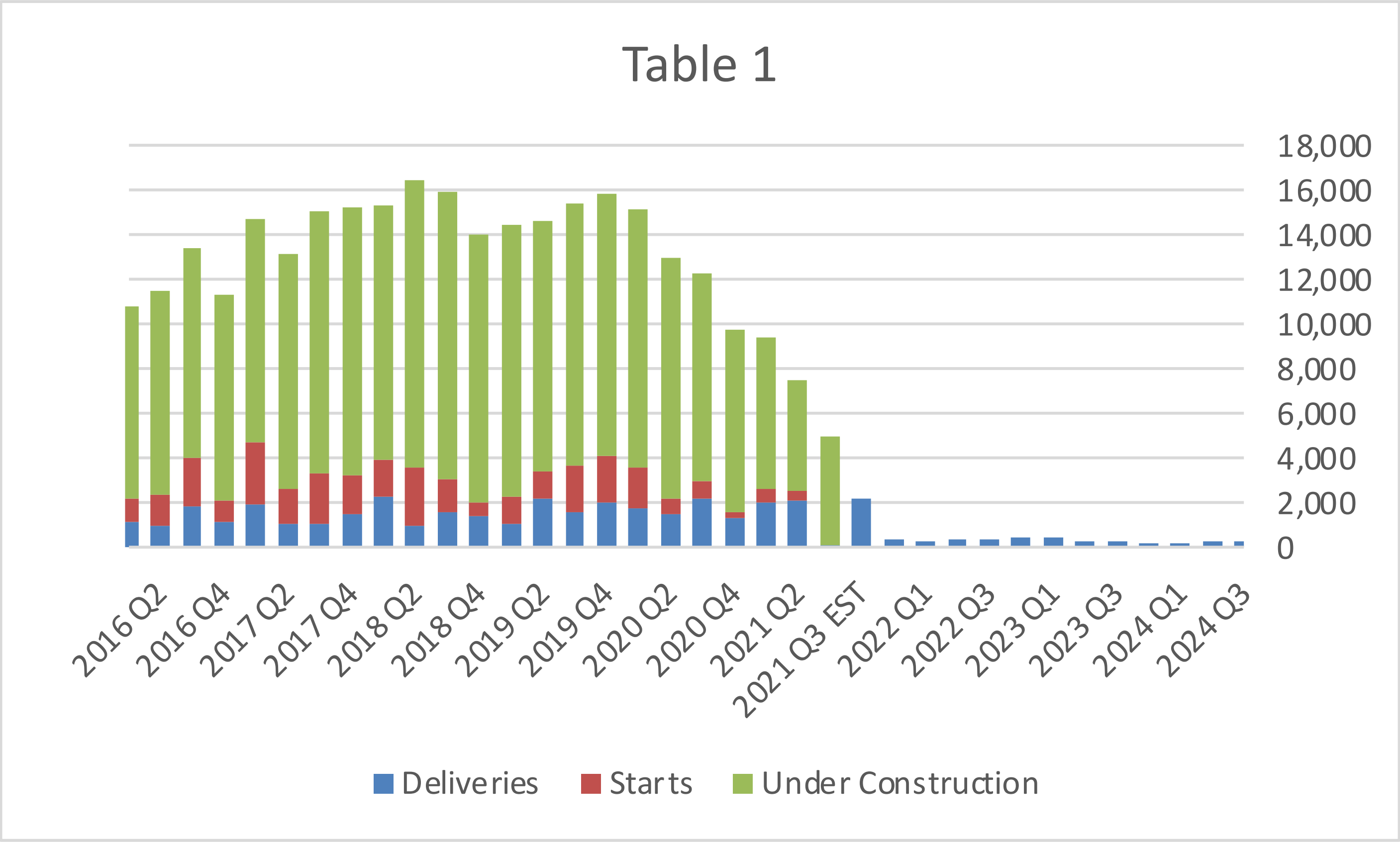
While we are still amid the pandemic, investors are confident that the floor is no longer falling and recovery, while slow, has begun. Children will be returning to school full-time this year, although mask and vaccination policies are still being figured out. Challenges are still upcoming as employers strategize solutions for having employees safely return to work. It is expected that there will be some degree of flexibility for remote working as high-risk individuals will need to continue to keep social distance from others, while the rise of Delta variant cases will also need to be closely monitored. Unemployment is steadily dropping as the hardest hit employers such as restaurants, entertainment venues, and retailers are opening back up.

Portland continues to lead the west coast in affordability which is driving new demand from more expensive metro areas like Seattle, Los Angeles, and San Francisco. Meanwhile, existing renters in the market shifted from the downtown/CBD submarket to the suburban submarkets, driving absorption and rent in those areas. The downtown/CBD recovery is the slowest in the metro area as the heart of the city was on full display nationally with both positive protests and negative riots.

However, consumers are once again out eating and shopping downtown. As employers in the downtown/CBD submarket continue to reopen their doors, increased foot traffic will decrease crime, and we should see the plywood in windows start to come down. Overall, Portland's economy and multi-family market was able to weather the pandemic and will continue to be a desirable destination for future investment.

SUPPLY AND PERMITTING

The Portland metropolitan area's supply continued to grow, adding 7,000 new units in 2020, with another 4,800 units recently completed or being delivered in 2021 (shown in Table 1). The

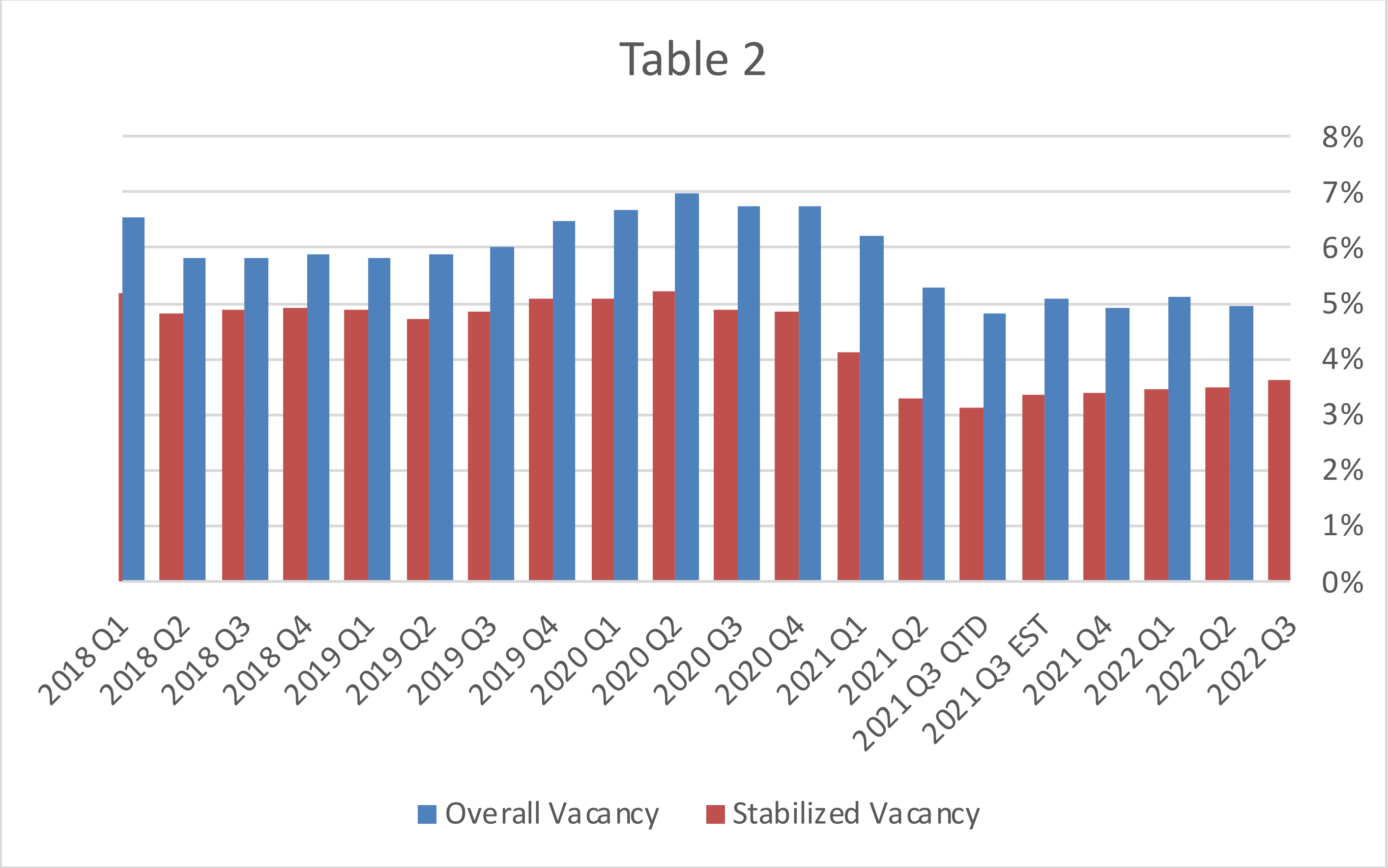


pipeline of multi-family units peaked in 2018 with 13,000 units delivered. As we approach the end of 2021, we are starting to get a better picture of deliveries for 2022. While deliveries continue to see delays due to supply chain issues, it is expected that at least 2,700 units will be added.

One highlighted project is the Alta Art Tower which expects to be delivered in early 2022. This 21-story tower expects to add 314 units to the urban core. However, it's important to note that it is the suburban submarkets that are really driving new supply. For example, the Vancouver submarket added 1,100 new units to the metropolitan market, accounting for 23% of total new inventory in the Portland metropolitan area. The suburban submarkets of Lake Oswego, Beaverton, Hillsboro and Vancouver are seeing 2% rent growth during the pandemic, indicative of the movement out of the downtown area.

The largest project underway in the metro area is the 352-unit AmberGlen South in Hillsboro, owned by American Capital Group and Artemis Real Estate Partners. Through April 2021, the largest project delivered was Zera at Reed's Crossing, a 324-unit lifestyle community in Hillsboro built by Holland Partners.

For urban living, northwest and southeast Portland have been the most desirable markets. Absorption remains high here compared to other parts of the urban core. We are still in a "wait and see" approach when anticipating future new supply. While some renters moved out to the suburbs, others are moving in from neighboring metropolises such as Seattle, San Francisco, and Los Angeles.

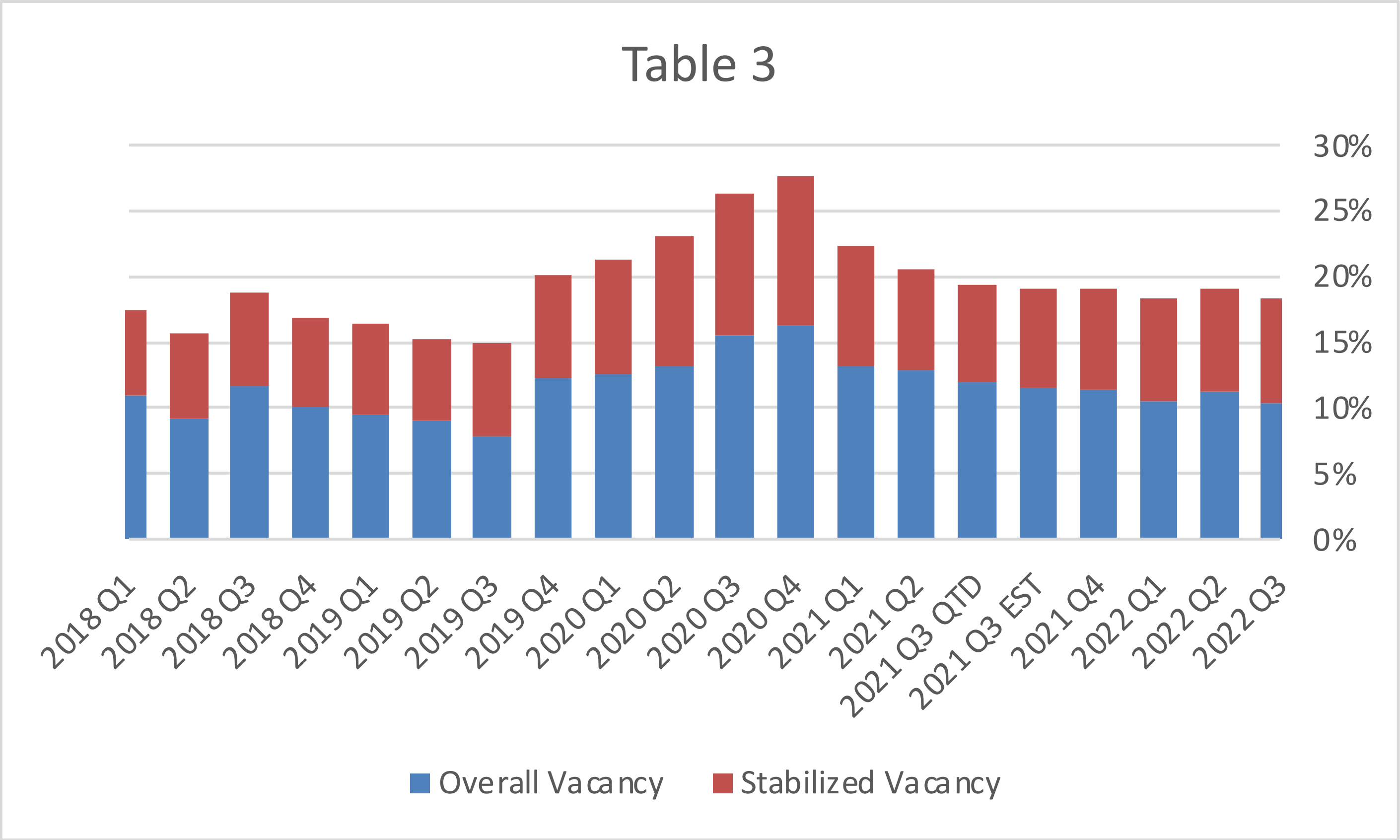


DEMAND AND ABSORPTION

Vacancy rates in the Portland metropolitan area decreased marginally during the second and third quarters, from 5.27% to 4.81% (shown in Table 2). Much uncertainty looms as the rent moratorium for Multnomah County expired on June 30th. Real time data is not accessible yet, but there are millions of Americans that are behind on their rent, and landlords aren't receiving mortgage relief to offset those balances. Renters face evictions and loss of their home while landlords face loss of their property if they are unable to make their mortgage payments.

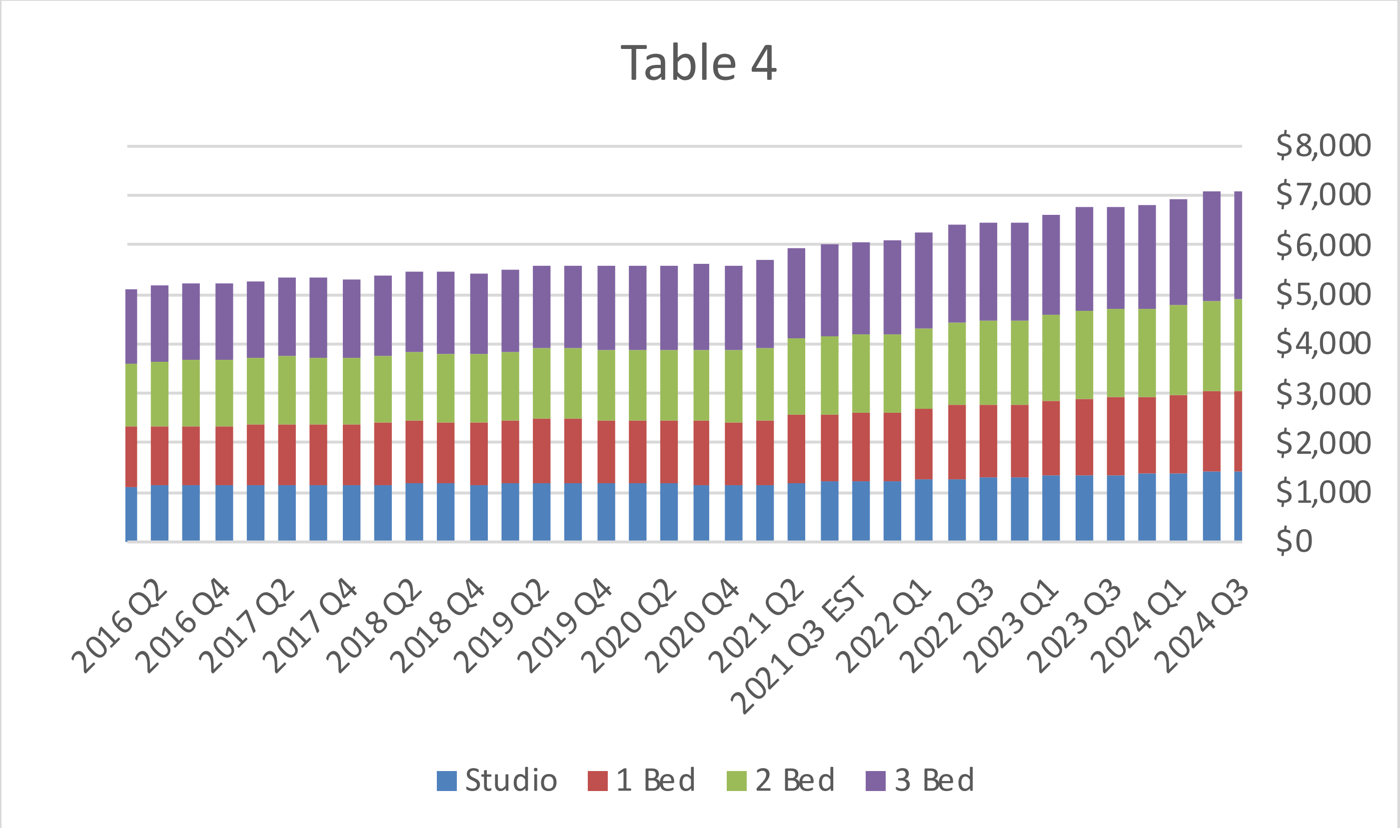
Those who were able to maintain income throughout the pandemic are prolonging the trend of moving to either larger units or units with more outdoor space.

Many renters are upgrading their units to a larger space or relocating to the suburbs because the difficulties of working from home have led to shifting preferences. This is evident as the downtown/CBD submarket currently boasts the highest vacancy rate in the market at 11.6% (shown in Table 3).



Tenants have had to learn to share their remote working space with spouses, roommates, and children, and this has proven to be a difficult test for some. For now, the start of this upcoming school year approaches, and children are heading back to school full-time. Most employers are beginning to put processes in place to get employees back to the office, though this could slow as the rise in Delta variant cases continues.

Rents are up overall in the market, showing a healthy recovery as units continue to be absorbed. Beaverton (190 units), Lake Oswego (118 units), and Vancouver (743 units) all set submarket records for absorption during the second quarter. It is evident that suburban markets have high absorption, and as long as the pandemic persists, we expect that renters will continue to shift their preferences towards suburban markets. The metropolitan area as a whole has weathered the storm better than most thanks to the robust job growth that occurred over the last decade.



RATES AND COSTS

The pandemic has been volatile to say the least, but as of the third quarter of 2021, average rent levels in Portland are rising fast. After considerable losses in the early and later months of the pandemic, a strong spring and early summer leasing season has helped to boost the market. Market rent metro-wide is currently $1,490 per month (shown in Table 4), reflecting year to year growth of 7.8%. As discussed previously, renter preferences have shifted as the importance of being downtown diminished, and Portland's suburban communities have posted the strongest rent growth. In Lake Oswego, Vancouver, and Beaverton, rents grew by more than 2% in 2020 despite the economic disruption. In contrast, rents were falling in the pricey, downtown submarkets that are coming off a wave of new construction. Rents fell by more than 6% last year in downtown Portland, and more than 5% in northwest Portland. However, the bottom was reached in late 2020 for these submarkets, as the first and second quarter of 2021 gave way to visible rent growth.

Construction costs continue to remain higher than national averages. According to Rider, Levett, and Bucknall's construction report, Portland's metropolitan area is seeing construction costs that are 5.7% higher than they were in 2020. Construction employment was a major issue in 2020 as 10% of the pool was not working, that number has dropped to 8.1% as of the first quarter of 2021. While labor is coming back, bottlenecks in the supply chain, volatile pricing, and extended permitting periods continue to disrupt the industry. This indicates that demand is driving cost increases while supply is struggling to keep up. The Portland metro area was ranked third in highest construction cost change behind New York City metro and Washington DC metro. Despite the rise in construction costs, developers are continuing to move forward with their projects, and all signs indicate that the Portland metro area remains atop the west coast in affordability.

SALES ACTIVITY

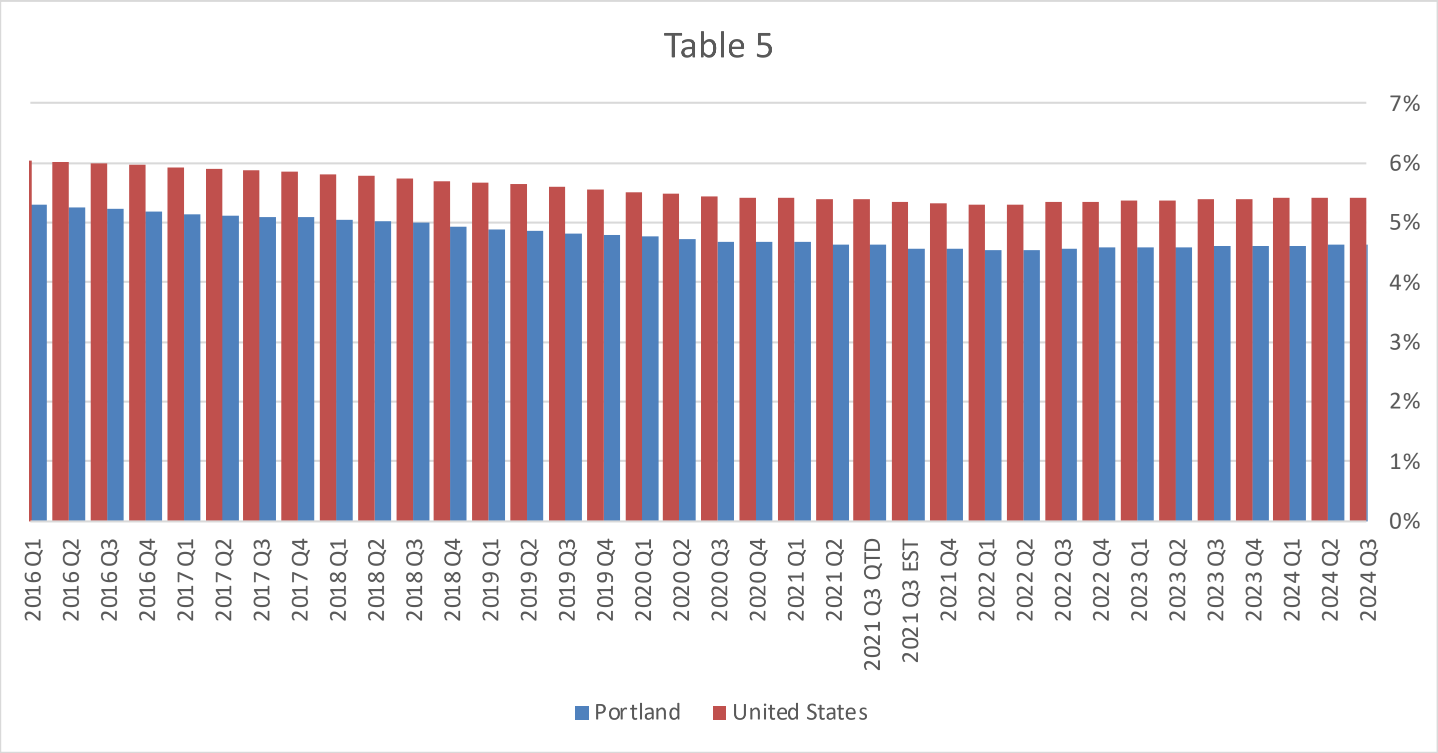
Over the past few years, Portland has started to attract a wider variety of investors. The multi-family cap rates have further tightened, trending well below 5% over the past few years. These are signals of a strong market for investment. Predictably, overall volume fell in 2020 as many investors waited for the market to settle in the wake of the pandemic. However, sales volume in 2020 still eclipsed 2017 figures, and several major deals at the end of the year and the beginning of 2021 provided evidence that Portland's strong performance during the slowdown is drawing investor interest from around the country.

In January 2021, real estate conglomerate the Blackstone Group purchased The Passage Apartments as part of a portfolio purchase. The 104-unit complex located in Vancouver sold for $23.2 million, or $223,077 per unit. The property was built in 1991 and renovated in 2015. The seller was TruAmerica Multifamily.

In May 2021, Arc Central, a 230-unit, 4-star mid-rise complex sold to St. Regis Properties, a California-based investor for $77 million at a 4.1% cap rate. At closing, the apartments were 87% occupied, and the $335,000 per unit price was well above the market average. The facility is well-located, within easy walking distance to the Beaverton Central MAX light rail station. Built in 2019, the mixed-use property contains nearly 6,000 SF of retail space on the ground floor.

In June 2021, new to market The Calida Group purchased the Autumn Grove apartments located in Vancouver. This 148-unit complex of one- and two-bedroom apartments was completed in 2020. It was approximately 10% vacant at the time of sale. RGNL disposed of this asset for $39.5 million, or $266,892 per unit. Lastly, in July of 2021, one of the higher profile sales in the metro was the Sky3 Place, a 196-unit complex located in the downtown/CBD submarket close to the Portland State University campus. It sold for $71 million, or $362,245 per unit and was 9.6% vacant at time of sale. This property was completed in May 2017, and the buyer was Scottsdale, Arizona based The Wolff Group.

These four recent sales highlight out of state investors' interest in the Portland market, as it weathered the COVID-19 storm well, and may be better positioned than most metro areas on the west coast as normal life resumes.



LOOKING AHEAD

In general, it is believed that despite the rise in Delta variant cases, the worst of the virus and the need for any further lockdowns are behind us. While we are still slowly recovering, we are seeing encouraging signs of improvement, and the multi-family sector has mostly recovered its market rent and vacancy losses.

One major question that looms is the effect that the end of the eviction moratorium will have on the current state of the market. There are programs in place to help renters who have fallen behind catch up, but money has been slow getting to them. Also, landlords who fell behind on mortgage payments are at risk of foreclosures.

Rental rates nationwide have returned to pre-pandemic levels. When looking closer at the Portland metro market, there has been active absorption of suburban units as renters have left the downtown/ CBD area in pursuit of larger units. In addition, there has been an influx of new demand from renters moving from other more expensive metro areas as Portland remains one of the more affordable west coast options. This shift from urban to suburban has helped give rise to great year over year rent growth for property owners in those markets. One would expect as the downtown/CBD offices reopen and start rehiring again, these buildings will once again be an attractive destination for those who wish to be close to work and have walkable amenities.

In March of 2021, the State of Oregon Economic Development Department published a report that detailed a strong economic response for this year. The report states, "As the pandemic continues to wane, pent-up demand will be unleashed, fueling growth in the months ahead. The shift in spending out of physical goods and back into labor-intensive, in-person consumer services will raise employment significantly. While the labor market remains in a deep hole today, a bit more than half of these lost jobs will be regained in 2021." The prediction is that Oregon's economy will return to full employment by early 2023.

The Portland metro's multifamily sector should continue to see year over year rent growth, strong absorption, and new demand. While growth will likely not be as explosive as in the 2010s, it should remain steady in the short- to medium-term.

RESOURCES

1. Costar Portland Multifamily Report Q3 2021
2. Yardi Matrix Portland Multifamily Summer Report 2021
3. Rider, Levett, & Bucknall Construction Cost Report Q3 2021
4. Norris & Stevens Spring/Summer 2021 Rent Survey Data

07

HOUSING INSIGHTS

Housing Production

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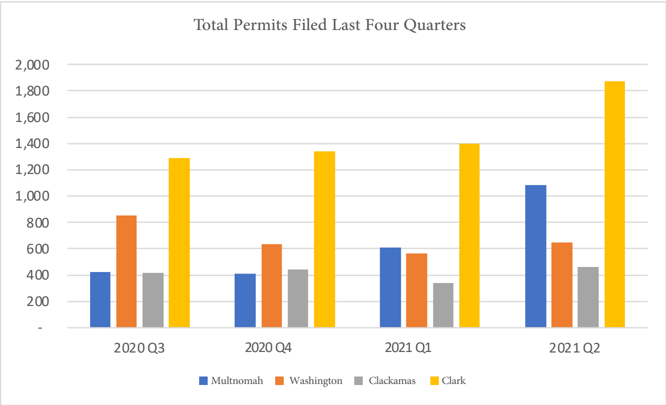


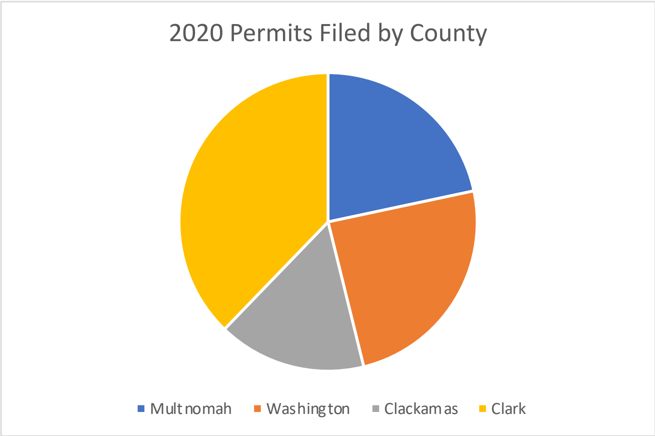
OVERALL OUTLOOK: NATION'S HOUSING CRISIS CONTINUES TO WORSEN

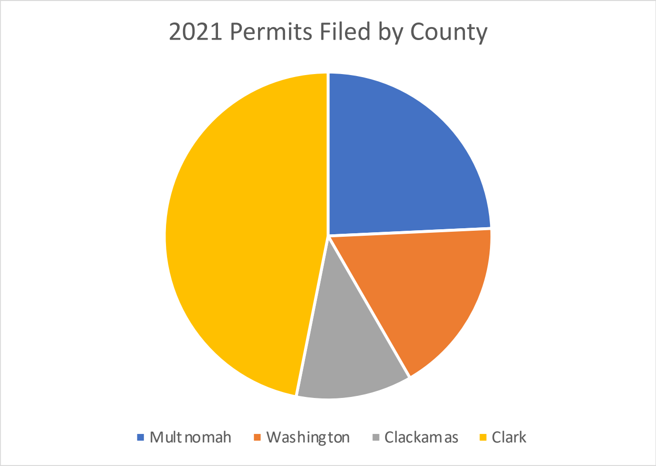
In both the rental and for sale markets, the effects of our nation's housing shortage are felt across the market. As of June 2021, the National Association of Realtors (NAR) reported an historic 23.4% year over year increase for national home prices, with the median existing home selling for a record high of $363,300. In Oregon, Zillow reported median home prices increased by 17.6% while Rentcafe reported rents increased by 5.0%. In the Portland metro area, home prices increased by 15.6% and rents by 4.0%. The sustained imbalance between supply and demand means price are projected to continue going up.

In 2020, a prevailing view was that these surging prices were due to the reemergence of suburban/exurban markets and consumers' desire for more space amid the pandemic. This was caused by many jobs transitioning to work-from home, as well as historically low interest rates intended to bolster the economy during pandemic recovery. These theories had optimists hoping that our nation's housing was in a bubble, likely to deflate once we return to post-pandemic normalcy.

Contrary to this view, there are other factors that paint a bleaker picture. According to a new NAR report, "1.225 million new housing units have been built on average each year from 2001-2020, down from an annual average of 1.5 million new units built from 1968-2000. This 5.5-million-unit deficit includes about 2 million single-family homes, 1.1 million units in buildings with two to four units, and 2.4 million units in buildings of at least five units." This shortage accounts for single-family, multi-family, market rate, and affordable housing production across the board. Experts believe it will take over a decade of higher-than-average production to close a gap that large.

Compounding this issue is the 72.2 million millennials that are either approaching or have already exceeded the median first-time home buyer age of 33. Analysis from Marcus & Millichap predicts 4.6 million new millennial homebuyers will be attempting to enter the market in the next five years. Additionally, many of the 34% of young adults 18 to 34 who currently live with their families are expected to move post-pandemic, indicating a need for another 4 million new households over the next two years. Millennials, a generation who have experienced many roadblocks to homeownership, are continually growing more frustrated with the housing market.





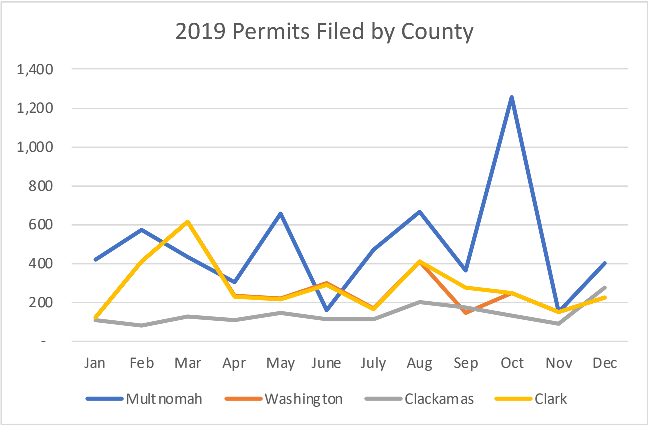
Several supply-side constraints have also exacerbated underproduction in the last decade, many of which were heightened by the pandemic. The National Association of Homebuilders (NAHB) CEO Jerry Howard testified before Congress in July, citing a "lack of skilled labor and buildable lots, tight lending conditions, shortages and rapidly rising prices for building materials, and excessive regulatory burdens on homebuilders that have added approximately 25% to the cost of a single-family home and 33% to a multi-family unit."

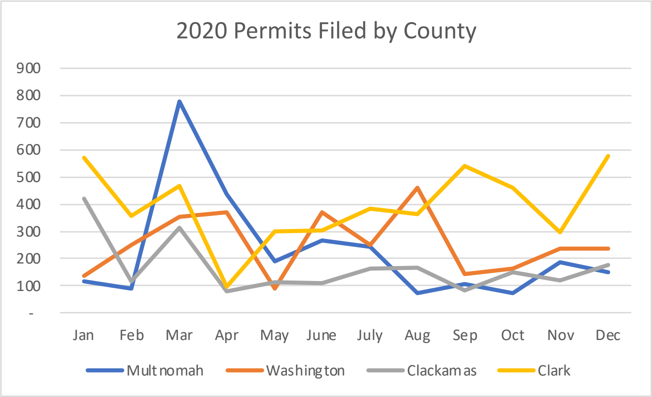
Solutions currently under Congressional consideration include: 1) correcting building material supply chain issues by removing tariffs on lumber, 2) passing H.R. 2573, the Affordable Housing Credit Improvement Act, which will finance 2 million multi-family units by increasing credits allocated to each state and expanding the amount of affordable housing projects that are funded using private activity bonds, and 3) replacing the federal mortgage interest deduction in favor of a permanent home tax credit that benefits lower-middle income earners. So far, no legislation has been passed.

LOCAL HOUSING PRODUCTION

Amid the backdrop of a national housing crisis, the Portland metro area faces an uphill battle. A 2018 report conducted by Up for Growth and EcoNorthwest revealed that from 2005 to 2015, housing was underproduced by approximately 155,000 units in Oregon. That same study suggests that if Oregon's pipeline supplemented those missing 155,000 units over the next 20 years, housing prices will be 5.5% less than they would be without the additional production. To achieve more housing in Oregon, Up for Growth advocates for "Smart Growth" principals such as encouraging development in high density cores and promoting a blend of housing types, especially 2-to-5-unit properties (known as "missing middle housing") in proximity to existing infrastructure and public transportation.

Unfortunately, pandemic related housing trends are putting Smart Growth principals further out of reach in the metropolitan area. In 2020, a total of 12,505 single-family and multi-family permits were filed in Multnomah, Washington, Clackamas, and Clark County, an 11.6% decrease from 2019. As cited earlier, many attribute this decrease to pandemic related setbacks. Projects were stalled, permitting timelines were extended, skilled labor was in short supply, and the cost to acquire building materials became unfeasible.





Changes in consumer behavior also impacted the development landscape in 2020. For the first time since 2004, Clark County exceeded Multnomah County in permits filed, accounting for 38% of the four-county total, followed by Washington (24%), Multnomah (22%), and Clackamas (16%). Despite, or perhaps because of the pandemic, development in Vancouver, WA exploded in 2020 as residents fled the urban cores for more spacious and affordable peripheries. From 2019 to 2020, Clark County's permits filed increased by an impressive 40.2%, and Clackamas increased by 20.5%. Washington suffered a modest decrease of only 5.9%. Multnomah, however, decreased in production by 53.7%. Right now, the million-dollar question is: are these trends towards the suburbs/exurbs here to stay, or will urban spaces make a comeback? Considering how unpredictable the pandemic has been, it is still far too early to tell.

Trends that were established in 2020 are persisting into 2021. Clark and Washington Counties are still developing at the fastest rate, but that is for total single-family and multi-family. Multi-family units in the pipeline have been steadily rebounding in Multnomah, up 36.8% since 2020 Q2, but still lagging behind Clark by 20.7%. Experts differ as to why development in Portland is winding down. Michael Wilkerson, senior economist with EcoNorthwest told OregonLive in March, "I don't think [inclusionary zoning and limits on rent increases] were huge movers of the market, but when you add both of those two things on… Then, you get the pandemic, the recession, the reputational damage suffered in Portland, and I think those accelerated those trends more."

CONCLUSION

As troubling national trends are reflected in Portland's housing market, increasing housing production will be critical to hedge against future volatility. Should the region continue to underproduce, it could put further upward pressure on housing prices and rents.

The City of Portland is currently planning for 135,000 new households by 2035 and will need to find ways to reduce the cost of delivery to meet these goals. Affordability challenges, experienced by both homebuilders and consumers, are continuing to push development farther from high density cores, and are simultaneously making Smart Growth goals even harder to actualize.

08

HOUSING MARKET

The Challenge of Oregon's Rent Relief Programs

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As the global pandemic persists, much uncertainty remains regarding the financial fate of landlords and tenants. The urgency of controlling the virus, preventing eviction-related infections, and the contentious US political situation has left us with an awkward mismatch of programs for rental assistance. Over recent months, many newly-created relief funds, congressional actions, emergency declarations, and new laws at both the federal and state levels have been hastily established to provide economic security and avoid financial collapse.

Though several distinct funds apportioning hundreds of millions of dollars have since been established to specifically aid tenants and landlords in Oregon, the rapid and constant change in program requirements have left some participants confused and scrambling to meet deadlines. Complicated application portals and forms and a perceived shortage of available staff have challenged tenants from correctly submitting applications, slowing down the ability to get relief funds into the hands of those who need them. In response to the slowdown, the Oregon Housing and Community Services (OHCS) has added an additional 63 staff and introduced a third party vendor to reduce delays in the tri-county area.

This article will discuss the evolution of the various relief programs in the state of Oregon, including changes aimed to provide additional tenant protections and increase landlord access to assistance funds. Thus far, the slow distribution of these programs and the looming expiration of federal and state eviction moratoriums have created additional pressure for many tenants. On August 3, 2021 the Center For Disease Control (CDC) extended the existing federal moratorium through October 3, 2021, which should allow tenants additional breathing room for the time being. However, the most recent Multifamily NW Monthly Rent Survey (June 2021) found that 12% of households in Oregon were unable to pay their rent by the 15th of the month, an improvement from the 13.2% reported in May 2021, but alarming nonetheless.

OREGON'S RENT RELIEF PROGRAMS

Oregon has two major funds for rent relief, with a combined total of more than $400 million in funding. Under the CARES Act of March 2020, approximately $204 million of Federal funds were made available to Oregon to help qualified renters meet their rent obligations. OHCS implemented this with the creation of the Oregon Emergency Rental Assistance Program (OERAP) overseen by OHCS. An additional amount of $76 million was also allocated to the City of Portland, and several surrounding counties. The second major source of relief funding was established in December 2020 at the state level with the passing of House Bill 4401. This created the Landlord Compensation Fund (LCF) in the amount of $150 million. The key difference in these programs is the party responsible for submitting an application. For the Federal program, tenants must apply for assistance themselves, while the state program directs landlords to apply for themselves. The two programs cannot be used simultaneously in a manner that would overlap the funds received, and participants are recommended to choose just one program. Several smaller county-wide and additional local programs also exist, which we will discuss below.

OREGON EMERGENCY RENTAL ASSISTANCE PROGRAM (OERAP)

The processing of applications to the federally funded OERAP has been very slow. As of August 4, 2021, OHCS reported that 25,000 households have requested $183 million in funds, yet only 1,290 have actually been paid an amount just less than $8 million – an abysmal 4.37% rate of distribution. When funds are distributed, OHCS makes a transfer to the landlord, who sends the approved tenants a notice regarding the rent paid on their behalf. If a landlord refuses to participate in the program, tenants are able to receive their rent directly (with some restrictions) in order to remedy their debt. The program itself is designed to provide up to 12 months of assistance for rental obligations from March 13, 2020 through the present, as well as a possibility of three months of future rent under certain conditions.

The official website for the OERAP states that the program is designed to serve renter households that have incomes less than 80% of the Area Median Income (which falls between roughly $51,500 - $77,350 for a family of four, depending on the county. Those households must meet the following conditions:

• Individuals in the household must have either qualified for unemployment benefits, experienced a reduction in household income, incurred significant costs, or experienced other financial hardship due to the coronavirus outbreak; and

• Individuals in the household must demonstrate a risk of experiencing homelessness or housing instability evidenced by a past due utility or rent notice.

Although the ambiguity presented in these requirements is helpful for tenants, the unclear definition of "financial hardship" has left some landlords wondering whether or not their tenants are being completely honest about their ability to come up with rent payments when they know government assistance is available. This potential dynamic, combined with the lag in assistance payment delivery, is shifting the financial burden to some landlords. This result is even more unfair when tenants may actually have the means to catch themselves up on rent without the added assistance.

LANDLORD COMPENSATION FUND (LCF)

The creation of the $150 million Landlord Compensation Fund (LCF) through House Bill 4401 at the end of 2020 was designed to avoid some of the administrative pitfalls suffered by the OERAP fund. Landlords can initiate the application process directly. However, the LCF program is not without its complexities. First, in order to qualify, a landlord must receive a signed declaration of hardship from each tenant affected. In the months since its initial funding, the LCF has seen multiple iterations and changes. In the earliest round of application and distribution, OHCS (who also ultimately oversees this fund) reported that only $40 million of the expected $50 million was claimed.

Under the initial version of the law, landlords were to receive repayment for 80% of the outstanding unpaid rent by tenants accrued between April 1, 2020 and June 30, 2021 - the day the statewide eviction moratorium was slated to end. The remaining 20% was to be forgiven and uncollectable from tenants, even in the case that they could indeed produce the rent after the fact. Landlord applications, which are approved by OHCS based on number of units (less units being favored) and percentage of unpaid debt, are then sent to the corresponding local Public Housing Authority (PHA), who is charged with distributing the funds directly to landlords, and notifying tenants of the rent paid on their behalf.

During the second round of funding, an additional $45 million was requested by landlords for a total of $85 million in relief funds. In partial response to the sluggish disbursement of statewide funds, the legislature passed Senate Bill 278 in June, 2021. This legislation added incentives to help increase the amount of funds that could be distributed. Under this revised law, landlords' reimbursement amount was increased from 80% to 100% of unpaid rent during the accrual period mentioned above, with a retrospective and automatic refund of the additional 20% to each landlord who previously applied under the initial rules.

Additionally, the bill expanded the collectability of unpaid rents to include pet rent and garage rent, and removed the requirement for OHCS to "score" each landlord before sending them to a local PHA. In addition, a new source of grant money was created to reward landlords who have not proceeded with an allowed eviction process. This new fund was designed to incentivize landlords to bear the burden just a while longer in order to prevent tenants from ending up on the street. To further speed things up, the monthly rounds for distribution were also reduced to a "weekly-rolling basis". Landlord applications to round three for the LCF closed June 23, 2021, with a potential $65 million dollars remaining to be allocated.

OREGON SENATE BILL 282

In addition to Senate Bill 278, another bill – Senate Bill 282 – was passed in May, 2021, to provide an extension of the eviction process grace period for renters who owe past-due rent through February 28, 2022. This extension became effective July 1, 2021 for all renters regardless of whether they submitted a declaration of financial hardship, and protects them from negative scrutiny regarding rent accrued between April 1, 2020 and June 30, 2021.

Commencing July 1, 2021, current rent is now due and payable for all renters as required in their lease agreements. The extension granted by the bill only applies to those who have the prior unpaid rent. This bill was also intended to protect tenants' credit from being negatively affected if they have unpaid rent from that accrual period. Landlords are now lawfully required to disregard any unpaid balances from the accrual period when accepting new rental applications, and current landlords cannot charge late fees on the unpaid rent unless it still remains after the February 28, 2022 expiration. Tenants are not being forgiven of any rent due, and the purpose of the bill is to allow them time to gather funds through the various relief programs, and potentially find new housing without running into additional credit issues.

ADDITIONAL COUNTY AND LOCAL RELIEF PROGRAMS

At the municipal level, several additional programs provide rental assistance in the Portland Metropolitan Area. The City of Portland was allocated funds under the CARES Act, and subsequently created the Portland COVID-19 Household Assistance Program (CVHAP) which issued one-time preloaded $500 bank cards to qualifying applicants in the early stages of the pandemic. Additionally, the Portland Housing Bureau, the Joint Office of Homeless Services, Multnomah County's Department of County Human Services, and Home Forward (Multnomah County's public housing authority) teamed up to provide $25 million of rent assistance through the COVID-19 Rent Relief Program (CVRRP).

In Washington County, all CARES funds have been exhausted as of August 2021. However, additional funding in the amount of $116 million is being made available from the American Rescue Plan Act (ARPA) passed by Congress in March, 2021, which can be used for relief through 2024. Distribution details are unclear at this time, but additional funding through ARPA will also be allocated to the state and other neighboring counties.

EVICTION MORATORIUMS

Included within Senate Bill 278 is an extension of the statewide eviction moratoriums for tenants who complete an application for rent relief funds. The extension will begin once the landlord receives the documentation, not necessarily the disbursement of funds. Specifically in Multnomah County, Ordinance 1296 was passed July 8, 2021 to extend this 60-day grace period to 90-days for those who live within the county. As mentioned previously, the federal CDC-mandated moratorium was recently extended to October 3, 2021.

CURRENT ISSUES AND DYNAMICS

The pandemic hasn't spared anyone - be it landlord, tenant, lender, or political leader. Through the quick passage of rent relief programs, it seems that we've avoided the worst outcomes. The sheer number of programs, requirements, applications, online portals, and amended laws isn't easy to keep up with, but they reflect the continuous adjustment to new circumstances.

Perhaps the worst aspect of the current system or rental relief payments is the strange dynamic that's been created between landlords and tenants. In order to safely navigate existing tenant privacy laws regarding health status, federally-funded programs in Oregon direct each tenant to apply individually, which can become an additional burden to an already struggling household. Those who require rental assistance likely also receive a combination of unemployment, SNAP benefits, TANF benefits, utility assistance and other benefits – each of which has its own distinct application rules, legal requirements, and application portals. In the age of COVID, local agency offices are often shuttered, forcing people to seek help via phone or online, navigating a maze of legal jargon and outdated documents.

The passage of Senate Bill 282 should help tenants avoid the fear of credit damage related to their unpaid rent, which even further discourages them from completing a rental assistance application. However, we've created a dilemma where a tenant's initiative is necessary to provide assistance their landlord. For those landlords who do manage to convince their tenants to apply - assuming they correctly fill out the application - the extremely slow processing and approval of applications forces landlords to finance unpaid rent for months at a time. For those who own many buildings and units, this cost differential could easily reach the millions of dollars – a tough pill to swallow for even the most well-capitalized landlords. As we continue to move towards the tail end of the pandemic, many landlords are holding their breath, just hoping to survive.

RESOURCES

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2. https://www.multifamilynw.org/news/cdc-moratorium-extension--october-3-2021
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09

HOUSING INSIGHTS

Missing Middle Housing

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INTRODUCTION

Across the United States, the housing crisis has been persistent and overwhelming for working class citizens for decades. The inability to secure affordable housing is an issue at the heart of the real estate industry and continues to impact millions of Americans, which results in a ripple effect in all sectors of the economy. The foundation of a healthy economy is the ability for citizens to afford living expenses and accrue disposable income to spend and invest. Wealth inequality and housing inequality have continuously widened the gap between Americans who can afford their living expenses and those who can't. The solution to this problem will require significant reform in multiple areas affecting personal finances, but a necessary starting point is the American housing market.

Key markets in the American housing industry suffer from significant lack of production due to multiple factors. Lack of available land, decrease in the capital supply, burdensome permitting fees and rising construction costs are some of the many factors which decrease supply and prevent the market from catching up to rising demand. The United States is currently experiencing a massive shift in demand as work-from-home, or WFH, becomes an increasingly permanent or semi-permanent part of the labor market. Commercial business districts, or CBD's, are experiencing a wave of migration of white collar employees escaping smaller multifamily units in search of larger homes to purchase rather than rent.

There are multiple methods to decrease average housing prices and rents but in the face of rising demand, the only true method of achieving market equilibrium must be focused on increasing supply. A common dilemma for renters trying to find affordable housing is the lack of housing inventory that is neither dense multifamily development and single family homes. People who cannot afford to purchase a home are forced to choose between market-rate housing and affordable housing and for those who do not qualify for affordable housing, the remaining options are often scarce, unaffordable and sometimes unappealing.

Inventory of market rate apartments are primarily large multifamily developments which can still demand high rents and are concentrated in CBD's, so the inventory in smaller cities and towns is limited. Developers target

CBD's for their investments as their target tenants are high-earning educated young professionals who seek amenities over space. However, there is a significant gap in available multifamily inventory for those seeking to live in suburban communities but cannot afford to purchase a home.

One category of housing which fits into this gap is middle housing. Middle housing is a real estate asset which consists of multifamily properties that are smaller, both vertically and horizontally, than traditional mid-rise or high-rise multifamily properties. Middle housing presents an opportunity for multifamily properties to absorb current demand in the multifamily demographic, lower costs and diversify housing options in smaller communities. The state of Oregon has passed House Bill 2001 which aims to increase development of middle housing by forcing smaller cities and towns to amend their zoning code to allow for middle-housing development in all residential zones. This paper will discuss the background of the Oregon housing market, analyze HB 2001 and how the development of middle income may have a powerful impact on the Oregon housing market.

OREGON HOUSING MARKET

The impact of WFH, paired with incredibly low interest rates tied to a 0-0.25% fed rate, created the perfect storm for historic housing price increases. Between June 2020 to June 2021, the national market saw homes increasing by over 17%. Oregon is on a familiar track, as reported by the Oregon Business Journal on June 21, 2021, which found startling increases in housing prices in both the Portland Metro area and smaller regions such as Bend. Oregon has become the 4th highest state in cost of living and 7th highest in cost of housing in the country, fueled by significant population growth without the necessary increasing in housing supply. Oregon is one of the fastest growing states in the nation, seeing a 10% increase in population between 2010 and 2020.

According to a 2021 report published by the National Low Income Housing Coalition, the average rent of a 2-bedroom home in Oregon is currently $1,307. In order to live in the average apartment affordably, meaning spending 30% or less of your monthly income, Oregon renters must earn $25.14 per hour at their jobs, yet the average renter wage in Oregon is $17.30. Renters

“Over the next 20 years, Oregon will need to build about 584,000 total new homes [in order to] overcome our state’s chronic underproduction of housing… To meet this need, Oregon’s housing developers would need to produce between 30,000 and 40,000 new homes every year. To put [this study’s] findings in context, over the past 5 years, [Oregon has] averaged just 20,000 units per year. [Oregon] would need to increase its total production of housing two-fold.”

(Oregon Housing and Community Services, EcoNW)

must work at least 65 hours per week at the average hourly pay to afford a one-bedroom home and 79 hours per week for a 2-bedroom home. There are 606,086 renters in the state of Oregon, which represents 38% of Oregon residents.

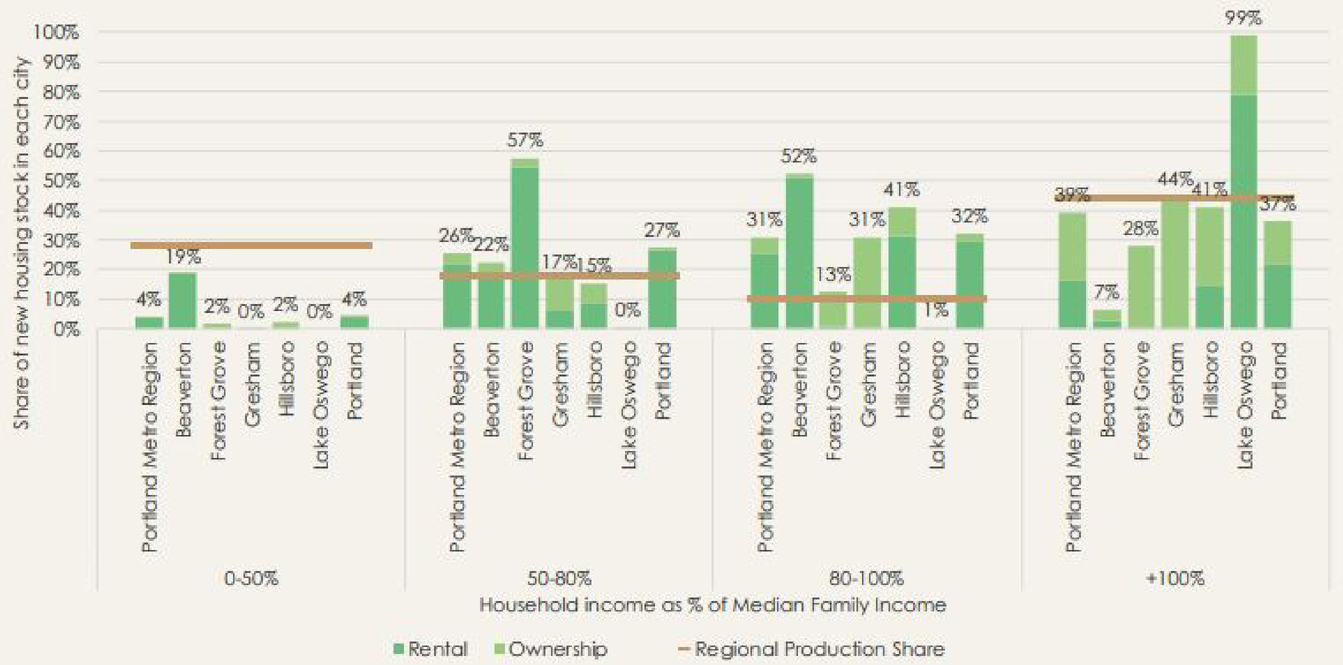
This problem is prominent in all parts of the state, however Portland is the destination of most people moving into Oregon, so the population increase is seen most dramatically there. A 2020 Bloomberg study predicted, “a projected 123,000 new households arriving in Portland by 2035.” A May 2021 report published by the Oregonian found that after seeing decreasing rental rates in 2020 as a result of residents leaving the Portland CBD and moving into the suburban areas, Portland rents increased 1.8% between March and April 2021. The median one-bedroom apartment now rents for $1,153 and two-bedroom for $1,344.

The extent of Oregon’s need for further development was highlighted in a study conducted by the Oregon Housing and Community Services and EcoNW and published in February 2021. This study found that, “over the next 20 years, Oregon will need to build about 584,000 total new homes [in order to] overcome our state’s chronic underproduction of housing… To meet this need, Oregon’s housing developers would need to produce between 30,000 and 40,000 new homes every year. To put [this study’s] findings in context, over the past 5 years, [Oregon has] averaged just 20,000 units per year. [Oregon] would need to increase its total production of housing two-fold.”

In addition to the standard issues regarding housing supply, one unique factor impacting the Oregon housing market is the series of wildfires that hit Oregon in 2020. According to the OHCS findings, “The 2020 wildfire season destroyed entire communities, resulting in the loss of 4,000 homes, nearly half of which were mobile homes providing housing that was affordable. As of mid-January 2021, over 1,000 people are still living in hotel rooms, in need of interim and permanent housing options.”

Oregon’s housing market is not just facing undersupply but demand not being for home prices that developers typically target.

Exhibit 6. New Housing Construction (2017-2019) by Affordability and Compared to Regional Production Share



SOURCE: ECONorthwest, based on data from Metro's Regional Land Information System and RHNA Findings

The above graph demonstrates the need for development at the mid to lower income brackets, however the new supply being added into the market is primarily focused on the high-income bracket, between 80% -100+ median family income. As the OHCS and EcoNW studies go on to state, "About one-third of all of the projected need (about 172,000 homes) would serve households who earn below 50% of median family income (MFI). Meeting this need will require public support, in the form of a construction subsidy to build a home that these households can afford, rent subsidies to help them access a unit, or both. This means providing access to nearly 9,000 new publicly supported units per year. Between 2016 and 2020, OHCS has funded an average of just over 3,0006 units per year."

Finally, one factor which remains a potential source of disruption in the Oregon housing market is the eviction moratoriums and their eventual expirations. There statewide eviction moratorium expired on June 30th, 2021, however "Between July 1, 2021 and February 28, 2022, tenants who have applied for rent assistance have a safe harbor from termination or eviction due to nonpayment of rent," according to the Portland city website.

The Associated Press reported in July 2021 that the impending surge of evictions is a rising concern for the state of Oregon, despite millions of dollars of federal aid being utilized to assist renters in avoiding eviction. The AP reports, "one indication of the scope of the problem is census data in July showing 38% of Oregon tenants who responded to a survey — or more than 35,000 renters — said that it was "very likely" or "somewhat likely" that they would be evicted from their home."

A wave of evictions would undoubtedly exacerbate the housing crisis across all parts of Portland. The housing market is being flooded with renters in need of new housing. Additionally, multifamily landlords are struggling to recoup extensive losses, following nearly two years of tenants failing to pay their rent. This is the perfect cocktail for rents increasing. The state of Oregon, counties and cities all have tools at their disposal which can prevent this wave of evictions and assist landlords in order to prevent a surge in rent prices. However, this still remains an unknown going forward and will remain a topic of interest for all parties in the housing market.

MISSING MIDDLE HOUSING AND ZONING

A 2018 student publication from Portland State University made several important points about the state of the Oregon housing market and the conditions of our land use regulations which lay the groundwork for an examination of missing middle housing. Ryan Winterberg-Lipp, on behalf of Portland State University, found that between 2010 and 2018, 62,000 housing units were permitted in Clackamas, Multnomah and Washington counties. However 40% of these permits were for single family house and 40% were for high-density urban units. The single family homes were predictably located in more rural and suburban areas while the urban multifamily units targeted high-income residents. Only 7% of new permits between 2010 and 2018 were for missing middle housing, however this may be the very asset type which could serve as a powerful tool to drive rents down and inspire new investments and innovation in the housing market.

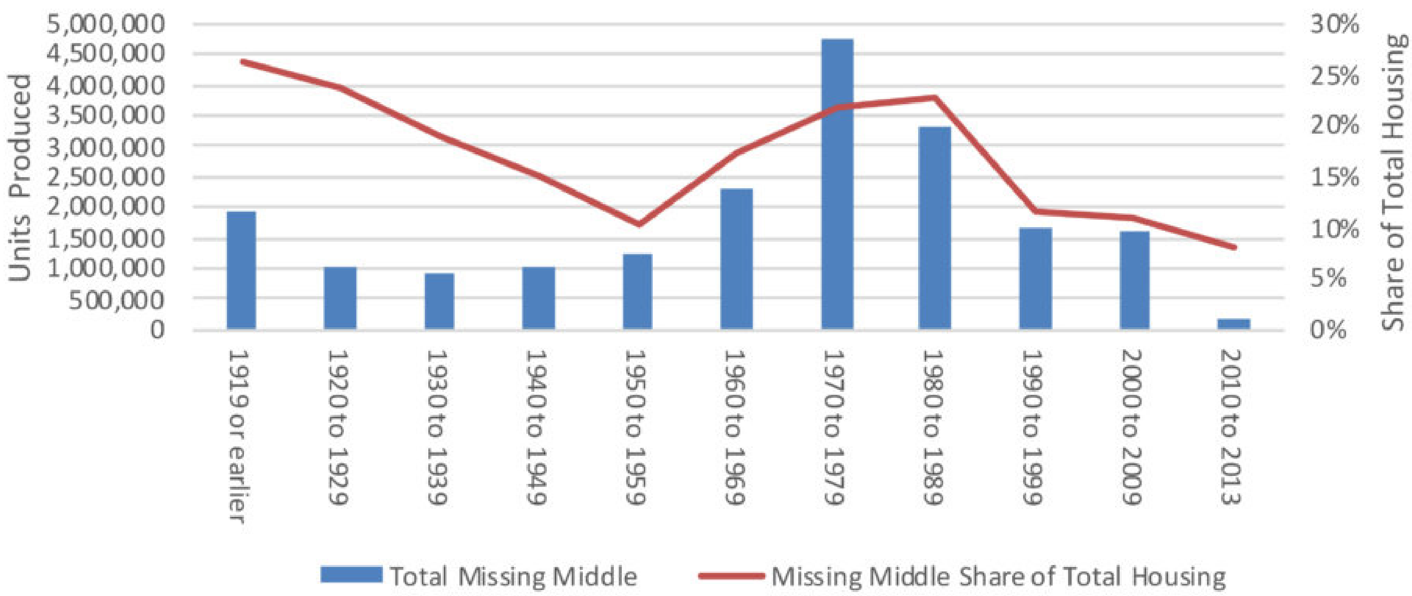
Middle housing is loosely defined as multifamily properties which offer less density than mid or high-rise properties. These are typically duplexes, triplexes, townhouses, courtyard buildings, multiplexes and other arrangements which offer renters the opportunity to live in a smaller development and offer developers the opportunity to construct multifamily properties smaller than the typical urban multifamily properties which demand high unit counts to deliver their desired ROI.

Middle housing is typically between 16 to 36 dwelling units per acre, depending on the lot size and building design. Daniel Parolek, author of Missing Middle Housing: Responding to the Demand for Walkable Urban Living, explains the benefits of developing middle housing. "Because of their simple forms, smaller size, and Type V construction, Missing Middle building types can help developers maximize affordability and returns without compromising quality…," explains Parolek. The benefits of middle family housing can be realized by the renter, owner and entire community.

Missing middle housing represents the gap between under-utilized and inefficient land usage in single family zones and the problems associated with dense urban developments with constant growth. Middle housing requires a footprint similar to large single family homes, with the largest type of middle housing built with a main body width of about 40-50ft. This demonstrates the capacity for middle housing to be developed without the need for massive land purchases or teardowns of multiple housing units.

Middle housing properties can be developed with the design planned or originally adapted from single family homes by adding additional dwelling units, or ADU's. An ADU can be added to any single family home if zoning allows for multifamily properties and the ADU is approved based on living conditions.

It's important to recognize the appeal of ADU's is not the same as duplexes, triplexes or other examples of designed middle housing. ADU's are typically detached garages or other small structures converted into a dwelling unit, however the space is typically not built with this use in mind. While adding ADU's may be the easiest method of converting a space into middle housing, it's also the option which is least comparable to a standard living space and likely would not demand the same rent as a duplex, triplex or otherwise designed middle housing. That said, ADU's represent a massive opportunity for existing homes to convert themselves into multifamily, thereby increasing the available volume of apartments in the area and increasing the value of the home for the owner. Yet with all these potential benefits, the graph below demonstrates that new construction of middle housing has decreased since 1970.



(Source: Daniel Parolek, Missing Middle Housing)

The increased demand for multifamily across Oregon is limited by the inefficient and wasteful land use across the state. Single-family zoning prevents the construction of middle housing and Oregon, as well as the country, has designated far too much landed for single-family. Winterberg-Lipp found in their study of Oregon zoning that, "within the Portland Metro urban growth boundary as of December 2015, single-dwelling residential zones comprised 48 percent of all land area and 77 percent of all land area currently zoned for housing." In metro areas across the state of Oregon, land use regulations are primarily geared towards single family homes and dense urban properties, so the middle housing remains missing.

The prevalence of single-family zoning in the state is partially rooted by the culture of NIMBY or not in my backyard, which is a generalized attitude of homeowners that densifying the surrounding area will cause problems, bring in lower-earning residents and lower the surrounding home values. Single-family homes are likewise at the root of decades-old segregation methods utilized across the state and nation. Land was historically divided into large lots for the development of single family plots in order to limit those who had access to houses and develop multifamily properties into areas deemed undesirable. Those who owned homes then used methods such as redlining and blockbusting to keep their neighborhoods exclusively white and create cycles of poverty in the areas populated by minorities. The impacts of these methods are seen today in the large land plots and exclusive R-1 zoning which continues to limit the inventory of housing and prevent lower-income residents from attaining affordable housing in areas that see appreciation.

HB 2001

In 2019, the state of Oregon passed House Bill 2001 as an effort to encourage the development of more middle housing and reduce the pace of urban growth boundaries. The bill, introduced by House Speaker Tina Kotek, was passed with a bipartisan majority but was primarily favored by the Democrats and is one of the biggest land use bills in the nation. The law requires updates of local city codes that have limited zoning to R-1, or single family housing, to allow the construction of middle family housing on that land and mandates necessary infrastructure be provided to accommodate the growth.

The bill virtually eliminates single family zoning in cities over a certain population, yet these cities are able to limit the addition of limited units and prevent density typically seen in CBD's. Cities of Oregon must allow for more density on all residential land, but the cities that are impacted here and the degree of density that must be allowed depends on the population of the city. Cities have dates in which these changes must be implemented into their zoning codes. If cities do not make the necessary changes by the deadline, a generic code change is automatically implemented by the state in those areas. Medium sized cities, defined as over 10,000 residents, must allow duplexes on all single-family zones.

There are 21 medium cities in Oregon that this bill impacts: Ashland, Baker City, Canby, Central Point, Coos Bay, Cottage Grove, Dallas, Hermiston, KIamath Falls, La Grande, Lebanon, Newberg, Newport, Ontario, Pendleton, Prineville, Roseburg, Saint Helens, Sandy, Silverton and The Dalles. According to an op-ed published on June 2021 in the Daily Journal of Commerce, "most of these cities have either made the changes necessary to accommodate the new legislation, or are in process to do so." These changes must go into effect by June 2021. It's noteworthy that while middle housing refers to a large variety of unit mixes, smaller cities are only required to allow the development of duplexes in order to let smaller cities set growth rates at a slower pace if they choose to do so.

Cities with a population over 25,000, such as Portland and Eugene, must allow significantly more density in R-1 zones including fourplexes, cottage clusters and townhouses. The bill also provides $3.5MM for assistance to cities in adjusting to these code changes. The Oregon state website states that cities are able to set "reasonable" siting and design requirements for middle housing and that the Oregon Department of Land Conservation and Development, or DLCD, has been directed to assist cities in setting their design guidelines. Michael Anderson of Sightline Institute reported July 2019 that HB 2001 would impact 2.8 million Oregonians, 2.5 million living in larger cities and only 300,000 living in medium-sized cities.

HB 2001 does not retroactively change any existing CC&R, or covenants, conditions and restrictions, and does not recommend city governments attempt to do so. HB 2001 does prohibit future CC&R's from prohibiting middle housing in all areas where HB 2001 applies. HB 2001 prohibits cities or jurisdictions from requiring owner-occupancy or off-street parking for ADU's.

Cities are also required to provide the necessary infrastructure, such as water, sewer, drainage and transportation, to support the projected growth based on adding residential units. The DLCD has been directed to assist cities in addressing the need for increased infrastructure and making the necessary investments. The DLCD has allowed cities to apply for infrastructure-based time extensions if the existing infrastructure is significantly deficient and cities are unable to implement the necessary infrastructure changes by the intended deadline. Infrastructure deadlines are intended to last for five years or less, granted the city is making a good faith effort to make the necessary investments into their infrastructure.

IMPLEMENTATION AND REACTION

Cities across Oregon have already begun implementing changes into their zoning code as well as expressing opinions in favor of and in opposition to HB 2001. Several cities have already implemented their own version of zoning code changes to eliminate single-family zoning, making HB 2001 either complimentary or redundant. The following are a selection of city change in compliance or defiance of HB 2001 and reactions.

The city of Portland has spent years developing their own methods of changing zoning codes in order to eliminate single-family zoning and encourage the development of middle housing. As reported in a Bloomberg article in August 2020, the city of Portland has approved and begun implementing the Residential Infill Project, which amends the Portland zoning code to allow up to four units on R-1 land. Developers are able to develop six units granted half of the units are rented as affordable housing. The city estimates this project could create between 4,000 and 24,000 new units and reduce displacement by 28%. Bloomberg found that this city project was complimented by HB 2001, which "helped shift the politics in support of sweeping zoning reform more locally," according to Cortright, the Portland-based economist and director of the City Observatory website.

The city of Bend announced in May 2021 that they will "soon consider new code changes following recent action at the State level to provide more housing opportunities for Oregon residents," according to the City of Bend website. Public hearings will be held in July and August so the city council and planning commission can receive public feedback on their plan to update the Bend Comprehensive Plan in compliance with HB 2001. Bend Affordable Housing Manager Lynne McConnell told concerned citizens at a community information session, "The only way we can absolutely guarantee affordable housing is if we have some skin in the game. We have

“The only way we can absolutely guarantee affordable housing is if we have some skin in the game. We have to invest in that property in some way in order to take a deed restriction or record a covenant on that property which allows us to keep it affordable over term.”

(Bend Affordable Housing Manager, Lynne McConnell)

to invest in that property in some way in order to take a deed restriction or record a covenant on that property which allows us to keep it affordable over term.”

Eugene principal planner Terri Harding has stated that Eugene must comply with HB 2001 and is also working towards a goal of “furthering equity and long-term affordability and enabling housing availability and diversity.” Eugene is in phase two of a four-phase plan to amend the city code to meet the new requirements and plans to begin writing this code in Spring 2021. Eugene is currently considering their method of paring requirements, determining whether they ought to require off-street parking or incentivize it, such as requiring no parking if some of the units are affordable or the property is nearby public transit.

Springfield has begun drafting housing code changes and plans to continue these changes through the end of June 2022. Senior Planner Mark Rust describes housing code changes as the first phase of a much larger project.

Nigel Jaquiss of the Willamette Week described the varied reactions among several cities of Oregon in an article published November 2019. West Linn Mayor Russ Axelrod expressed concerns about increasing density in areas with the necessary infrastructure and transit. Axelrod referred to HB 2001 as “stupid” and considered launching legal challenges against the law. The city council of Lake Oswego considered implementing increased fines for any home demolition, a method of disincentivizing the teardown and rebuilding of middle housing.

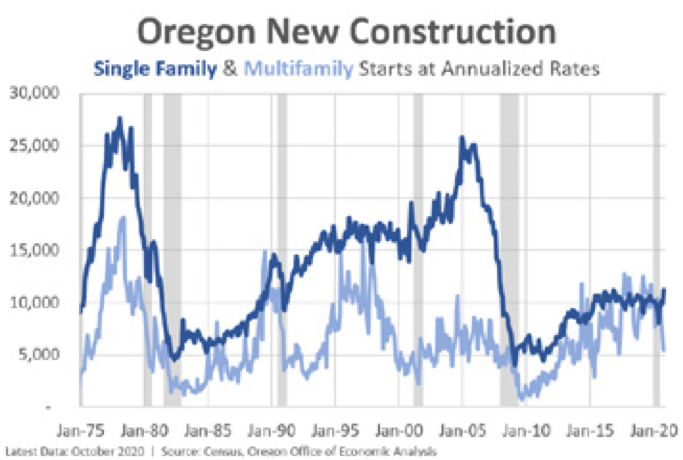
ANALYSIS OF HB 2001 AND MIDDLE HOUSING

The question at the center of middle housing is whether or not to amend zoning codes to end single-family zoning. Land currently designated as R-1 property will always be able to remain a single-family home if the owner chooses, however the restriction of any further density could have dramatic impacts on how communities design their neighborhoods and create growth.

The practice of increasing the density allowance in a zoning code, otherwise known as upzoning, has been utilized as a proven method of lowering average costs of living by increasing the supply of units in the market.

Todd Litman, founder and executive director of the Victoria Transport Policy Institute, published an article in April 2021 discussing the benefits of upzoning and the extensive research done on the topic. "Extensive research, using various data sets and analysis methods, supports the conclusion that upzoning can increase affordability," states Litman. He goes on to discuss a study conducted by NYU's Xiaodi Li, which found that in New York City, rents and sales prices decrease by 1% for every 10% increasing in multifamily housing supply.

The additional housing units added into the housing market via middle housing lowers the price of existing rents in an event known as the filtering model. This is the process of older properties decreasing in sales and rental price as newer properties are built. Multifamily units are built at standard costs and require strong rental income to make their target returns. However, as the property remains stabilized, the landlord's risk associated with the property decreases as there is a record of successful tenancy and steadfast cash flow.



At the same time, the demand for these older buildings decreases as the tradeoffs for renters increase in quantity and quality. From the renter's perspective, if they're able to afford a higher rent, they will choose to "filter" up to the newer, higher quality buildings. The combination of increased vacancy and long-term stabilization means the landlord will lower their rent and can do so without being at risk of default or foreclosure. The relevancy here being that as middle housing units are constructed and demand for those drives renters into those units, existing units will see rents decreasing. The lack of new construction rates, as demonstrated by the chart below, demonstrates the need for new policies to drive construction numbers higher in order to see the filtering model work.

The success of HB 2001 in increasing housing inventory is based on the state's ability to enforce these zoning changes. Many neighborhoods have enacted CC&R's in order to set guidelines on what can be built in that area. CC&R's are agreed to by all residents in the neighborhood, so if a resident wishes to add an ADU to their property or construct a triplex, code changes based on HB 2001 may conflict with their local CC&R's. While CC&R's represent a roadblock to enforcing HB 2001, they're also an important tool of neighborhoods in unincorporated areas to ensure guidelines are set to the desire of the community.

“Probably the most important characteristic of [middle housing] is that they need to be built within an existing or newly created walkable urban context. Buyers or renters of these housing types are choosing to trade larger suburban housing for less space … and proximity to services and amenities…”

(Daniel Parolek)

One concern in the face of increasing density is parking. Increasing density and encouraging growth within a community will also create a need for more parking spaces. A single-family home converted into a triplex has tripled the parking required for that property in the blink of an eye and this can start to spillover into the street. Conflicts can arise when neighborhoods unexpectedly fight for parking spaces. Also, overcrowding of street parking can have a negative impact on home prices. New development can plan to have the necessary off-street parking to accommodate the new residents, however this is an additional expense for the developer that will require an increase in rent.

A 2016 study by Housing Policy Debate found every surface space costs roughly $5,000 to build, which increase to $25,000 for above-ground space and $35,000 for subterranean parking. The typical renter pays an average of $142 per month for parking, which is an increase of 17%.

The issue of parking, however, does highlight a strength of middle housing: walkability. One of the key components of middle housing is designing a community layout which enables residents to walk and utilize public transportation rather than relying on their car. As Daniel Parolek explains in high study of middle house, “Probably the most important characteristic of [middle housing] is that they need to be built within an existing or newly created walkable urban context. Buyers or renters of these housing types are choosing to trade larger suburban housing for less space … and proximity to services and amenities…”

Walkability is a prime example of an advantage realized by all parties involved in middle housing where off-street parking is not required. As explained above, renters typically see a 17% increase in their rent for parking, which is a potential savings when excluding parking from construction plans. Developers eliminate a major construction cost and use of land, which can then be added into living spaces, bike racks, or other uses besides off-street parking. Local businesses benefit from having a local population within walking distance who are able to access their business with ease. Finally, the dependency on cars is one of the largest factors in emission of greenhouse gasses.

The necessary fight to slow climate change starts with planning cities and communities to become less dependent on cars and utilize walking, biking and public transportation. Jeffrey Spivak published an article in 2018 for the American Planning Association where he advocates for the elimination of off-street parking requirements for new construction. He points out the multiple cities who have experimented with parking requirement policies, such as Buffalo, Lexington and Spokane, and found these changes have spurred more incentive for housing development without crippling transportation methods in the area.

One aspect of middle housing which may appear as a positive but should be examined more critically is the reduction in inventory of single family zoning. There is a growing call to end single-family zoning across all parts of the country and HB 2001 is clearly a method to this end. However, it's important to examine both sides of action which is aimed at having a significant impact on the housing inventory of the state. The historic methods of segregation were enforced with both legal powers abused by those in power and the state of the housing market being scare and difficult to acquire. The lack of affordable housing to purchase created a bar for working class residents to clear and because supply was intentionally limited, the generational concentration of wealth was able to continue accumulating without disruption.

While middle housing does create an increased multifamily supply, every single-family home that is converted into middle housing is one unit of housing that is taken out of the single-family market and likewise increases in value as an income property. Simply put, converting single-family homes into middle housing creates one more apartment and one less house. As demand for single-family homes persist, competition will cause the remaining supply of single-family homes to increase and purchasing a property that is now middle housing requires even more capital upfront than the original single-family home.

NATIONAL CONVERSATION

It would not be an exaggeration to say the country will be watching Oregon and how HB 2001 impacts the housing market in determining what other states, even the federal government, will do regarding land use regulations. Oregon is the most aggressive state in their statewide determination of land use requirements, but the United State is still in the midst of a housing crisis which has led to many proposing an end to single-family zoning. USA Today reported in April 2021 that President Biden's original $2 trillion infrastructure plan included grants and tax credits to cities which implement zoning code changes to reduce single-family zoning. While this portion was not passed in the eventual bipartisan infrastructure bill, there are growing calls to encourage upzoning, and many believe single-family zoning ought to be eradicated.

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