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# INDUSTRIAL MARKET ANALYSIS

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Portland's industrial market continued to improve in the second quarter, with vacancy rates at historic lows and rental rates on the rise. Net absorption saw a slight decrease in the quarter, not including Intel's Mod1 project, but remains positive year-to-date. A significant construction pipeline of over 2 million square feet, much of it speculative space, will hit the market in the second half of the year – and industry experts believe that there is demand for all of the space.

## VACANCY AND RENTS

The Portland area's industrial market continued to show strength in the second quarter, with a declining vacancy rate and an increase in asking rents. A review of quarterly research reports from four leading commercial real estate firms revealed a metro-wide vacancy rate of 4.9 percent in the second quarter, 22 basis points below the prior quarter and 91 basis points below this time last year. This tightening market is mostly being driven by demand for distribution, warehouse, and manufacturing spaces, which together had a vacancy rate of 4.6 percent in the second quarter. Flex space, in contrast, had a vacancy rate of 10.7 percent, a slight decrease from the prior quarter but a 45 basis point increase year-over-year.

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

**Table 1: Portland Industrial Quarterly Report Survey Q2 2015**

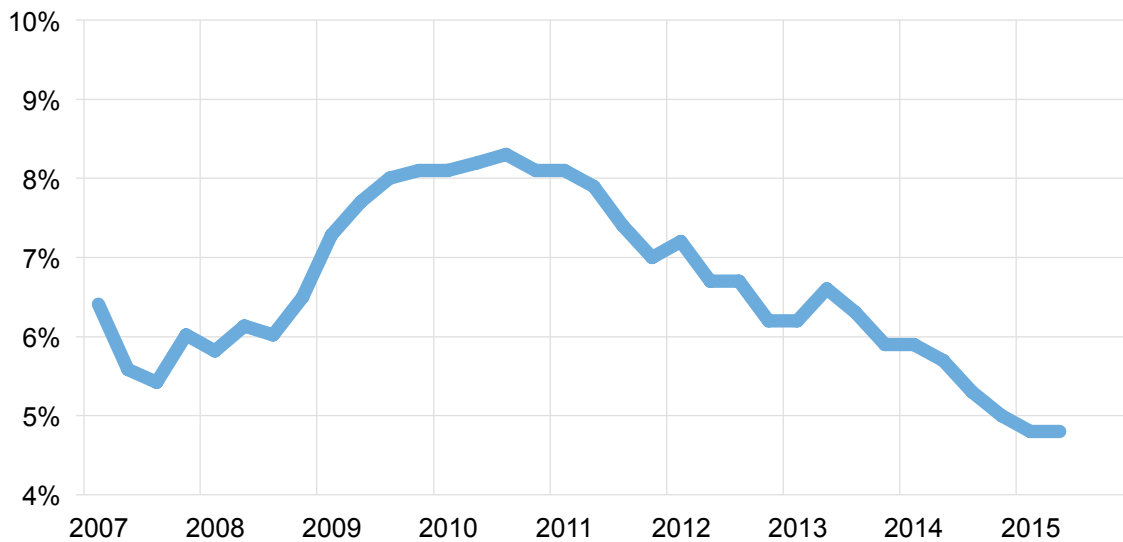
	Colliers	JLL	CBRE	Kidder Mathews	Average - Q2 2015	Chg vs Prior Qtr	Chg vs Prior Year
<b>Vacancy</b>							
- Industrial *	4.9%	4.2%	-	-	4.6%	-20 bps	-90 bps
- Flex	11.6%	9.8%	-	-	10.7%	-05 bps	45 bps
- Weighted Average	5.5%	4.7%	4.7%	4.8%	<b>4.9%</b>	<b>-22 bps</b>	<b>-91 bps</b>
<b>Rents **</b>							
- Industrial *	\$0.47	\$0.50	\$0.40	-	\$0.46	-0.4%	7.0%
- Flex	\$0.95	\$0.95	\$1.02	-	\$0.97	6.8%	15.0%
- Weighted Average	\$0.51	\$0.54	\$0.46	\$0.48	<b>\$0.50</b>	<b>1.7%</b>	<b>8.5%</b>

\* Includes distribution, warehouse, and manufacturing

\*\* Asking rents for finished space (blended); CBRE Industrial rents are for shell space

Sources: Quarterly Reports

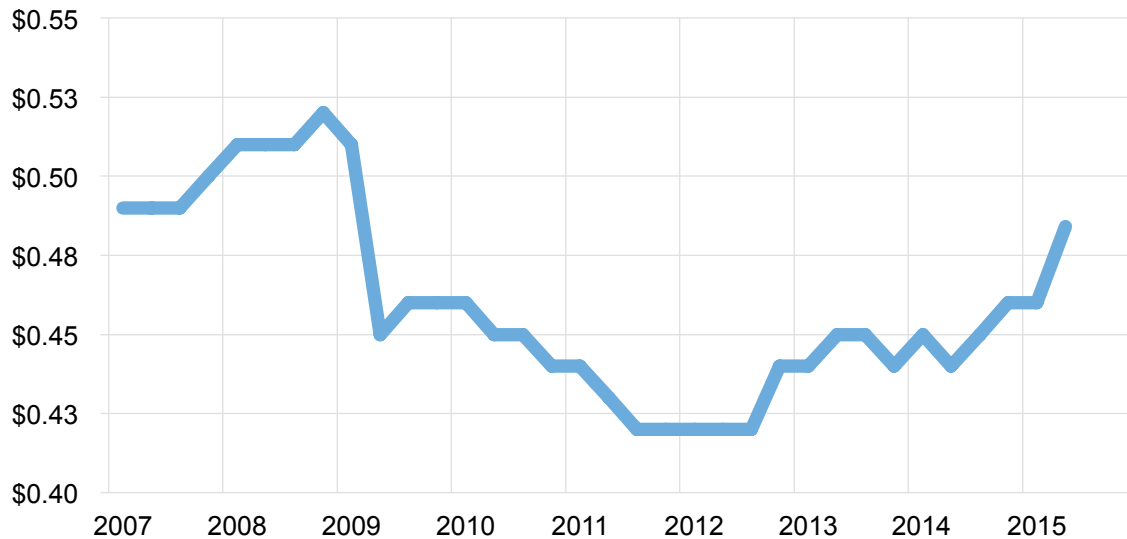
According to Kidder Mathews, this is the eighth consecutive quarter in which vacancy rates either decreased or stayed flat. JLL says that vacancy in the market is at its lowest point in over 20 years, encouraging a rise in speculative construction, with only one-third of upcoming deliveries spoken for (i.e. build to suit, owner-built). Colliers reports that the improving technology economy contributed to the lowest flex vacancy rate in the Sunset Corridor in more than a decade.

**Figure 1: Portland Industrial Market Vacancy Rate, 2007–2015 Q2**

Source: Kidder Mathews

Along with decreasing vacancy rates, asking rental rates continued their upward trajectory in the second quarter. The quarterly report survey showed monthly industrial asking rates of \$0.46/square foot and flex rates of \$0.97/square foot, for a combined weighted market average of \$0.50/square foot. Industrial rates dipped slightly from the first quarter but are up a strong 7 percent year-over-year. Flex rates exhibited very strong quarterly growth of nearly 7 percent and annual growth of 15 percent.

**Figure 2: Portland Industrial Market Asking Rents, 2007–2015 Q2**



Source: Kidder Mathews

## ABSORPTION AND DELIVERIES

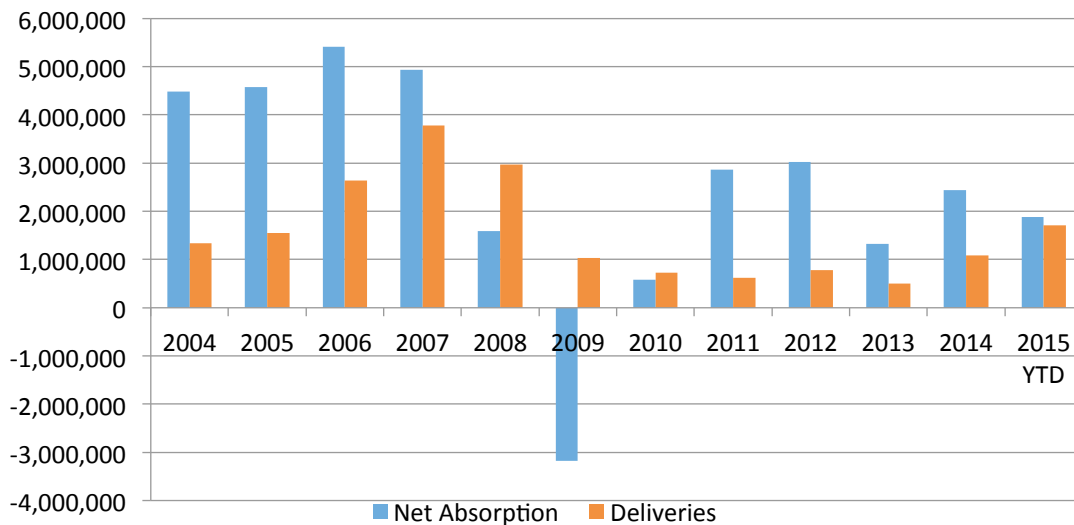
Colliers reported positive net absorption of 825,000 square feet in the second quarter, down from over 1 million square feet in the first quarter. However, Intel's Mod1 at D1X accounted for 1.1 million square feet in the quarter – factoring out this space, the overall market actually saw negative net absorption of about 275,000 square feet. Over the past four quarters, the market has absorbed 2.75 million square feet of space (not including Mod1). This net absorption run rate is slightly higher than the market's average annual net absorption from 2004-2014 of 2.55 million square feet.

**Table 2: Portland Industrial Net Absorption Last 4 Quarters**

	<b>Industrial</b>	<b>Flex</b>	<b>Total</b>
<b>Q3 2014</b>	949,800	-45,116	904,684
<b>Q4 2014</b>	848,170	14,689	862,859
<b>Q1 2015</b>	1,129,776	-68,708	1,061,068
<b>Q2 2015</b>	-318,067	1,143,713	825,646
<b>Total</b>	2,609,679	1,044,578	3,654,257
<i>w/out Intel</i>	2,609,679	-55,422	2,749,573
<b>AVG 2004-2014</b>			2,549,245
<i>Peak Annual</i>	2006:		5,412,028
<i>Trough Annual</i>	2009:		-3,169,003

Source: Colliers International

**Figure 3: Portland Industrial Net Absorption and Deliveries, 2004–2015 Q2**



Sources: Colliers Quarterly Report and Colliers/Capacity Commercial Presentation

Excluding Intel's Mod1, deliveries for the first half of the year totaled just over 600,000 square feet. Notable deliveries included 215,000 square feet at the Gateway Corporate Center and 97,000 square feet at the speculative Koch Corporate Center.

**Table 3: Notable Portland Industrial Lease Transactions Q2 2015**

<b>Tenant</b>	<b>Building</b>	<b>Submarket</b>	<b>Size (s.f.)</b>	<b>Type</b>
Georgia Pacific	Rivergate Corporate Center 2	Rivergate	607,000	Renewal
Bridgestone Tire	ProLogis PDX 20	East Columbia	204,280	Relocation
CEVA Logistics	Alderwood Corporate Center	Airport Way	154,675	Renewal & Expansion
Bay Valley Foods	Kelley Point Distribution Center	Rivergate	150,000	Renewal
Oregon Wine Services	Southwest Industrial Park	Tualatin	145,136	New

Sources: Colliers and CBRE

## UNDER CONSTRUCTION

Local real estate firms estimate that there is current tenant demand for between 2 million to 4 million square feet of industrial space in the Portland metropolitan market. JLL notes that there are 15 users seeking spaces over 100,000 square feet – significantly larger than the typical lease of between 10,000 and 50,000 square feet.

To meet known and speculative demand, there are 15 projects currently under construction with over 2 million square feet of space. This does not include Intel's 1.6 million square feet at Ronler Acres. Over 800,000 square feet is located in just two projects in the Northeast submarket – Holland's Cameron Distribution Center and Specht's Interstate Crossroads Distribution Center. Both of these projects are speculative.

Since 2009, annual deliveries in the market have averaged 800,000 square feet. Assuming that the 2 million square feet under construction are delivered in the second half of 2015, the projected yearly total deliveries will equal 2.6 million square feet. This amount of space is the most delivered since 2008 and is equal to more than 3 years of deliveries (given the average of the past 6 years).

## INVESTMENT ACTIVITY

Kidder Mathews reported that transaction volume for the second quarter was \$143 million, in-line with 2014 quarterly averages and up from \$121 million in the first quarter. The average sales price in the second quarter was \$71.72 per square foot, up slightly from the first quarter average of \$70.56. Notably, the average market capitalization rate decreased to 6.41 percent in the second quarter, down from 7.02 percent in the previous quarter.

**Table 4: Notable Portland Industrial Sales Transactions Q2 2015**

<b>Address</b>	<b>Location</b>	<b>Size (s.f.)</b>	<b>Price</b>	<b>Price/s.f.</b>	<b>Type</b>
Tualatin Corporate Center	Tualatin	401,000	\$ 36,100,000	\$ 90.02	Investment
13635 N Lombard Street	Portland	139,000	\$ 7,550,000	\$ 54.32	Investment
17600 NE San Rafael Street	Portland	94,634	\$ 7,300,000	\$ 77.14	Owner/User
11555 SW Myslonny Street	Tualatin	126,625	\$ 7,000,000	\$ 55.28	Owner/User
20495 SW Teton Avenue	Tualatin	100,000	\$ 6,000,000	\$ 60.00	Investment

Source: Kidder Mathews

## LOOKING AHEAD

With 2 million industrial square feet under construction, 2015 is on pace to deliver the most space in any year since the Great Recession. Strong tenant demand in the market, especially for larger spaces, will likely lead to the absorption of this space in 3 to 4 quarters. As much of this space is speculative, vacancy rates may rise in the near-term from their historic lows, but not significantly higher. Absorption of space in the two largest speculative projects currently under construction, consisting of over 800,000 square feet, will offer clues to the continuing strength of the market. Another trend to watch over the next few quarters will be the impact of marijuana legalization on the industrial market, especially on rental rates and property sales. ■