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## RETAIL MARKET ANALYSIS

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The combination of Hurricane Sandy and the fiscal cliff did not bode well for retailers, as the Conference Board's index of consumer confidence fell to 65.1 in December, its lowest level since August. However, buyers came out in full force for the holidays, with retailers enjoying a 4 percent overall increase in sales from 2011. Retail property owners and retailers alike move into 2013 with tempered expectations for slow, continual growth while the economy strengthens.

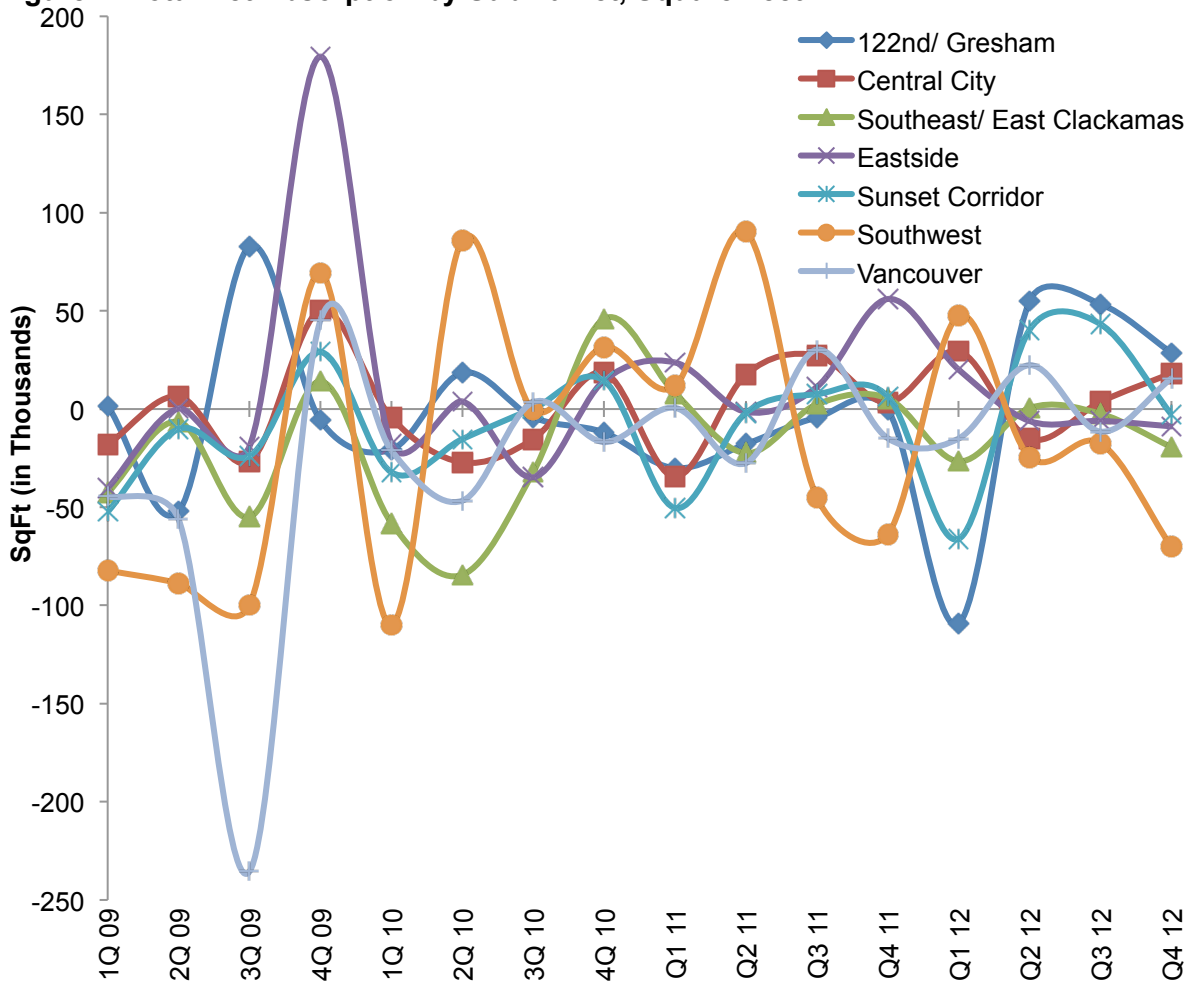
Cushman & Wakefield reports an overall retail vacancy rate of 5.7 percent, up three tenths of a percentage from the same period last year. Absorption totaled 141,586 square feet for the year, and rents are up by 0.4 percent to 15.83 per square foot. These metrics are expected to improve in 2013, which will lead to higher rental rates.

Mixed-use projects drove much of the retail development in 2012, with developers taking advantage of pedestrian traffic around new department development, reports Kidder Mathews. Cushman & Wakefield report that 469,684 square feet of retail space were delivered to the market in 2012. Most development was build-to-suit or owner-user oriented. Speculative retail construction remains mostly absent, save for smaller infill projects, or ground floors of apartment buildings.

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Oregon’s economy continues to steadily recover, with activity expected to pick up in 2013. As job growth continues on an upward trend, the retail sector should see increased demand as consumers return to the market. Consumers have been spooked by the election and natural disasters, but have been encouraged by a slow turn-around in the housing market. Consumer confidence is expected to rise alongside news of job creation and a residential housing market turnaround. Retailers continue to lose money to online sellers, and have made efforts to level the playing field. Legislation has been proposed that charges a sales tax for online purchases.

**Figure 1: Total Net Absorption by Submarket, Square Feet**

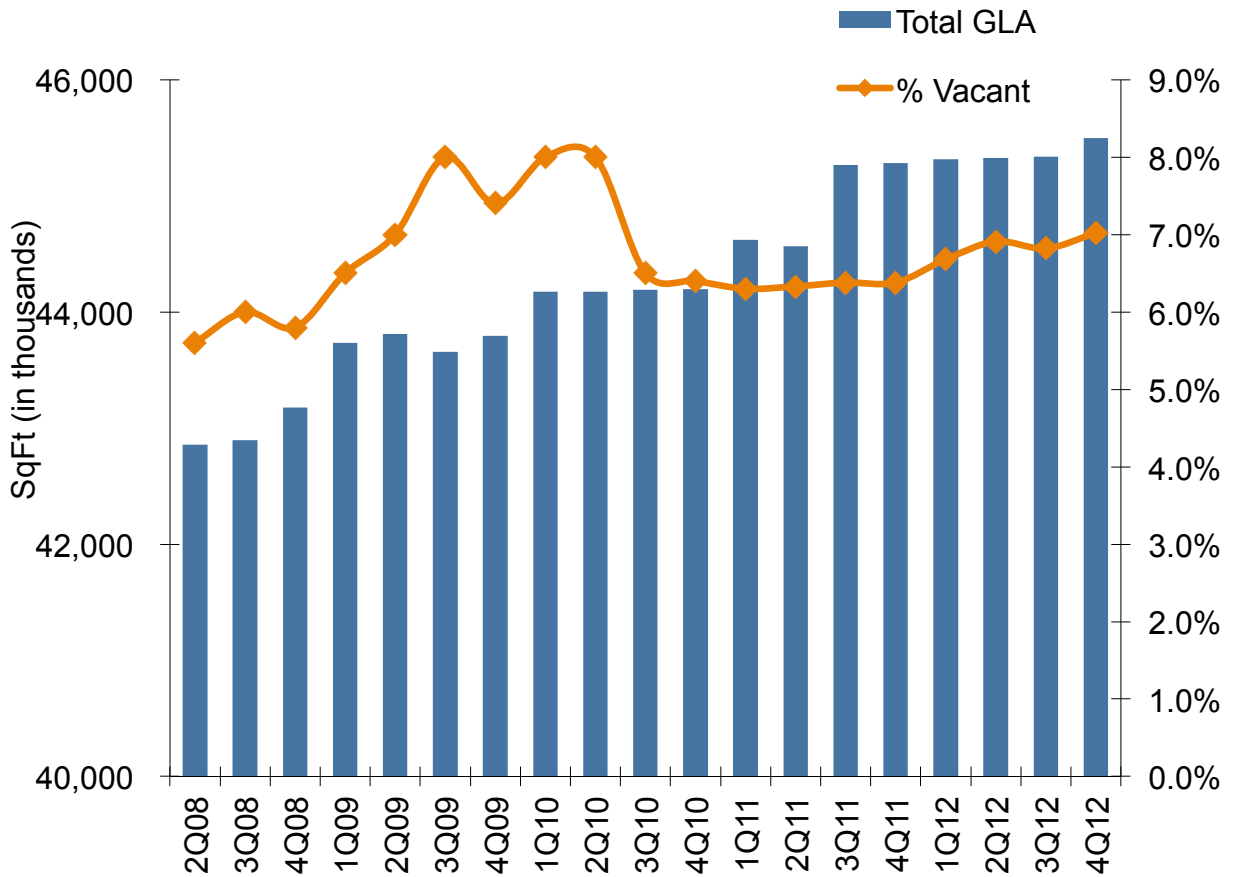


Source: Norris, Beggs, & Simpson Retail Reports

Norris, Beggs & Simpson reports negative net absorption in four of the seven major submarkets. The Southwest district lost the most, reporting a negative 70,201 square feet. 122<sup>nd</sup>/Gresham led all submarkets with a gain of 28,713 square feet of positive net absorption. Vancouver was a distant second, with a net 15,571 square feet absorbed. The Eastside, Central City, Clackamas, and Sunset Corridor all experienced losses of 8806, 10,840, 19,379, and 2,809 square feet, respectively.

In contrast, Kidder Mathews reports a positive net absorption for the quarter of 212,380 square feet, but a negative 83,458 square feet for the year, along with a vacancy rate of 5.9 percent. The Central City appears to be the only submarket with continuous improvement each quarter in terms of net absorption, with other markets subject to more stark fluctuations.

**Figure 2: Total Gross Leasable Area (GLA) and Vacancy (%)**

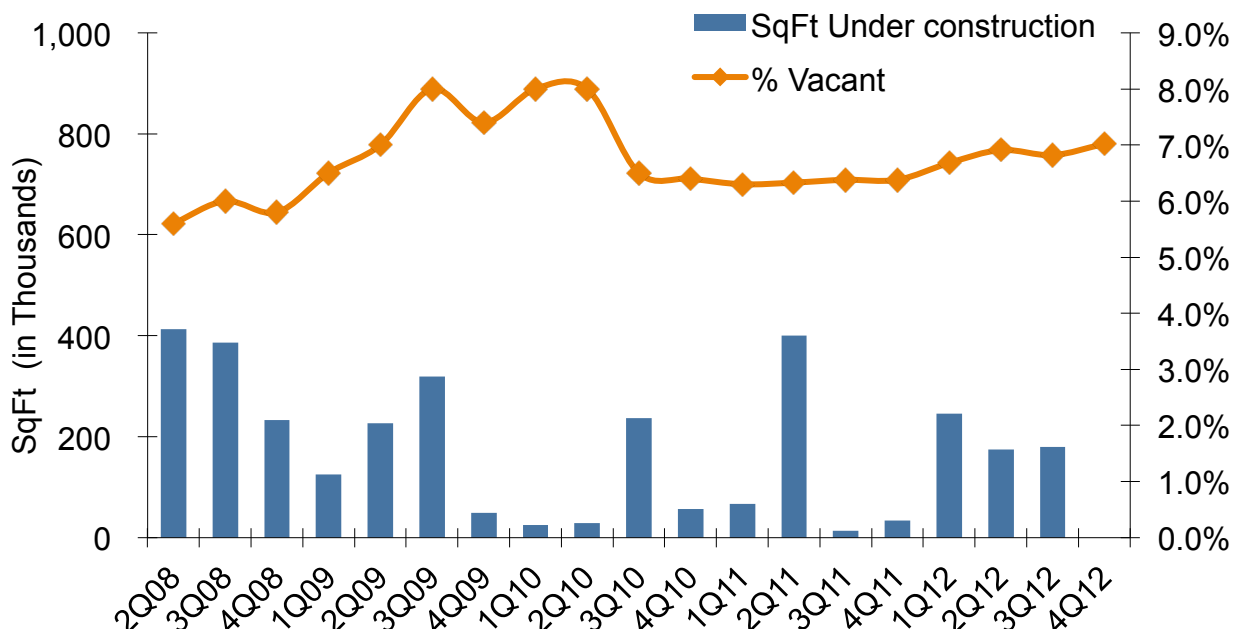


Source: Norris, Beggs, & Simpson Retail Reports

The total amount of gross leasable area (GLA) has remained relatively flat over the past six quarters, with little square footage delivered to the market. This past quarter saw 47,243 square feet delivered to the market with a 5.9 percent vacancy rate, according to Kidder Mathews. Vacancy rates have remained relatively flat for over two years, but have had a slight uptick in 2012. Negative absorption, tenant concessions, internet sales and weak market fundamentals have inhibited recovery.

The fourth quarter saw two large deliveries to the market in the 137,000 target store in the Jantzen Beach SuperCenter and the 95,000 square foot Stafford Hills Tennis Club.

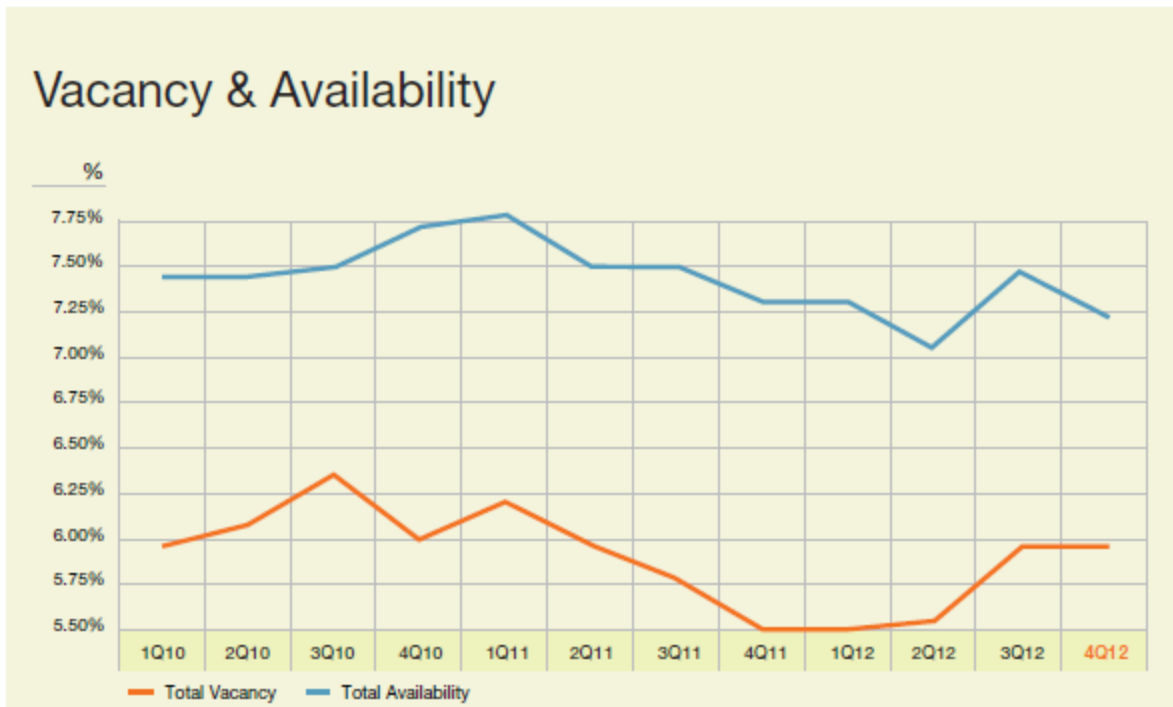
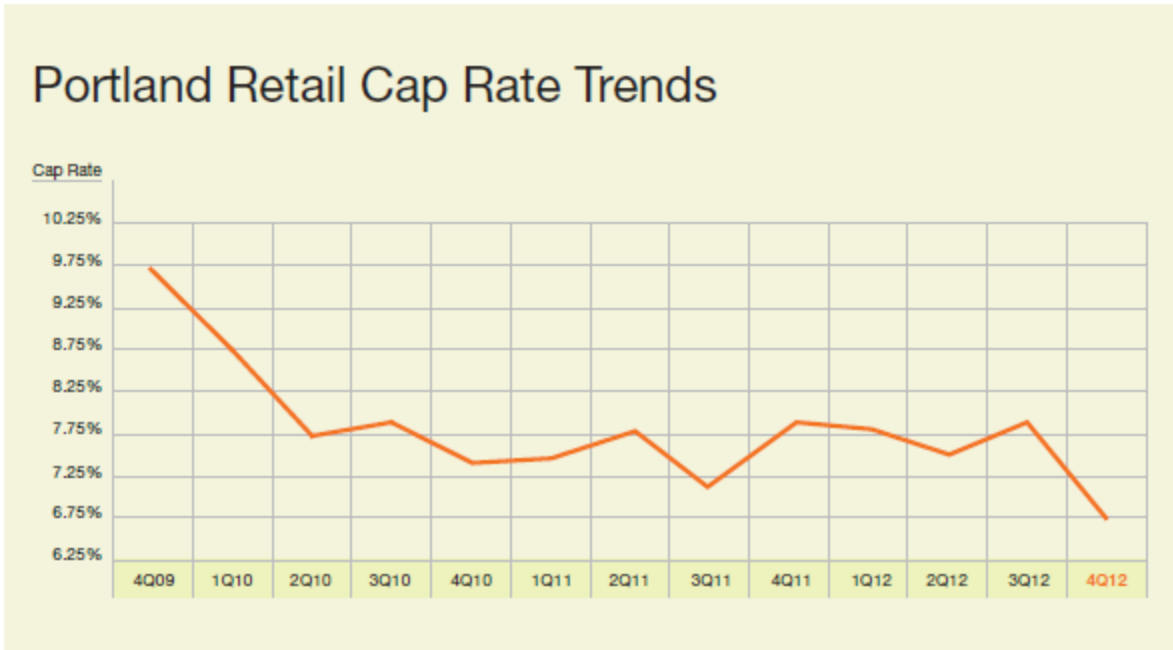
**Figure 3: SqFt of Retail Space Under Construction and Vacancy (%)**



Source: Norris, Beggs, & Simpson Retail Reports

Norris, Beggs & Simpson report zero space under construction, and Kidder Mathews reports a scant 47,240. Developers appear to be sidelined by a difficult market, and retailers have been constrained by weak economic fundamentals and uncertainty. Despite this, vacancy has remained between 6-7 percent for the past ten quarters.

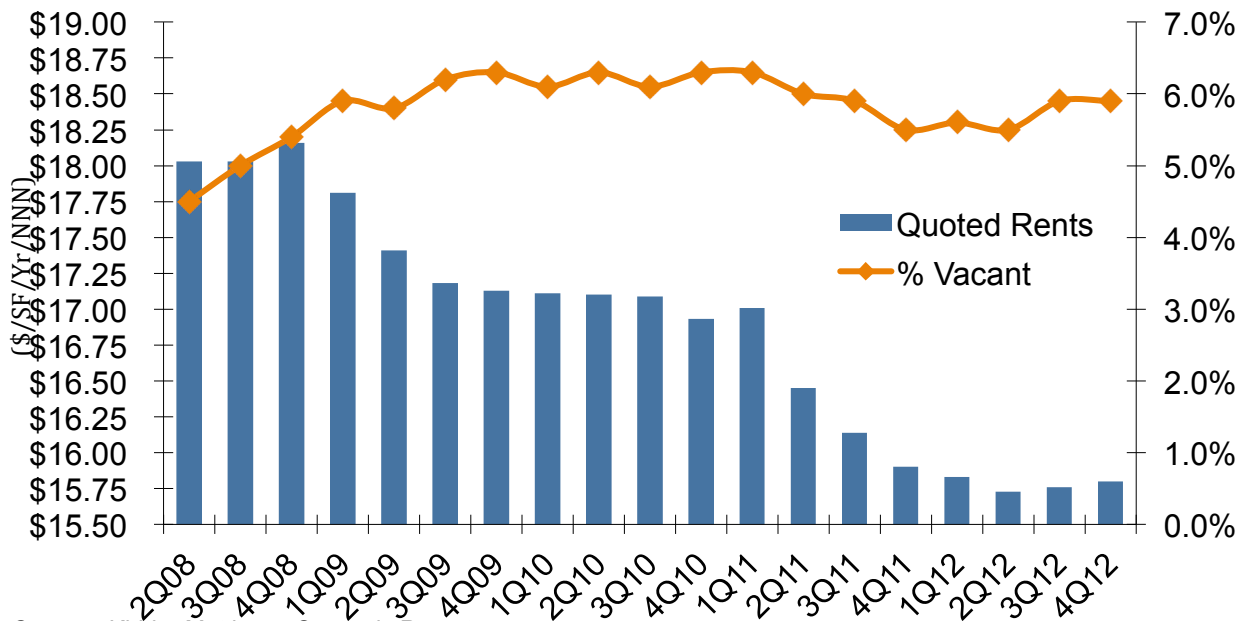
Construction numbers have been low for several quarters. Historically, the numbers being delivered to the market have been very low for some time and has led to a contraction in vacancy rates. This, along with the destruction of existing obsolete buildings will contribute to this eventual turnaround in the market.



Source: Kidder Mathews Retail Reports

Overall, capitalization rates have been headed downwards, which is good news for owners who are looking to sell. Not a lot of selling has been happening, owing mostly to the depressed state of many retail projects, along with the positive economic outlook for the future.

Figure 4: Quoted Rents and Retail Vacancy (%)



Source: Kidder Matthews Quarterly Reports

Kidder Matthews reports a small uptick in vacancy in the third quarter, coupled with a very slight increase in rents. For the most part, the market remained flat. While this is not ideal, it must be considered that this was during a period of great economic uncertainty. It is expected that 2013 will bring changes in retail market fundamentals, along with general economic prosperity. This should lead to lease rates reaching their 2008 high water mark within a year or two.

## 2012 Sale Activity of Note

Property Name	Location	Size (SF)	Vacancy	Date of Sale	Sale Price	Price Per SF	Cap Rate
Wood Village Town Center	Wood Village, OR	149,806	4%	Oct-12	\$27,600,000	\$184	6.40%
Tigard Marketplace	Tigard, OR	136,879	0%	Aug-12	\$16,000,000	\$117	N/A
Riverstone Marketplace	Vancouver, WA	13,837	0%	Jun-12	\$27,977,000	\$246	N/A
Fisher's Mercantile Center	Vancouver, WA	36,014	36%	Jul-12	\$4,000,000	\$111	8.50%
Salmon Creek Square	Vancouver, WA	21,816	7%	Sep-12	\$8,000,000	\$367	7.42%
Tanasbourne Town Center	Hillsboro, OR	12,000	0%	Mar-12	\$4,473,500	\$373	6.80%
Aaron's Furniture	Portland, OR	11,429	0%	Oct-12	\$1,900,000	\$166	7.10%
Hansen's Corner Retail Strip Center	Lake Oswego, OR	10,905	0%	Nov-12	\$2,650,000	\$243	7.25%

The largest retail transaction of Q4 was the sale of the Wood Village Town Center in Wood Village, OR. This transaction carried a low cap rate (6.4 percent) for a Gresham area project. Cap rates are expected to rise in the coming years as inventory is added and competition heats up for prime space. Fisher's Mercantile Center sold at a higher 8.5 percent cap rate, but has a vacancy factor of 64 percent. Investors seeking to rehabilitate or restore existing product have ample supply from which to choose, so long as new construction remains infeasible on spec.

The Portland area retail market has improved by some measures and declined in others, but most agree that it has done well given the circumstances in 2012. Other property types such as multifamily have rebounded impressively in recent quarters. While this type of hot market is not expected for the retail sector, retail remains a key component of many of these projects. The ground floor retail element of many apartment projects should add new, class A space to the market and prove to developers that there is room in the market for more retail product.

Nationally, a portion of the success of the retail market will be determined by pending legislation regarding mandated sales tax in online transactions. This could help bolster retail sales across the board. This, along with little construction, improving market fundamentals, and increased consumer confidence is likely to spur an uptick in demand in 2013. ■