
OFFICE MARKET ANALYSIS

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In the U.S. and Oregon, the third quarter of 2013 saw office markets hit a plateau. Office deliveries are low, but the pipeline is being filled. Vacancy in the Portland office market is down slightly, even though vacancy in the CBD is up. Absorption is barely positive. Rents are ticking up in response to slow deliveries and low absorption.

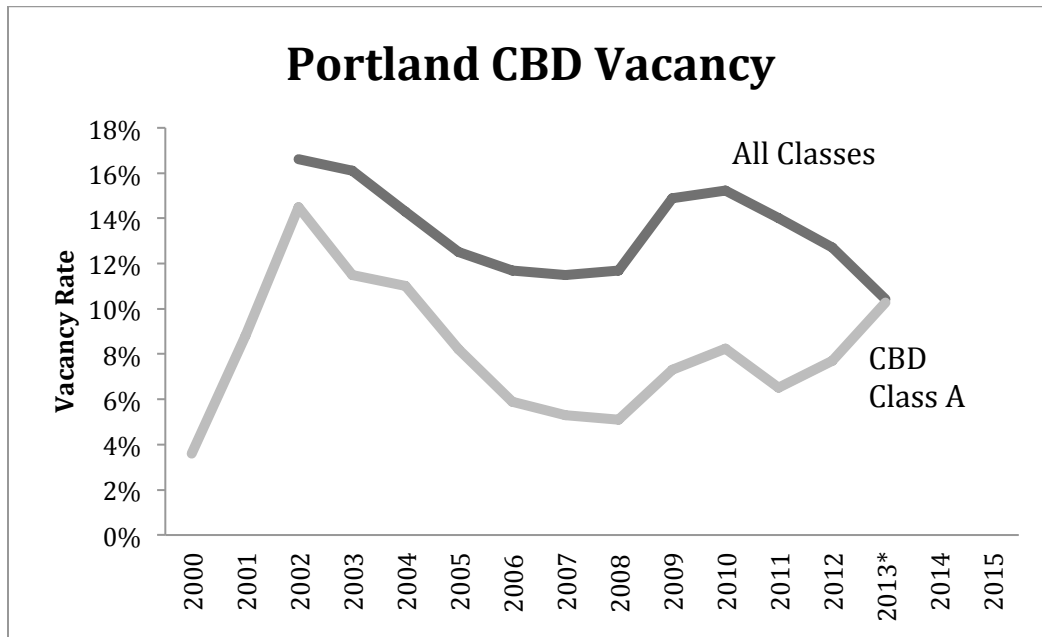
VACANCY

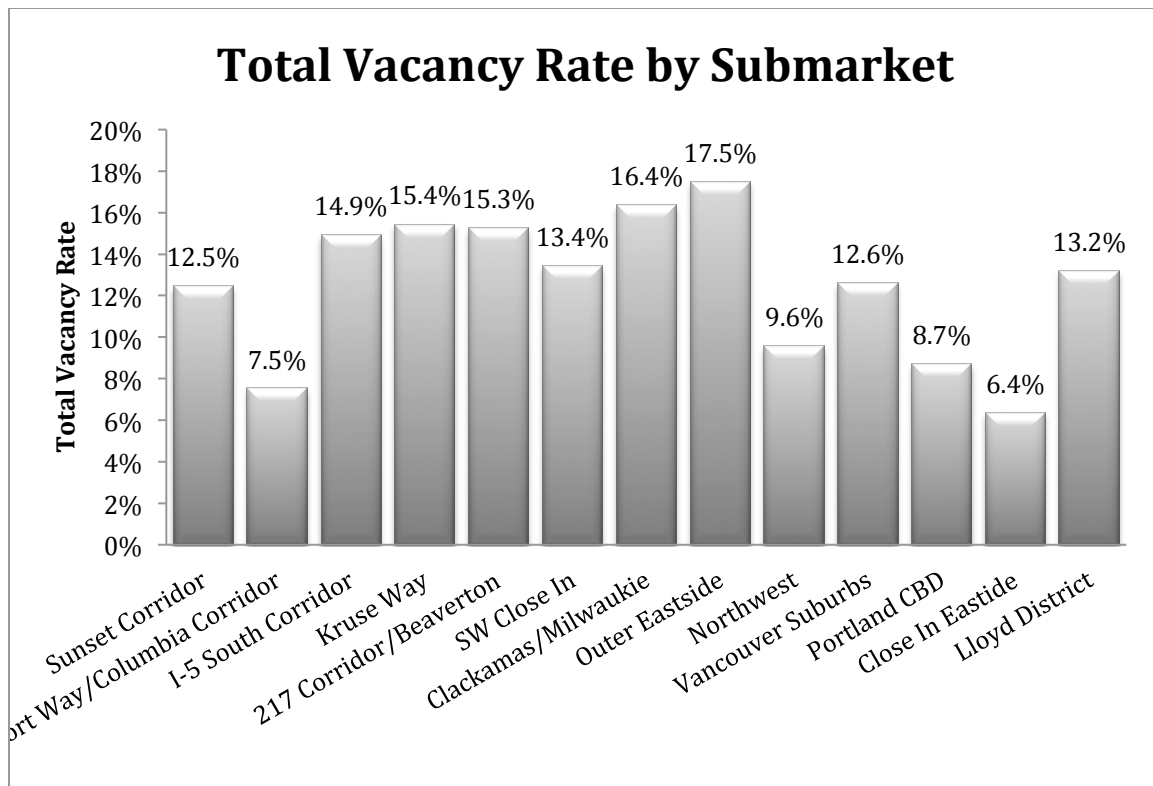
In the Portland MSA vacancy has decreased to 11.2%. On the other hand, vacancy in the CBD has risen to 7.8%, as reported by Jones Lang LaSalle. Despite the rise in vacancy in the CBD, market gazers' sentiment is still pro Portland. The vacancy uptick is due specifically to federal agencies vacating large, contiguous, blocks of office space as the Edith Green/Wendall Wyatt Federal Building came on line. In addition, a 150,000+ square foot section of the Block 300 building, south of Burnside, was vacated by Bureau of Land Management, bringing a prime cut of space to market. Market observers expect expanding creative businesses located north of Burnside to be lining up to tenant this rare, large contiguous space.

Class A office vacancy stands at 10.5% at the end of the third quarter, 9.9% at the end of the second quarter, and 10.3% at the end of the first quarter 2013.

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Outside of the CBD, John's landing has rebounded significantly. Space availability is dwindling, this will put more pressure on the vacancy rate in the CBD as this "CBD-alternative" continues to run dry. Also, the Westside submarket saw the largest decrease in vacancy within the last 12 months. Vacancy has dropped 330 basis points to 10.3%, this is mainly due to Salesforce.com tenanting nearly 117,000 square feet of space.





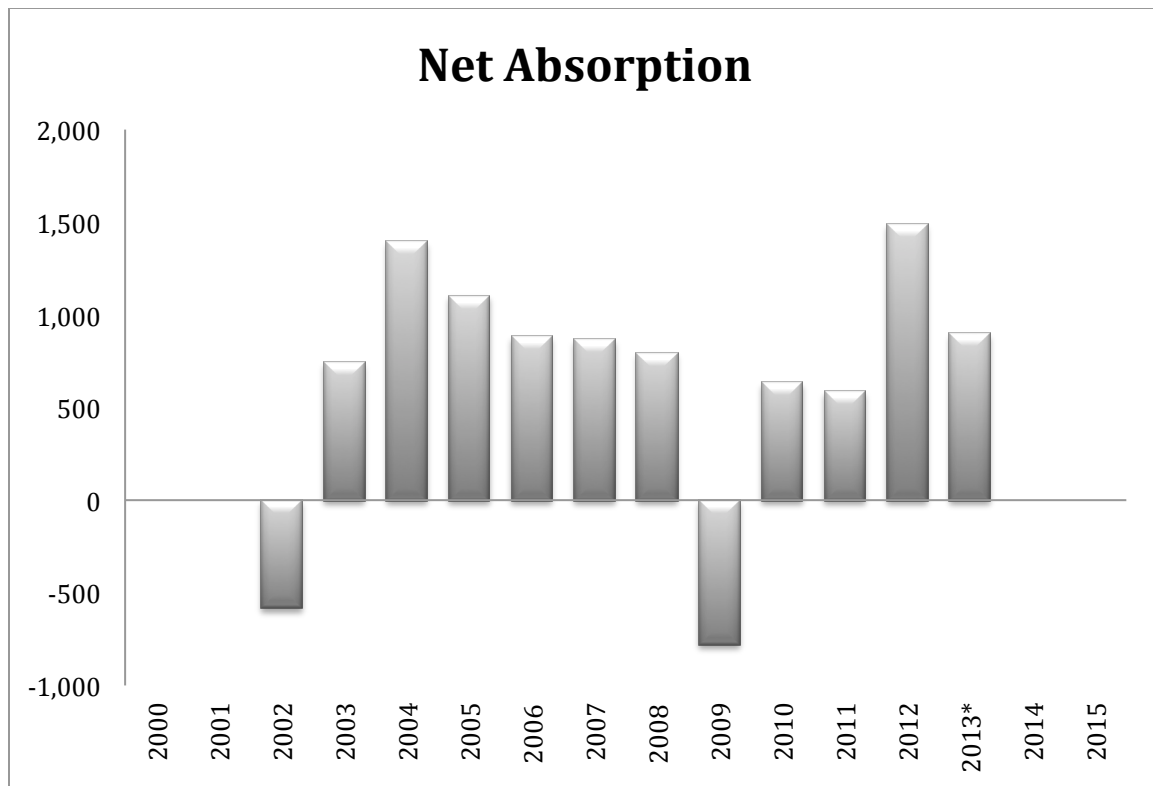
ABSORPTION & LEASING

Although absorption remains positive for the year, last quarter saw absorption at a negative 143,051 square feet. This is compared with a positive 259,909 square feet in the second quarter of this year, and a positive 509,720 from the first quarter of this year.

The third quarter saw Stream Global Services move into 119,077 square feet at the Wilsonville Corporate Plaza, and the large moves by Salesforce.com and Bureau of Land Management.

Most of the negative motion came from Class-A office space with a net movement of negative 141,300 square feet, compared to 100,139 square feet in the second quarter of 2013, and 376,964 square feet in the first quarter 2013.

For the leasing activity and absorption that did take place, the lions share came from the Westside suburbs, with 69% of all absorption coming from this area.

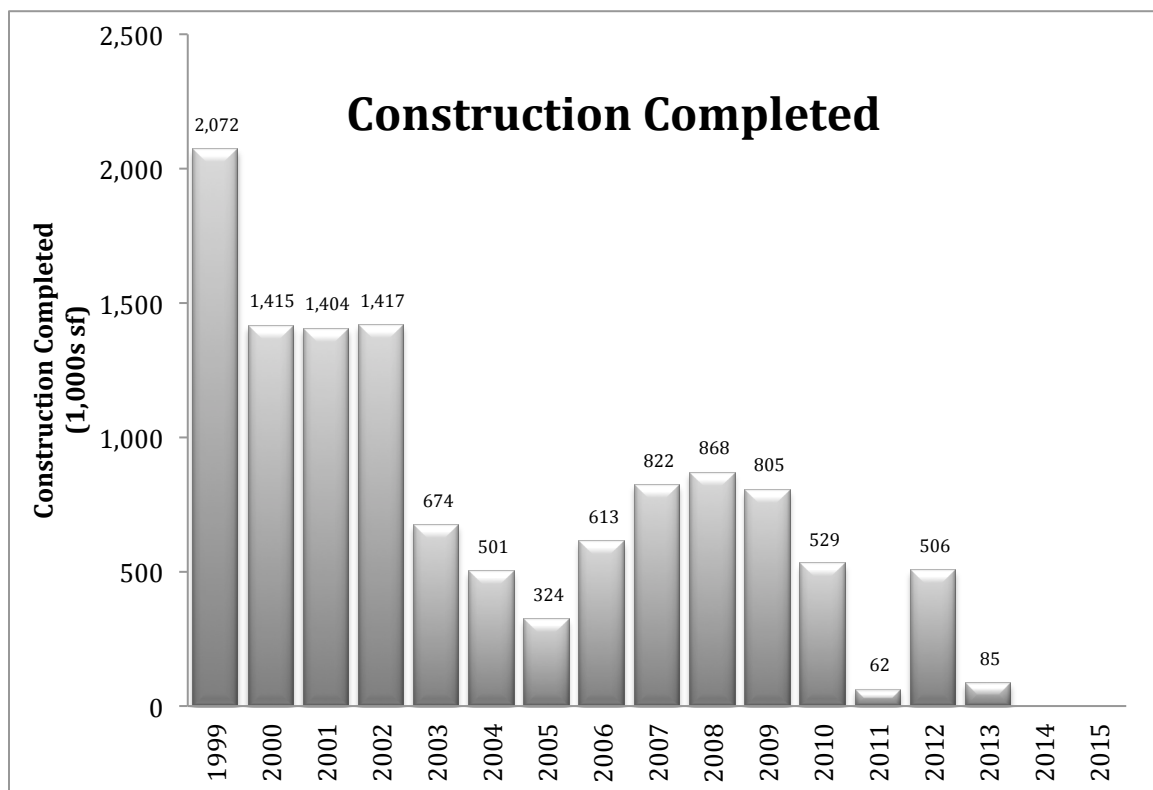


Completed lease transactions				
Tenant	Building/Address	Submarket	SF	Type
FIServ Solutions	Rock Creek Corporate Campus	Sunset Corridor	77,226	Renewal
Ball Janik	One Main Place	CBD	41,750	Renewal
OIA Global	2100 River Parkway	CBD	32,661	New
AT&T	South Place	I-5 South Corridor	27,529	Renewal
Legacy Health Systems	Fremont Place	CBD	19,934	Expansion
Parsons Brinckerhoff	400 Sixth Avenue	CBD	18,733	Extension
Summit Semiconductor	Sunset Corporate Park	Sunset Corridor	16,189	Renewal
Avanti Destinations	Columbia Square	CBD	14,531	New
Hart Crowser	Nimbus Corporate Center	217 Corridor/Beaverton	14,300	Renewal
A&I Benefit Plan Administrators	Terminal Sales Building	CBD	14,251	Renewal
Chrome Data Solutions	Lloyd 700 Building	Lloyd District	13,661	Renewal
Regus	US Bancorp Tower	CBD	13,583	New
American Family Insurance	Tigard Triangle Commons	I-5 South Corridor	13,417	Renewal
Swift	1714 NW Overton	CBD	12,900	Expansion
InComm Digital	US Bancorp Tower	CBD	11,933	New
Fluor Engineering	AmberGlen 1400	Sunset Corridor	11,363	New

CONSTRUCTION AND DELIVERIES

In the last 12 months developers have completed 130,000 square feet of office space, increasing the stock by a mere 0.2%. In 2012 a total of 575,000 square feet of office space was introduced to the Portland MSA. The lack of new supply and increasing need for more and larger space as the economic position of Portland continues to improve has fueled the trend of redevelopment. At the moment there are 12 large scale redevelopment projects taking place in the Central City submarket, as the need for more creative space is being met. Though there is so much redevelopment going on there were several noteworthy new developments brought to the market in the last quarter. In particular, Tanasbourne Professional Office with 34% of its 20,000 square feet occupied and 333 Warner Milne Rd with 10,916 square feet, now 52% occupied.

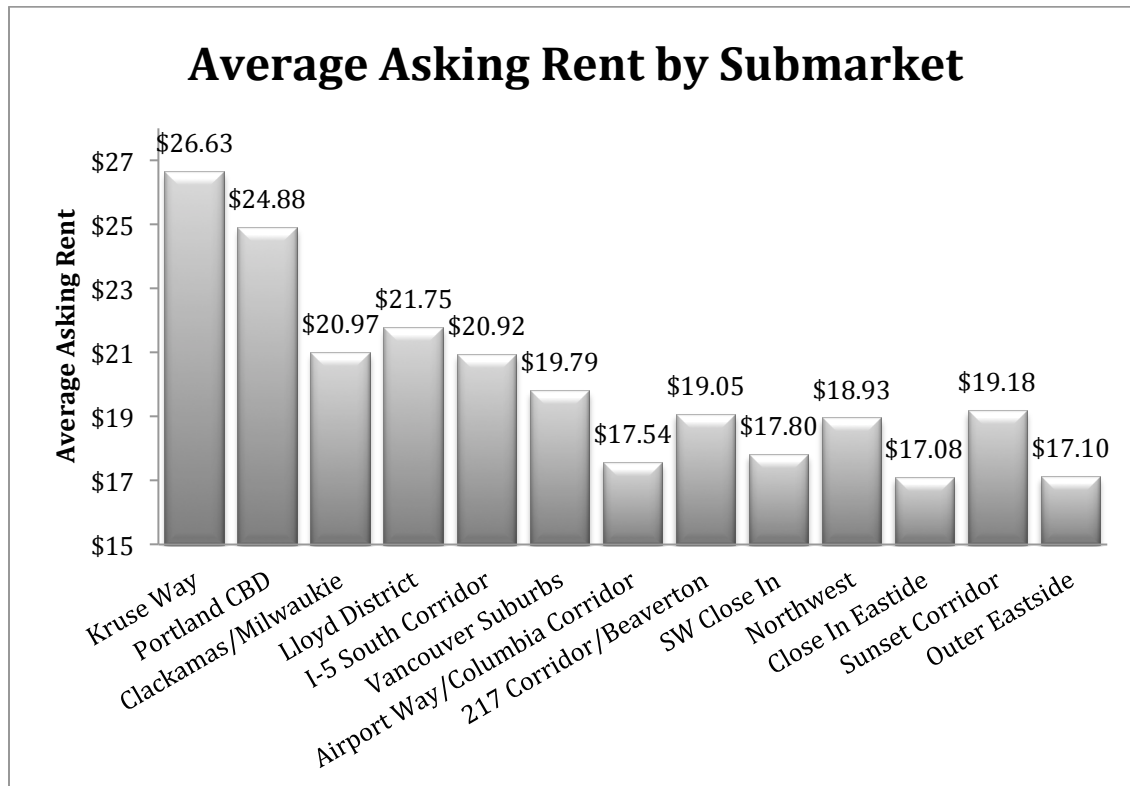
At the end of the third quarter there were two large projects underway, 4310 SW Macadam Ave, with 55,000 square feet 100% preleased and 56 S 1st St, with 12,000 square feet 0% preleased. Also, TMT development announced the recommencement on Park Avenue South that will bring 13 floors of office space to the CBD.



RENTAL RATES

For all classes of available office spaces, the average asking rental rate stands at \$19.91 per square foot, a 0.5% decrease from three months ago. In this number resides the rub of Portland's rental rate, though on average there was a minor drop

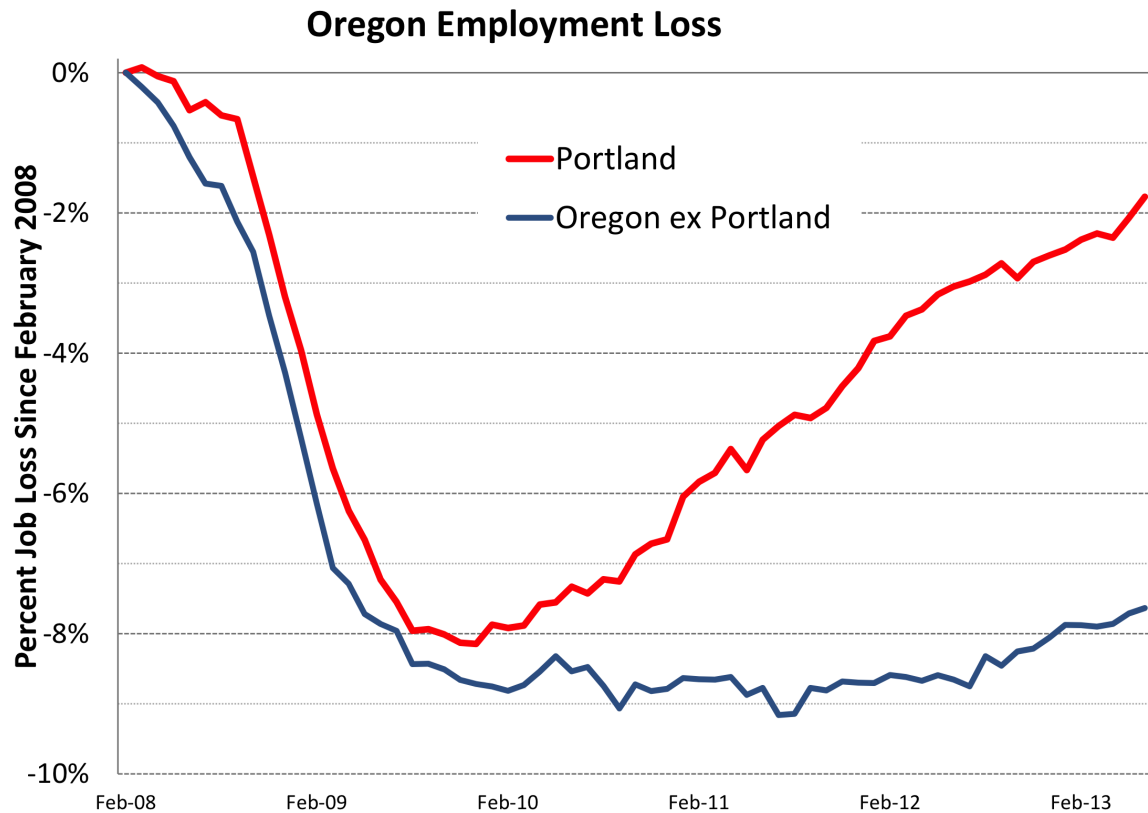
there are many bright spots with the MSA, and to say bright spot is something of an understatement. In the vein of positive signs in the Portland MSA, Couch Street stands as the prime example, as it has moved into 18th place for the most expensive office space in the U.S. at an average of \$37 per square feet.



Over the past several quarters the CBD has shown continuous improvement. Class-A rents are up 2.6% on the quarter and 5% year over year, rising to \$24.54 per square foot. Class-B rents are up 4.5%, year over year. The CBD, as a whole, has experienced the largest increase in rents, up to \$24.88 per square foot.

As rents for Class-A and Class-B office space continue to converge we may see some historical Class-B creative space actually overtake more traditional Class-A space in asking rent. Also, as demand continues to expand and development does not, owners will continue to lift rents at the fastest pace seen since the Great Recession. Marcus & Millichap anticipates that average asking rents will rise to \$20.40 per square foot within the next quarter.

Portland's employment situation is improving more quickly than the rest of the state. As shown in the figure below, the Oregon Office of Economic Analysis finds that Portland's employment is only 2 percent lower than pre-recession levels, while the rest of the state remains approximately 8 percent lower than pre-recession levels. Thus, Portland's office market is predicted to outperform the rest of the state for quite some time.



NOTEWORTHY EVENTS

Calming fears of layoffs and closure, on Daimler Trucks North America announced in September 2013, that it would consolidate and expand its headquarters at a new Swan Island location. The anticipated \$250 million project is projected to add an additional 265,000 square feet office space in Portland, and 400 new jobs with Daimler.

On September 30th, Nike purchased a Class-B office with 25,565 square feet for \$6,484,721, located at 15500 SW Jay Street, as a part of their headquarters expansion

In late September ScanlanKemperBard dropped its option to purchase the 321 Glisan project. They were unable to find an appropriate tenant and walked away from the troubled project

Despite a somewhat sideways step in the third quarter 2013, Portland's office market remains on solid footing and continues in upward trajectory as the CBD and outlying areas keep rising. Cap rates are no longer leveling off, but rather continue to dropping, bringing more impetus to the market to either move sale transactions forward or to move developments forward; in either case rising rents will continue these trends for some time. ■