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## OFFICE MARKET ANALYSIS

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The State of Oregon gained recognition as one of the strongest economies in the nation during 2015, with Bloomberg's Economic Evaluation of States declaring Oregon as the best-performing economy in the US over the year and with JLL reporting total 2015 job growth at 3.3 percent for the Portland region. This compares to just 1.8 percent for the US as a whole. While the fallout of Intel's job cuts is still unknown, 2016 looks poised to continue recent trends, with the economy showing strong signs of continued expansion. Oregon's Office of Economic Analysis (OEA) reported a 4.4 percent seasonally adjusted unemployment rate for the Portland Metro economy in January 2016—a 15-year low and decreasing from 5.7 percent a year ago.

The first quarter brokerage reports focused on strong economic fundamentals underpinning continued strength in the office market.

- **JLL** points to Portland and Oregon's historic levels of economic growth, with its headline labeling Portland as "Boomtown, USA." JLL data show 4 million square feet of tenants in the market—11 percent higher than any previous month on record—with 32 percent of this demand from high tech/information services tenants and 12 percent from professional and business services tenants. 66 percent of this demand is for close-in urban areas—continuing the focus on urban office expansion seen so far during this cycle.

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- **Colliers** emphasized Portland’s strong economic fundamentals, highlighting the 50 percent job growth for professional, technical, and business services office-users since 2011—four times the rate of growth for semiconductor manufacturing officer users. However, Colliers suggests that some tenants may have begun to abandon the CBD for the affordability and flexibility of the suburbs, with its data showing Class B and C vacancies increasing in the CBD during the quarter.
- **CBRE** looks to Portland’s 2.2 million square feet of ground up and fully renovated office space in the development pipeline scheduled to deliver over the next 24-months. Finding 50 active tenants looking for 1.94 million square feet of office space, CBRE suggests that Portland’s appetite for additional office space will support strong office market fundamentals through 2016. Leading the way, and marking Portland’s first new high-rise in six years, Park Avenue West delivered during the first quarter and was 80 percent preleased. Downtown Class A rental rates continue to shine, gaining 11.4 percent year-over-year, compared to 3.9 percent growth for suburban markets.

## VACANCY

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

| <b>Brokerage</b> | <b>Total</b> | <b>CBD</b> | <b>CBD Class A</b> | <b>CBD Class B</b> | <b>CBD Class C</b> | <b>Suburban</b> |
|------------------|--------------|------------|--------------------|--------------------|--------------------|-----------------|
| <b>CBRE</b>      | 10.6%        | 8.7%       | 9.5%               | 8.5%               | 7.8%               | 12.3%           |
| <b>Colliers</b>  | 8.6%         | 9.4%       | 9.0%               | 10.3%              | 8.3%               | 8.3%            |
| <b>JLL</b>       | 8.3%         | 6.9%       | 7.1%               | 6.9%               | 6.3%               | 9.7%            |

Source: Brokerage Quarterly Reports

CBRE’s data show vacancy holding below pre-recession levels, with total rate of 10.6 percent for the Portland metro region. Downtown vacancy increased slightly to 8.7 percent from 8.5 percent, while the Lloyd district continued to shine with a 3.6 percent vacancy rate. The Suburban market vacancy rate continued its impressive downward movement, ending at 12.3 percent for the first quarter. JLL reported total vacancy at 8.3—according to JLL, this is the lowest value on record since before 2000 and one of the lowest rates in the country. JLL predicts demand will far outpace supply in 2016, with strong pent up demand waiting for projects to deliver during the second and third quarters.

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

| <b>Location</b>                  | <b>Q1</b>   | <b>Change from Q4</b> |
|----------------------------------|-------------|-----------------------|
| Portland CBD                     | 6.6%        | -0.1%                 |
| Lloyd District                   | 3.8%        | -0.7%                 |
| <b>Portland Central City</b>     | <b>6.3%</b> | <b>-0.1%</b>          |
| Clackamas / Milwaukie Totals     | 9.5%        | -0.7%                 |
| Airport Way/Columbia Corridor    | 6.8%        | -0.6%                 |
| Close In Eastside                | 4.2%        | -0.1%                 |
| Outer Eastside                   | 12.2%       | -2.1%                 |
| <b>Portland Eastside Suburbs</b> | <b>7.2%</b> | <b>-0.5%</b>          |
| 217 Corridor / Beaverton         | 13.9%       | 0.3%                  |
| I-5 South Corridor               | 13.4%       | 1.2%                  |
| Kruse Way                        | 7.6%        | -0.5%                 |
| Northwest                        | 3.7%        | -10.8%                |
| Sunset Corridor                  | 7.8%        | 0.2%                  |
| SW Close In                      | 6.8%        | -1.9%                 |
| <b>Portland Westside</b>         | <b>9.8%</b> | <b>-0.8%</b>          |
| Cascade Park/Camas               | 6.3%        | -1.6%                 |
| CBD/West Vancouver               | 9.8%        | -1.2%                 |
| Hazel Dell / Salmon Creek        | 6.0%        | -2.0%                 |
| Orchards/Outer Clark             | 11.7%       | -0.5%                 |
| St. John's Central Vancouver     | 24.8%       | -0.3%                 |
| Vancouver Mall                   | 5.7%        | 0.4%                  |
| <b>Vancouver Suburbs</b>         | <b>9.3%</b> | <b>-1.1%</b>          |
| <b>Portland Metro</b>            | <b>7.9%</b> | <b>-0.6%</b>          |

Source: JLL

## RENTAL RATES

CBRE data show overall average FSG asking rates hitting new highs during each of the last quarters, with average rates across the Portland metro increasing 8 percent on a year-over-year basis, by 11.4 percent in the Downtown submarket, and by 3.9 percent in the Suburban submarkets over the same period. JLL notes that rents for new construction Class A product hit an all-time high with asking rents from \$37.50 to \$41.50 full service gross. Class B rents, though, increased at the quickest rate, increasing by 14.2 percent year-over-year to \$23.67.

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

| <b>Brokerage</b> | <b>Average</b> | <b>CBD</b> | <b>Suburban</b> | <b>CBD Class A</b> | <b>CBD Class B</b> | <b>CBD Class C</b> |
|------------------|----------------|------------|-----------------|--------------------|--------------------|--------------------|
| <b>CBRE</b>      | \$25.07        | \$28.78    | \$21.78         | \$31.28            | \$26.92            | \$25.76            |
| <b>Colliers</b>  | \$23.89        | \$28.41    | --              | \$31.31            | \$27.64            | \$22.02            |
| <b>JLL</b>       | \$25.12        | \$30.28    | --              | \$31.14            | \$30.53            | \$26.91            |

Source: Brokerage Quarterly Reports

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

| <b>Location</b>                  | <b>Q1</b> | <b>Change from Q4</b> |
|----------------------------------|-----------|-----------------------|
| Portland CBD                     | \$30.28   | \$0.42                |
| Lloyd District                   | \$25.95   | (\$0.30)              |
| <b>Portland Central City</b>     | \$29.96   | \$0.36                |
| Clackamas / Milwaukie Totals     | \$21.35   | \$0.02                |
| Airport Way/Columbia Corridor    | \$19.78   | \$0.19                |
| Close In Eastside                | \$25.44   | (\$0.15)              |
| Outer Eastside                   | \$19.83   | \$1.51                |
| <b>Portland Eastside Suburbs</b> | \$21.59   | \$0.61                |
| 217 Corridor / Beaverton         | \$21.25   | (\$0.17)              |
| I-5 South Corridor               | \$22.26   | \$0.42                |
| Kruse Way                        | \$28.94   | \$0.13                |
| Northwest                        | \$33.98   | (\$1.19)              |
| Sunset Corridor                  | \$20.60   | \$0.04                |
| SW Close In                      | \$19.29   | \$0.86                |
| <b>Portland Westside</b>         | \$23.61   | \$0.47                |
| Cascade Park/Camas               | \$19.77   | \$0.12                |
| CBD/West Vancouver               | \$20.63   | \$0.38                |
| Hazel Dell / Salmon Creek        | \$21.46   | \$0.48                |
| Orchards/Outer Clark             | \$19.74   | \$0.34                |
| St. John's Central Vancouver     | \$19.89   | (\$0.01)              |
| Vancouver Mall                   | \$18.26   | \$0.57                |
| <b>Vancouver Suburbs</b>         | \$19.99   | \$0.12                |
| <b>Portland Metro</b>            | \$25.12   | \$0.53                |

Source: JLL

## ABSORPTION AND LEASING

Portland continued to experience strong absorption during the first quarter. CBRE data show the Downtown submarket accounting for 85 percent of total absorption, largely as a result of the delivery of Park Avenue West. However, the suburban submarkets also continued to experience positive absorption growth, with absorption increasing on a year-over-year basis. JLL is tracking 4 million square feet of tenants in the market while CBRE is tracking 1.94 million square feet of tenants in the market. Expect high levels of absorption as deliveries pick up during the second and third quarters.

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

| <b>Brokerage</b> | <b>Overall</b> | <b>CBD</b> | <b>Suburban</b> |
|------------------|----------------|------------|-----------------|
| CBRE             | 248,470        | 198,439    | 36,409          |
| Colliers         | 256,843        | (36,554)   | 293,427         |
| JLL              | 178,251        | 30,299     | 128,209         |

Source: Brokerage Quarterly Reports

**Table 6: Notable Lease Transactions, First Quarter 2016**

| <b>Tenant</b>                   | <b>Building/Address</b>           | <b>Market</b>                  | <b>Square Feet</b> |
|---------------------------------|-----------------------------------|--------------------------------|--------------------|
| DAT Solutions                   | Creekside Corporate Park          | 217<br>Corridor/Beaverton      | 53,793             |
| Simple Vacasa                   | Killian, Phase II                 | SE Close In                    | 50,000             |
| Puppet Labs                     | RiverTec                          | CBD                            | 37,441             |
| Qmedtrix                        | Block 300                         | CBD                            | 37,389             |
| Bank of America (Merrill Lynch) | 8909 SW Barbur Blvd.              | SW Close In                    | 35,945             |
| Greatbatch LTD                  | Pacwest Center                    | CBD                            | 35,197             |
| CTS Language Link               | Nimbus Corporate Center - Bldg 10 | 217<br>Corridor/Beaverton      | 34,987             |
| Zoom+                           | Evergreen Place                   | Cascade Park/Camas             | 34,834             |
| nLight Photonics                | Pearl West                        | CBD                            | 30,193             |
| Ruby Receptionist               | Panther Building                  | St. Johns Central<br>Vancouver | 30,000             |
| EmpRes Healthcare               | The Lovejoy                       | CBD                            | 27,621             |
| Vectrus Systems                 | Parkway Plaza III                 | Vancouver Mall                 | 25,648             |
| Alliant Systems LLC             | InfoMart Hillsboro                | Sunset Corridor                | 24,178             |
| Act-On Software, Inc            | 351 NW 12th                       | CBD                            | 23,000             |
| DexCom                          | Bank of America Financial Center  | CBD                            | 18,197             |
| Centrl Office                   | Block 300                         | CBD                            | 16,501             |
|                                 | Block 75                          | Lloyd District                 | 15,268             |

Source: JLL; Colliers International

## SALES TRANSACTIONS

CBRE reported a total of \$175 million in sales activity during the first quarter with an average capitalization rate of 5.3 percent. JLL reported a total of \$177.7 million in sales during the quarter.

**Table 7: Notable Sales Transactions, First Quarter 2016**

| <b>Building Address</b>        | <b>Submarket</b>          | <b>Price</b> | <b>Price/SF</b> | <b>SF</b> |
|--------------------------------|---------------------------|--------------|-----------------|-----------|
| RiverEast Center               | Close In Eastside         | \$33,500,000 | \$335           | 99,860    |
| Tanasbourne<br>Commerce Center | Sunset Corridor           | \$31,100,000 | \$169           | 183,907   |
| The Round                      | 217<br>Corridor/Beaverton | \$29,325,000 | \$201           | 146,028   |
| Rock Creek<br>Corporate Center | Sunset Corridor           | \$23,000,000 | \$161           | 142,661   |
| Sunset Corporate<br>Park       | Sunset Corridor           | \$22,000,000 | \$108           | 203,244   |
| Ballou & Wright<br>Building    | CBD                       | \$14,000,000 | \$252           | 55,500    |
| 811 @ Waterfront               | CBD                       | \$12,600,000 | \$222           | 56,700    |
| Merchant Hotel<br>Building     | CBD                       | \$12,188,000 | \$134           | 90,810    |

Source: JLL; Colliers International



## DELIVERIES AND CONSTRUCTION

Colliers expects 1.6 million square feet to deliver during the remainder of 2016. JLL also reports a total of 1.6 million square feet under construction, with 57 percent already preleased. Furthermore, JLL reports that a lease signed during the second quarter by Elemental Technologies, a video encoding company purchased by Amazon in 2015, for the top four floors of the 1320 Broadway Building, has pushed pre-leasing for 2016 deliveries to 73 percent. CBRE reports a total of over 2 million square feet in the pipeline. Of this, 1.3 million square feet is expected during 2016 and CBRE reports 69.2 percent of this space has been preleased. 854,497 square feet is expected during 2017. None of the deliveries slated for 2017 are reported to be preleased.

Killian Pacific completed its 48,000 square foot Hudson Building in Vancouver this quarter. While the delivery points to a possible renaissance underway in Downtown Vancouver, the three-story structure built with load bearing brick and exposed heavy timber also lays further precedence for renewed use of these historic building materials in the region.

Use of exposed heavy timber caters to demand for a creative office feel, provides potential stimulus to rural Oregon economies dependent on timber, and reportedly has net environmental benefits through its sequestration of carbon. Cross-laminated timber (CLT), a particular type of heavy timber, promises to allow for expanded use of heavy timber products, with the potential for timber high-rise construction. However, its use has thus far been limited as a result of supply and engineering obstacles. With Oregon's D.R. Johnson now manufacturing CLT panels, the federal government providing grant funding to early adopters, and support from the State of Oregon, costs should begin to decrease to a point where the material becomes more competitive.

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

| <b>Location</b>                  | <b>Deliveries</b> | <b>% of Total Deliveries</b> | <b>Under Construction</b> | <b>% of Total Construction</b> |
|----------------------------------|-------------------|------------------------------|---------------------------|--------------------------------|
| Portland CBD                     | 34,749            | 54%                          | 740,413                   | 46%                            |
| Lloyd District                   | --                | --                           | 216,038                   | 13%                            |
| <b>Portland Central City</b>     | 34,749            | 54%                          | 956,451                   | 59%                            |
| Clackamas / Milwaukie Totals     | --                | --                           | --                        | --                             |
| Airport Way/Columbia Corridor    | --                | --                           | --                        | --                             |
| Close In Eastside                | --                | --                           | 277,059                   | 17%                            |
| Outer Eastside                   | --                | --                           | --                        | --                             |
| <b>Portland Eastside Suburbs</b> | --                | --                           | 277,059                   | 17%                            |
| 217 Corridor / Beaverton         | --                | --                           | --                        | --                             |
| I-5 South Corridor               | --                | --                           | --                        | --                             |
| Kruse Way                        | --                | --                           | --                        | --                             |
| Northwest                        | 29,933            | 46%                          | 71,600                    | 4%                             |
| Sunset Corridor                  | --                | --                           | --                        | --                             |
| SW Close In                      | --                | --                           | 96,681                    | 6%                             |
| <b>Portland Westside</b>         | 29,933            | 46%                          | 168,281                   | 10%                            |
| Cascade Park/Camas               | --                | --                           | 206,000                   | 13%                            |
| CBD/West Vancouver               | --                | --                           | --                        | --                             |
| Hazel Dell / Salmon Creek        | --                | --                           | --                        | --                             |
| Orchards/Outer Clark             | --                | --                           | --                        | --                             |
| St. John's Central Vancouver     | --                | --                           | --                        | --                             |
| Vancouver Mall                   | --                | --                           | --                        | --                             |
| <b>Vancouver Suburbs</b>         | --                | --                           | 206,000                   | 13%                            |
| <b>Portland Metro</b>            | 64,682            | 100%                         | 1,607,791                 | 100%                           |

Source: JLL