

RETAIL MARKET ANALYSIS

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

Last year for the retail sector ended on a high note. Rental rates ticked up to \$19.68 per square foot, a 2.5 percent increase from 2017 according to Kidder Mathews. While rental rates increased, vacancy rates decreased to three percent, a telling sign that the industry is moving in the right direction. Retail space accumulating upwards of 330,000 square feet was delivered in 2018 with over 190,000 square feet still being constructed as we move into 2019. Investors are still purchasing retail assets in full force, with average cap rates at 6.05 percent and \$216 per square foot.

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ABSORPTION

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

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

VACANCY

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

RENTAL RATES

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

NOTABLE SALES IN THE RETAIL SPACE

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

Table 1: Submarket and Property Type Breakdown

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

Source: Kidder Mathews

Table 2: Year Over Year Trends

	2018	2017	2016	Annual % Change
Direct Vacancy Rate	3.00%	3.40%	3.60%	-11.78%
Availability Rate	4.30%	4.10%	4.80%	4.88%
Asking Lease Rate	\$19.68	\$19.20	\$18.12	2.50%
Leased SF	1,821,849	2,236,534	2,358,350	-18.54%
Sold SF	4,338,188	4,285,759	4,230,895	1.22%
Net Absorption	841,065	869,592	867,632	N/A

NOTABLE TRANSACTIONS

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

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

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

Source: Capital Pacific

WHAT TO KEEP AN EYE ON

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

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

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

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

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