

# RETAIL MARKET ANALYSIS

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Nationally, the retail landscape in the first quarter of 2018 was calm. The underlying market fundamentals remain relatively unchanged. News articles about the “retail apocalypse” continue to come out despite the overall health of the market. There were a few big announcements from national companies affecting the retail landscape in the quarter. Toys “R” Us declared it is going out of businesses and will be winding down all of their stores in the coming year. Albertson’s is pushing to acquire the drug store chain Rite-Aid. Sears has been struggling for some time now and announced another round of store closures for 2018. On a more positive note, Old Navy announced plans to open 60 stores across the country despite Gap Inc. making plans to close under-performing Gap and Banana Republic stores.

The national vacancy rate ended the quarter at 4.5 percent and the average asking lease rate was \$16.49 per square foot. This is a 1.6 percent increase in asking rates above the end of 2017 and a 3.94 percent increase over the past four quarters. Cap rates have been trending upwards slightly to end the quarter at 7.12 percent.

Portland’s retail market continues to stay in sync with the national retail market. After a strong 2017, the Portland retail market started the first quarter of 2018 relatively



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unchanged. The market experienced 282,839 square feet of positive absorption which helped push the vacancy rate further down from 3.3 percent at the end of 2017 to 3.2 percent.

As part of the Sears closures, it was announced that Sears will be closing their location at Lloyd Mall. Lloyd Mall has had difficulties in the past few years, including the loss of Nordstrom and with another major anchor vacating the mall, the outlook for the property is not good. The challenge of Lloyd Mall isn't unique to that property. Poorly positioned and uninteresting retail projects will continue to struggle. Fred Bruning, founder and CEO of CenterCal Properties, succinctly puts the problem of under-performing retail projects as such.

I believe the challenges many traditional anchor-driven malls are facing is more about the declining strength of the anchor department stores, coupled with the fact that most malls are just not very interesting places to visit. Creating a compelling place today is equally, if not more, important than the precise tenant mix in the center. Gathering places, gardens, seating areas, entertainment components and generally creating places where people really want to be is a major key to success in attracting the customer base needed to make your tenants successful.

The "retail apocalypse" stories will continue as the traditional retail model is challenged. However, landlords and retailers that can adapt to the market changes and create compelling reasons to visit will thrive.

## VACANCY

The vacancy rate at the end of the first quarter of 2018 was a very strong 3.2 percent. This is a 10 basis point drop from the end of the fourth quarter 2017. The vacancy rate should continue to hold in that range as the overall lack of new construction and strong market fundamentals will keep inventory low.

**Table 1: Portland Retail Vacancies by Submarket, First Quarter 2018**

| Submarket                  | Q1 2018 Vacancy Rate | Q4 2017 Vacancy Rate | Change from Previous Quarter |
|----------------------------|----------------------|----------------------|------------------------------|
| CBD                        | 10.5%                | 9.3%                 | 1.2%                         |
| Clark County/<br>Vancouver | 4.8%                 | 5.1%                 | (0.3%)                       |
| I-5 Corridor               | 4.6%                 | 4.8%                 | (0.2%)                       |
| Lloyd District             | 3.0%                 | 2.5%                 | (0.5%)                       |
| Northeast                  | 3.1%                 | 3.1%                 | 0.0%                         |
| Northwest                  | 2.3%                 | 2.9%                 | (0.6%)                       |
| Southeast                  | 3.1%                 | 3.3%                 | (0.2%)                       |
| Southwest                  | 3.4%                 | 3.0%                 | 0.4%                         |
| Sunset Corridor            | 2.2%                 | 3.4%                 | (1.2%)                       |
| Total                      | 3.7%                 | 3.9%                 | (0.2%)                       |

Source: Kidder Mathews

VACANCY

**Table 2: Portland Retail Vacancies by Product Type, First Quarter 2018**

| Property Type    | Q1 Vacancy Rate | Q4 Vacancy Rate | Change from Previous Quarter |
|------------------|-----------------|-----------------|------------------------------|
| Malls            | 2.2%            | 1.9%            | 0.3%                         |
| Power Centers    | 2.4%            | 2.8%            | (0.4%)                       |
| Shopping Centers | 6.1%            | 6.6%            | (0.5%)                       |
| Specialty        | 0.0%            | 0.0%            | 0.0%                         |
| General Retail   | 2.6%            | 2.6%            | 0.0%                         |

Source: Kidder Mathews

ABSORPTION AND LEASING

Absorption is up to start the year. The first quarter ended with a positive 282,839 square feet of absorption. Kidder Mathews highlights the expansion of restaurant chains in the first quarter of the year. Pink Taco, a Los Angeles based restaurant chain is taking over 7,941 square feet at the Porter Glisan Building. The space was formerly occupied by tiki themed bar and restaurant Trader Vic's. Local food and beverage chains have also been making expansion moves in the first quarter. Tea Bar is set to open its fourth location in the ground floor of Park Avenue West while Coco Donut added two locations in the quarter, one at the Alberta Apartments and the other in the Happy Valley area at Sunnyside Plaza. Some of the larger leases signed in the quarter include 31,214 square feet at Mall 205 and 29,452 square feet was taken by Circus Trix at Santa Clara Square in Eugene, OR. Big box retailers continue to struggle but experiential concepts like Circus Trix have been able to backfill former anchor spaces.

**Table 3: Portland Retail Absorption, First Quarter 2018 and YTD.**

| Submarket               | Q1 2018 Net Absorption | YTD Net Absorption |
|-------------------------|------------------------|--------------------|
| CBD                     | (42,657)               | (42,657)           |
| Clark County/ Vancouver | 107,892                | 107,892            |
| I-5 Corridor            | 14,353                 | 14,353             |
| Lloyd District          | (34,223)               | (34,223)           |
| Northeast               | 90,695                 | 90,695             |
| Northwest               | 3,130                  | 3,130              |
| Southeast               | (19,459)               | (19,459)           |
| Southwest               | (62,929)               | (62,929)           |
| Sunset Corridor         | (5,306)                | (5,306)            |
| Total                   | 53,938                 | 53,938             |

Source: Kidder Mathews

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### RENTAL RATES

Rental rates are relatively unchanged through the first quarter of the year. The average asking lease rate was \$19.37 per sq. ft. This is a 3.7 percent increase year-over year. Rates have been consistently climbing due to strong tenant demand and lack of speculative retail development.

**Table 4: Portland Retail Asking Rents, First Quarter 2018.**

| Brokerage      | Kidder Mathews | CoStar  |
|----------------|----------------|---------|
| CBD            | \$21.02        | \$21.02 |
| Lloyd District | \$24.44        | \$24.36 |
| I-5 Corridor   | \$19.66        | \$16.89 |
| Clark County   | \$18.29        | \$20.40 |

Source: CoStar and Kidder Mathews

### DELIVERIES AND CONSTRUCTION

A total of eight retail projects were delivered to the market this quarter, which added 81,836 square feet to the market. This adds to the 454,363 square feet of retail space constructed in the last four quarters. The 38,000 square feet Restoration Hardware concept was delivered to the market in the quarter at NW 23rd and Glisan. Additionally, 20,000 square feet was delivered in the ground floor of The Union apartment project. Currently there is an additional 1,088,080 square feet of retail under construction across the market. Much of the retail being constructed in Portland is part of mixed-use apartment projects. Kidder Mathews notes that there are 20 mixed-use projects under construction in Portland with some retail component to them.

**Table 5: Notable Retail Developments, First Quarter 2018**

| Building/Address                      | Market                     | SF      | Delivery Year |
|---------------------------------------|----------------------------|---------|---------------|
| Cedar Hills Crossing Community Center | North Beaverton            | 128,652 | Q2 2018       |
| Cedar Creek Plaza                     | I-5 Corridor Retail Market | 70,000  | Q3 2018       |
| The Union at St. Johns                | Rivergate                  | 80,000  | Q1 2018       |
| The Waterfront Vancouver              | Clark County               | 28,528  | Q2 2018       |

Source: CoStar and Kidder Mathews

### SALES TRANSACTIONS

Sales volume at the end of 2017 was down from the 2016 year end total. Heading into 2018, signs for whether sales volume will continue the downward trajectory are being closely watched. There were a few large shopping center sales to start the year off. The first was Wood Village Town Center. This 143,334 square foot center sold for \$26.55 million, which is \$182 per square foot. Just a little south west of Portland, McMinnville Plaza, a 89,626 square foot shopping center sold for \$17.4 million which is \$194 per square foot.

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### **SALES TRANSACTIONS**

Average cap rates have been trending upward, ending the year at 6.71 percent in Portland. The previous year, cap rates averaged around 6.24 percent. The expectation is that cap rates will continue to rise in the coming year further depressing prices. However, strongly positioned properties with good credit tenants still command above average cap rate valuations in the market. Portland's cap rates are well positioned to the national average of 7.12 percent.