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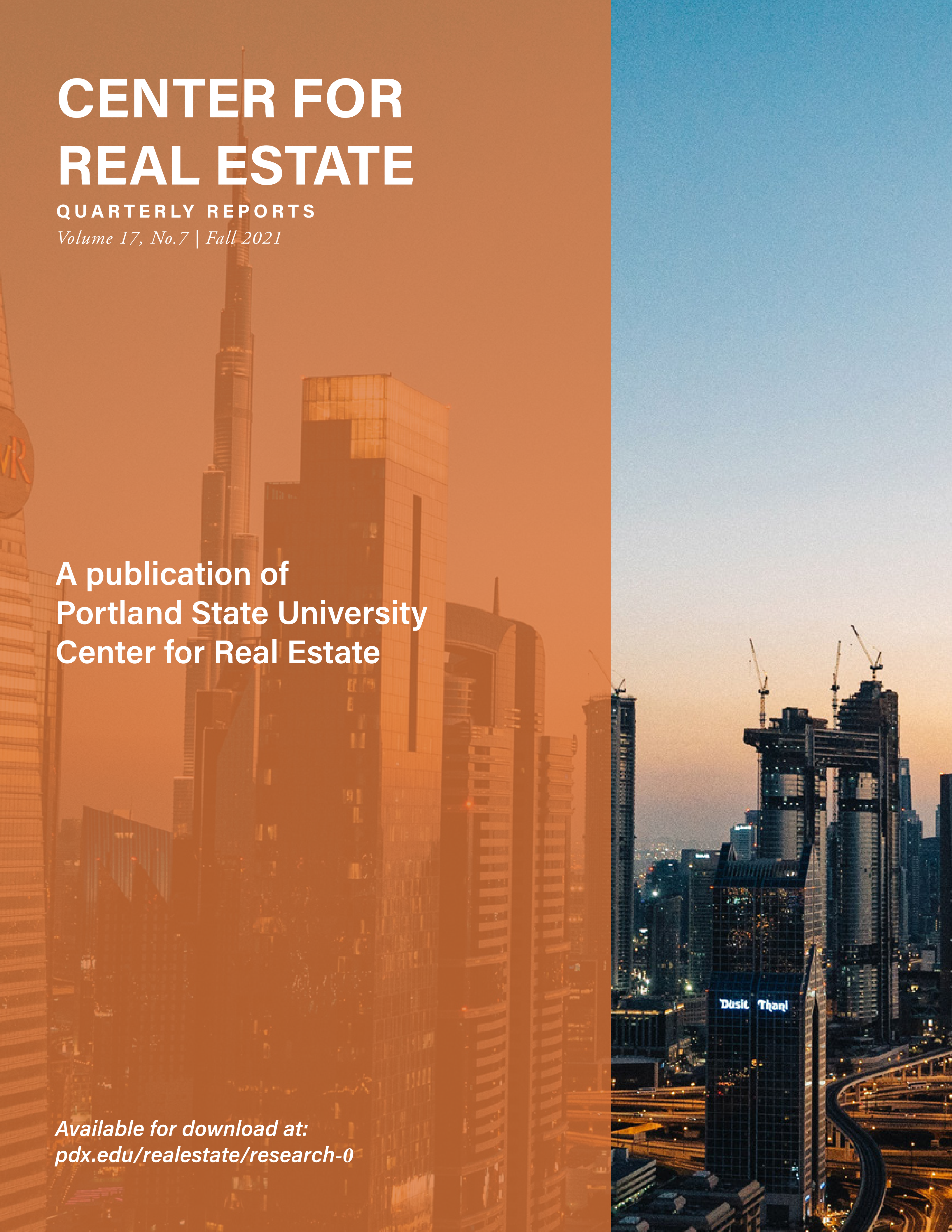

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ECONOMIC OVERVIEW

Economic Analysis

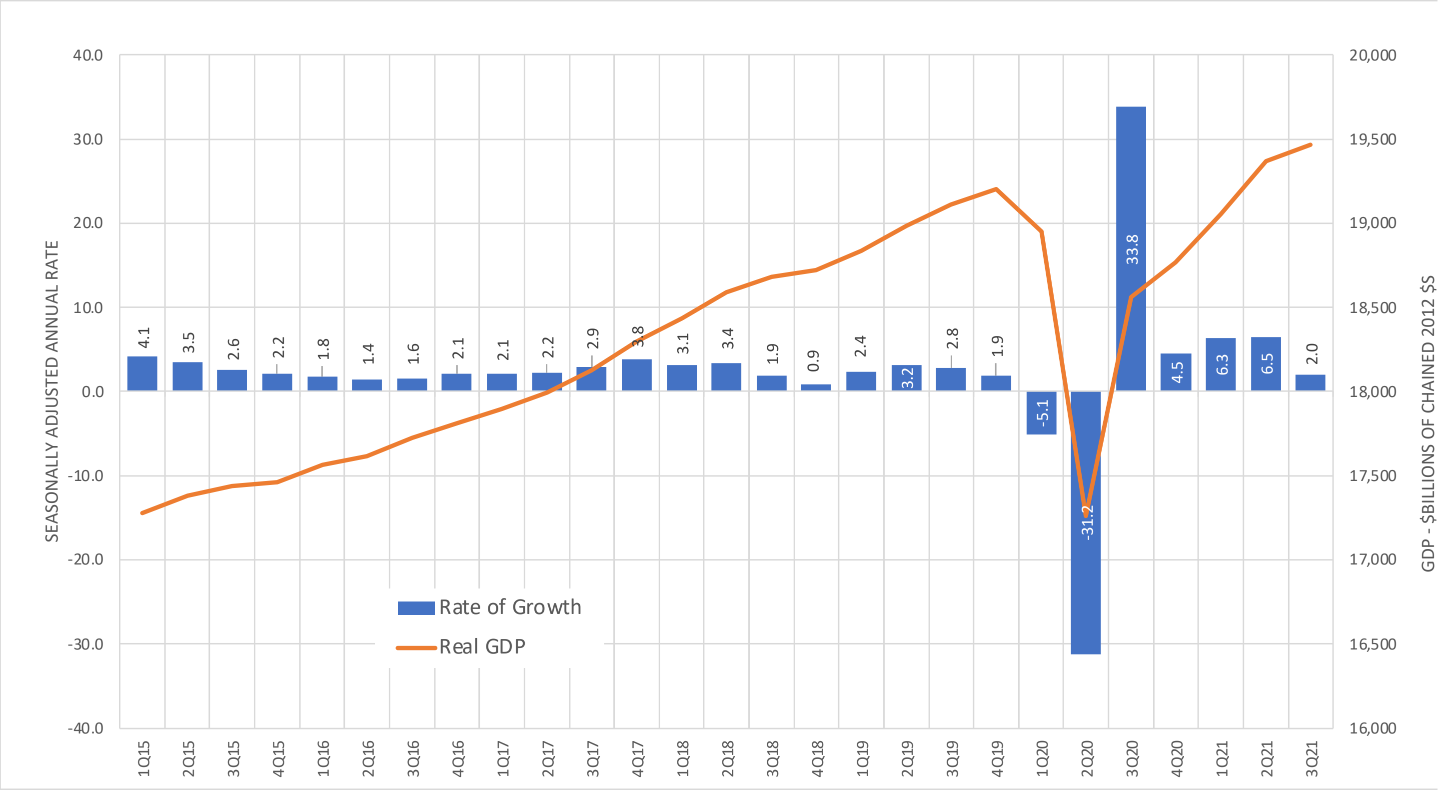
Jerry Johnson

Portland State University

Jerry Johnson is an adjunct professor at Portland State University's Center for Real Estate. He is also the Managing Principal of Johnson Economics, a consultancy based in Portland.

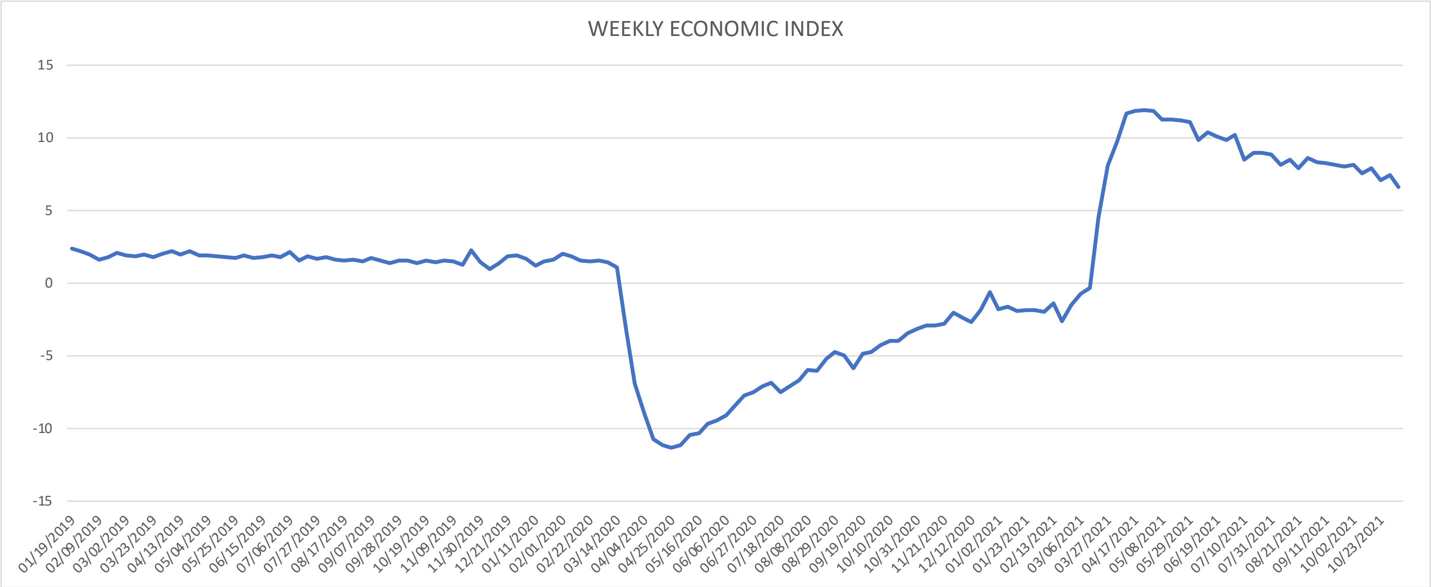
The national recovery continued during the third quarter of 2021, although the rate of growth has declined, and inflation has become a significant concern. The rate of expansion in GDP slowed to an estimated 2.0% during the third quarter, following four strong quarters after the unprecedented drop during the second quarter of 2020. The overall real GDP is now above pre-pandemic levels but still below the historic trendline.

REAL GDP TRENDS



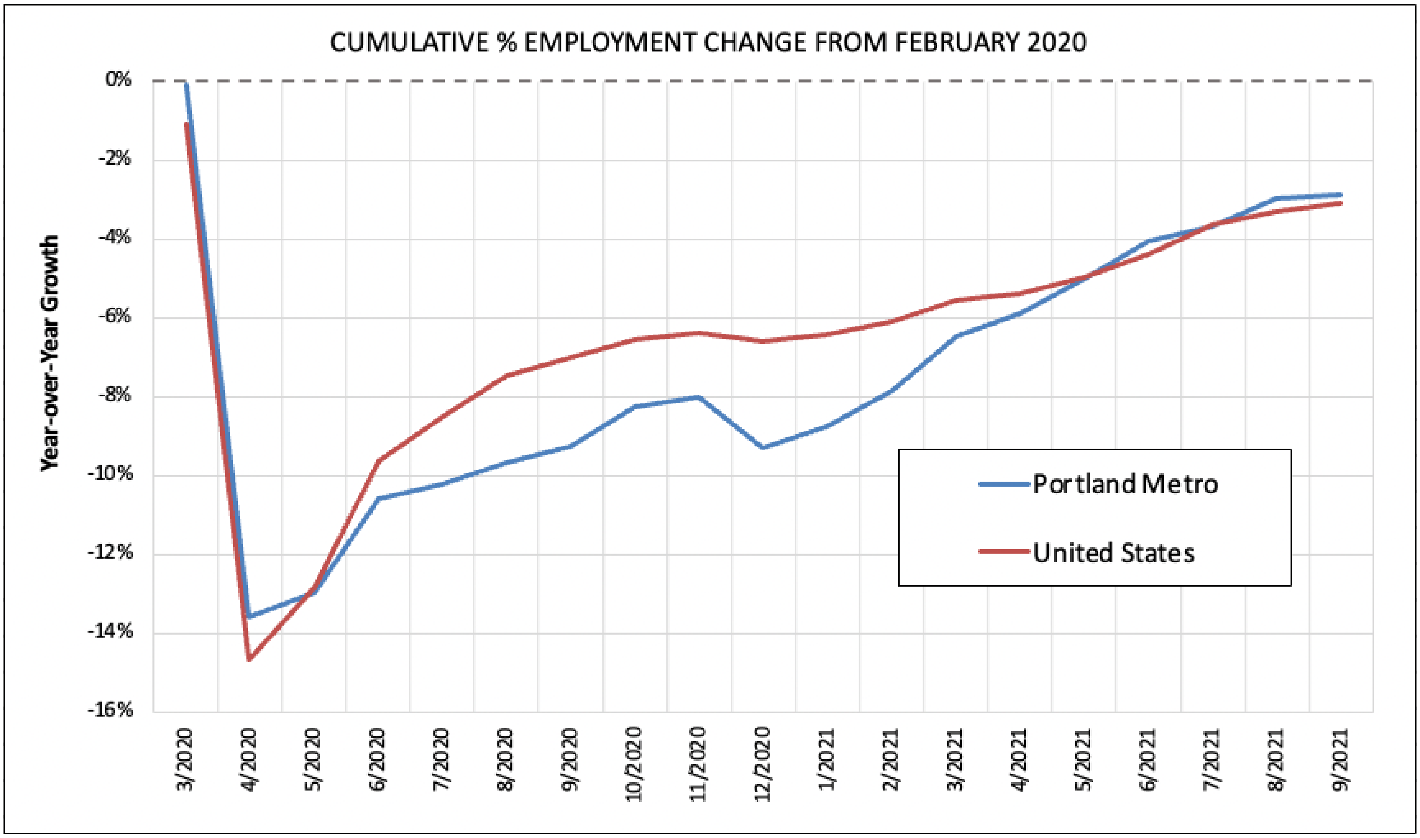
U.S. Bureau of Economic Analysis

The Delta variant wave appears to have crested in the State of Oregon, but the number of hospitalizations remains elevated. New cases exceeded 50 per 100,000 in the State overall, and over 110 for unvaccinated individuals. The slowdown can also be observed in the weekly economic index, which is an index of ten indicators of real economic activity.



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

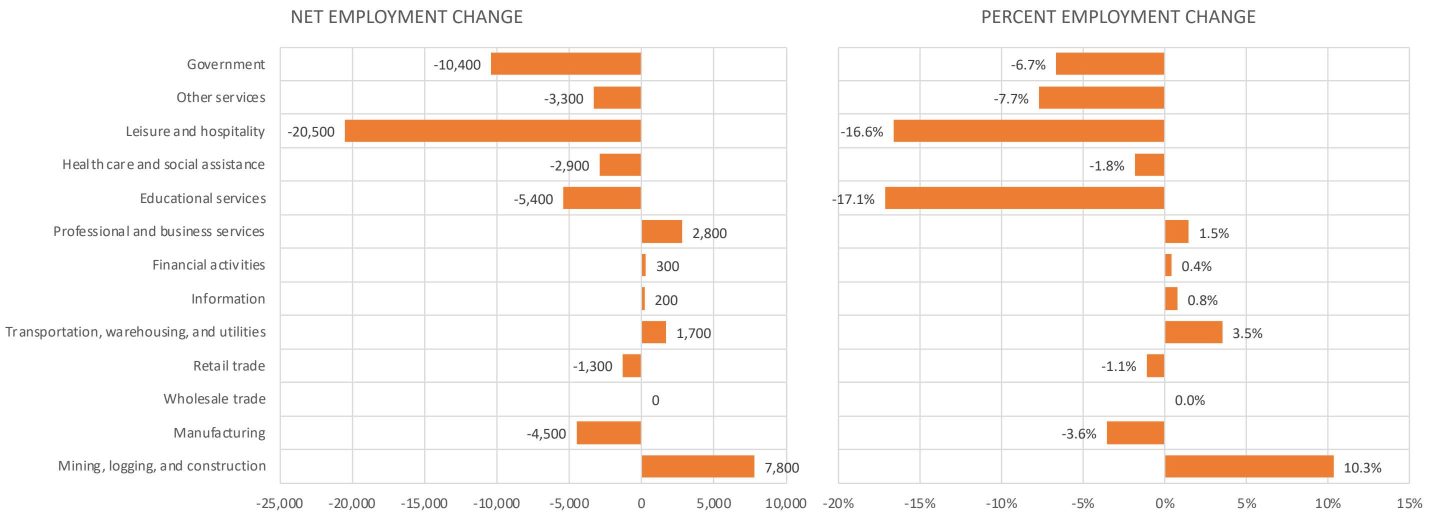
After lagging the national recovery in the latter half of 2020 and early 2021, employment levels in the Portland metropolitan area are now consistent with national levels. Estimated current employment levels in the metro area are 2.9% below pre-pandemic levels (February 2020). At the current rate of growth, the region is not expected to regain its previous employment level until the first quarter of 2022.



State of Oregon Employment Department & U.S. Bureau of Labor Statistics

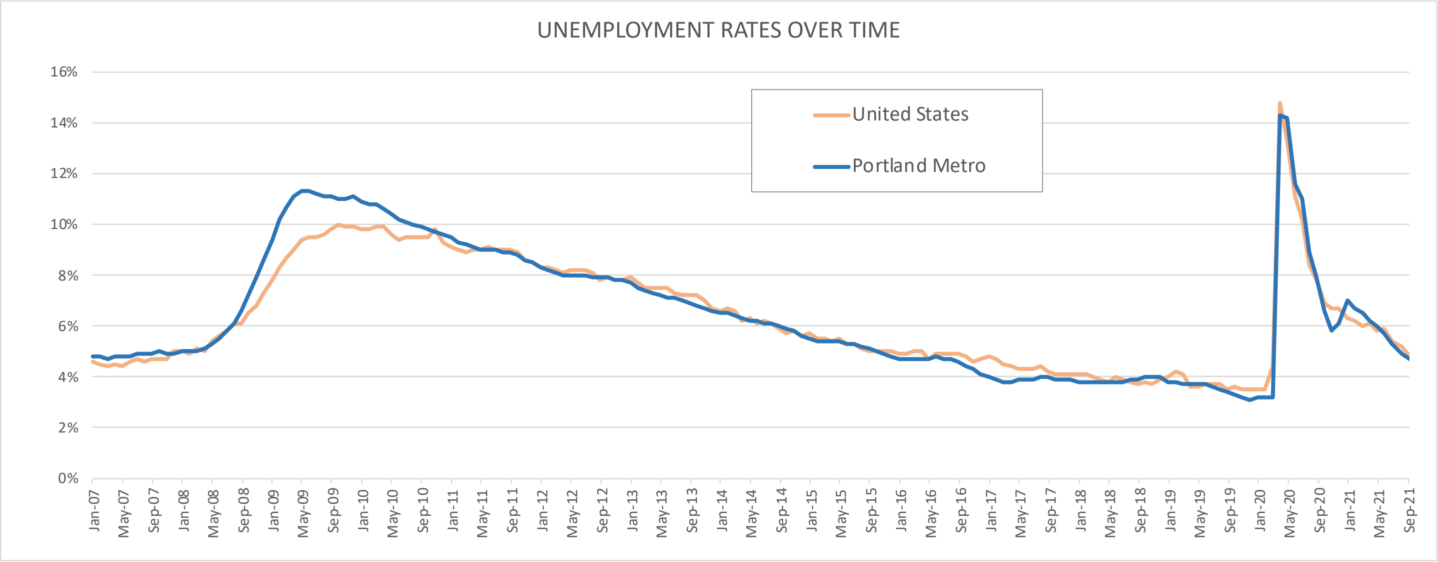
On an absolute basis, employment losses have been greatest in the leisure and hospitality, government, and education services sectors. Gains have been strongest in construction; professional and business services; and transportation, warehousing, and utilities. On a percentage basis, educational services (17.1% decline) and leisure and hospitality (16.6% decline) remain well below their pre-pandemic employment levels.

NET EMPLOYMENT CHANGE BY INDUSTRY, FEBRUARY 2020 THROUGH SEPTEMBER 2021



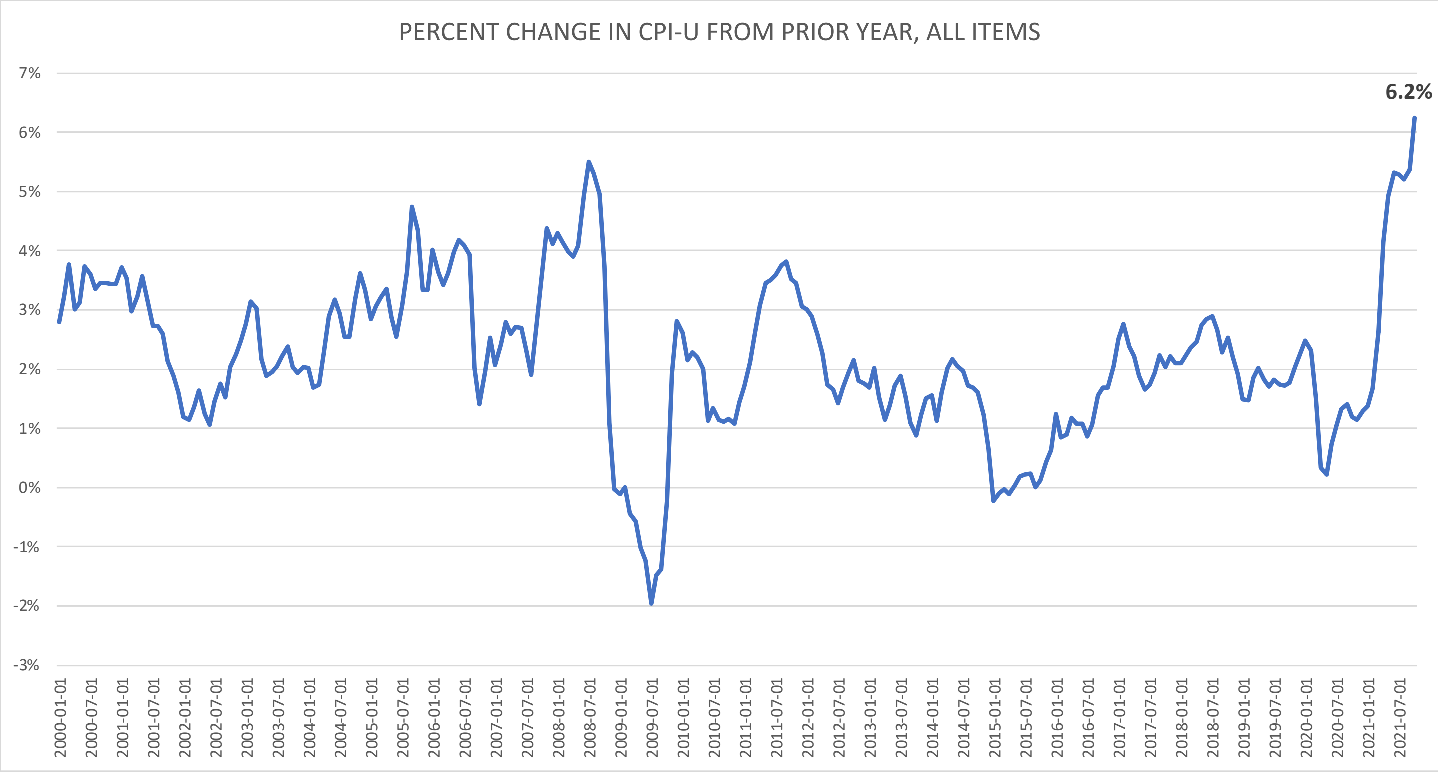
State of Oregon Employment Department

While the region has not yet recovered on an employment basis, the unemployment rate has dropped to 4.7% in the metro area. This reflects a decline in the labor force participation rate, with a record high number of employees voluntarily leaving positions. This is both a statewide and national pattern. The Oregon Employment Department surveys private employers on a quarterly basis, with a focus on job vacancies they are currently trying to fill. Oregon businesses reported almost 107,000 vacancies in the second quarter, an increase from 97,800 vacancies reported in the first quarter. The dropping unemployment rate, as well as inflation throughout the economy, is placing pressure on wage rates.



State of Oregon Employment Department

Following decades of historically low rates, inflation has recently emerged as a major concern. The consumer price index indicates a year over year inflation rate of 6.2% in October 2021. This is the highest monthly rate since December 1990 and reflects significant price escalation in several sectors.



U.S. Bureau of Economic Analysis

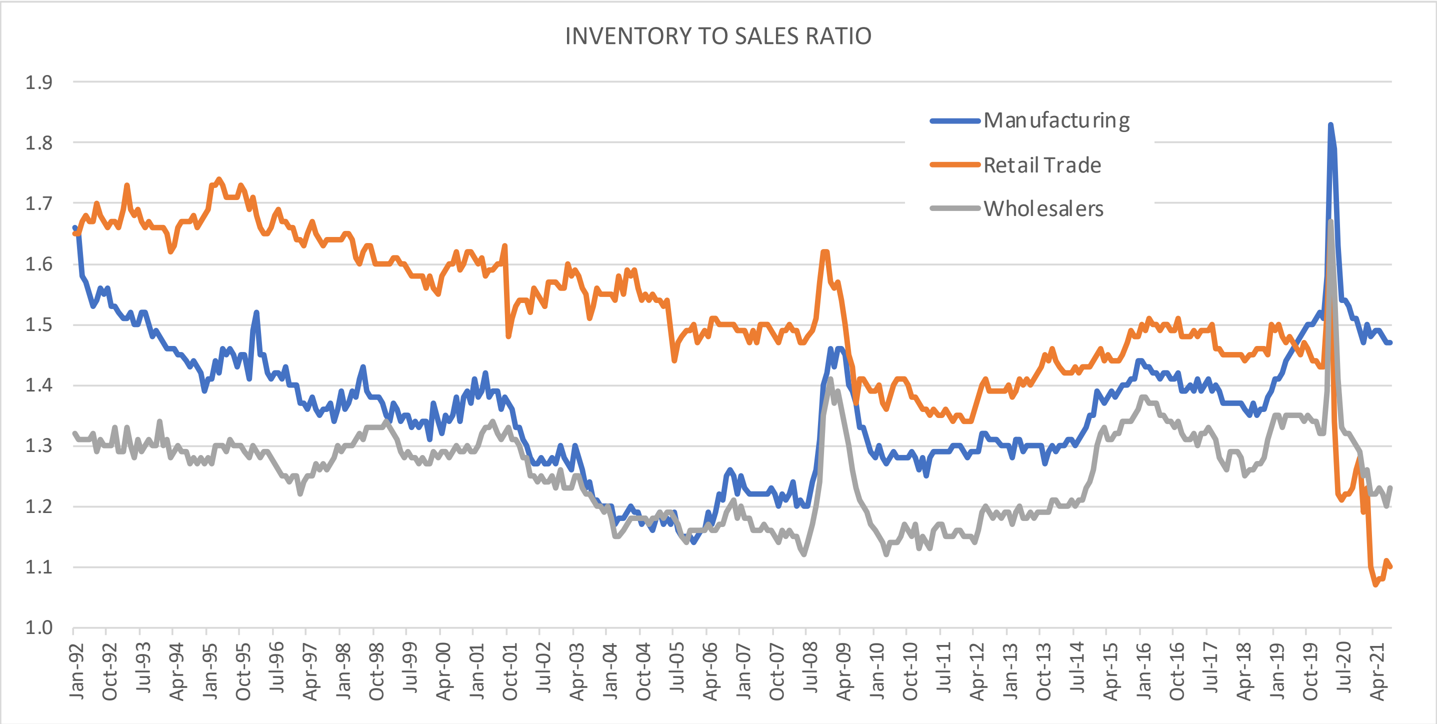
Household energy reported the highest percentage price change at 12.7%, followed by new vehicles at 9.8%. Price levels are up over a broad range of goods, although airline fares have dropped. Core Consumer Prices, which excludes food and energy, rose 4.6%.

CHANGE BY SELECTED CATEGORIES

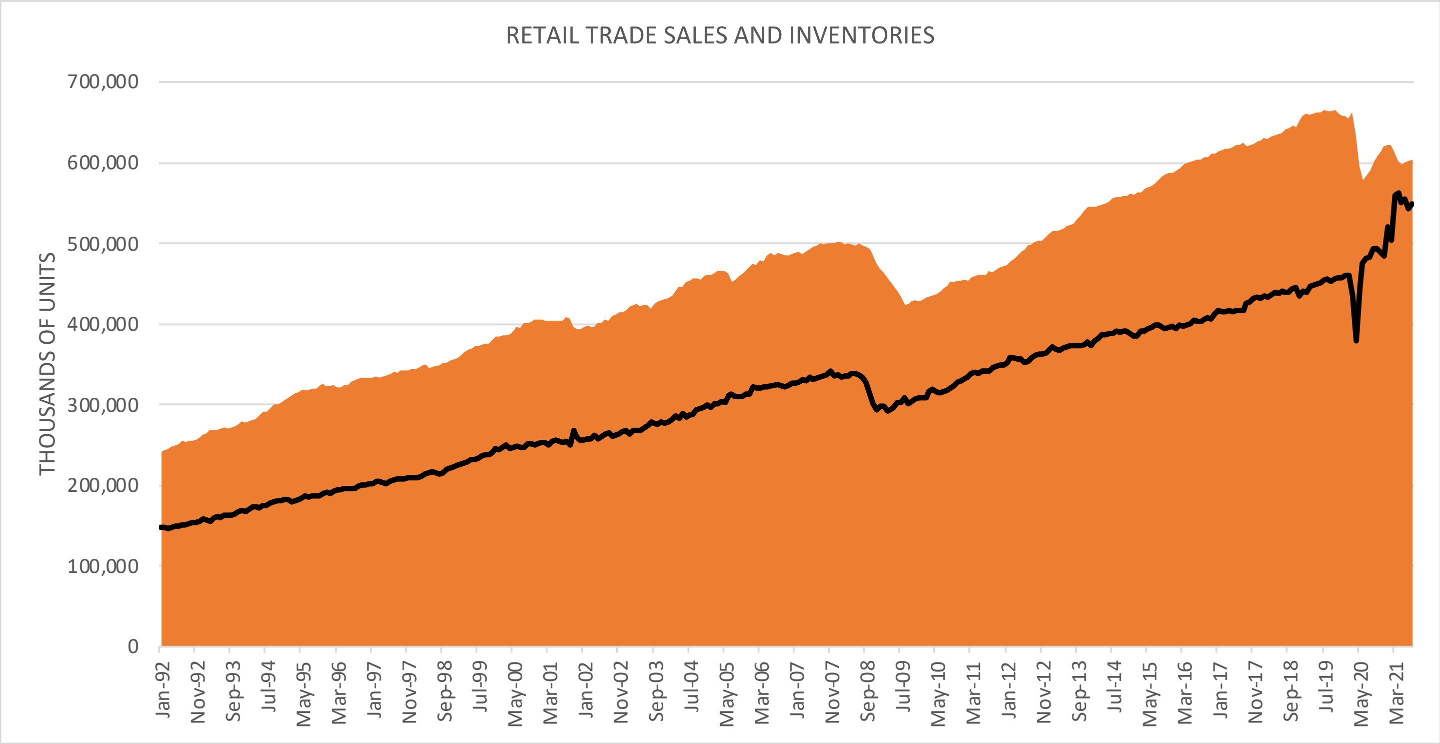
All Items	6.2%
Household Energy	12.7%
New Vehicles	9.8%
Furniture	6.2%
Groceries	5.4%
Restaurants	5.3%
Apparel	4.3%
Shelter	3.5%
Alcohol	2.2%
Medical Care	1.3%
Airline Fares	-4.6%

The shelter component of CPI tends to be significantly understated during times of rapid escalation, as ownership housing pricing is self-reported and lags actual market pricing substantially. The reported rate of 3.5% is inconsistent with double digit rates reported in most data sources. A recent report by the Dallas Fed found that there is a 16-month lag between BLS inflation series and real time market pricing. Assuming this holds true, recent escalation in home prices and rents will add 0.6 to 1.2% to the core CPI in 2022 and 2023.

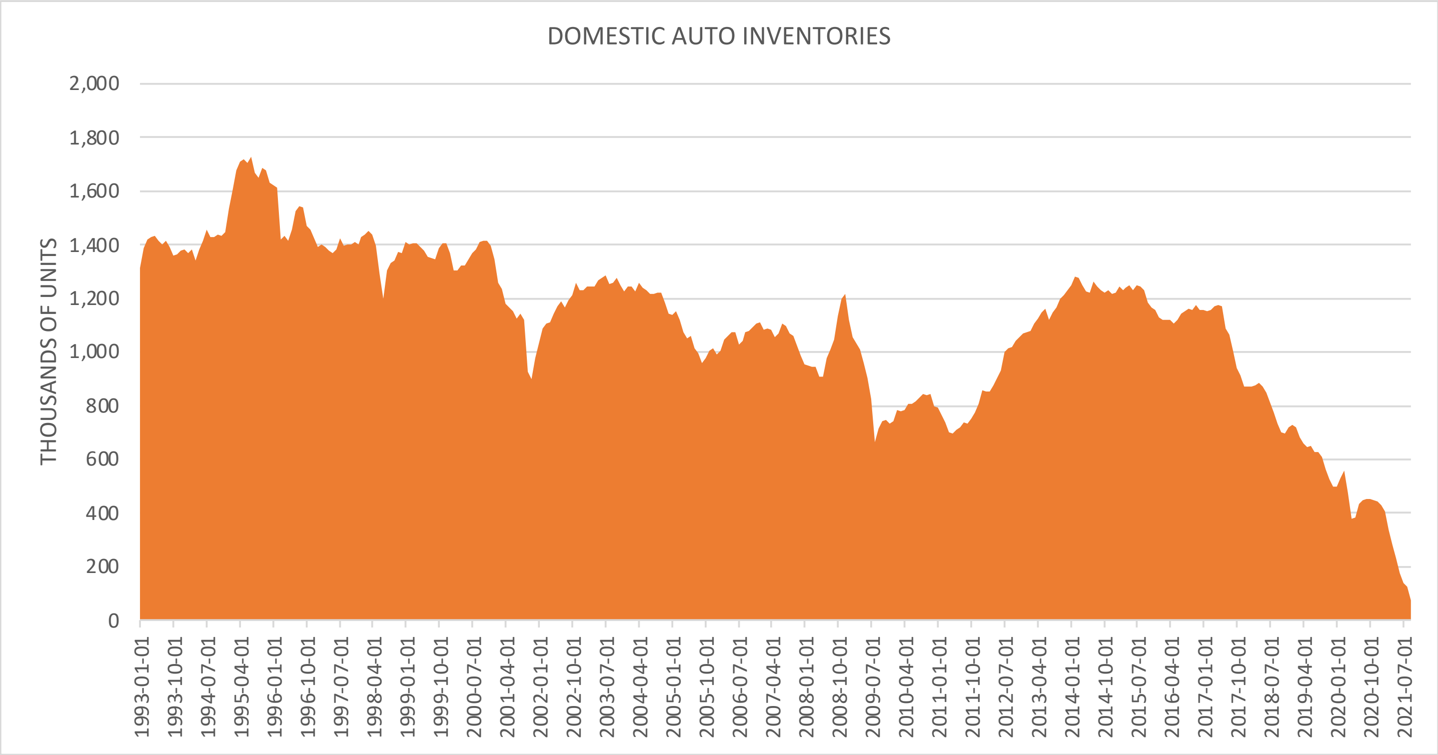
Inflation has proven to be less "transitory" than many economists predicted, and supply chain issues as well as sustained demand are expected to continue to place pressure on pricing. Following a sharp increase in the first quarter of 2020 as the economy initially shut down due to the pandemic, the inventory to sales ratio has been declining for manufacturing, wholesalers, and retail trade. The most notable shift has been for retail trade, which has seen a sharp increase in demand that the supply chain has been unable to keep pace with. Overall retail inventory was estimated at 1.1 months of sales in August 2021, the lowest ratio in the thirty years that it has been tracked. Supply chain limitations have contributed to the lack of inventory, and the general trend has been towards maintaining a more limited just-in-time inventory. However, a sharp increase in retail sales has been the main factor.



Census Bureau, Manufacturing and Trade Inventories and Sales report



Census Bureau, Manufacturing and Trade Inventories and Sales report



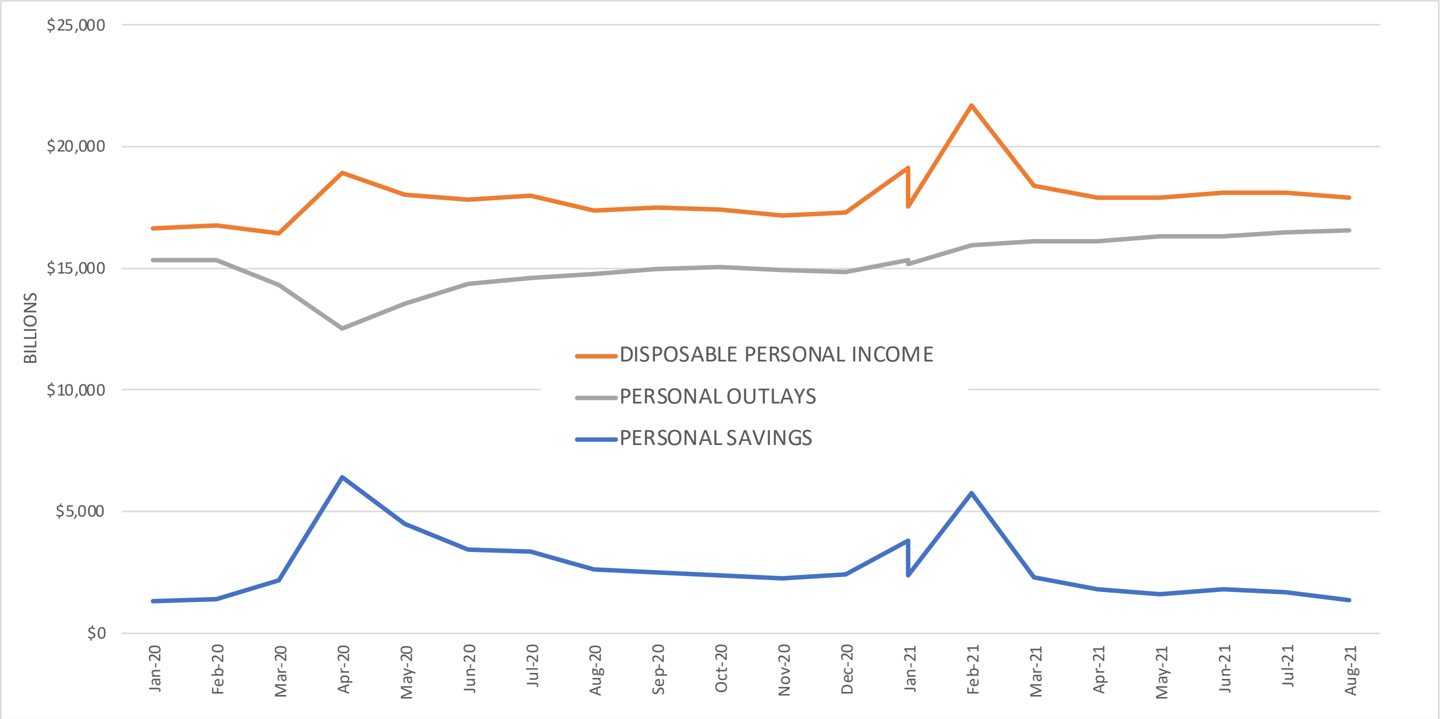
Federal Reserve Bank of St. Louis

The drop in retail inventories is broadly based, but the drop in domestic auto inventories is illustrative of the pattern. The auto industry has been slowed by supply chain limitations, most notably a shortage of computer chips. Logistical problems associated with a shortage of shipping capacity, truck drivers, and labor shortages are adding to these problems. Automakers are facing shortages in steel, labor, and inputs such as resin. A recent forecast expects supply chain problems will reduce automaker production by 7.7 million vehicles globally.

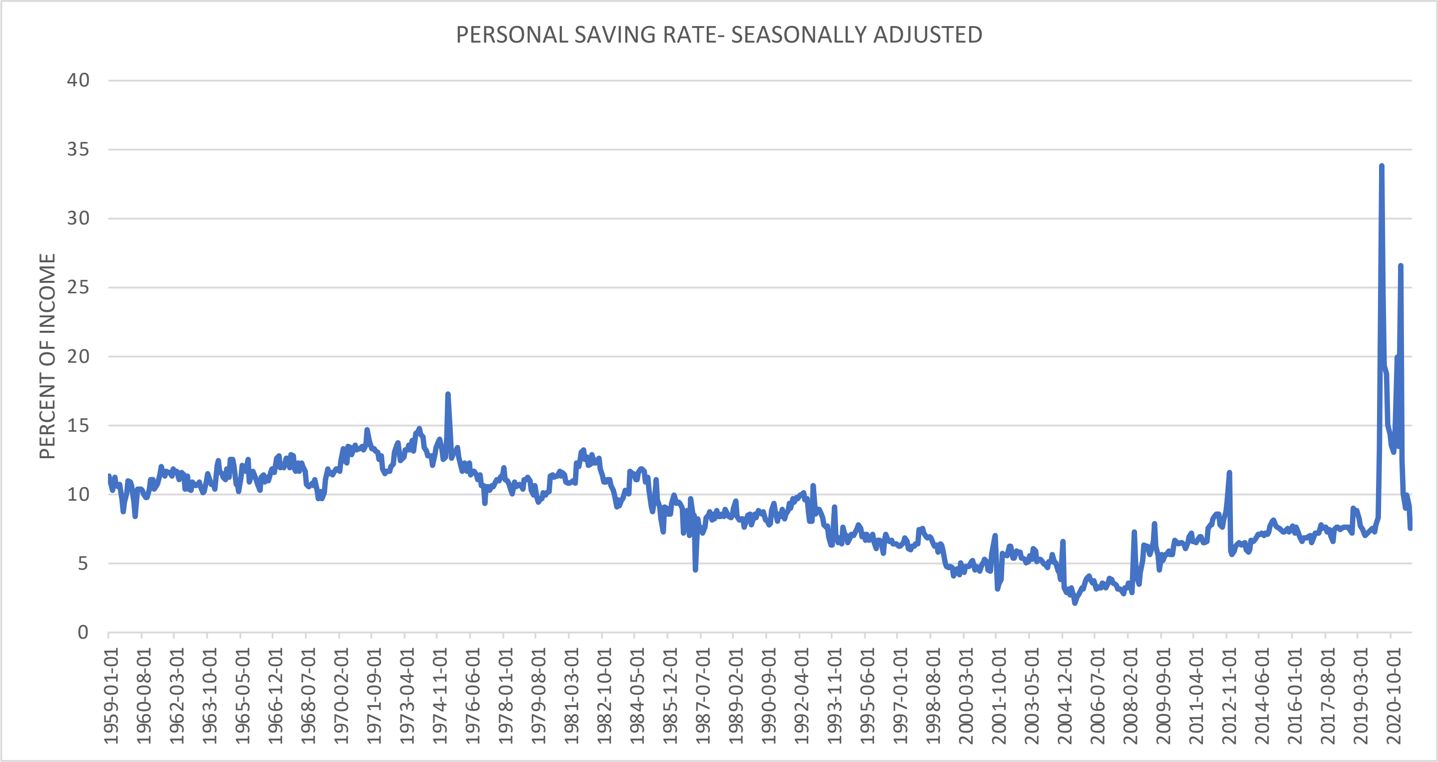
Inflation tends to have a regressive effect on lower-income families and seniors, as a greater share of their income is spent on consumer goods (most notably food and energy). It can also impact key variables impacting real estate, including the cost of debt, construction costs, and threshold rates of return. Higher interest rates would also increase the government's debt servicing costs.

Total personal income has been boosted by an unprecedented level of federal stimulus and assistance. Despite a significant reduction in employment and earned income, total personal income rose significantly during the pandemic-induced recession. While some of this fueled an increase in personal expenditures, most of this was reflected in a higher personal savings rate. Current estimates are that there is $2.5 trillion in "excess personal savings" since the start of the pandemic. The Oregon Office of Economic Analysis recently completed an instructive decomposition of how the excess savings have accumulated. The $2.5 trillion reflects a $1.1 trillion reduction in consumption and a $1.4 trillion increase in disposable income. The consumption of goods increased $420 billion, but this was offset by a $1.5 trillion reduction in expenditures for services. An estimated $550 billion drop in earned income was offset by roughly $2.0 trillion in federal aid.

TOTAL PERSONAL INCOME, OUTLAYS, AND SAVINGS

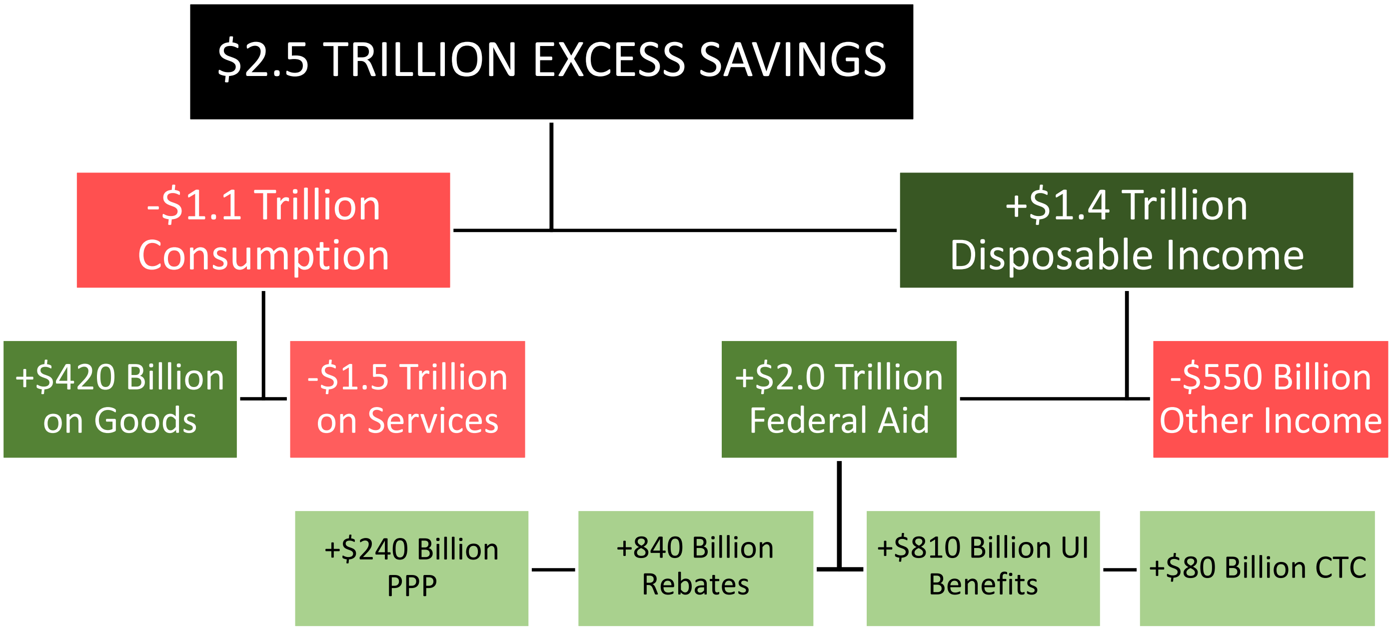


Bureau of Economic Analysis



Federal Reserve Bank of St. Louis

EXCESS SAVINGS BREAKDOWN



Oregon Office of Economic Analysis

The longer-term impact of excess personal savings is that consumers have a stronger balance sheet, which can support a sustained increase in consumption. Demand exceeding supply is likely to continue to place inflationary pressure on pricing, and current actions to further increase federal stimulus spending is likely to aggravate the underlying pressure by increasing aggregate demand further.

HOUSEHOLD FORMATION

Economic growth supports workforce and population growth, which then typically fuels household growth, which supports residential development. While population growth has remained positive nationally and in the metro area, we have seen residential demand that is greater than would be indicated by underlying population growth. At the national level we have seen occupancy in both ownership and rental units increase by roughly 2.0 million during the pandemic. The increased demand in the single-family market can easily be explained with an outflow from high-rent urban apartment markets, but it is more difficult to explain how the apartment market has been back-filled and even expanded during COVID.

We can think of a few factors that have contributed to the additional household formation. First, a reduction in roommates is likely part of the explanation. We have heard from several property managers that roommate arrangements became less popular as the pandemic unfolded. We assume this is mostly due to fears of COVID exposure, but possibly also due to "fatigue" in the relationships among roommates forced to spend more time together than initially conceived.

Similarly, we hear reports from divorce attorneys and other anecdotal information suggesting the same fatigue may have caused an increase in divorces. Data that might confirm this is not yet available. We do, however, have some data on young adults moving back in with their parents early in COVID, and then moving back out already by September 2020, with a net outflow by the end of 2020. Maybe here as well the "relational fatigue" was part of the cause. Though the higher number of unemployed should have slowed the rate of household formation, the lower household spending and additional cash infusion by the government has facilitated some apartment absorption among these young adults, even if it is via generous parents eager to help their children on their way – or maybe out of the parents' way.

One additional factor should be mentioned. The apartment market currently has an excess number of delinquent renters in occupied units, whether through the goodwill of property owners, eviction bans, or eviction protection programs. The share of renters who are more than 30 days past due has been two percentage points higher than pre-COVID in recent months. These renters contribute to the current occupancy. Without these two, the net absorption during COVID would have been lower than pre-COVID. Regionally, this segment represents 5,500 renters, compared to total above-trend absorption of 3,600 during COVID.

Nationwide, the two percent represent 550,000, compared to above-trend absorption of 250,000. In other words, evictions of delinquent renters could put downward pressure on occupancy and thus on asking rents going forward. Ironically, these renters might have made up for some of their missing payments by contributing to occupancy pressure and accelerated rent growth, allowing their property owners to collect more rents from the renters who are paying.

02

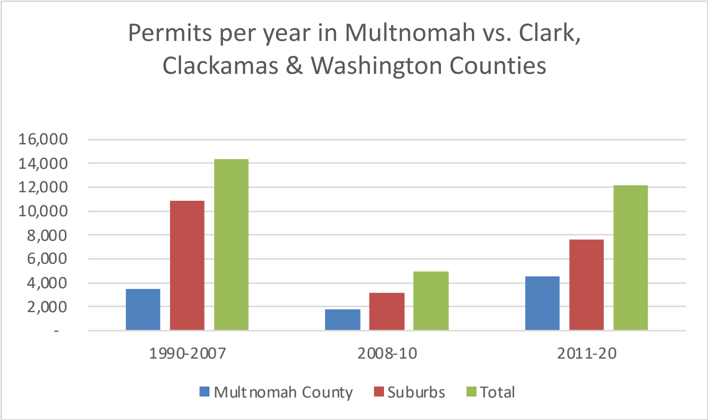
REAL ESTATE INSIGHT

Portland's Midas Touch

Gerard C.S. Mildner

Portland State University

Gerard C.S. Mildner is an Associate Professor of Real Estate Finance in the School of Business at Portland State University.



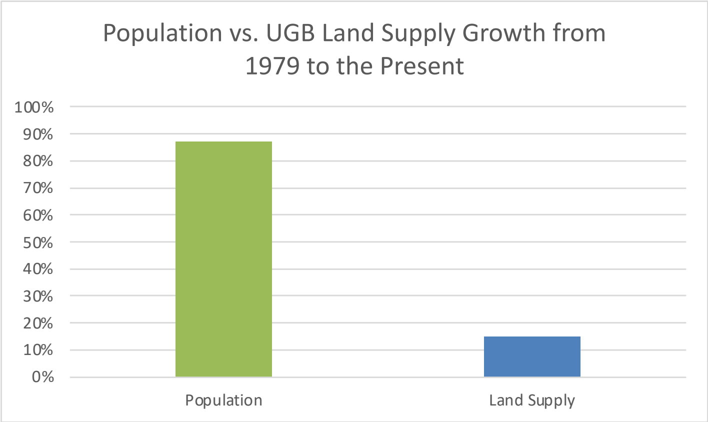
Housing appreciation is one of the biggest problems facing the Portland metropolitan area and the Willamette Valley. Among the 40 metro areas covered by the Case-Shiller house price index, Portland is the sixth fastest appreciating market in the US since 2000, sitting uncomfortably with places like San Francisco, San Diego, and Los Angeles. Unfortunately, most of our policy makers are focused on trying to mitigate the housing appreciation with expensive and ineffective subsidized housing programs, rather than treating the underlying factors behind the price increases.

Housing prices and rents in metropolitan areas are determined by supply and demand, and our demand factors are significant, but manageable. Each year, the metropolitan region grows by about 28,000 people, including net births and migrants from California and elsewhere. However, our growth rate is less than other markets, which experience little housing appreciation.

The explanation for Portland's Midas Touch is the lack of housing supply. If you look at 1990-2007, the 4-county region produced 14,300 housing units per year. In 2011-19, we produced only 12,200 housing units per year. That's a 15% decline, despite our much higher population base and substantially higher home prices and rents. Housing production is up in Multnomah County but down by 30% and 40% in suburban Clackamas and Washington County. Measured by structure type, we are producing much less suburban, single-family housing, which tends to offer more square footage than apartments. If I included the housing recession years of 2008-10 when we produced only 4,900 units per year, things would look worse.

Our housing supply problems begin with our outmoded land use planning system, which was designed by young Baby Boomers in the 1970's. The system we've inherited promises a system of well-defined community plans and a 20-year supply of developable land inside a flexible urban growth boundary (UGB), so that we would avoid the housing calamity of our neighbors in California. In theory, infrastructure is built to accommodate new development, and developers can proceed without the concerns of NIMBY objections.

In practice, the land use system has been manipulated so that NIMBY objections are raised to a regional level, blocking needed housing development. Since the advent



of the system in 1979, our regional population has increased by 87%, but the UGB has been expanded by only 15%. The Metro Council expanded the UGB by a meager 0.8% in 2018 and is waiting for a 5-year window to expire before reviewing that decision. For a region that grows in population by 1.3% per year, increasing the UGB by only 0.8% creates a pressure cooker in the land market. Our regional government, Metro, justifies this starvation land diet by measuring housing capacity by the theoretical level of housing production allowed by zoning, rather than the likely development outcome determined by cost of construction and consumer demand.

Metro leaders have succumbed to the belief that we can replace master planned communities on the suburban fringe (think Bethany, Forest Heights, Villebois, Reed's Crossing, Cooper Mountain, Happy Valley) with higher density projects inside the UGB. However, multi-family construction delivers space that's much higher on a square foot basis.

For apartment developers to switch from 2-story garden apartments to 5-story structures requires rents that are approximately 50% higher. Moving beyond 5-stories requires steel and concrete or mass timber construction, resulting in rents that are another 50% higher. And when we make expensive rents in high density apartments our marginal housing supply, we consign ourselves to California-style housing prices.

The potential for housing demand in the suburbs is enormous, but it is being suppressed by regulation. At the fringe, there's a 20:1 land price differential on either side of the UGB – 2-story construction on one side of the road, farms with grass seeds and strawberries on the other. An appropriate reform of our UGB system would recognize this gross misallocation of resources and devote more land for human habitation. That reform could preserve the high-value vineyards and farms that we all cherish, while at the same time create new corridors for growth, creating new housing options for Oregonians and new employment opportunities for skilled-trades workers.

At the same time, we should recognize and reform the many new barriers to development that have happened in the last four years: statewide rent control, Portland's harmful inclusionary zoning, design review delays, and permitting delays, among others. We should applaud the easing of single-family zoning by the state legislature and the efforts of Portland Commissioners Dan Ryan and Mingus Mapps to streamline permitting processes, but these are only part of the answer.

2022 promises vigorous primaries for both political parties to nominate a new candidate for Governor and a three-way race in November. Let's hope several of the candidates take up the banner for new housing construction.

03

COMMERCIAL MARKET

Office Market Analysis

Anthony Bertenelli
Portland State University

Anthony Bertenelli is a Master of Real Estate Development (MRED) candidate at Portland State and a Society of Industrial and Office Realtors (SIOR) Real Estate Student Fellow.

EMPLOYMENT OVERVIEW

In the third quarter of 2021, employees began to return to offices vacated at the start of the COVID-19 pandemic. This was due to slowly improving but still lackluster hiring by employers. Unemployment in Oregon maintained a quarterly average of 4.9% which matches the Portland-Vancouver-Hillsboro MSA. This statistic disguises a weak hiring recovery from the depths of the pandemic recession. As an example, the MSA gained just 1.4% manufacturing jobs year-over-year to a total of 121,500. The decline in the unemployment rate reflects not only employment growth but also a decline in labor force participation rate, with many workers leaving the workforce. Still, the trend towards lower unemployment and more employment gains are obvious, with the metro area unemployment rate dropping from 5.7% in April 2021 to as low as 4.4% in August 2021. Hiring in these circumstances can be best described as a slow, steady, and deliberate rollout.

During this quarter, employees from blue collar manufacturing to white collar professionals and technology companies returned to their offices across the Portland metro area. The return policies are best described as “hybrid” with each employer making staffing decisions on a case-by-case basis. An example of this hybrid approach was done by Daimler Trucks North America, which employs 3,000 workers in the Portland MSA. All of Daimler’s Portland workers are compelled to return to their offices but only for a limited number of days per week. However, the intentions of employers to begin to return to office operations are being stymied with concerns and demands from employees.

Many of these employees have adjusted to virtual employment and do not wish to return to old offices especially in the face of strong safety concerns. Not only does the downtown Portland business core have back-to-office COVID-19 concerns, but crime and public safety problems have grown far worse during the pandemic layoffs. The concept of a “soft reopening by invite” has become common with white collar professionals. In this case, employers bargain with workers over working-from-home provisions as a perk of employment. This hybrid soft reopening return model has also spread to government offices including the City of Portland, the State of Oregon, and many Multnomah County agencies.

One possible key limitation on job growth in the Portland area is a reported shortage of workers to fill available jobs, a frequent storyline in media reports and news broadcasts. Anecdotal evidence of worker shortages abounds, from restaurant owners who cannot fill shifts to factories which have curtailed some production hours. Yet, with an unemployment rate in Oregon at nearly 5.0% and a labor participation rate at a mere 62.4% there are plenty of unemployed people without jobs who don't seem to want employment or show concern that they are jobless. This employment paradox is frustrating state and local policymakers in Oregon who had hoped the expiration of extended pandemic unemployment benefits in September 2021 would spark a return of job seekers. This has not been the observable case in Oregon or nationwide. In fact, the reverse has occurred quite frequently with many workers expressly refusing return to the office callbacks and relying instead on part time employment, virtual side hustles, and other forms of online income.

OFFICE MARKET RATES

The office market improved in Portland in the third quarter of 2021, year-over-year and over the second quarter, but the overall office vacancy rate average remains historically high. At the end of the third quarter of 2021 suburban office vacancy was 9.7%. In contrast, the same rate in the Portland Central Business District ("CBD") was 18.4%. What is striking about these figures is their significant discrepancy. The suburban vacancy rate was up only thirty basis points year-over-year while the CBD rate was up a whopping 400 basis points in the same time frame. Part of this chasm in rates can be explained by large blocks of Class A space recently becoming available downtown (in total about 327,368 square feet) and stronger than anticipated leasing activity in the suburbs. For example, technology company Q5id signed a new 67,000 square foot lease in Hillsboro. It should be noted that Portland's 9.7% vacancy rate is the lowest rate for any major city on the West Coast of the United States.

SPACE DEMAND / DELIVERIES

Direct asking rents for Class A space now exceed $30 per square foot triple net in much of the Portland area with a metropolitan-wide average of $30.39. The highest metropolitan rates are in premier properties in Close-in Northwest and East of Broadway, which are often above $35 or more. What is most notable in the current Class A leasing paradigm is that there is plenty of new space on a square footage gross basis being constructed in the Portland metro region. There is also a perennial shortage of Class A space for lease even in the current pandemic environment. The reason for this paradox is that most of the new Class A office space was pre-leased before construction. For example, of the 370,000 square feet of newly delivered Class A space in Portland's CBD more than half has already been pre-leased. Another factor driving the Class A shortage in the suburbs is the fact the footprint sizes on many of the buildings are smaller. This means that tenants who want large blocks of Class A office are relegated to more urban areas like Portland's CBD, since this is where the larger footprints can be found.

However, not all the news on the Portland Class A office front is good. While there is a significant amount of pre-leased space, commercial demand for Portland Class A going forward is projected to be historically weak. Portland was regarded as the third best market for office development out of eighty U.S. markets surveyed by the Oregon Office of Economic Analysis in 2017. Today, Portland is ranked 66th out of 80. Even considering the rank of #3 in 2017 to be a statistical outlier, the drop in national standing for Portland office development is still staggering. Portland currently ranks low not only for projected tenant demand but also investor demand for office investments in the area. This means that the availability of debt and equity capital is projected to be tighter and more costly. By these estimates, the historic economic expansion of downtown Portland which began in the mid-2010s may have run its course. These statistics are currently reflected in the Portland construction activity crane count which has dropped in half in just one year.

TOP UNDER CONSTRUCTION

Property	Address	Submarket	SF	Owner	Delivery Date
Intel Expansion Project	2501 NE Century Blvd, Hillsboro	Sunset Corridor/Hillsboro	1,500,000	Intel Corporation	4Q 2021
Ridgefield Industrial Center	S Union Ridge Pky	Clark County	468,793	Specht Properties, Inc	2Q 2022
Portland - Hillsboro 3	4091 NE Constable St, Hillsboro	Sunset Corridor/Hillsboro	358,000	Flexential	4Q 2021

SUBLEASING MARKET

Portland's subleasing market is still strong, but it is coping with the large blocks of Portland CBD Class A office space which were abandoned or went vacant during the early days of the pandemic. So-called

"doomsday driven" bargain priced deals are becoming more difficult to find as desirable empty spaces are slowly filled. Still, there is plenty of sublease space available in Portland. In the third quarter of 2019 there was just 750,000 square feet of Class A available for sublease across all of Portland. That number reached 1.6 million square feet in the second quarter of 2021, and today this number has fallen to 1.47 million square feet.

The trends in the office subleasing market, especially in the CBD, bode well for the overall Portland office leasing market for the next few quarters. Of the ten largest Class A leases signed in the third quarter of 2021, five have been for sublet space. This fact is consistent with the overall absorption rate for office space in the Portland metro area at negative 459,435 square feet. At first glance, this looks worse than it is, since much of this sum is merely from space listed as "available" in previous quarters now considered "vacant".

Portland currently has 424,700 square feet of Class A office space under construction and another 230,305 of office space under substantial renovation. However, the bulk of these properties are in the CBD or nearby, not in the suburbs where much of the new demand for Class A is situated. Also, these CBD office properties under construction still conform to the traditional mix of office, condo, and retail components which has been growing increasingly unpopular with tenants and investors, especially given the collapse of the retail sector in the CBD during the pandemic.

TOP LEASE TRANSACTIONS FOR 3Q 2021

Property	Submarket	SF	Sale Date	Landlord	Tenant
4800 NE 30th Ave	Sunset Corridor/Hillsboro	269,975	August 2021	Trammell Crow Company	GXO Logistics
14300-14340 N Lombard St	Rivergate	242,250	September 2021	Port of Portland	Undisclosed
2001 Kotobuki Way	CBD/West Vancouver	142,800	July 2021	Port of Vancouver	Western Partitions

The current Class A office market in the metro area is a case study in submarkets, especially Class A in the CBD versus the suburbs, but also Class B which saw greater vacancy rates during the height of the pandemic and is now rebounding even slower due to bargains available at the Class A level. The submarket fragmentation is often striking. For example, there is currently more than 60,000 square feet of Class A space available at 300 Fore Street in Portland but no space above 10,000 square foot available elsewhere in the neighborhood.

Despite the volume of leasing activity, the drop in transaction volume has been profound especially with respect to large new leases for Class A. For example, only one lease of more than 100,000 square feet, the new Sunlife building at Portland Foreside, was signed for office space in the Portland metro area in the third quarter of 2021. Given current sublease supply and new Class A under construction, it may be another two years or more until another lease of more than 100,000 square feet of office is signed.

RESOURCES

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04

COMMERCIAL MARKET

Industrial Market Analysis

Rodrigo Flores

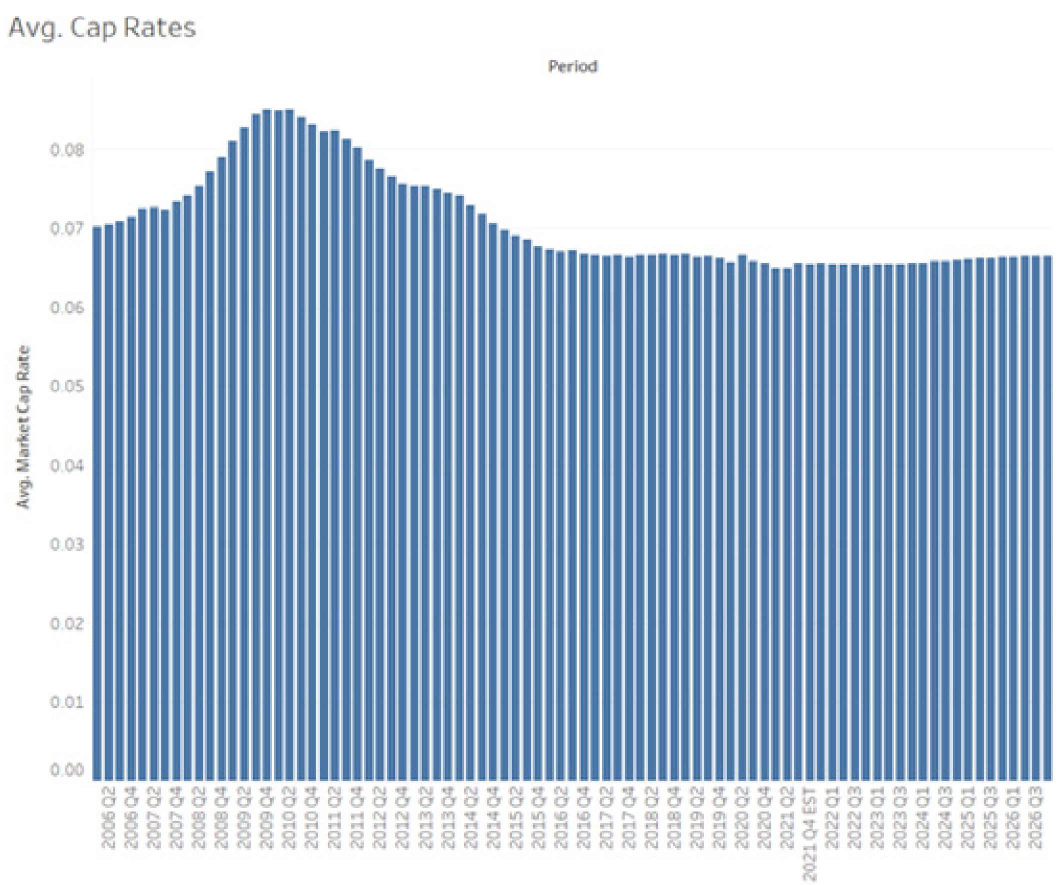
Portland State University

Rodrigo Flores is a graduate student in the Master of Real Development (MRED) program and a TigerStop Real Estate Student Fellow at the Center for Real Estate.

The industrial sector has been one of the darlings of the pandemic over the past year, and it has continued to be a robust sector of the industry in the third quarter of 2021. Demand for industrial space continues to outpace the supply across the country.

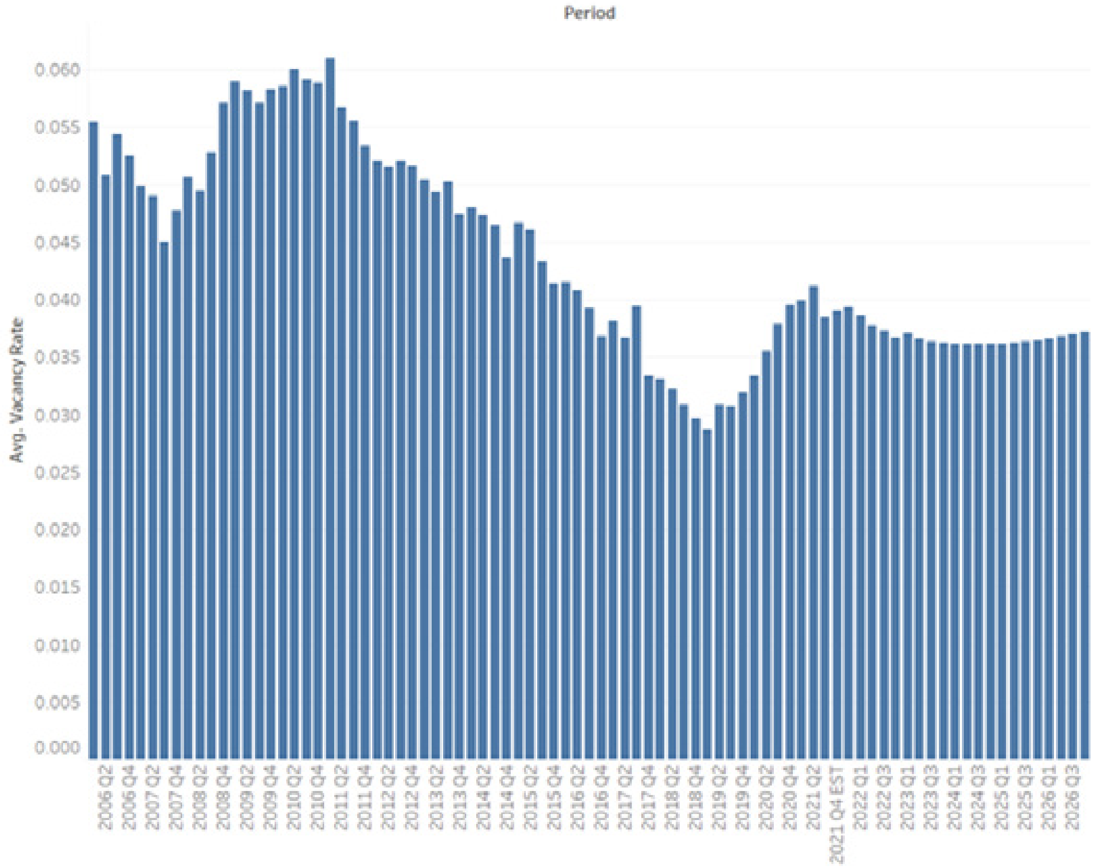
With sustained low vacancy, higher lease and absorption rates, the allure of the industrial product type is expected to continue (Commercial Edge). Among the many drivers of demand for industrial space, shifting consumer preferences toward e-commerce and changing supply chain dynamics from "just in time inventory toward just in case," are expected to bolster the industrial property type (CBRE).

This positive outlook is evident in NAIOP's most recent Sentiment Index where 62.7% of respondents said they expect to be most active in the industrial sector over the next twelve months (NAIOP). These favorable market conditions have precipitated an increase in the number of institutional investors interested in industrial assets. Greystar's acquisition of Thackeray Partners earlier this year (Greystar) and Amazon's continued commitment to industrial space in the Portland region are examples of this (Costar). These trends will be further explored by examining the Portland industrial market.



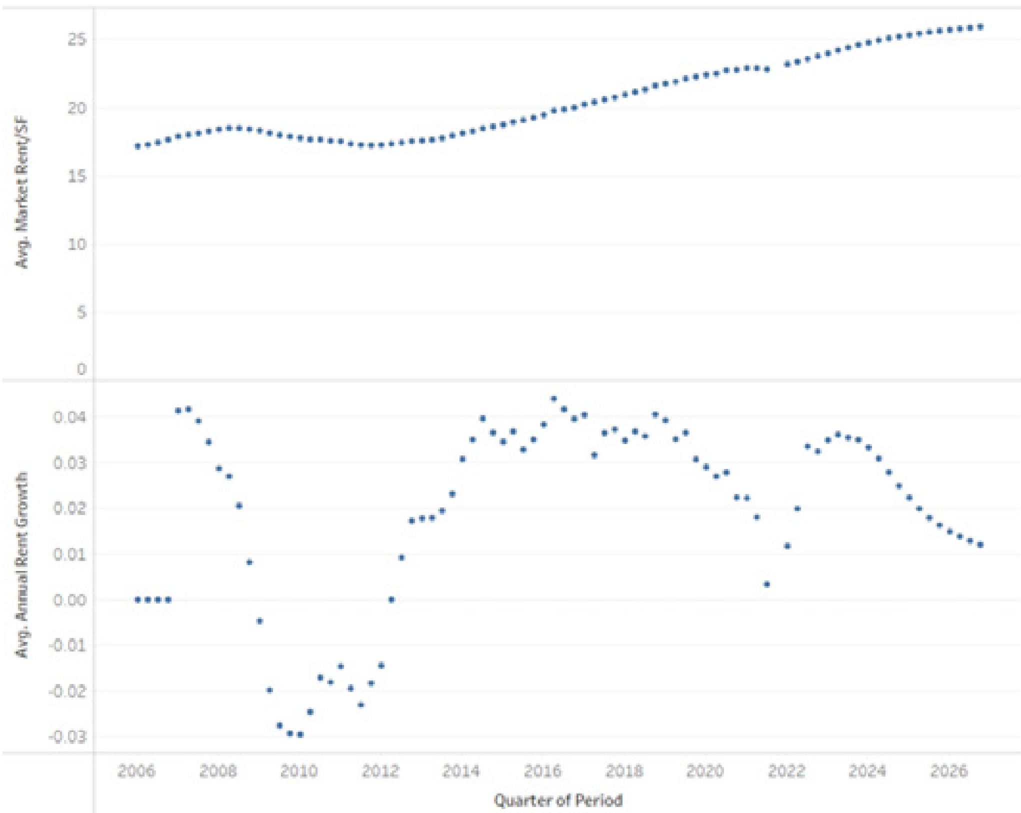
Average of Market Cap Rate for each Period.

Avg. Vacancy Rate



Average of Vacancy Rate for each Period.

Avg. Rental Rate



The trends of average of Market Rent/SF and average of Annual Rent Growth for Period Quarter. Details are shown for Period. The view is filtered on Period Quarter, which keeps non-Null values only.

The Portland metropolitan area has experienced the industrial renaissance firsthand. The growing population and demographics of the region continue to be major drivers for industrial development in the area. In the third quarter, cap rates remained flat at 5.8%, vacancies continued to tighten to 4.6%, and rents increased at the fastest rate since 2016 (JLL). From a logistical perspective, the rise of e-commerce has kept demand for warehouse and distribution space high and there is steady absorption of these speculative spaces in the Portland market. These strong market fundamentals in concert with the region's growing population have trended up in recent years.

This steady growth has made the region hard to ignore, and institutional investors are increasing their presence in the region. The percentage of industrial properties over 50,000 square feet held by owners of at least 30 properties has nearly doubled over the past five years (IBID). These dynamics can help explain Amazon's continued investment in the region: totaling more than $7.5 billion in investment in the region since 2010. The e-commerce titan is expected to expand its presence in the region with projects in Woodburn and Canby over the next few years.

The increase in institutional players in the Portland market is not the only factor keeping rents up though. Land availability also plays a role in determining rents. The increased demand on existing inventory will likely keep rents high and push development toward the fringes of Portland's urban growth boundary (JLL), or to exurban locations such as Woodburn, Ridgefield and Canby. The lack of available industrial land has limited the expected deliveries for next year and will likely promote demand-induced compression of vacancy rates and increase rental rates for industrial space (Colliers).

Scarcity of available land coupled with increasing demand from institutional capital will likely continue to sustain record high escalation of industrial rents.

The industrial sector is expected to continue its renaissance into the foreseeable future, which begs the question: how long can this sector run so hot before it burns out? Increases in institutional capital and physical scarcity of suitable land will keep industrial rents rising, but tenants' ability to meet rising rental rates is dependent on their profitability and further contingent upon continued consumer spending. In a market still distorted by the threat of inflation, supply chain disruptions, and a shifting labor force, continued profitability of industrial tenants may be a limiting factor to this sector's growth rate in the long-term.

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05

COMMERCIAL MARKET

Retail Market Analysis

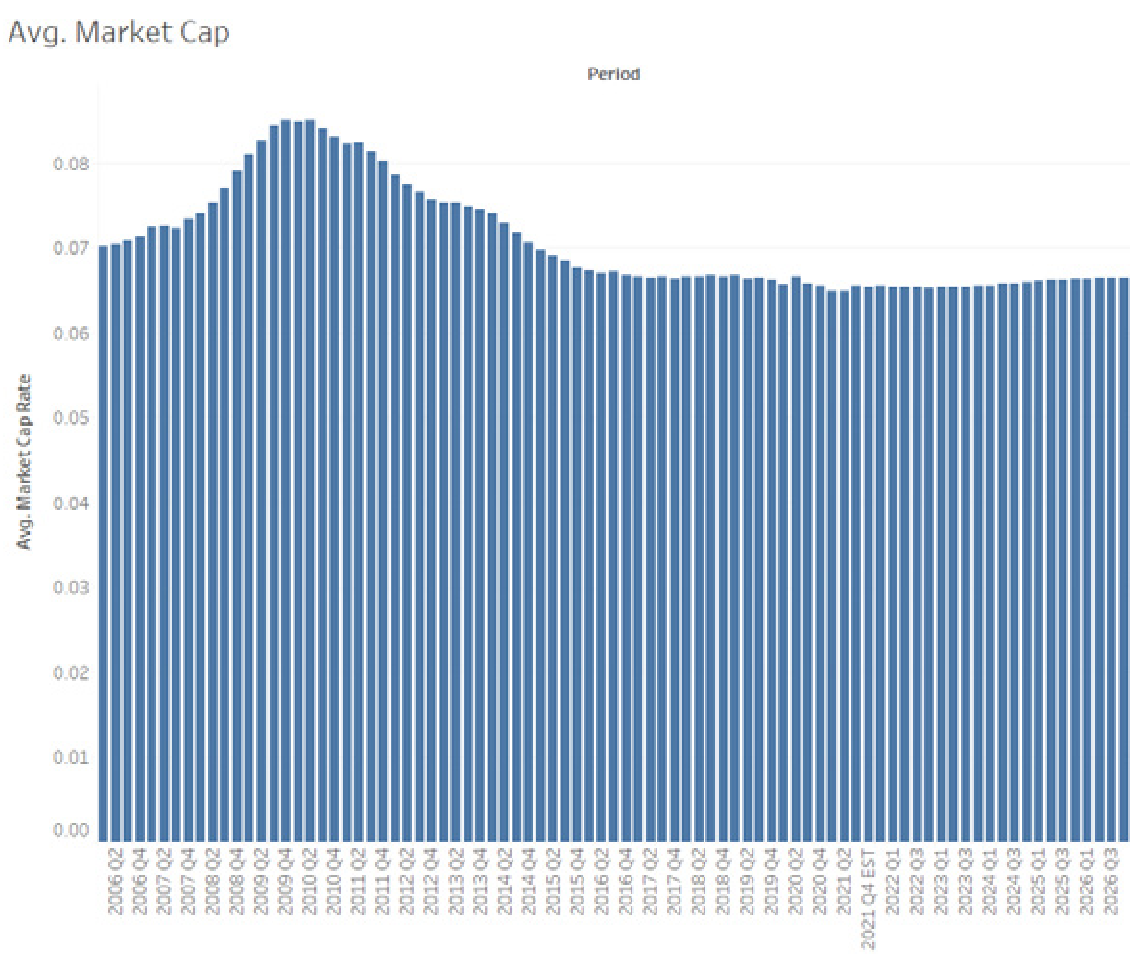
Rodrigo Flores

Portland State University

Rodrigo Flores is a graduate student in the Master of Real Development (MRED) program and a TigerStop Real Estate Student Fellow at the Center for Real Estate.

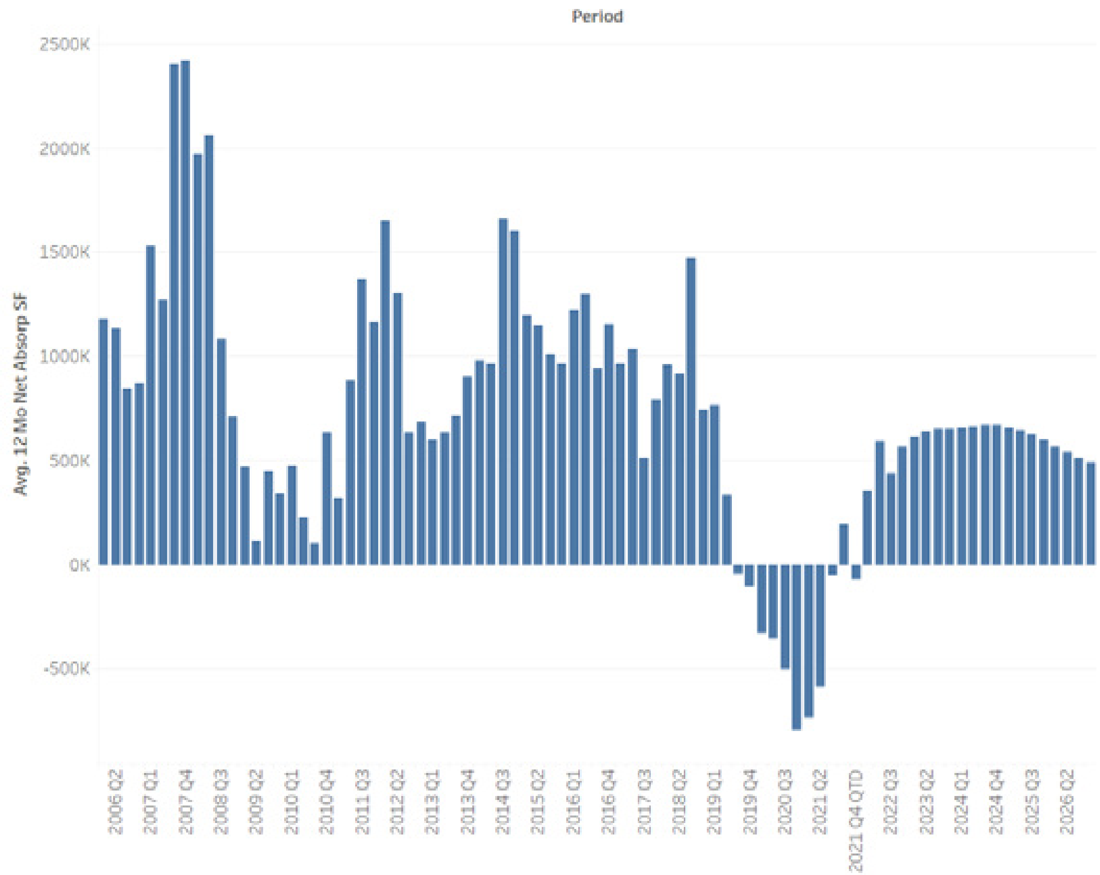
The retail sector has continued its steady rebound from the pandemic induced lows of the last year. With pandemic-related restrictions largely lifted and vaccines widely distributed, foot traffic is expected to pick back up and drive the retail sector's incremental recovery into the holiday season. The retail sector is not just on the rebound, it is changing. Demand for retail space remains in flux as retail strategies continue to evolve to suit recovery-era consumer preferences. Across the country, e-commerce has been driving a major change in retail for years and the pandemic expedited this process.

The transition from traditional retail toward hybrid, experiential, and fulfillment-oriented retail spaces is a point of interest for retailers as they look to adapt to a post-COVID economy (CBRE). Moreover, pandemic restrictions and the increased acceptance of telework have disproportionately affected central business districts and impacted their daytime populations. (ULI). These trends in concert with rising inflationary concerns, declining consumer sentiment, and ongoing supply chain issues are changing the retail landscape and putting significant stress on retailers to adapt. These factors at the national level are also playing out locally, and this article will explore them.



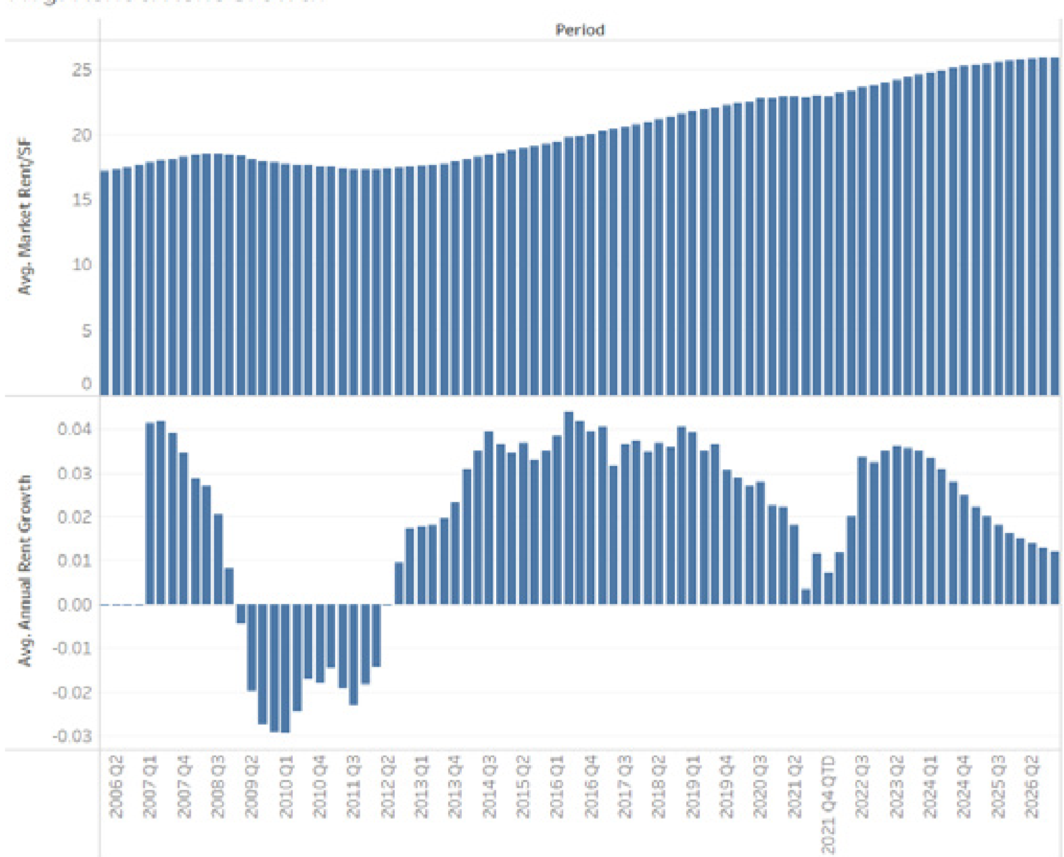
Average of Market Cap Rate for each Period.

Avg. 12 Mo Net Abosbtion



Average of 12 Mo Net Absorp SF for each Period.

Avg. Rent & Rent Growth



Average of Market Rent/SF and average of Annual Rent Growth for each Period.

Portland's retail sector continues to recover from many of its pandemic-induced impacts. Although Oregon lifted most of its pandemic health and safety restriction at the end of June, concerns over the Delta variant stymied the recovery. Demand for retail space this quarter showed signs of improvement as vacancies fell to 3.8% and sales were the highest since the fourth quarter of 2019. Average asking rents fell to $22.79 per square foot, and absorption remained negative during the quarter, although it is trending in the positive direction (Costar). The Portland retail market is undoubtedly recovering from its pandemic woes, but structurally it is still reckoning with the prominent rise of e-commerce, much like the rest of the country.

For years, retailers have seen an increasing share of online sales at the expense of brick-and-mortar locations, and the pandemic accelerated this trend (UN). Consumer preference for e-commerce is expected to lead to continued decrease in the demand for retail space. As a result, many malls and stores across the country that were struggling before the pandemic were set for closure by the end of 2020. Portland's long struggling Lloyd Center mall is a local example of this trend as its foreclosure has been recently announced by KKR Real Estate Finance Trust Inc. (KGW8). Traditional retail centers like the Clackamas Town Center and Washington Square are having to innovate toward experiential or hybrid retail spaces in order to compete with online retailers (Colliers). While e-commerce alone did not drive the Lloyd Center to foreclosure, retail spaces like the Lloyd Center has been on the decline, and the convenience of e-commerce is a part of the new normal.

Retail's shift to a more online presence is not the only trend affecting the demand for traditional retail space. Another trend that is influencing the retail market is the change in daytime populations in commercial and business centers. Pandemic-related health and safety restrictions sharply increased the level of remote working, with telecommuting likely to remain for many job types. As a result, sales haven't just been going digital, they are also being dispersed from central business districts toward less densely populated suburban and residential localities (Mastercard Economics Institute). In tandem with e-commerce, competition from surrounding shopping centers likely aided in the Lloyd Center's ultimate foreclosure.

The retail industry is still pivoting to match the needs of the recovery. As a result, many shopping centers may share the same fate as the Lloyd Center as this product type is primed for redevelopment.

The retail sector is expected to continue its transformation and incremental recovery into the new year. Heralded as a retail apocalypse in the pandemic, the sector is still showing signs of life as it continues to recover in 2021. The resilience of the sector is being challenged again as changes in consumer shopping habits are forcing the industry to adapt to the new normal of e-commerce. Retailers who can show ingenuity and accommodate the changing environment they exist in are poised to capitalize on the latest evolution in the retail industry.

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06

RESIDENTIAL MARKET

Rental Housing Market

Jason Guralnick

Portland State University

Jason Guralnick is a graduate student in the Master of Real Development (MRED) program and a TigerStop Real Estate Student Fellow at the Center for Real Estate.

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

INTRO

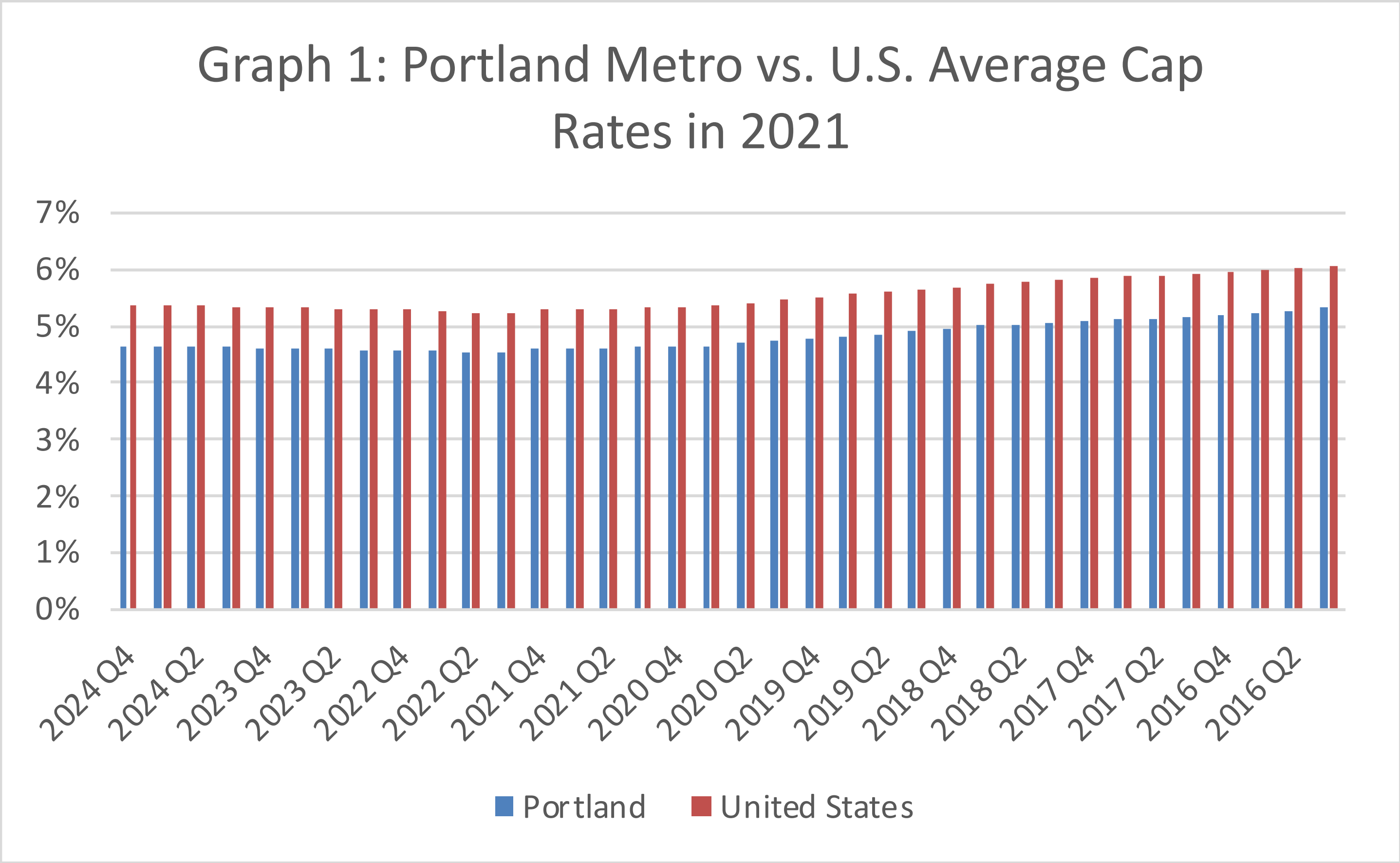
Portland's multifamily sales have been impressive this year as the market is about to eclipse the previous record from 2016 of $2.9 billion. Currently, of the eleven west coast metro areas with at least one million residents, only Fresno has cheaper average apartment rents than the Portland metro area. Vacancy and concessions have receded to pre-pandemic levels adding to the strong fundamentals that continue to drive investors into the Portland market. The Portland metro area experienced a massive construction boom over the past decade, but with global supply chain issues and rising construction and labor costs, there is a risk that supply will not be able to keep up with future demand.

According to a CoStar report, "vacancies in Portland are already declining at the fifth-fastest rate among the nation's largest metropolitan areas. So far in the third quarter, Portland's vacancy rate has declined by 0.7%. Only Orlando and Fort Lauderdale, Florida; San Jose, California; and Nashville, Tennessee, have posted greater rates of compression over the same period." Low vacancies and rising rents have led to record breaking sales prices on a per-unit basis.

Cap rates have continued to decline year-over-year and remain below the national average. New groups of investors to this market are recognizing this and are seeking out opportunities within the market at a record pace. At one time, supply seemed overwhelming, but it now appears to be insufficient to keep pace with future demand. High construction prices, new zoning regulations, and extended permitting times are warding off new development within the city of Portland, but opportunity remains in the suburbs.

CAPITALIZATION RATES

The overall average cap rate for the Portland metro market for 2021 is 4.6%, which is significantly stronger than the national average of 5.2%. When comparing the submarkets within the metro area, Hillsboro, Wilsonville, Sherwood/Tualatin, and Tigard have recorded the lowest cap rates of 4.2%, while East Portland has the highest cap rate at a still impressive 5.2%. The Downtown/ CBD submarket held strong at 4.5% which is the same rate for Clark County, Beaverton, and NW Portland. This article will continue to dive into the factors that are contributing to a decreasing cap rate environment including, but not limited to: increased asking rents and expectations of escalation, lower vacancy rates, and high absorption.



SALES ACTIVITY

Portland is closing in on a record-breaking year for sales, eclipsing the $2.9 billion mark set in 2016. Larger suburban developments changed hands in addition to urban high rises. Two of the most active players include Greystar and The Wolff Company with each spending over $600 million in the market. Jeff Sakamoto, VP of Development for The Wolff Company believes, "Portland will continue to experience long term growth," due to its "strong underlying fundamentals," and that, "when compared to other west coast markets, Portland's cost of living is still affordable." Following is a list of the ten biggest sales in the metro area.

LARGEST SALES OF 2021 IN PORTLAND METRO

	Apartment Name	Address	Buyer	Seller	Sales Price	Sale Month (2021)	Cap Rate at Sale	Vacancy at Sale	Units	Sale Price Per Unit	GBA (SF)
1	Seven West at the Trail	"14790 SW Scholls Ferry Rd., Beaverton, OR"	Greystar Real Estate Partners	La Salle Investment Management	$145,250,000	October		3.60%	423	$343,381	347,240
2	Zera @ Reed's Crossing	"7001 SE Blanton St., Hillsboro, OR"	MG Properties	Holland Partner Group	$120,000,000	June	4%	5.25%	324	$370,370	324,000
3	Arbor Creek	"3280 SW 170th Ave., Beaverton, OR"	BentallGreenOak	Security Properties, Inc.	$115,250,000	October			440	$261,932	338,040
4	Avana One Zero Nine	"3708 NE 190th Ave., Vancouver, WA"	Greystar Real Estate Partners	Vista Investment Group	$104,000,000	August		6.90%	387	$268,734	340,500
5	Avana @ Happy Valley	"8800 SE Causway Loop., Happy Valley, OR "	Greystar Real Estate Partners	Brookline Investment Group	$93,000,000	June	4.60%	3.80%	372	$250,000	236,280
6	Arc Central	"12875 Crescent St., Beaverton, OR"	St. Regis Properties	Rembold Companies	$77,000,000	May	4.10%	3.50%	230	$334,783	245,888
7	Anthem PDX	"1313 E Burnside St., Portland, OR"	The Wolff Company	Alliance Residential Company	$75,620,000	September		5%	211	$358,389	166,400
8	Bridge Creek	"29697 SW Rose Ln., Wilsonvile, OR"	TIAA-CREF	TruAmerica Multifamily	$72,000,000	January	4.85%	8%	162	$228,571	192,357
9	Ella	"3833 SW Bond Ave., Portland, OR"	The Wolff Company	Alamo Manhattan	$71,500,000	June		7.04%	199	$359,296	184,285
10	Sky3 Place	"1221 SW 11th Ave., Portland, OR"	The Wolff Company	Molasky Ventures	$71,000,000	July		9.18%	196	$362,245	224,000

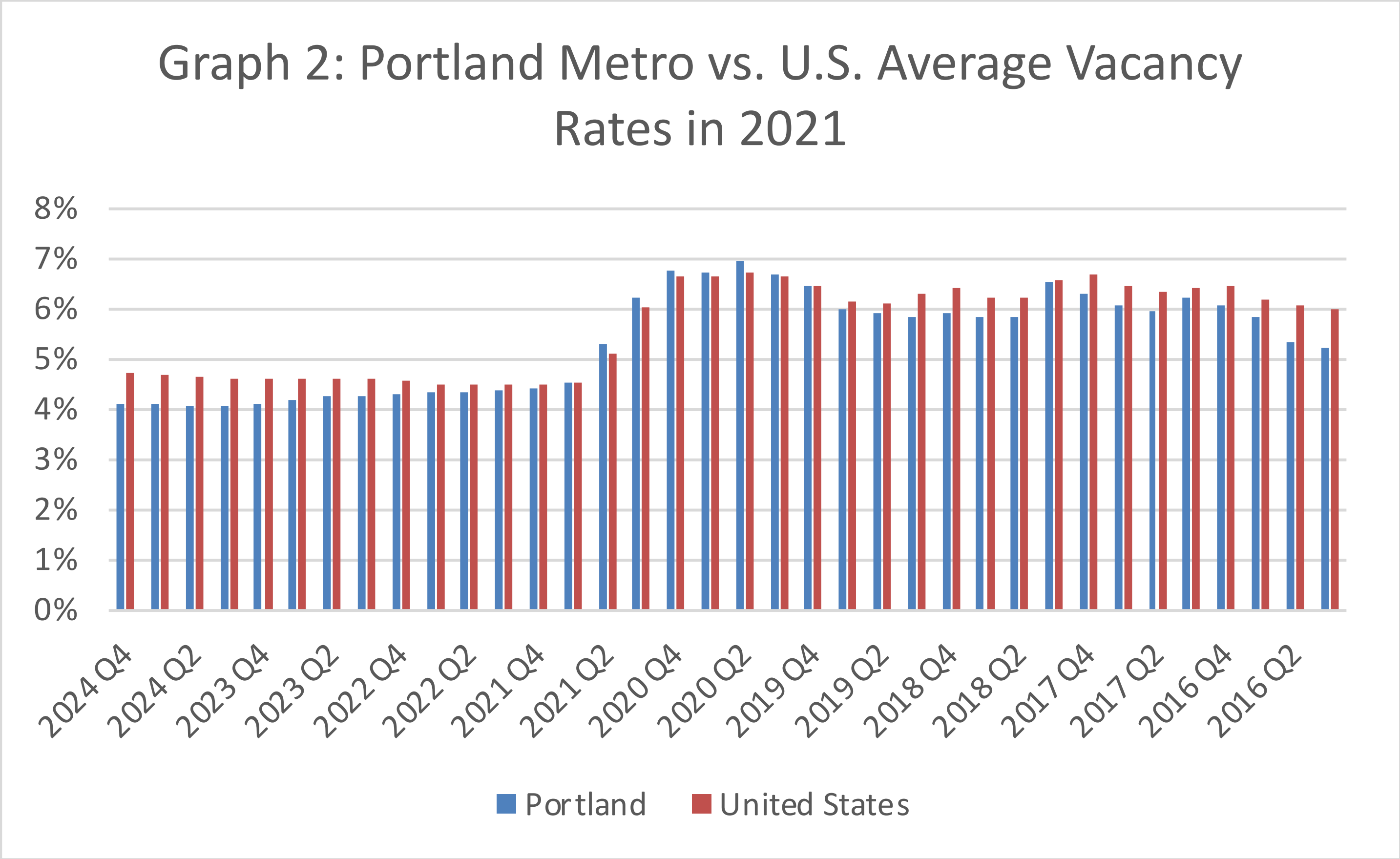
Average sales price per unit also set a record this year of $285,000 per unit. Zera at Reed's Crossing a 324-unit community located in Hillsboro achieved an outstanding $370,000 per unit. All this activity in the region drew international attention as Canadian REIT Bentall Green Oak purchased Arbor Creek, a 440-unit transit-oriented community in Beaverton for $115 million. Lastly, institutional investor TIAA-CREF purchased Bridge Creek a 162-unit community in Wilsonville as part of a portfolio purchase. Bridge Creek when purchased was 8% vacant and priced at a 4.8% cap rate in January.

Vancouver has accounted for over $600 million in sales in the metro region. Consistent with the larger metro area, multifamily investment slowed in the early months of the pandemic, but a flurry of large deals closed this year. Multifamily investments are increasingly drawn to Vancouver in the wake of Oregon's new rent control law and increasing regulations in the City of Portland. Throughout the past ten years, most Vancouver trades have involved private investors and were valued under $10 million, but institutional transactions are now becoming more common. Since the start of 2010, the market price per unit has tripled, while cap rates have compressed by close to 300 basis points.

DEMAND AND ABSORPTION

Vacancy rates in the Portland metro continue to decline, dropping from 4.8% in the second quarter of 2021 to 4.4% in the third quarter. The Downtown/CBD submarket, which experienced the greatest vacancy swing during the pandemic, dropped from 11.6% to 8.7% this quarter, indicating that stabilization is imminent. During the pandemic, some tenants exited the urban area for the suburbs and have been slow to return to the city. The level of highly marketable urban amenities in the CBD are reduced with less daytime population in the office spaces.

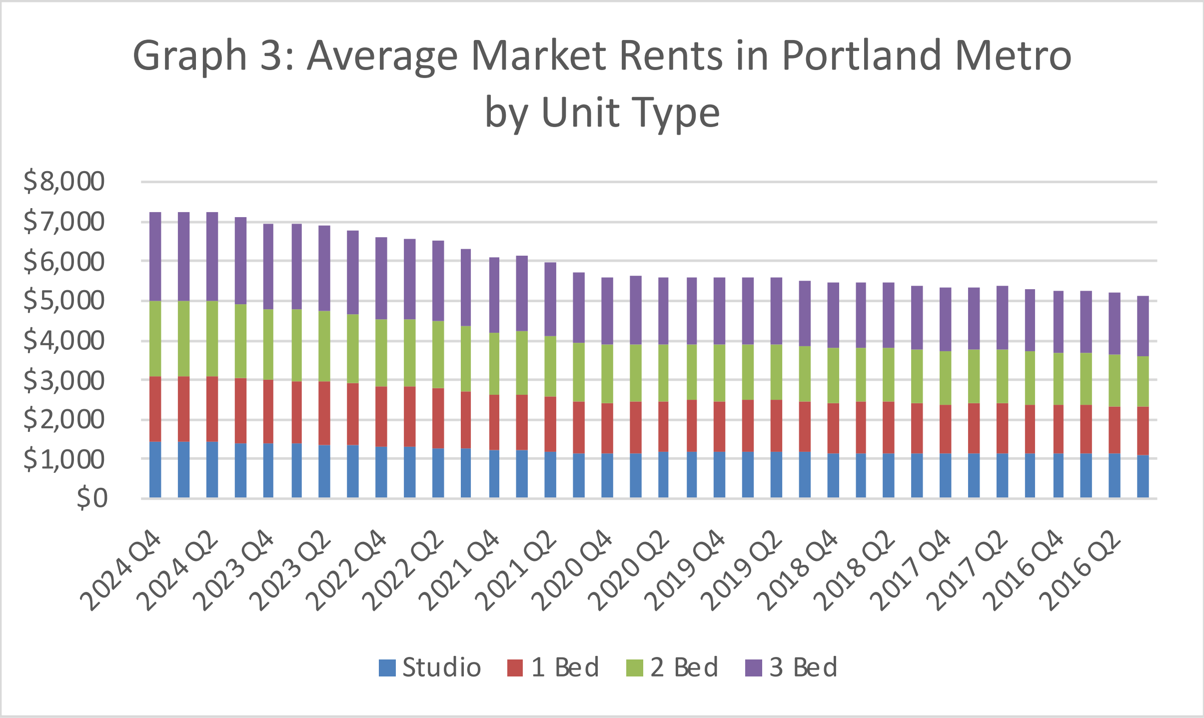
There are five submarkets with vacancy rates below 2.5%, which includes Tigard, Lake Oswego/West Linn, Oregon City, East Vancouver, and West Vancouver. The submarkets with the highest vacancies include NW Portland, Downtown/CBD Portland, SW Portland, and N Portland/St. Johns. The submarkets with the highest vacancies are almost all urban and areas that have experience the highest rates of construction in recent years. Graph 2 shows that CoStar's analytics are predicting Portland's vacancy rate to drop below the national rate in the coming months.



Throughout the past year Vancouver has led the way in net absorption with over 1,900 units absorbed. The Downtown/CBD submarket, which suffered negative absorption in 2020, has had 1,320 units absorbed in 2021. According to CoStar, “Renters comprise just over 45% of Portland households,” a significant shift from the historic norm that can be attributed to homeownership being out of reach for many. Portland’s median home price remains well above the national figure. The Urban Growth Boundary was expanded in December 2018, but new single-family residential construction remains limited, especially in areas with access to an urban lifestyle. People searching for suburban properties have found a shortage of affordable, well-located homes. Because of this the rental market will continue to grow. Vancouver continues to lead the metro market in all categories as $640 million in sales occurred in this submarket this year.

RENTS

As of the fourth quarter of 2021, average rent levels in Portland are trending upward at a brisk pace. After considerable losses in the early and later months of the pandemic, a strong spring and summer leasing season has helped to boost the market. Average market rent metro-wide is currently $1,520 per month. More detail by unit size is summarized in Graph 3. The average year-over-year rent growth in the metro area was 9.0%, compared with the national average growth of 10.7% over the same period.



Portland's outlying suburban communities continue to post the strongest rent growth. As renter preferences shifted and the importance of a central location diminished during the worst of the pandemic, tenants found suburban apartments more appealing. The reduced importance of commuting and the need for a home office space supported the shift in preference. This is still boosting demand in suburban areas and allowing property owners to push rents at a rapid clip. Notable, significant year over year rent growth includes the submarkets of Vancouver (22.5%), Wilsonville (16.8%) and Hazel Dell (15.3%). In contrast, rates in the Pearl District only rose 4.9%.

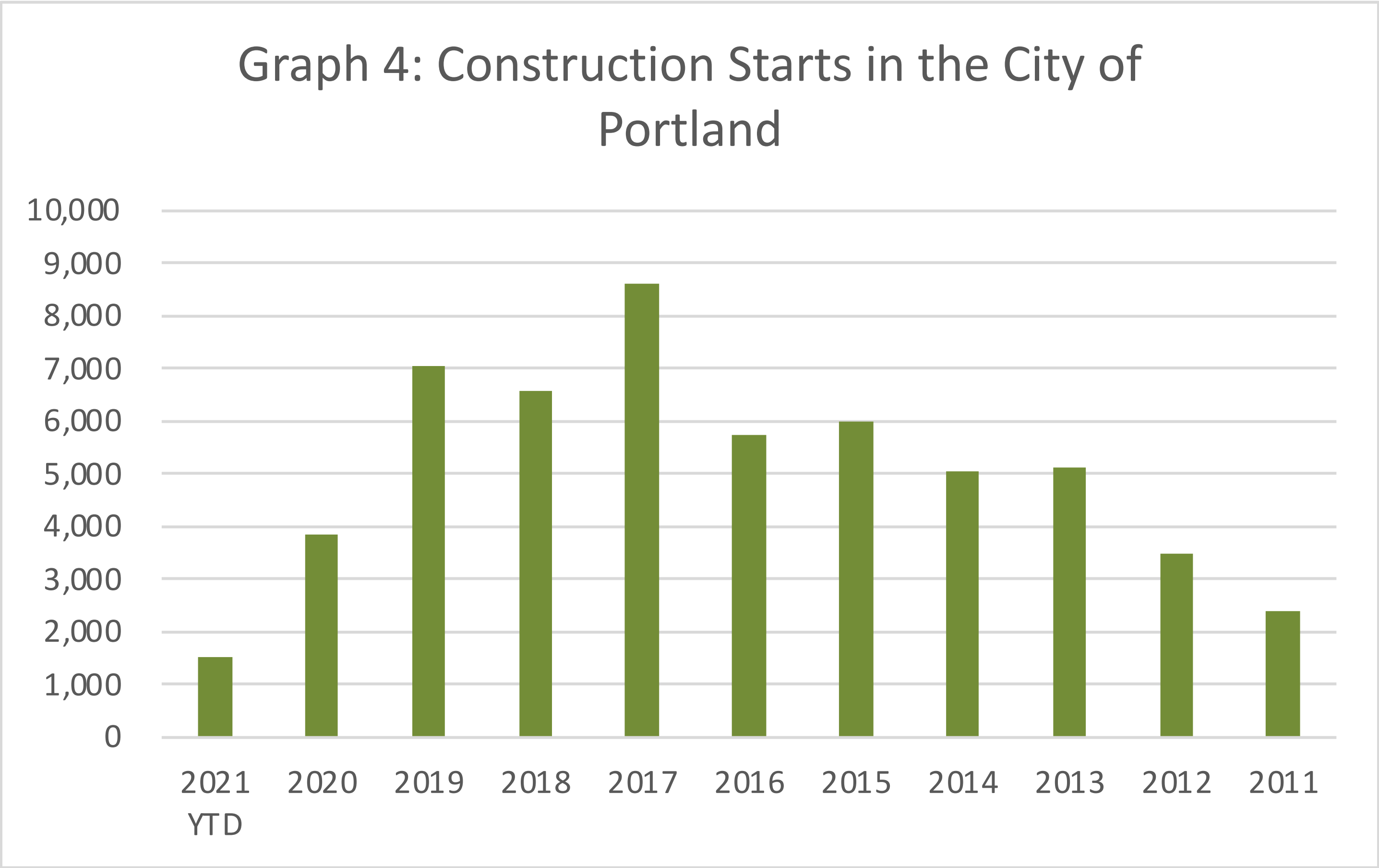
SUPPLY AND PERMITTING

The Portland metro area has approximately 8,000 units under construction as of August 2021, with 76% aimed at high-income earners. In addition, the metro area has an estimated 37,850 units in the planning and permitting stages. As of August, the City of Gresham led the way with 748 units across five projects underway, Vancouver has 572 units coming soon, and Goose Hollow 492 units.

Alta Art Tower will account for 314 units being delivered in Goose Hollow. As a side note, Alta Art Tower will be the first high-rise built incorporating the city of Portland's inclusionary housing ordinance. The building will feature three-bedroom units as well as units available to those earning less than the area median income. Building with the inclusionary zoning resulted in a FAR of 8.5 to 1 for this project (allowed FAR was 9:1, part of the project involved restoration of the attached Artists Repertory Theatre).

Construction starts hit a ten-year low of only approximately 1,500 units starting year to date in 2021. According to an article published October 13, 2021, by KOIN6 news, "The City of Portland currently has 848 commercial permits and 1,585 residential permits waiting to be issued." One developer even told the reporter that, "they will no longer build in Portland because it took the city three-and-a-half years to issue permits for one of their housing projects."

Because of issues like this, "Commissioners Mapps and Ryan are now leading a task force that aims to streamline the process," (Nadrich, 2021). In the summer issue of the Quarterly, it was reported that, "Construction costs continue to not only remain high but are higher than national averages; Portland's metro is ranked third highest in construction costs behind New York City metro and Washington DC metro." This continues to remain true as costs have inflated 5.7% this year compared to 2020.



LOOKING FORWARD

Despite the ongoing pandemic, multifamily rental housing in the Portland metro area has recovered and is growing once again. Steady job growth coupled with relatively affordable west coast living has kept the Portland metro a desirable place to live. The Vancouver submarket has led the way in year over year rent growth, vacancy decline, construction starts, cap rates, and sales. Vancouver will continue to remain attractive for investors as Oregon's rent control bill and Portland's inclusionary zoning do not affect this part of the metro area. There is still desire from consumers to live in transit-oriented communities within Portland's metro area, but due to the City's logjam with permits, developers will start seeking out projects along these transit corridors within the suburbs. The City of Portland should continue to see more sales as residents now fill once-empty buildings at higher rents and with less concessions.

In this analyst's opinion, multifamily developers should seek opportunities in the fringe suburbs of Portland, but near transit, or major employers such as Intel, Nike, and Columbia, as job growth remains steady, and construction can be done timelier and more cost effectively. Many have recognized opportunities in Vancouver and capitalized them into pricing, which is making finding new opportunities expensive. The City of Portland is very desirable for buyers looking to get into a market that shows signs of steady year of year rent growth and occupancy. Lastly, the Portland metro area is lagging in meeting its housing needs, creating a vacuum for rising rents. If this continues unchecked for too long, Portland will no longer be considered an affordable west coast option.

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07

HOUSING INSIGHTS

Portland's Development Landscape: Opportunities and Limitations of HB 2001

Jordan Mulvihill
Portland State University

Jordan Mulvihill is a graduate student in the Master of Real Estate Development (MRED) program at Portland State University and an Oregon Association of Realtors© student fellow with the Center for Real Estate.

In August 2019, Oregon made history by becoming the first state to essentially end exclusive single-family zoning. House Bill 2001 now allows for duplexes in cities with more than 10,000 residents, and up to fourplexes and cottage clusters for cities with over 25,000 residents. Following suit, California recently passed Senate Bill 9 which lets any single-family lot to be split for the creation of duplexes. Minneapolis, Austin, and Seattle have also adopted similar amendments to single-family zoning restrictions at the city level. Albeit highly contentious, discussions about zoning reform are underway across the country.

SINGLE-FAMILY ZONING REFORM IN STATES AND MUNICIPALITIES

STATE LEVEL

map source: pixy.org

MUNICIPAL LEVEL

map source: pixy.org

Taking HB 2001 a step further, Portland's Residential Infill Project now allows up to four units on any residential lot, or up to six if low-income housing is included. To help encourage these small-scale developments, the City has set up a System Development Charges Exemption program for developers who either cap sales prices at $412,000 (qualifying buyers only) or rent at allowed rates for 60% median family income households. Passed in tandem with HB 2001, SB 458 requires cities to allow homes in middle housing projects to be divided into individual lots for homeownership opportunities and creates a uniform, streamlined process for the review and approval process of land divisions.

All of this creates new opportunities for housing development, but also highlights certain shortcomings.

One of the primary objectives of these new laws is to encourage homeowners to develop ADUs on their own properties. This group is most incentivized by the new changes and most benefitted from conventional sources of financing. But while these new entitlements allow homeowners the option to subdivide lots for sale, the additional cost and risk associated with condominium conversion will likely keep many of these ADUs as rental housing. For this reason, development at this scale will benefit the rental market by putting more units online. However, it will not meaningfully contribute to local homeownership opportunities.

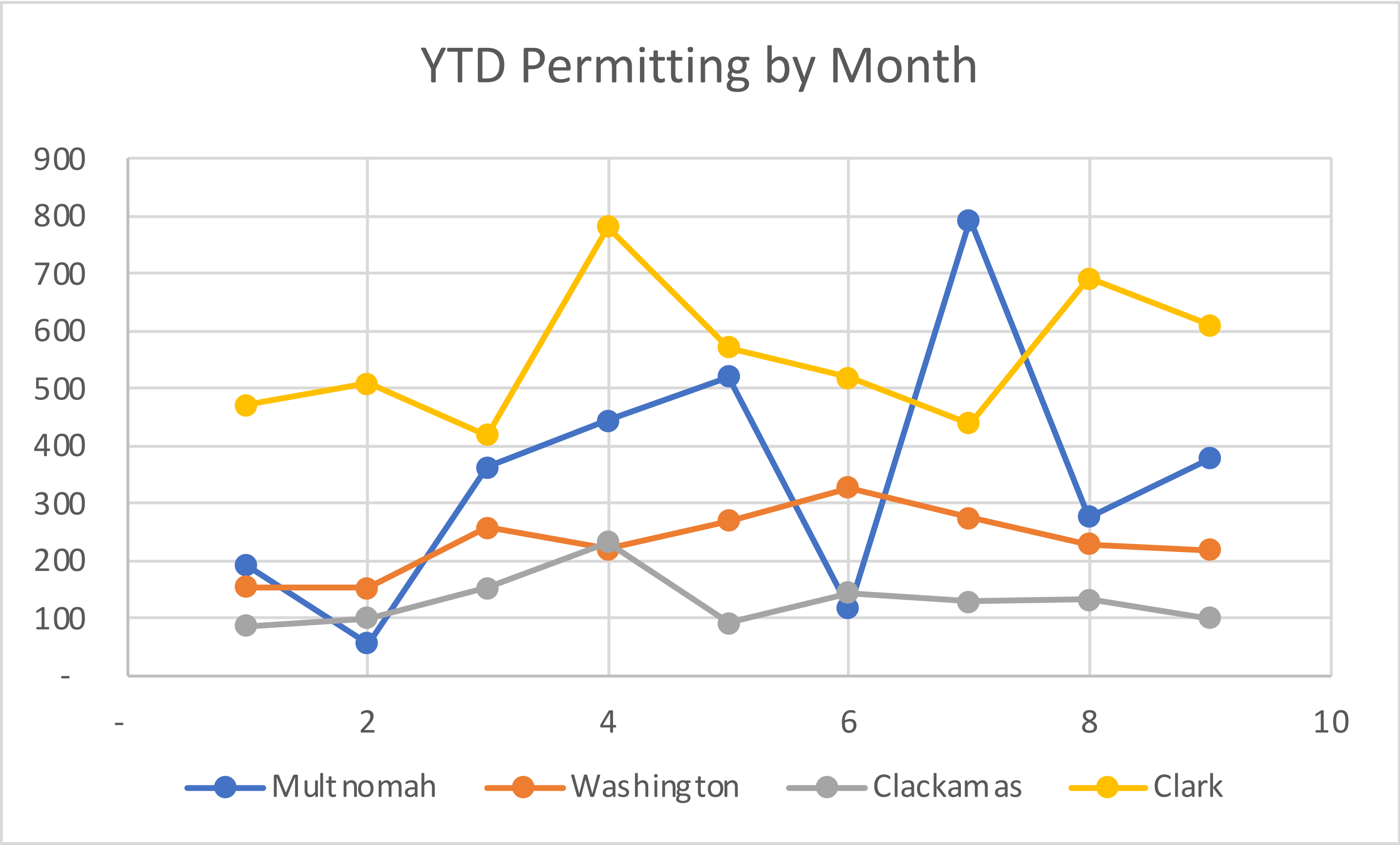
Non-owner-occupied developers – who are the more likely to take advantage of new zoning opportunities and more meaningfully contribute to the housing supply – face more challenges than homeowners developing in their backyard. Unlike large scale developers with access to inexpensive (subsidized) debt, small- and medium-scale developers need to rely more on cash up front, equity investors, or lines of credit on collateralized properties to fund their projects. Without that, the most accessible source of capital are private equity funds, wealth funds, and hedge funds. These "hard money" loans have more expensive interest rates and are often considered a last resort. Missing middle housing development is going to need better access to conventional financing sources to help HB 2001 make its intended impact.

Financing aside, there are additional reasons why developers are reluctant to build missing middle housing. First off, vacant land in Portland is expensive and hard to find. The land division process is slow and costly, although that will theoretically be improved with the passing of SB 458. The corporate activity tax on projects over $1 million make duplexes and triplexes difficult to pencil. Subsequently, scaling up to fourplexes triggers commercial codes and additional development fees. But the greatest hurdle cited by local "for sale" developers are the varying impacts of construction defect litigation associated with condominiums.

Recognizing the serious need for condominium liability reform to promote a diversity of housing types, Washington passed SB 5334 in 2019. SB 5334 amended current laws by reducing the personal liability of condo-association officers, who could previously be sued for defect repairs if they themselves did not sue the builders before the window expired. It also raised the the bar for what owners can sue over. Condo owners will now have to prove not only that the defect exists, but also that it would cause harm or an unreasonable safety risk. Passing similar amendments to Oregon's condo laws can enhance HB 2001's impact by complementing urban infill initiatives, creating new home ownership opportunities, and promoting a blend of housing types.

Despite certain limitations highlighted by HB 2001, single-family zoning reform's long-term benefits are numerous. It is the first step in acknowledging and undoing a racist legacy of housing discrimination, one which has deeply exacerbated inequities in wealth, health, and education. It also promotes environmentally responsible growth by limiting sprawl and maximizing public infrastructure investments. It allows for a diversity of housing types which can increase naturally occurring affordability. Additionally, single-family zoning reform expands property rights and entitlements. The list goes on and on. But as exciting as all this change is, it's going to take time before its benefits can be meaningfully quantified.

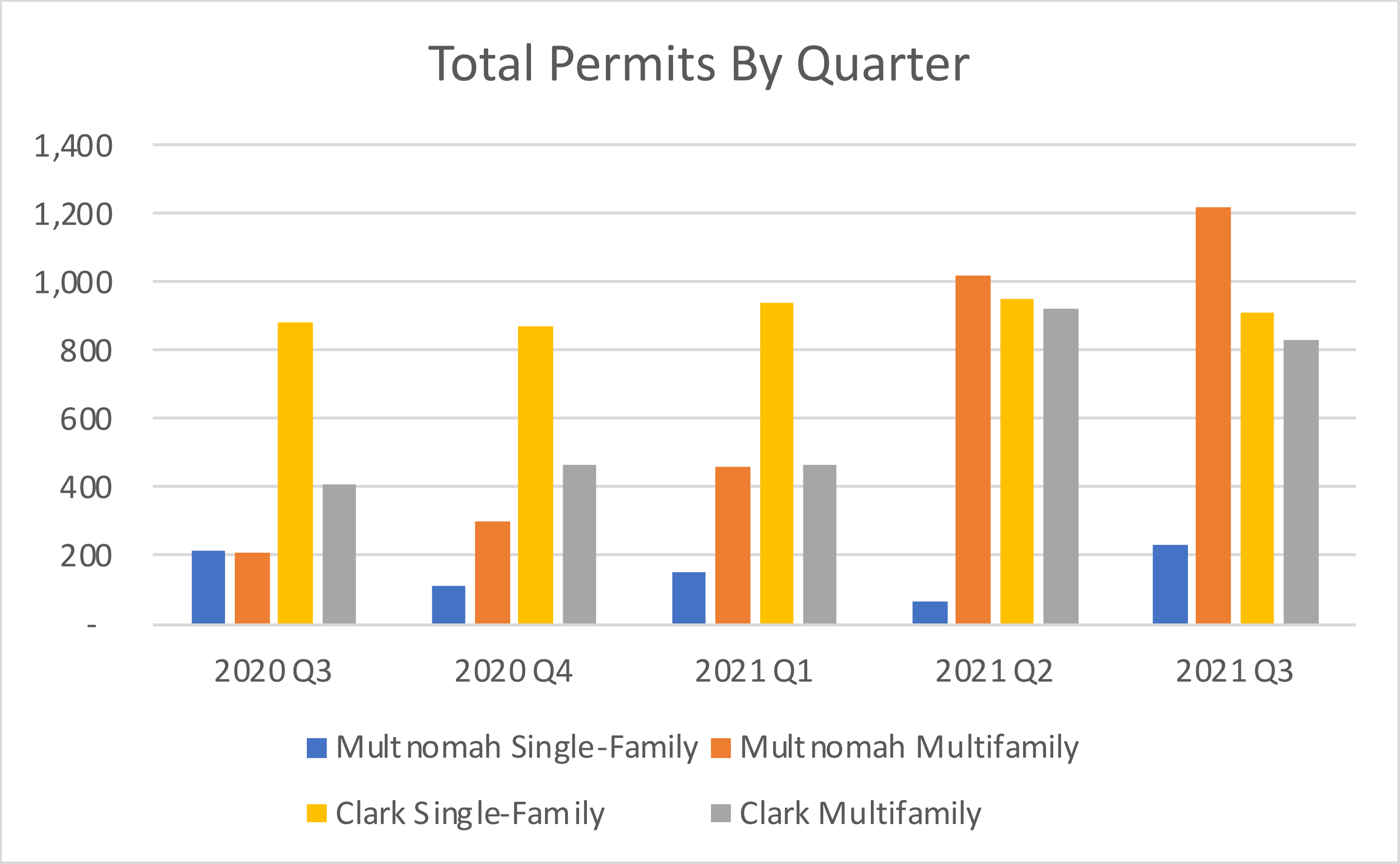
As a society, we have traditionally relied on large-scale developers to produce sizeable complexes in dense urban cores. The developers get to capitalize on economies of scale and the cities get housing, a "win-win." But this model, alongside single-family zoning restrictions, inadvertently established an unsustainable dichotomy of housing of types. Since the focus has now shifted on promoting missing middle housing, there also need to be changes that promote the missing middle developer. Because without the favorable financing awarded to large corporations, or being able to capitalize on size, small- and medium-scale development will be off to a slow start. HB 2001 is a bold first step into unchartered waters, and the rest of country will be watching to see how it plays out. *CodeNEXT, Austin's first revision to their land code development code in over 30 years, is currently on hold as it's being challenged in court



As permitting data for the third quarter was recently published, it was a relief to see that the four-county area is on track to close out 2021 with a stronger performance than 2020. Clark County's steady growth continues to make up the greatest share of permitting activity, with 1,741 permits filed representing 41% of the total. Continuing a much-anticipated rebound, Multnomah trailed Clark with 1,448 permits files (34%) while Washington (17%) and Clackamas (8%) filed 723 and 363 permits, respectively.

Vancouver's development boom continues to go strong with little signs of slowing. While remaining more or less steady, year-over-year permits filed is up 26% from Q3 2020. Of the 1,741 permits filed, 53% are for single-family homes, continuing the trend of Clark County as a more attractive homeownership opportunity than its neighbors in Oregon. Multifamily fundamentals also remain strongest in the market and are forecasted to continue attracting institutional interest to the area.

On the other end of the pendulum, Portland is finally starting to show positive signs of market growth. July 2021 had the most permitting activity since 2019, an optimistic signal that the pandemic pause might be slowly easing. Total permits filed this quarter is up 71% from last year with a steady upward trend. In contrast to Clark, 21% of the third quarter's permits were for single-family while 79% were for multifamily. However, Multnomah County filed 130 single-family permits in Sept 2021, the most since June 2016 (155). While more data is needed, this could be an early indicator that Portland's SDC waiver program is working as intended and more ADUs are already in the pipeline.



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08

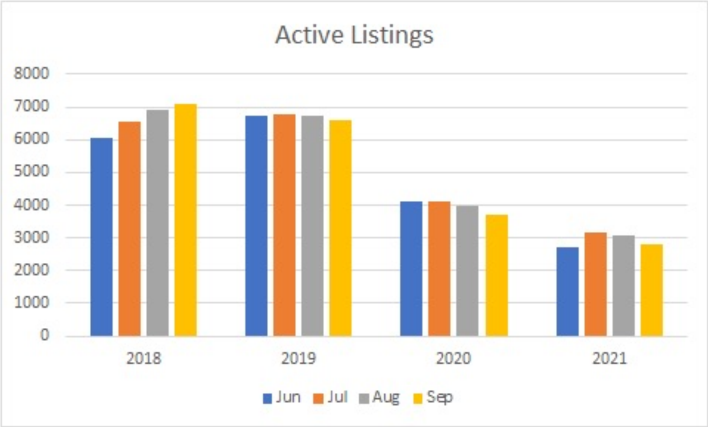
RESIDENTIAL MARKET

Ownership Housing Market

Parker Webb

Portland State University

Parker Webb is a candidate in the Master of Real Estate Development (MRED) program and a Regional Multiple Listing Service (RMLS) Student Fellow.



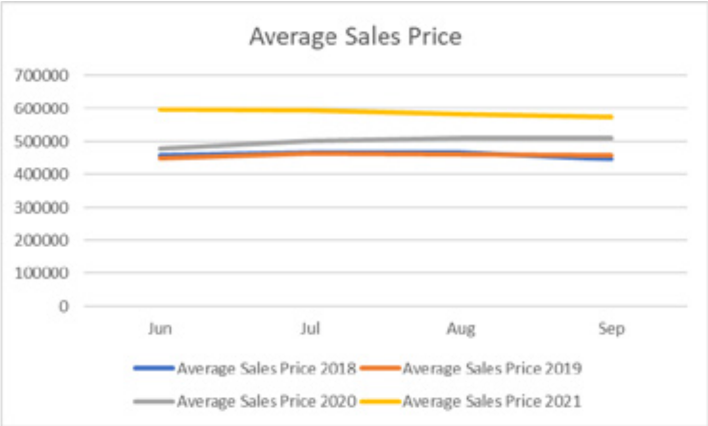
Even with the struggles caused by the COVID-19 pandemic, the ownership housing market in the Portland metropolitan area is strong. There has been a high demand for homes, and the total number of homes on the market has consistently decreased since the yearly high in June 2021. While there has been a decrease in homes on the market, the homes that are on the market are taking more time to sell. Janet Eastman states, “Sellers are still in the power position, but asking prices are dropping for homes that linger on the market” (The Oregonian).

The article Portland Housing Market: Prices, Trends, Forecast 2021-2022 by Marco Santarelli gave insight into how the average sales price differs by submarket in the Portland metro. He also gave a good example of how each section of the Portland Metro housing market contrasts to each other when it comes to average sales price. By far, the regions with the highest price homes is Lake Oswego/West Linn with an average sales price of $760,000. The region with the lowest average price of single-family homes are SE Portland at $500,000 and Hillsboro/Forest Grove at $500,500.

When looking at the demographics of these parts of Portland, it isn’t surprising that there is an 81.6% rate of home ownership. Almost 89% of homeowners in West Linn are married while only 11.1% of married couples are currently renting in West Linn. Hillsboro has significantly different demographics with a homeownership rate of 28%, in contrast to the 53% rate in West Linn. For married couples, the ownership rate is only 64.7% while the renting rate is 35.3%. This shows that the demand for families buying homes in West Linn is much higher than in Hillsboro because these residents can afford to purchase a home when it makes more sense to rent in Hillsboro.

PORTLAND METROPOLITAN AREA

The median sales price in Portland was $460,000 at the beginning of the year. These numbers continued to increase each month through August, which recorded the yearly high at $524,900. This trend stopped in September when the median decreased by $14,900 to $510,000, reflecting a 2.8% decline. The median sales price hadn’t dropped since December 2020 when there was a modest 0.44% decrease according to Regional Multiple Listing Service (RMLS). This decrease is caused by the increasing amount of time houses are on the



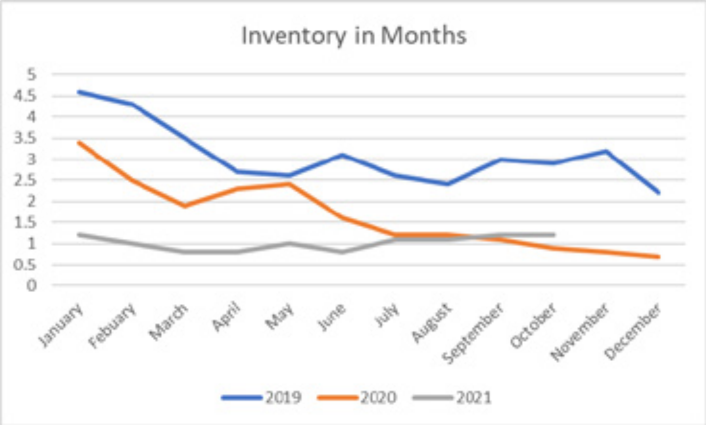
market. Sellers are willing to continue to lower their asking price to try and reach a buyer's needs. The number of active listings hit a yearly high of 3,180 in the month of July. Going into August and September there has been a slight decrease. August active listings were at 3,066 which was a 3.6% decrease from the previous month. This trend continued into September at 2,819 which was an 8.1% decrease from August.

Broker Dustin Miller states that we will face a lot of uncertainty in the economy with rising interest rates and inflation's negative effect on the market. Although as of right now the homes are not selling as fast as they have in the past, the Oregonian quotes Jeff Tucker who gave his insights on the inventory of homes, "Homes are still selling quickly and prices have not receded, but it's not quite as extreme a sellers' market as we saw back in the spring and summer." August is most likely going to be the peak of the market in 2021. Looking at 2020's median days on the market, January was at an all-time high at 37 days, according to RLMS. Going into the third quarter of 2021, the days on the market decreased to an extremely low nine days in September.

The Portland metro has had a consistent increase in average sales price starting at $514,428 in January and rising to a yearly high of $596,152 in June. The beginning of the third quarter had a shift in prices and the market reported a slight decrease in average sales. Going into July, there was a 0.6% decrease in average prices to $592,505. These numbers continued to decrease as time went on by 1.6% in August and 2.0% in September. The current average sales price for single-family homes stands at $571,483. As expected, these numbers are much different compared to the 2020 pandemic. It is not surprising that March, April, and May had the lowest average sales prices at $465,500, $477,400, and $467,500. Since then, the housing market experienced a strong recovery with a steady increase in pricing. "Experts see this seasonal cool down as a welcomed trend after an unpredicted, scorching-hot residential real estate market during the coronavirus pandemic" (Eastman, The Oregonian).

SALEM/KEIZER METROPOLITAN AREA

Similar to Portland, the costs of homes have been consistently rising in Salem. The median sales price prior to the third quarter in Salem/Keizer metro had a slight increase that peaked in July at $412,400. Since



July, there has been a modest decrease in single-family homes, which declined 0.51% in August to a median price of $410,278. September had an even larger decrease of 4.87% with a median price of $390,300. At the beginning of the year, The Salem Metropolitan area median sales price was $347,305 according to RMLS. This is about $43,000 below September because the prices have been consistently rising throughout the pandemic. These prices are expected to continue to rise going into 2022.

The market in Salem is not as competitive as Portland but there are still more buyers than homes available. Most of the Pacific Northwest is experiencing an inventory shortage. Portland and Seattle are suffering the most, but it is also affecting smaller cities like Salem. Looking at Polk and Marion Counties as a whole, the inventory in months is having a slight increase. June 2021 was reported at .08 and this number jumped to 1.2 in September 2021. The pandemic had a significant impact on inventory because January of 2019, the inventory in months was at 4.6 and the market has not reached that number sense according to RLMS.

LOOKING AHEAD

Looking into the future, home prices are expected to continue to grow. According to Zillow, from September to the end of the year 2021, the value of homes is expected to go up 4.4%. This would reflect a 19.5% increase from the end of the year 2020. Throughout the pandemic the value of homes has skyrocketed, and we are seeing no signs of that slowing down. Along with the increasing values, Zillow is also predicting a 15.2% increase in home prices going into September 30, 2022.

"As of now, Portland is a "seller's market" which means that there exists a limited supply of homes, and buyers are forced to compete often resulting in higher prices and/or quicker sales that tend to benefit sellers. That's the reason why Portland metro home values have gone up 19.2% over the last 12 months and Zillow predicts they will continue to rise at roughly the same pace in the next twelve months." (Santarelli, Norda). The demand for homes is already very high.

In the future I can only see this demand increasing with the inventory staying the same. This will lead to an increase in prices which forces buyers to either settle for a home that is completely above their budget or wait until the market goes back down. If buyers continue to wait, then the number of days on the market for single-family homes will also continue to increase. Realtor Stephen FitzMaurice gave his insights on how mortgage rates will adjust going into 2022, “mortgage backers (like Freddie Mac) are more concerned that these mortgage rates will increase in 2022 to help offset the economy’s recent rising inflation” (Team at eXp Realty, FitzMaurice). He goes on to say that these rates could get up to 4% but will most likely be 3%.

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09

HOUSING INSIGHTS

Oregon's Rent Relief Programs: Where Are We Now?

Dan Noyes

Portland State University

Dan Noyes is a graduate student in the Master of Real Estate Development (MRED) program and a Multi-Family Northwest Student Fellow.

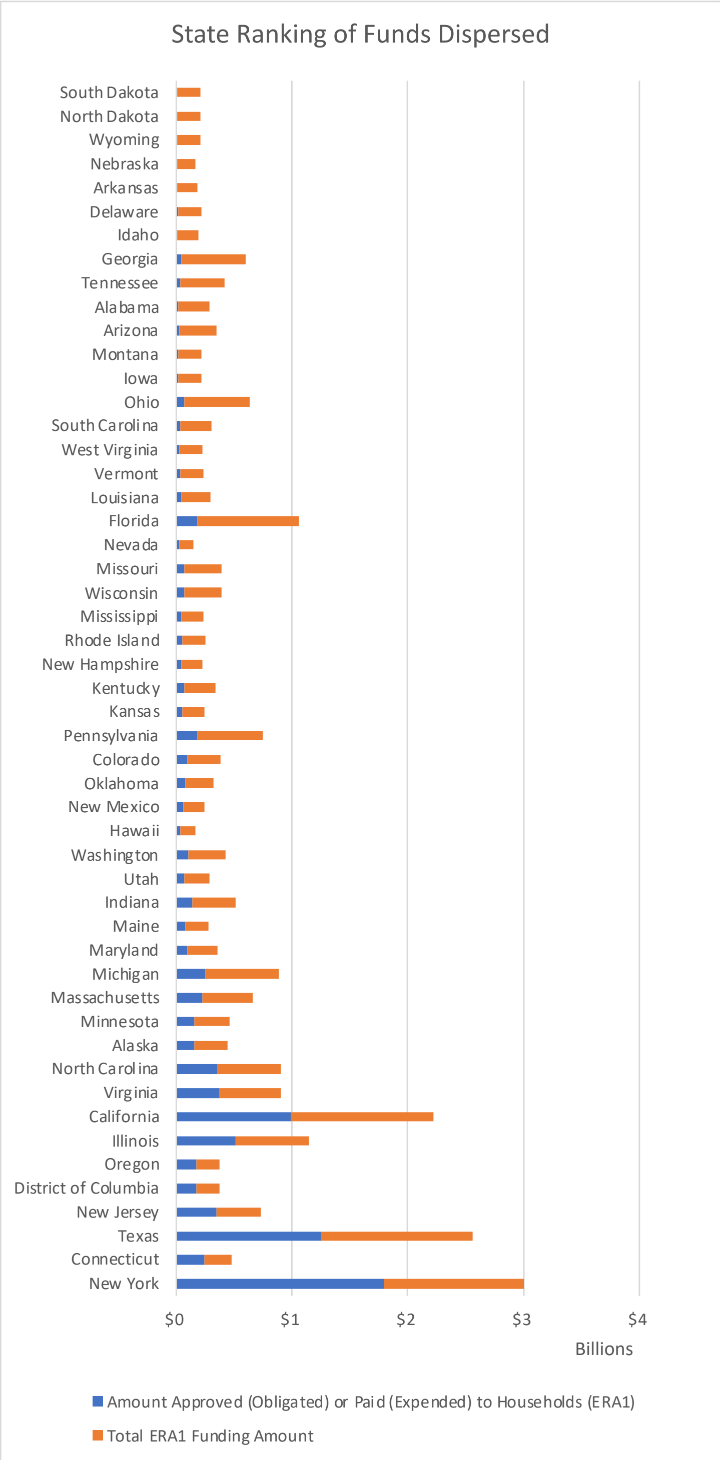
Rent remains one of the largest household expenses incurred by the working class. While relief efforts established early in the pandemic were designed to bring immediate help to those in need, the benefits are only beginning to be realized. A variety of rent relief funds have been established at the federal, state, and local levels to address nonpayment of rent. The funds' primary goal is to mitigate financial pressure for both housing providers and tenants, by providing a source of easily accessible capital for those who were negatively affected by the pandemic. However, the implementation of these funds has thus far suffered from several major logistical challenges, which caused a slow start early in the pandemic.

Progress in the State of Oregon appears to have accelerated greatly since the doldrums of this past summer. However, many other states have not performed as well. This article will discuss the progress made by each major rent relief program in Oregon – particularly within the Portland metropolitan area – and seek to provide some commentary on why the rollout was so slow, and how states can overcome similar challenges in the future.

OREGON EMERGENCY RENTAL ASSISTANCE PROGRAM ("OERAP")

Under the CARES Act of March 2020, Oregon was granted $204 million in federal Emergency Rental Assistance (commonly referred to as "ERA 1"). These funds were to be distributed to individuals earning 80% or less of the median family income and experiencing "financial hardship" as a result of the ongoing pandemic, causing an inability to pay rent. While the description of financial hardship was likely left vague to promote greater participation and promote a speedier recovery, that was not quite the effect. As was reported in the Summer 2021 Quarterly, as recently as August 4, 2021, less than $8 million of the relief funds had been paid out. This represents a shockingly low 4.37% of the $183 million of which had been applied for at the time. This slowdown was primarily caused by issues within application processing, largely due to a mix of software bugs and understaffed agencies.

At this time, the approval and payout of the relief funds has improved rapidly. As of November 1, 2021, Oregon Housing and Community Services ("OCHS"), which oversees distribution of funds, reports that $174



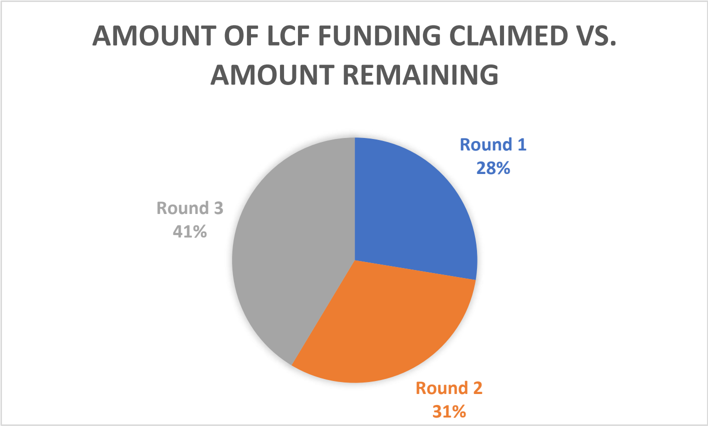
million has been paid or was due to be distributed within a few business days. Total funds of which are paid or obligated to be paid is now equal to 86% of the initial $204 million allocated via ERA 1 through the CARES Act. This turnaround can be attributed to an increase in application processing personnel through the aid of third-party staffing, as well as the passage of time. Oregon now ranks as the state with the 6th largest percentage of ERA 1 funds paid out and is on track to remedy the backlog of applications within a few weeks' time.

LANDLORD COMPENSATION FUND

The Landlord Compensation Fund ("LCF") was introduced by House Bill 4401 in late 2020, as a second major source of rent relief. The $150 million fund was designed to alleviate some of the administrative pitfalls suffered by the Federal OERAP program, by allowing the housing provider to apply for funds themselves on behalf of their tenants. Housing providers may choose which source of funds they wish to utilize (OERAP or LCF), but have been encouraged to select one source consistently, and are not allowed to receive overlapping funding from both programs.

In theory, the LCF would provide reprieve to tenants who must navigate the application requirements of the federal relief programs. However, the initial implementation of the LCF fell somewhat flat, offering housing providers only 80% of their uncollectible rent, and stipulating an ever-changing catalog of requirements which caused confusion and ultimately discouraged its use. During the first round of funding, only $40 million was claimed, well below the $50 million which was expected to be applied for.

After this slow start, Senate Bill 278 was issued in June 2021. This altered the LCF to make it a bit more attractive and usable to housing providers. A few major changes were made, most notably the increase of relief funds to now cover 100% of uncollectible rent retroactively, as well as reducing some administrative burdens on those tasked with processing the applications. In the second round, an additional $45 million was claimed. The third round of funding closed on June 23, 2021. As of November 1, 2021, OHCS did not provide any updated summary information regarding the current status or availability of the LCF.



LANDLORD GUARANTEE PROGRAM

Senate Bill 278 also established the lesser-known Landlord Guarantee Program ("LGP"), which is administered by Home Forward to provide Portland area housing providers with an additional source of funding. The LGP essentially rewards owners who have opted not to instigate an eviction process for non-paying tenants. Another goal of the program was to compensate housing providers for the assistance funds yet to be received due to the slow application processing across the state. Senate Bill 278 introduced a new 60-day safe-harbor period (90 days for Multnomah County) protecting tenants from eviction as long as they have applied to receive rent relief funds. If the outstanding application for funds is not processed by the State during this period, the LGP will administer up to two months of missing rent, essentially a "bridge" payment to keep housing providers afloat.

To be eligible for this program, each tenant is required to submit their application for relief funds between July 1, 2021, and March 1, 2022. This triggers the start of their safe-harbor period. While this program comes as a much-needed reprieve for housing providers who have been desperately waiting for relief payments, it has its own issues. The program's structured incentivizes tenants to wait as long as possible before triggering the start of their safe-harbor period by delaying the submission of this required form. In other cases, applications are being denied based on ineligibility caused by submitting safe-harbor documentation before the July 1, 2021, start date. There are logistical issues with advertising such a program, especially to smaller housing providers who are likely unaware or uninformed about the most current legislation, and how it may apply to them. This has caused this program to be underutilized.

As of November 2021, Oregon has made significant progress in its follow through and delivery of payments from its various emergency relief funds, especially the Federally sourced funds in the OERAP program. The recent U.S. Treasury recently claiming that any state deemed unable or unwilling to obligate or pay out at least 65% of their allocated funds by September 30, 2021, may potentially become ineligible for subsequent rounds of funding. So how did we find ourselves here? In a mid-September presentation conducted by OHCS, officials examined the various strategies implemented over the course of the past year and identified areas in which the system could be improved.

COVID-19 RELIEF FUNDS

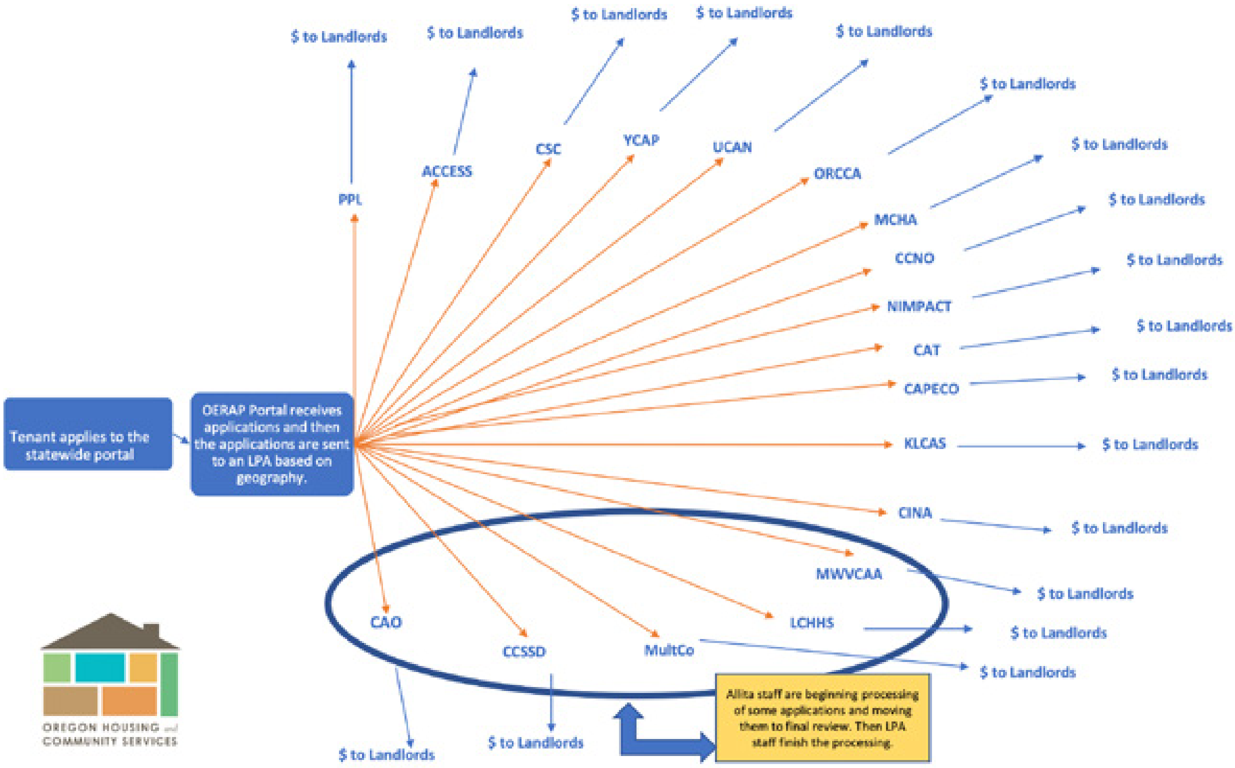
The first round of federal COVID-19 Relief Funds ("CRF"), which provided $16 million to local programs, involved the use of 18 different Community Action Agencies ("CAA"). These CAAs all had varying policies and procedures, causing confusion amongst those responsible for overseeing the back-end of each program. The decentralized method made it difficult for each individual agency to align policies and actions with one another, and it became a challenge to educate and direct tenants in need to the proper programs.

LESSONS LEARNED FROM OERAP

With the first allocation of Federal OERAP funds (ERA 1, $204 million), OHCS implemented a central web portal for struggling tenants across the state to access the program and submit their applications at a single point. After receiving the data via the portal, OHCS would then pass on the application to an appropriate Local Program Administrator based on the tenant's location.

This program is subject to robust and rigorous reporting requirements, which were built into the centralized platform. Often, software issues causing incomplete or incorrect application data to be submitted would result in further delay of processing. Applications were processed based on both State and U.S. Treasury priorities.

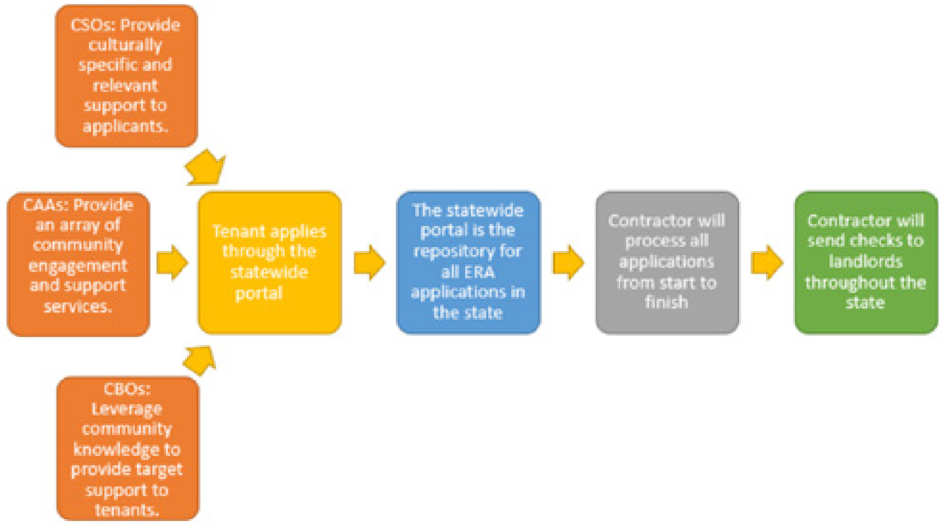
In Multnomah County, further complications arose as some applications were initially processed by third-party software vendor Allita 360, and then passed on to an LPA to complete the review. Later, with the introduction of Public Partnerships, LLC, OHCS was able to increase the manpower available to process and expedite applications. This process showed that the decentralized processing hindered the program's efficiency and made it especially challenging to train employees and align policy updates across the State.



Over the past year, much of the confusion and slowdown can be traced back to a few key decisions which were made early on during the pandemic, mostly regarding the structures used to accept and process applications. It is no wonder that the system broke down with the added complexities brought on by rapidly changing regulation and federal guidance. Additionally, the constant alterations of state program requirements and changes being made seemed to contradict the federal point of view. Because of the inherently slow nature of rolling out updates to state law, Oregon has been left with what it's created so far, for better or worse.

FEDERAL RELIEF FUNDS IN THE MEDIUM-TERM

The next iteration of federal relief funding includes $21.55 billion via the American Rescue Plan Act. Of these funds, $156 million (deemed as "ERA 2") is allocated to Oregon to spend by September 2025. OHCS has decided to reevaluate their upcoming approach for the future, with a new emphasis being placed on educating and funding community agencies with the tools they need to reach and inform struggling tenants.



The new application process will be rearranged to place CAAs at the forefront, using their resources to educate and connect with the community and direct them to a singular application portal. From there, a contractor will process all applications from start to finish and will distribute the funds to housing providers around the state. This newly simplified approach will likely speed up the process and provide much-needed help to those navigating the system.

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10

HOUSING INSIGHTS

The Surprising Status of Oregon Evictions

Rachel Luoto

Portland State University

Rachel Luoto is a candidate in the Master of Real Estate Development (MRED) program at Portland State and a Multi-Family Northwest Student Fellow.

During the COVID-19 pandemic, one of the chief concerns for landlords, tenants, and policymakers has been the potential for evictions due to the hardships and economic upheaval of the pandemic. On August 26, 2021, the Supreme Court ruled to end the federal eviction moratorium in a 6-3 vote. Oregon's eviction moratorium ended on June 30, 2021. People who applied to aid have until February 28, 2022 to make up back rent. With the moratoria ending, there was fear that there would be a tidal wave of evictions as a result. This could compound Portland's problem with homelessness. Policymakers were worried that there would be evictions en masse, with landlords biding their time until they could finally evict the tenants.

This article aims to clarify the actual status of evictions in Oregon, and the impact the COVID-19 pandemic has had on the financial situation of those most at risk for eviction. Here we offer comparisons of pre- and post-pandemic eviction numbers, savings rates, and impacts on minority communities.

There have certainly been evictions now that the moratoria are ended. It is helpful to know what our baseline was for evictions, pre-pandemic, and compare to how many evictions are being filed now. EvictionLab is Princeton University's research center that is tracking and creating a national database of evictions up through 2016. According to them, Oregon's 2016 eviction filing rate was 2.9%, while the actual 2016 eviction rate was 1.1%, or a little more than 19 evictions per day. In comparison, in 2016 the national average rate of eviction was 2.3%. This puts Oregon's rate at less than half the national average. In a list of 100 cities in the United States with the most evictions, Portland does not appear. North Charleston was the highest-ranking city, at a 16.5% eviction rate in 2016.

Under the "Safe Harbor" Amendment to SB-278, tenants will be entitled to 60 days of eviction protection, provided they show proof that they have applied for rental assistance. With June 30, 2021 the latest date for the moratorium to end in Oregon, we feasibly would start to see eviction filings starting in September. So, where do we stand?

According to eviction data collected by Multifamily Northwest, in September of 2019, our last pre-pandemic year, there were 1619 eviction filings in the state of Oregon. However, in September of 2021, there were 915 filings, 476 of which were for non-payment. This means that the number of evictions filed in 2021, post-moratorium, is almost half of what was filed pre-pandemic in 2019 – eviction filings have gone down, not up.

So, why are there fewer evictions being filed? It may have to do with equity, wealth, savings rates, and stimulus checks. According to David Leonhardt of the New York Times:

> "… the financial cushion of most households still is not large. The median cash savings of the bottom quarter of households (ranked by earnings) has risen by 70 percent over the past two years — but it's still only about $1,000, Fiona Greig of the JPMorgan Chase Institute points out," (Leonhardt).

If savings have increased by 70% to $1,000 from two years before the pandemic, that means that at the start of those two years, the average bottom quarter of earners had $588 in their savings accounts. Is that enough to cover one month of rent in an emergency? Not in Multnomah Country, where according to RentCafe, only the bottom 4% of rentals available are less than $1,000 per month. It might not seem like a big difference, $588 vs $1,000, but when you think about the types of unexpected expenses that fall within that range, like car repairs or medical bills, it can make a big difference in whether you are able to get ahead financially or are falling behind.

Since 2013, the Federal Reserve has published the Survey of Household Economics and Decisionmaking, or SHED. One of these questions is if you could cover a $400 emergency expense with cash or cash equivalents. Since 2013, the percentage of people who said "yes" has risen from 50% to 65%. However, in Bankrate's recent Jan 2021 survey, only 4/10 people could cover a $1,000 emergency expense from their savings.

So, taken all together, this means that the savings of the bottom quarter of earners has increased slightly, but not exceeding $1,000. However, in an emergency for a one-time $1,000 expense, that makes all the difference in whether people can stay in their homes. Homeless prevention programs, like Portland Homeless Family Solutions, recognize that the one-time emergency expenses are what make the difference, and they are stepping in with one-time grants to help. According to their website, "It is this exact lack of a safety net that sends working parents into a tailspin when unexpected costs arise. The average investment to prevent a family from experiencing homelessness is only $1,200 per family."

These amounts – $1,000 and $1,200 – are coincidentally similar to the amounts cut in the stimulus checks. $1,200 was distributed at the beginning of the pandemic in April, $600 was distributed at the beginning of 2021, and $1,400 was distributed in March 2021. What if, all at once, everyone had a one-time emergency – and everyone got money, from the government, to cover it? That is essentially the accidental experiment in economics that COVID-19 forced on us.

We cannot talk about evictions, income, and net worth without also addressing the disproportionate impact on minority communities, who have historically been denied access to generational wealth and income opportunities. According to the Federal Reserve's 2019 Survey of Consumer Finances:

> "Black families' median and mean wealth is less than 15 percent that of White families… patterns of inequality in the distribution of wealth across all families are also evident within race/ethnicity groups; for each of the four race/ethnicity groups, the mean is substantially higher than the median, reflecting the concentration of wealth at the top of the wealth distribution for each group," (Bhutta, et al).

That is to say, there are outliers possessing large amounts of money skewing the data set, while the reality is the majority of people have much less. Again, the Federal Reserve reports:

> "White and other families are considerably more likely to report being able to obtain $3,000 from a family member or friend in a financial emergency than Black or Hispanic families," (Bhutta, et al).

Meanwhile, the federal stimulus checks had no application process. You didn't have to know someone with money, and you didn't have to be born into a family with money. All you had to do was be an American in the COVID-19 pandemic. The Reserve agrees that the stimulus checks have helped with racial wealth disparities:

> "…Bhutta, Blair, Dettling, and Moore (2020) find that without the substantial cash assistance included in the Coronavirus Aid, Relief, and Economic Security (CARES) Act, there would be large disparities by race and ethnicity in the share of families who could cover their normal, recurring expenses if they were to lose their job for six months or more. They find that just 10 percent of Hispanic families and 14 percent of Black families have enough savings to cover six months of expenses, compared to 36 percent of White families and 27 percent of other families. But with the cash assistance in the CARES Act (i.e., unemployment insurance and direct stimulus payments), over 90 percent of all family-groups could cover their expenses for six months."

To summarize, the number of eviction filings are actually down from pre-pandemic levels, and low-income/low-net worth households, of which a disproportionate number are BIPOC, are experiencing a temporary financial reprieve. Will households be able to build on this financial foothold as the stimulus checks go away? Are landlords just slow to start filing for eviction again? Rather, it is possible that in this time of extreme hardship, something good may have happened for those most in need.

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11

HOUSING INSIGHTS

Inclusionary Housing Zoning Regulations

Nate Grein

Portland State University

Nate Grein is a graduate student in the Master of Real Estate Development (MRED) program and a Multi-Family Northwest Student Fellow

INTRODUCTION

With the long-term escalation of housing prices across the United States, particularly on the coasts, local jurisdictions are pursuing innovative approaches to producing below-market housing units. Inclusionary zoning is one such approach. Unlike other affordable housing programs that provide direct subsidies to owners (e.g. Section 8 or LIHTC), inclusionary zoning is structured as a developmental mandate that requires multifamily developers to restrict newly constructed housing units to low-income families.

In exchange, the developer receives incentives that vary program to program, but generally involve tax abatements, FAR or density bonuses, fee waivers, or expedited permitting. Some programs are required for all new construction or rehabilitation projects, while others are voluntary, meaning that a developer can elect to restrict units below market rent and receive a jurisdiction's incentive. In general, the goals of these programs include linking affordable housing production to private development and thus expanding the supply of below-market housing; protecting locales from concentrating low-income renters in a select group of neighborhoods; and ensuring high-opportunity metropolitan areas remain accessible for low-income families.

At the core of this comparative article are two different approaches to inclusionary zoning in the Portland metropolitan area. The first is the City of Portland's mandatory Inclusionary Housing (IH) program, which went into effect February 1, 2017, with City Council's passing of Ordinance 188163. The other is the City of Vancouver's voluntary Multifamily Tax Exemption (MFTE), a statewide exemption authorized under state law RCW 84.14 and the Vancouver Municipal Code VMC 3.22. By comparing the regulatory structure of both programs, I shed light on how different inclusionary housing policies tie private development to income-restricted affordable units.

I will detail program goals, general and affordability requirements, options for complying, geographic focus, and reporting and compliance rules. After the policy examination, I detail the latest updates on the number of units both programs have produced, contextualize both programs with the broader, local market-rate trends, and raise considerations about the programs' futures. Particularly at a time when market-rate production is needed to meet consumer demand in the region, it is important to weigh the net benefits and costs of well-intentioned programs like these.

STATED GOALS, ADMINISTRATION, AND POLICY IMPLEMENTATION

Portland's Inclusionary Housing program emerged out of an identified need to expand affordable housing production in light of metropolitan population growth and rising housing prices. The City Council declared a Housing Emergency in 2015, which paved the way for a number of strategic initiatives around affordable housing. In addition to Portland's Housing Bond and the Supportive Housing Plan, City Council passed Ordinance 188163, a mandatory Inclusionary Housing (IH) policy for all new construction and rehabilitation projects over 20 units. The program officially went into effect February 1, 2017.

The City of Portland and Portland Housing Bureau identified four goals for the program:

(1) Link affordable unit production to market rate production
(2) Support development of affordable units in high-opportunity areas
(3) Increase housing opportunities for families and individuals facing disparities
(4) Promote a wide range of affordable housing type options

In achieving these IH-specific objectives, the City of Portland claims it would make considerable progress towards the 2035 Comprehensive Plan's stated goal of producing 10,000 new income-restricted housing units by 2035. Regarding the program administration, Portland Housing Bureau (PHB) is charged with reviewing proposed development applications, with overseeing rules and regulations compliance, and with periodically monitoring programmatic outcomes.

Where Portland's IH program operates just at the city level, Vancouver's Multifamily Tax Exemption (MFTE) is part of a statewide tax exemption program. Passed in 1995, RCW 84.14 intends to stimulate the construction and rehabilitation of multifamily housing in Washington's urban centers, particularly those with insufficient market rate and affordable housing opportunities. The state law enables city entities, as well as Pierce County, to participate if the local population exceeds 15,000. As of 2019, of the 102 eligible cities, 49 have adopted an MFTE program and 27 have approved exemptions. In 1997, the City of Vancouver began participating in the MFTE via Chapter 3.22. Administered by the Community and Economic Development Department (CEDD), the City of Vancouver's MFTE is a voluntary program with the stated purpose of encouraging private multi-housing development and redevelopment within designated target areas. In doing so, the city is working to accommodate future population growth; provide places to live close to employment, shopping, entertainment, and transit; and drive affordable housing development. The target areas for the program are Downtown Vancouver and the Fourth Plain.

Figure 1 - Program Summaries and Comparison

City and Program Name	Portland's Inclusionary Housing (IH) Program	Vancouver's Multifamily Tax Exemption (MFTE)
Program Type	Mandatory	Voluntary
Administrative Body	Portland Housing Bureau	Community and Economic Development Department
Authorizing Document	City Council Ordinance 188163 Administrative Rules Adopted by City Council and PHB as HOU-3.04	State Law: RCW 84.14 Local Authorization: Chapter 3.22 of Municipal Code
Year Implemented	2017	1997
Stated Goals	(a) Link affordable production to private market; (b) increase affordable housing in high opportunity neighborhoods; (c) increase opportunities for families facing disparities; and (d) promote diverse affordable housing types	(a) Accommodate and anticipate future population growth; (b) promote densification; and (c) encourage affordable housing development

POLICY EXAMINATION: PORTLAND'S MANDATORY INCLUSIONARY HOUSING POLICY

The City of Portland's IH requires that all residential buildings proposing 20 or more units of new construction or rehabilitation provide a percentage of those units at rents affordable to households between 0% and 80% of the median family income (MFI). This is a mandatory program. In exchange for providing below-market rental units, the applicant receives an incentive package, which includes, but is not limited to tax exemptions, parking requirement exemptions, and density bonuses. PHB mandates that IH Units must be reasonably equivalent to market rate units with the same bedroom count, as measured in square footage. Participation in the program begins at the permit application stage when a developer informs PHB about how a proposed project will satisfy the IH requirements. There are five core options available to developers. Refer to Figures 2, 3, 4, and 5 below for more information on the programmatic options.

Figure 2 - 2021 Maximum Household Income

% AMI	1 Person	2 People	3 People	4 People	5 People	6 People
80%	$54,150	$61,900	$69,650	$77,350	$83,550	$89,750
60%	$40,620	$46,440	$52,260	$58,020	$62,700	$67,320
30%	$20,300	$23,200	$26,100	$29,000	$31,350	$35,580

Figure 3 - 2021 Maximum Monthly Rent

% AMI	Studio	1	2	3	4
80%	$1,353	$1,450	$1,741	$2,011	$2,243
60%	$1,015	$1,088	$1,306	$1,509	$1,683
30%	$507	$543	$652	$754	$889

Figure 4 - Central City Plan District (CCPD) and Subdistricts

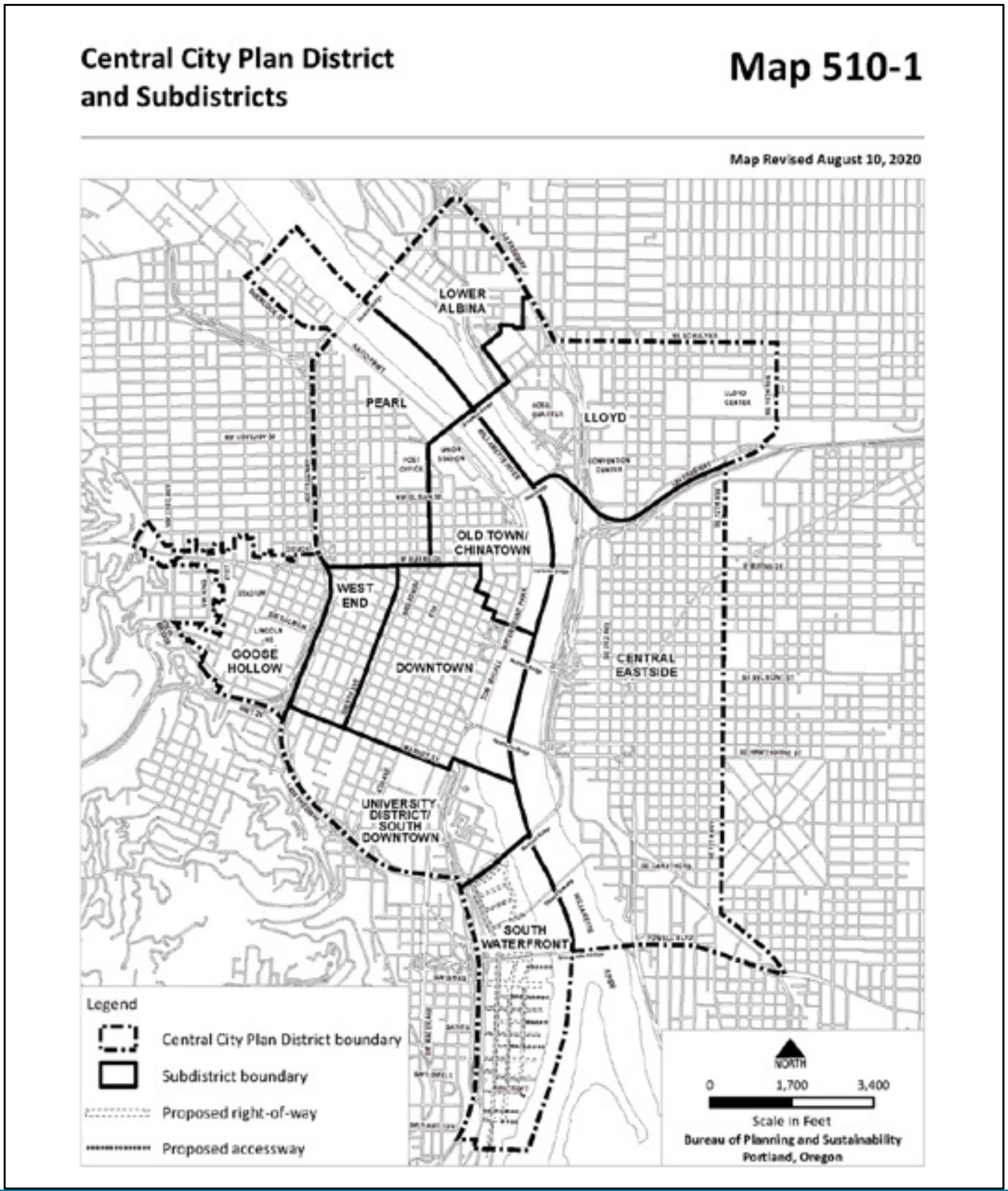
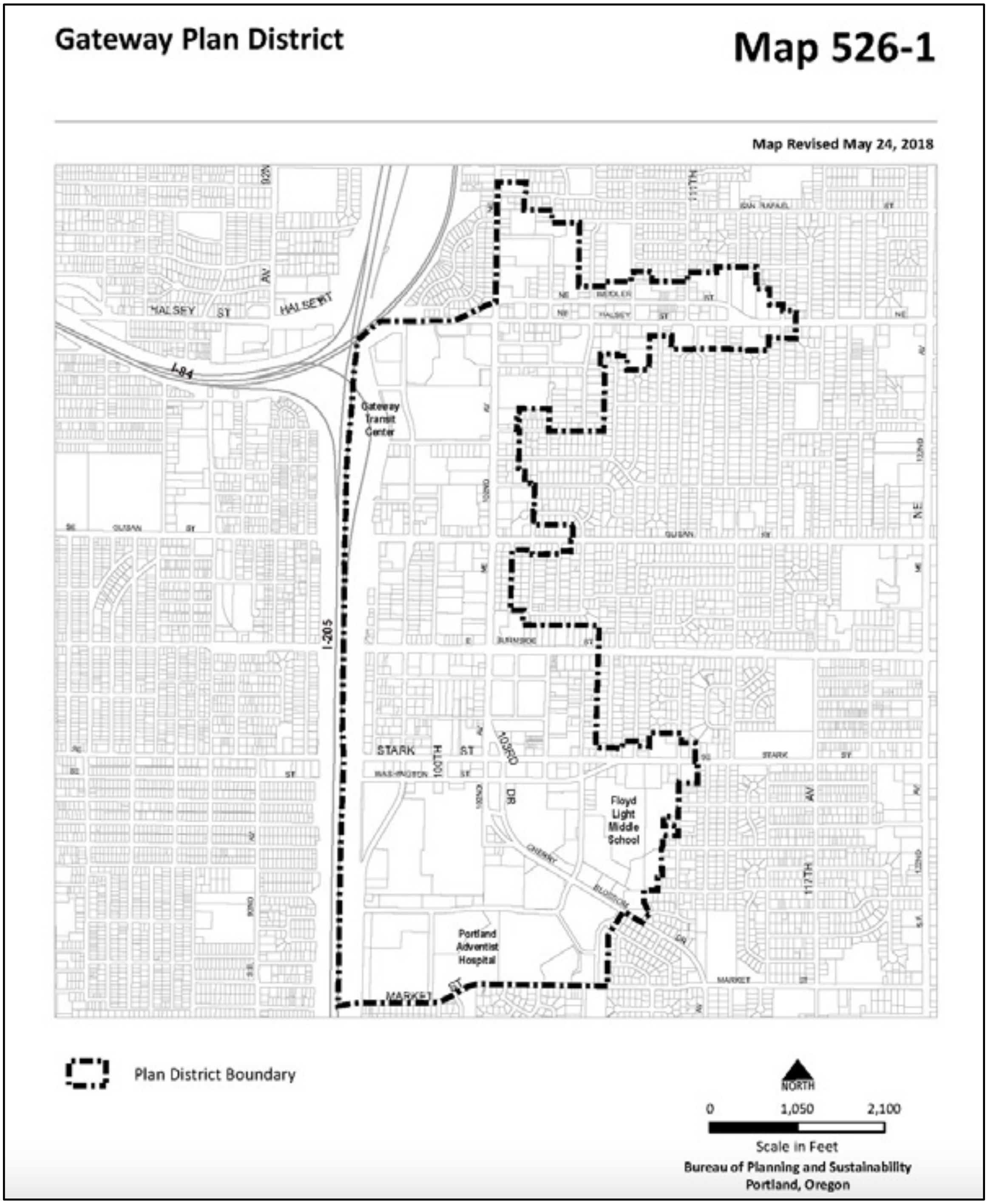


Figure 5 - Gateway Planned District (GPD)



OPTIONS FOR INCLUSIONARY HOUSING

a. Option 1: Build On-Site at 80% MFI

Option 1 requires developers to deliver below-market rental units for families at 80% MFI at the site of the proposed project. The total number of affordable units depends on site location: 20% of total units must be restricted if the property is situated in the Central City Plan District (CCPD) or Gateway Plan District (GPD), while all other Portland areas must restrict 15% of total units. Incentives for Option 1 are consistent across jurisdictions and include:

- 10-year property tax exemption on IH units and applicable percentage of residential related square footage
- Affordable Housing Construction Excise Tax (AHCET) exemption on affordable units and applicable percentage of residential related square footage
- Buildings will be exempt from parking requirements as detailed in Title 33 Planning & Zoning
- Density/FAR bonus as detailed in Title 33 Planning & Zoning

An important caveat to the incentives detailed above is that for properties in the CCPD with a base or built FAR of 5:1 or greater, the 10-year property tax exemption applies to all rental residential units and related square footage, not just the IH units.

b. Option 2: Build On-Site at 60% MFI

Option 2 requires developers to deliver below-market rental units for families at 60% MFI at the site of the proposed project. Again, the total number of affordable units is tied to the site location: projects located in the CCPD or GPD must restrict 10% of total units, while all other Portland areas must restrict 8% of total units. The incentive package offered for Option 2 is identical to those detailed in Option 1, including the CCPD's unique density rule regarding buildings with an FAR of 5:1 or greater.

Note that Options 1 and 2 have optional program components called Reconfiguration and On-Site Consolidation. Reconfiguration allows buildings to alter the minimum number of units required under IH by redistributing restricted bedroom requirements into units of two bedrooms or larger. In effect, Reconfiguration enables a developer to satisfy the IH requirement by meeting the minimum number of bedrooms rather than units. On-Site Consolidation is available to properties with multiple buildings and enables one or more building(s) to transfer their IH unit obligations to another building on the same site. Thus, all restricted units would be integrated into a select number of buildings.

c. Option 3: Build Off Site - New Construction

Option 3 describes the process for relocating the required IH units for a development to another new construction project. There are two eligible scenarios. The first is for the developer to deliver restricted units at the 'receiving building' equal to 20% of the total units from the proposed development (the 'sending building'). The IH units at the receiving building will be restricted to families at 60% MFI. The second scenario is for the developer to deliver restricted units at the receiving building equal to 10% of the sending building's total units; in this case, the receiving building's IH units will be restricted to families earning 30% of MFI. For either scenario, the incentive package for Option 3 is the following:

- Sending building retains any FAR or density bonus
- Sending building will be exempt from parking requirements as detailed in Title 33.266
- Receiving building's affordable units are eligible to receive an AHCET exemption
- Receiving building's affordable units are eligible to receive SDC exemptions
- Receiving building's IH Units may be eligible for 10-year property tax exemption

In addition to the approaches and incentives above, PHB has clear compliance rules for this option. Rules of note include:

- Receiving building has met its own IH requirement before approval to receive another
- IH units in the receiving building are reasonably equivalent to those in the sending building
- Receiving building is within one-half mile of the sending building or in an area of equal or higher opportunity map score
- IH units in the receiving building are not supported by another PHB subsidy

d. Option 4: Designate Units in an Existing Building

Option 4 mirrors Option 3 but applies to developers seeking to designate IH units into an existing property. Two scenarios are eligible. In the first, the developer provides restricted units at the receiving building equal to 25% of the total units from the sending building. The IH units at the receiving building will be restricted to families at 60% MFI. The second scenario is for the developer to deliver restricted units at the receiving building equal to 15% of the sending building's total units. The IH units at the existing receiving building will be restricted to families at 30% MFI. Only two incentives are offered for this Option: that the sending building retains any FAR/density bonus; and that the sending building will be exempt from parking requirements. The compliance rules of note described in Option 3 also apply to Option 4.

e. Option 5: Payment in Lieu

The fifth and final option is a fee-in-lieu in place of providing IH units. This is a one-time payment due at permit issuance. The total incurred fee is equal to the gross square footage (GSF) multiplied by an area-based Fee-in-Lieu Factor. The fee rates are as follows: $23 per GSF outside the CCPD; $27 per GSF inside the CCPD; and $24 per GSF for buildings not subject to IH, but seeking bonus FAR. A project in the CCPD with 45,000 GSF will thus be assessed a fee of $1,215,000. All fees-in-lieu paid out by developers will be contributed to the City's Inclusionary Housing Fund. There are no incentives offered for Option 5.

While IH is mandatory for all projects over 20 units, the program does offer some structural flexibility. First, developers can choose one of the five unique paths above in order to satisfy the requirement. Also, incentives vary considerably between options, indicating that City Council and PHB prefer some options to others. Option 5's fee-in-lieu offers no incentives to offset the new costs to the developer, so the development community will likely pursue Options 1 through 4 instead. Finally, the program's current iteration targets families at a maximum of 80% of MFI and at a minimum of 30% of MFI, showcasing the program administrator's interest in reaching Portland residents across the low-income spectrum.

PROGRAM COMPLIANCE

In addition to meeting Option-specific rules and regulations, program compliance for developers is contingent upon, but not limited to, four key factors:

1. IH units are restricted for a compliance period of 99 years, beginning with the final certificate of occupancy. That restriction period will appear on an IH covenant recorded on the title of the property and, even in situations with transfers of ownership, will run with the land.

2. Owners will be responsible for annual recertifications with tenants via the Tenant Income Certification (TIC) reporting cycle. During this process, owners will review any household and/or income changes and, depending on that data, determine (1) if the tenant of an IH unit still satisfies income qualification rules and (2) if there will be any rental adjustments based upon the applicable rental maximum (see Figures 2 and 3).

3. After owners submit annual tenant and IH unit information to PHB, the department will deliver an Annual Compliance Test (ACT). ACTs will include comments and action items for the owner; issues not resolved within the 90-day resolution period will face default.

4. At any time and with advance notice, PHB reserves the right to physically inspect properties containing IH units. These inspections may also include file audits.

Failure to comply with the above requirements for more than one reporting cycle may result in PHB-determined penalties, which range from Option 5's fee-in-lieu to repayment of any financial incentives and exemptions received by the developer. Legal action may also be taken.

POLICY EXAMINATION: VANCOUVER'S VOLUNTARY MULTIFAMILY TAX EXEMPTION (MFTE)

The City of Vancouver's MFTE program offers developers an 8, 10, or 12-year tax exemption for newly constructed or rehabilitated residential units in exchange for delivering income-restricted units or an approved Development Agreement project. Upon the expiration of the tax-exempt period, owners may transition the MFTE units to market-rate. Only projects in two target areas—Downtown and Fourth Plain—are eligible to participate in the MFTE. Significantly, the program is offered to developers on a voluntary basis—developers can opt in and are not mandated to comply. The administering body for the program is the Community and Economic Development Department (CEDD). Refer to Figures 6, 7, 8, and 9 below for more information on relevant program rules and requirements.

Figure 6 - MFTE Program Income Limits

% AMI	1 Person	2 People	3 People	4 People	5 People	6 People
115%	$77,855	$89,010	$100,165	$111,205	$120,175	$129,030
100%	$67,700	$77,400	$87,100	$96,700	$104,500	$112,200
80%	$54,160	$61,920	$69,680	$77,360	$83,600	$89,760
60%	$40,620	$46,440	$52,260	$58,020	$62,700	$67,320

Figure 7 - MFTE Rent Maximums

% AMI	Studio	1 Bedroom	2 Bedroom	3 Bedroom	4 Bedroom
115%	$1,946	$2,085	$2,504	$2,892	$3,225
100%	$1,692	$1,813	$2,177	$2,515	$2,805
80%	$1,354	$1,451	$1,742	$2,012	$2,244
60%	$1,015	$1,088	$1,306	$1,509	$1,683

Figure 8 - Downtown Multifamily Tax Exemption Zone

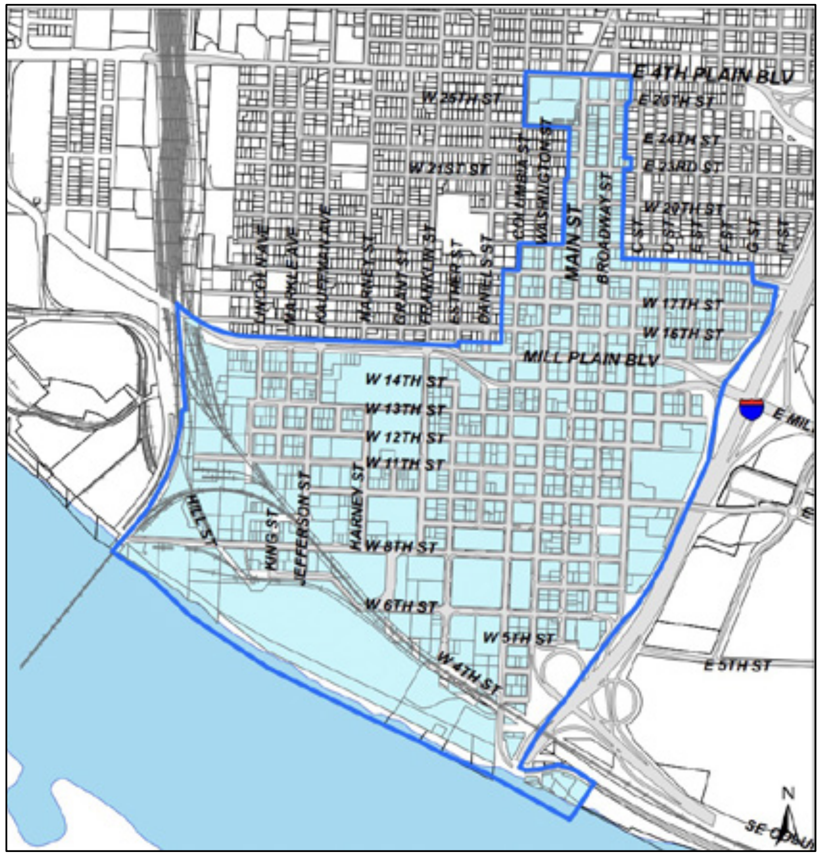


Figure 9 - Fourth Plain Multifamily Tax Exemption Zone

PROJECT TYPES AND INCENTIVES

a. Income-Based Housing Options

Developers opting in to the MFTE program can select one of three options related to the provision of income-based units in new construction or rehabilitation projects. The incentive offered in exchange is an ad-valorem property tax exemption, an exemption covering the entire property.

- 8-Year Option: Owner received an 8-year property property tax exemption in exchange for restricting 20% of total units to households earning up to 100% AMI.
- 10-Year Option: Owner received an 10-year property tax exemption in exchange for restricting 20% of total units to households earning up to 80% AMI.
- 12-Year Option: Owner received an 12-year property tax exemption in exchange for restricting 20% of total units to households earning up to 60% AMI.

Thus, targeting lower income groups generates the longest tax exemption period. For all options, MFTE-unit rents are household-specific; the rental amount charged for restricted cannot exceed 30% of household income.

b. Market Rate Housing

Projects are also eligible to participate in the MFTE program through a Development Agreement. Under this option, the developer is not required to deliver income-restricted units, but rather to provide a property amenity that serves the greater community. Examples include, public art projects, structured parking in excess of 10% of minimum parking requirements, public plazas, and enhanced pedestrian features. All proposed Development Agreements must be reviewed and approved by the City of Vancouver. Additionally, the owner must provide documentation that the proposed amenity will cost no less than 25% of the estimated tax benefit. Upon project completion, the agreed upon amenity will be inspected and valued prior to the certification of occupancy.

REQUIREMENTS

In addition to project-specific requirements, the CEDD details general requirements for the MFTE. Requirements of note include, but are not limited to:

- The property must be located within a residential target area, including either the Downtown Multifamily Tax Exemption Zone or Fourth Plain Multifamily Tax Exemption Zone.

- The project must construct a minimum of four units and, for rehabilitation projects, four new units must be built.
- Projects must be intended for permanent residential occupancy and 50% of building space must be reserved for this use type.
- The project must not displace any existing residential tenants from the property proposed for development unless a relocation plan is approved by the City.
- If pursuing the Development Agreement program type, the applicant must enter an agreement with the City to implement the development and comply with any additional conditions contained in that agreement.
- The project must be completed (as measured by Occupancy Permit issuance) within a period of three years from the date a conditional certificate of tax exemption is issued. Extension may be conditionally granted for a maximum of 36 additional months.

COMPLIANCE

Similar to the IH program, the MFTE mandates that participating project owners monitor tax-exempt units and tenant household characteristics. Household incomes will be reviewed during the lease-up process annually or anytime the lease changes (whichever comes first). Tenant files and household information will be maintained by the property owner, which the City of Vancouver staff can request access to at any time.

Each December, the owner will submit an annual report on market-rate units, designated income-based units, and tenant information to the CEDD. That data is then reviewed by each participating city or county entity and reported to the Washington State Department of Commerce. For any project found in violation of the MFTE agreement, the tax exemption will be cancelled, and the Clark County Assessor's office retains the right to impose an additional tax on the property. The City may execute a cancellation during an annual review or at any other time when non-compliance has been identified.

PROGRAM COMPONENT COMPARISON

Figure 10 shows a comparison of the major program components for both Portland's IH program and Vancouver's MFTE. Key programmatic components include income targeting, geographic focus, percentage of units restricted by the program, length of required affordability, incentive types offered, compliance and reporting elements, and the ability to participate in the program without the provision of income-restricted units.

Figure 10 - Program Component Comparison

City and Program	Portland's Inclusionary Housing (IH) Program	Vancouver's Multifamily Tax Exemption (MFTE)
Income Targeting	30% - 80% MFI	60% - 100% AMI
Geographic Focus	Citywide Unique rules apply to CCPD and GPD	Downtown and Fourth Plain Multifamily Tax Exemption Zones
Units Restricted by Program	8% - 25% of total units Dependent upon income targeting, geography, and option	20% of total units
Length of Affordable Restrictions	99 Years	8, 10, or 12 Years
Incentive(s) Offered	Property Tax Exemption (IH Units Only) Excise Tax Exemption (IH Units Only) FAR and Density Bonuses Reduced Parking Requirements	Property Tax Exemption (All Units)
Compliance and Reporting Elements	Owners Determine Tenant Eligibility and Rent Amount Owners Manage Tenant Files and Household/Income Changes Owners Compile Annual Reports PHB Retains Right to Inspect Property and Files PHB Retains Right to Find Owner in Violation for Non-Compliance	Owners Determine Tenant Eligibility and Rent Amount Owners Manage Tenant Files and Household/Income Changes Owners Compile Annual Reports CEDD Retains Right to Inspect Property and Files CEDD Retains Right to Find Owner in Violation for Non-Compliance
Participation Without Affordable Element	Fee-In-Lieu	Market Rate Housing Option with Development Agreement

Compared to Vancouver's program, Portland's IH targets deeper affordability by restricting units to families between 30% and 80% MFI. The IH program also has a broader geographic focus in that it is citywide, whereas Vancouver's MFTE only targets two specific areas. The MFTE does not offer a percentage range for the number of affordable units required and, for all three options, mandates 20% of total units be restricted; the IH, on the other hand, requires that 8% to 25% of total units be restricted, depending on income targeting, geography, and selected programmatic option. Regarding the length of restrictions, Portland's IH requires a 99-year restriction that runs with the land, while the MFTE enables restricted units to revert to market rate at the end of the tax exempt period (8, 10, or 12 years). The IH utilizes four unique incentive types for its IH, where Vancouver's MFTE only offers one, a property tax exemption.

In general, the compliance and reporting components for both programs closely mirror one another. Both require participating owners to determine tenant eligibility and max rents, to manage tenant files and household/income changes, and to provide annual reports to the program's administrative body. Also, both programs allow for owners to participate in the program without delivering affordable units, albeit in different ways. The IH enables participation via the fee-in-lieu, where the MFTE allows participation via a Community Agreement that provides some type of community benefit.

IMPACTS AND FUTURE CONSIDERATIONS

The efficacy of programs like these hinges upon a relatively straightforward set of economic analysis. For a mandatory policy, if the cost of providing below-market units exceeds the offered incentives, inclusionary housing will operate as a tax on new housing development. In turn, the newly incurred costs associated with the program will reduce new supply and increase prices of market-rate housing. An optional program, on the other hand, allows a developer to participate if the incentives offered exceeds the cost of delivering affordable units; the anticipated results should either have no effect due to non-participation or increase housing supply and supply lower pricing. These results are, of course, in addition to the expansion of the affordable housing supply if developers elect to participate.

Evaluating the impact of these programs—particularly Portland's relatively young IH policy—poses many challenges. It is important to highlight three key elements for each: units produced, contemporary market context, and considerations for the future.

a. Units Produced

In October 2021, Portland Housing Bureau posted a permitting progress report for the Inclusionary Housing Program. As seen in Figure 11 below, the IH program currently has an overall pipeline of 185 total projects. Of those, 100 projects have received building permits from the Development Services (BDS) (54%), while 85 have not (46%). Fifty-one total projects have received a final permit or certificate of occupancy (28%), thereby contributing those IH units to the affordable supply; 134 projects (72%) have not completed the construction and lease-up process.

Figure 11 - Permitting Progress Report Summary by Project

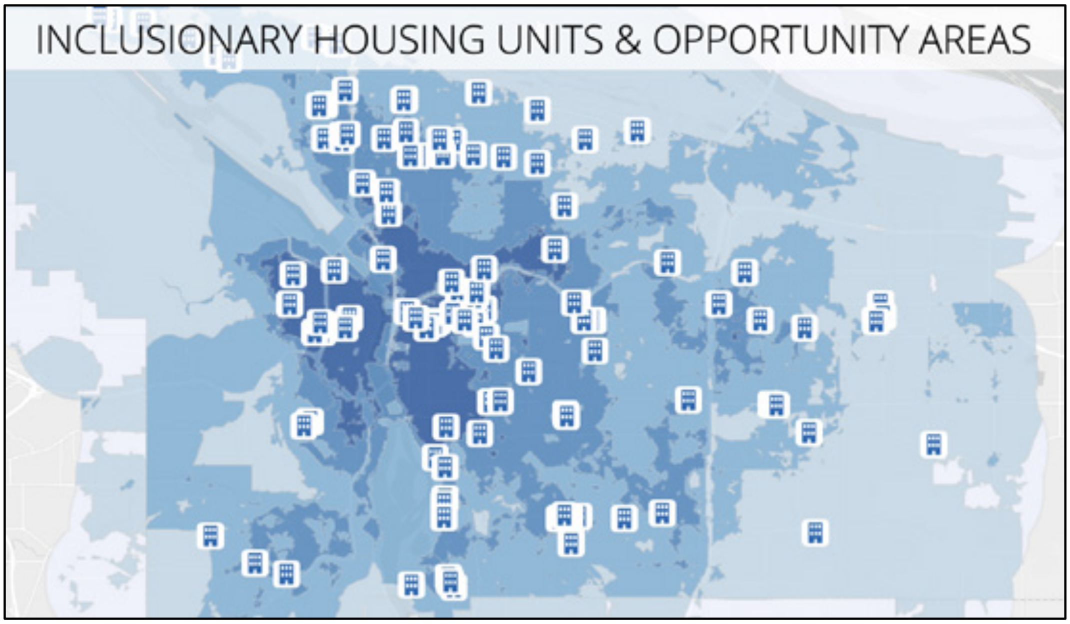
	Initial BDS Permit	**Final Permit/CO**
Projects with Permit	100	51
Projects without Permit	85	134
Total Projects: 185		

Regarding individual units, and as shown in Figure 12, the overall pipeline includes 1,188 affordable units. Six hundred ninety-one IH units (58%) are in projects that have received a building permit, while 497 (42%) are in projects without a building permit. A total of 389 units (32%) of the overall IH unit pipeline are currently occupied, while 799 units (68%) are pending a final permit or certificate of occupancy.

Figure 12 - Permitting Progress Report Summary by IH Units

	Initial BDS Permit	Final Permit/CO
Units in Projects with Permit	691	389
Units in Projects without Permit	497	799
Total Units: 1,188		

Figure 13 - Distribution of Projects with IH Units in Portland Metro



PORTLAND HOUSING BUREAU

To contextualize this impact, Portland Housing Bureau oversees 14,692 regulated units and, between 2011 and 2019, added an average of 625 affordable units to its portfolio. Therefore, at this time, the number of IH units currently leased comprises 2.6% of PHBs portfolio. If all 185 proposed projects are completed, that percentage will rise to 8.4%.

Figure 14 provides detail on Vancouver's MFTE restricted-unit production. The City of Vancouver currently has 32 projects in the overall pipeline, comprising 333 total units. There is a close to even split between units in pre-development (165) and units currently renting (168). Of the two target areas, Downtown Vancouver is heavily preferred, capturing 91% of proposed and completed projects.

One key point of interest is the recency with which this program has gained traction. Peggy Sheehan, Program Manager with the City of Vancouver's Community and Economic Development Department, reported an uptick in overall developer interest in the program despite some hesitations around program compliance. In line with that sentiment, of the 32 projects participating, only two were completed prior to 2017, despite the program's implementation 20 years prior.

Figure 14 - Vancouver MFTE Restricted-Unit Production

	Projects In Predevelopment	**Completed Projects**
Number of Projects	14	18
Number of Units	165	168
Target Area Distribution - VCCV / Fourth Plain	100% / 0%	79% / 21%
Number of Projects Completed Prior to January 1, 2017	-	2

b. Contemporary Market Context: Portland Metro Area

Contextualizing these programs with broader market-rate data helps us anticipate their relative success in producing affordable units—recall that market-rate multifamily and affordable production are directly linked for both. Moreover, in the City of Portland's case, the IH program may negatively impact overall production if incentive offerings do not outweigh the incurred costs of producing below-market units. Because Vancouver's program is voluntary, the MFTE will not negatively impact market-rate production.

Figures 15 from Multifamily NW's Fall 2018 report provide insight into the market's performance over the last decade. Between 2013 and 2020, Portland saw extensive growth in apartment construction. However, construction in the metropolitan area declined by 63% in 2020. CoStar data suggests that the number of units currently under construction approximates 2012 or 2013 numbers.

The result will likely be continued declines in vacancy and upward pressure on pricing. The construction trends coincide with four consecutive years of declining permitting between 2017 and 2020. Compared to 2017, 2020 saw 4,596 fewer projects permitted, a 45% decrease. One positive sign is the amount of permitting in 2021, which has already exceeded 2020 by 1,366 permits. Within the four-county metro, 52% of permit applications occurred in Multnomah County, 39% in Clark County, 7% in Washington County, and 2% in Clackamas County.

The Portland metro is experiencing some trends that are slowing construction on the national level. For example, many areas are struggling with labor shortages and the rising cost of construction materials. Having said that, and as Patrick Barry notes in his report, other factors are specific to Portland: rent control, reputational damage and ensuing investor wariness, and the uncertainty of local regulatory change are all contributing to declining production.

This is the context in which the IH program, which requires 99-year affordability, is operating. If the costs of the program—both in terms of decreased rental collections from IH units and the labor costs incurred from program compliance and monitoring—do not outweigh the incentives, owners may pursue other development options. They may look at projects outside the jurisdiction, build smaller projects so as not to apply, or take other approaches to avoid these costs. From this perspective, then, IH has the potential to exacerbate declining market conditions, thereby having an opposite net impact to the program's goals. Less multifamily production will not only intensify the upward pressure on rents due to the housing shortage and low vacancy, but fewer affordable units will also be generated.

Figure 15 - Apartment Permits for Four County Metro Area

Year	Apartment Permits Annualized for Four County Metro Area
2011	2,045
2012	3,280
2013	5,821
2014	6,799
2015	6,657
2016	7,302
2017	10,319
2018	7,647
2019	8,830
2020	5,723
YTD 2021 (As of September)	7,089

c. Future Considerations

This analysis, which has compared the City of Portland's Inclusionary Housing program and the City of Vancouver's Multifamily Tax Exemption, has described two creative policy tools for producing affordable housing. Vancouver's MFTE offers voluntary developer participation and has seen increased interest due to recent investment in the community's downtown. In contrast, Portland's IH program functions as a mandate. While it is actively contributing units to the affordable supply, it holds the potential to deter market-rate production and aggravate an existing housing shortage.

This article will conclude with three considerations for the future or for additional research:

- How should practitioners measure and understand the impact of the Inclusionary Housing program on the market? Many real estate economists and land-use analysts have described the challenge of evaluating inclusionary zoning's effect on housing market outcomes. Identifying strategies to assess program efficacy is vital for the metropolitan region, particularly given the current market conditions.

- Should the City of Vancouver expand the MFTE program in general and to other target areas? Peggy Sheehan, the Program Manager reported that the CEDD is exploring those precise options. In particular, she highlighted providing new or more incentives for income-based housing, in hopes of anticipating future investment. The growth of this program in the future should provide an interesting case study with which to compare Portland's IH.

- Should the City of Portland change the IH policy from a mandatory to a voluntary program? Given the program's potential to worsen, not improve the housing shortage, this feels like an option worth weighing. Seemingly in response to this type of logic, PHB states the following on its website: "As multifamily unit permitting continues to advance, despite signals that the market cycle is beginning to ebb, the Housing Bureau is recommending program refinements to support this continued progress and allow the market additional time to adjust." What 'program refinements' are being debated? And significantly, how long constitutes 'additional time'? When the market is in such desperate need of supply, it is instrumental that IH's administrative bodies conceptualize the program holistically and take action accordingly.

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