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The Threat
With the recent City action to approve the concept for development of a soccer stadium at PGE Park and a minor league baseball stadium at the Rose Quarter to replace the Memorial Coliseum, a valuable asset owned by the City stands in jeopardy. Combined with Paul Allen’s Arena Corporation’s desire to develop an entertainment district at the Rose Quarter, there are twin threats to the Coliseum that magnify the importance of understanding both the value of the historic modern icon and the opportunity cost of bowing to the calls to demolish it.

The Asset
The 272,000 SF Coliseum, valued at $57.1 million tax RMV, a fraction of its replacement value, was designed in the modern International Style by the internationally renowned architecture firm Skidmore, Owings and Merrill (SOM) and built 50 years ago, just long enough to qualify it for placement on the National Register of Historic Places. Its design and construction are at one
and the same time elegantly simple and enormously sophisticated. There is a concrete bowl sitting inside a square glass box, 360 feet long on each side. The two structures are disconnected from one another. The entire 130,000 square-foot box is held up by only four cruciform concrete columns, outside the bowl. That provides unobstructed sight lines inside the bowl, which is ideal for large events.

In fact, after the four columns were constructed, the steel truss roof was the first thing built for an elegantly simple reason. In the rain-soaked Northwest, the roof was built as an umbrella to
shelter the construction of the concrete bowl inside. That concrete bowl is a very sophisticated structure with a graceful curve at its perimeter, (shown in the photograph on page 3 above and the image below), rising along the east and west sides to give more seating in the middle. Moreover, the concrete bowl is cantilevered, not only lightening its profile but also creating about 30,000 square feet of usable but unused space under its sheltering form. This is particularly felicitous because standing on the concourse on the west side, one overlooks the Willamette River, all the downtown Portland skyscrapers and the burgeoning Pearl district.

The Coliseum still has 40,000 square feet of space, as large as a Portland city block, in an exhibition hall under the plaza on the east side [left]. Formerly, it had been 60,000 square feet but the construction of the Rose Garden reduced its size. Nevertheless, that can be very useful space not only because of its size but also because it is accessible at grade from the north side.

The Memorial
A sunken courtyard between the exhibition hall and the Coliseum provides a calm, reflective space, with a reflecting pool, for the Veterans’ Memorial. But perhaps the real memorial to the veterans is the clear expression of American ideals that are expressed in simple, transparent forms and innovative engineering for a civic space in which all Portlanders can gather for a variety of communal functions.

Note that the glazed Coliseum is transparent, in contrast with the Rose Garden, and has worked equally well housing Portland State University graduations, Barack Obama and Ralph Nader political rallies, concerts and a wide variety of sports including basketball, hockey games and tennis matches.

The undulating concrete bowl was designed not only to be visible from across the river but also to be lower than the roof to admit natural daylight into the bowl, as one can see in the image below. Therefore, the space was ahead of its time in interacting with the environment. Moreover, when in use, the Coliseum acts as a beacon visible
from downtown inviting citizens to it. The blackening curtains that surround the bowl when darkening was needed are no longer operable and are left closed, thereby depriving the interior of the benefit of daylight. The glass box is recessed to float above a concrete plinth.

**Sustainability**

In many ways the Coliseum is located and designed to better fit a sustainable future than most of the buildings of its age. It is now one of the most accessible sites in Portland by both rail and road. It is situated at the intersection of two light rail lines, north-south and east-west, one of which goes directly to the airport.

If high-speed rail is ever to come to Portland, it must come on the east side and would pass below the Coliseum right where it connects to a major transcontinental rail line. At the intersection of the major north-south and east-west freeways in Oregon, travel to and from it is direct and easily accessible.

The Coliseum’s 130,000 square-foot roof, the size of 3.25 city blocks, is totally unshaded and flat, lending it well to an enormous array of photovoltaic solar collectors. Its glass walls on all four sides are only single-paned windows ostensibly making it an energy hog. However, with the addition of a second glass skin on the interior, what is an energy waster could become an energy producer because the glass walls themselves would become solar collectors trapping heat. With appropriate ducts at the roof, that heat generated could be moved to where it is needed, or it could be exhausted, providing insulation and cooling. As the sun moves around its glass walls, the Coliseum could collect more heat than most other kinds of structures. In fact, progressive buildings in Europe, like the Commerzbank tower in Frankfurt, were designed according to the same principle. Therefore, the Coliseum could be a trailblazer in retrofitting iconic historic buildings for energy efficiency far more sustainably than would its demolition and replacement by new construction of a baseball stadium.

**Efficiency**

Constructing the Coliseum’s pure form also produced great efficiency. To build the Coliseum, concrete trucks drove right in on a depressed entry on the north side and out on the south. They can still do that, which makes it simple to bring large shows into and out of the lower
level. It also permits the demolition of the bowl in such a manner as to maintain the integrity of
the glass box for other uses in the unfortunate case that it should not be feasible to find a
valuable program and uses for both the bowl and the box.

Reuse Options
It is critical to review some of the options for reuse of the Coliseum. Seven years ago in the
Spring of 2002, I taught a 3-month long Real Estate Development Workshop in my class of
graduate urban planning and development students at the College of Urban Affairs at PSU
which produced four alternative uses for the Coliseum that deserve consideration – a
headquarters hotel, an arts complex, a sustainable technology center and an urban home
center. We also considered two more options - the Howell proposal to transform it into the
Coliseum Transportation Center for high-speed rail, commuter rail, light rail and streetcar
integration [above] and the Obletz plan to convert it into the Memorial Athletic Recreation
Center (MARC) with pools, ice rink, basketball and tennis courts, [below and next page].

The last flurry of creative proposals seven years ago followed the City’s commissioning of an
urban design plan in 2001 by Pittsburgh-based Urban Design Associates that would have
demolished the Coliseum in favor of an urban street grid and Pearl District style development.
After widespread public resistance and an outcry by the veterans, that plan was abandoned. Similar resistance greeted developer proposals to convert the Coliseum to a Costco or Home Depot. Why should its total demolition for a minor league baseball stadium now be acceptable?

The PSU workshop was based on separate class sessions we had with a broad cross-section of stakeholders including, among others, developers J. Isaac of the Oregon Arena Corp. [current proponent of an entertainment center], Doug Obletz of Shiels, Obletz Johnson [SOJ, current proponent of the MARC athletic complex], Jim Winkler of Winkler Development Corp. and developer of the nearby Adidas Village.

We also had separate sessions with other mentors including: Michael McElwee [PDC headquarters hotel project manager]; architects Paul Falsetto of SERA [Coliseum historian], Randy Higgins of HOLST, Jim Howell [transit advocate formerly of Tri-Met and BOORA] and Doug Nichols of OTAK as well as market economist Jerry Johnson [Johnson Gardner], contractor Darhl Edwards [Hoffman Construction]; planners David Knowles of SOJ [formerly City Planning Director] and Larry Dully [formerly PDC Development Director] who conducted the studies on the Coliseum for the City of Portland; botanists Fred Nilson [Hoyt Arboretum] and Carolyn Devine [Berry Botanic Garden]. Presentations were critiqued by Oregonian architecture critic Randy Gragg, Portland city finance executive David Logsdon, former chief-of-staff for Commissioner Charles Hales Ron Paul [proponent of the James Beard Public Market], and architect and planner Nohad Toulan, founder and Dean Emeritus of the College of Urban & Public Affairs.

In an effort to help inform public debate and assist public policy decision-makers, here is a brief summary of the four adaptive re-use plans the workshop developed at that time:

**Headquarters Hotel**

At the intersection of three light rail lines, the two main interstate highways and the potential high-speed rail corridor, and served by over 12 bus routes within Fareless Square, a 650-room headquarters hotel built within the glass box would permit conventioneers to take light rail directly from the airport to their hotel and convention center and easily go downtown. When inter-city high-speed rail is built, the hotel's west side would become its front door to Portland.

Re-using the enormous glass box, measuring 3.25 blocks and more than seven stories high, the project was conceived as a hotel inside a botanic garden. Unlike enclosed central atrium hotels, four glazed corner atria, each a glass cube 60 feet per side, would look out over the city and across the Willamette and each would form a microclimate representing the diversity of Oregon biomes. Every room would have a view. Cafés and restaurants...
would fill the base of each atrium and would become inviting places not only for conventioneers but also for other Oregonians and visitors open to the public on a 24 hours-a-day, 7 days-a-week basis, much more accessible than even wholly public uses.

Unlike the potential headquarters hotel site across MLK Boulevard from the Convention Center, the Coliseum is visible from the I-5 freeway and from downtown, primary criteria for hotel location. And since a headquarters hotel cannot survive on convention business alone, the short 5-minute walk from the Coliseum to the Convention Center, through three existing public plazas, gives it just enough separation to attract Rose Garden guests, business travelers and tourist visitors, thereby assisting its economic viability. The two hotels and OCC are already connected by a light rail line and pedestrian streetscape on Holladay Street.

Some critics have said that a headquarters hotel needs at least 800 rooms. But in fact, PDC’s criterion is a block of 400 to 500 rooms, which can easily be accommodated in the Coliseum and would be the only nearby hotel to do so. There is more than enough space for an additional 400+-room tower to be built when, as and if the market can support more rooms. This phasing option would lower the development risk.

Why would this work when prior PDC efforts failed?

- The City already owns the land, building and parking.
- The Coliseum already has 40,000 SF public space, a large extra cost for new facilities.
- Coliseum requires the lowest possible public subsidy.
- Lower subsidies mean less resistance from existing hoteliers.
- No new taxes are required.
- Adaptive reuse cost savings lower required capital.
- The separate hotel identity could better attract business and leisure markets.
The Coliseum hotel would be a less expensive public-private project that is feasible because the public would continue to own the land, building and parking, which it need not finance, as well as the capital improvements, which would be financed with tax-exempt revenue bonds as many other cities have done for their headquarters hotels. Private developers under contract with the city would assume the risks of cost overruns and private hotel management companies would assume the risk of operating losses. Profits would be divided between the public and private sectors.

The Coliseum headquarters hotel would use all of the transit advantages of the site, re-use an architecturally historic building, re-invigorate the Rose Quarter, support the Convention Center, minimize on-site parking demand, act as a transit center, bring both weekday daytime and nighttime use on a consistent basis to an area used sporadically, provide both construction and permanent jobs and increase the tax base. Moreover, it would do so in a less costly and less risky way than any other headquarters hotel alternative. And it would be the only re-use option that meets all those criteria.

Portland Memorial Arts Center

At the time when the BODS [Ballet, Opera, Drama, Symphony] group were each seeking new venues, [an Oregon Ballet Theater, Portland Opera House, Portland Center Stage Theater and Oregon Symphony Hall] the Coliseum offered the only site where all four could be accommodated at the lowest capital costs and with the greatest operating savings. In turn this could lead the organizations to lower ticket prices, to expand the market to younger and less affluent groups and achieve greater solvency, a rare feat among arts organizations.

A Portland Memorial Arts Center [PMAC] could adaptively re-use both the existing bowl as well as the glass box, preserving its architectural heritage. The bowl could be divided into four main spaces housing the major users, and there would be enough space for a variety of other uses in the large complex:

- 2,200-seat symphony hall
- 2,000 seat dance and opera house
- 500-seat dramatic theater
- 200-seat black box theater
- 2,000-Seat Cinema [or up to 10 smaller ones]
- 10,000 SF Northwest Film Center studios
• 80,000 SF broadcast center for Blazer Cable, KXL & Action Sports Network
• 20,000 SF rehearsal, storage and rentable practice space
• 15,000 SF restaurant and cafés expanding to a 10,000 SF terrace overlooking Willamette River & downtown
• 10,000 SF art books and music store
• 400-space parking garage built into the western bank topped by a restaurant terrace

The benefits of co-locating this broad array of users and uses are several. Combining broadcast studios bearing uplink capacity with live performing arts facilities permits simulcasts of special events that can increase both the audience for, and income stream to, arts organizations. Increasing the capacity for events of varied scales can expand the penetration of the market for arts to younger and less affluent segments. Moving to the east side of the river could also demonstrate the city’s commitment to support the arts beyond its traditional base on the west side and among what some call middle-aged culture vulture patrons.

The economic development impact can be considerable. Studies have estimated that over 10,300 people were employed in the arts in Portland producing an economic impact of more than $318 million and attracting more than 6.3 million attendees to Portland arts events in 2006. That has helped Portland expand its population of the 25 to 34 age group to the top tier of American cities, and has led to the creation of a growing group of new local businesses based upon both the arts and new communications media. The variety of auditoriums and meeting spaces less than five minutes from the Convention Center could expand the venues in which Convention events could be held during the daytime when the arts facilities are less used.

In 2002, estimated capital costs of the PMAC were $47 million, far less than the total of separate facilities, and comparable to the cost of the baseball stadium. The capital cost savings of housing a variety of performance facilities means that expensive infrastructure such as bathrooms, kitchen facilities, loading docks, HVAC and security systems can be shared among many users, unlike the initial BODS proposals for separate facilities.

Operating savings could be continuous using shared employees for such things as box office activities, lighting and set
design and construction, technology equipment operation and maintenance, janitorial and security services. Adding the broadcast center, retail shops, restaurants and cafés would provide over $1 million of annual income. The Oregon Film & Video Office could relocate and/or stimulate more arts production at PMAC. These income streams, combined with an increase in the revenue stream flowing from market expansion and media programming, coupled with all of these operating economies, could assist the PMAC to become a self-sustaining arts and media center for the region, a truly sustainable development.

**Sustainable Technology Center [STC]**

The Coliseum could also be a place to create an urban center of sustainable technology that would house applied research and development, manufacturing, and services, which would be anchored by energy and environment related government offices. The large footprint and seven+-story height of the building can be used create an urban alternative to suburban flex-space with over a 560,000 square feet on four floorplates. The 130,000 square-foot flexible floorplates are larger than commonly available in the suburbs. Supported by light rail and streetcar transit, as well as about 2,500 existing parking spaces at the Rose Garden that are vacant during the day, the STC would have a parking ratio of 4.5 spaces per 1,000 square feet, far more parking than most suburban flex-space projects. At the intersection of three light rail lines and within Fareless Square, it is likely that transit could serve most of its users.

This plan could create space for over 2,000 jobs in the central city at a location that is especially attractive to the creative young urban dwellers likely to work at the STC. To make the project feasible, it would be anchored by the energy and environmental programs of nearby government offices and utilities, all of which have headquarter offices only blocks away.

1. BPA
2. State of Oregon
In addition, other targeted users could be private research, development and manufacturing, academic research and other institutional users, energy and environmental engineering firms and an array of green technology companies. The PDC has listed solar cell production, fuel cell production and power control equipment as three areas in which the Northwest could build a niche. Electric vehicle design and engineering could be another. Sustainable technologies also include those connected with wind, geothermal and hydropower energy design and development and as well as conservation materials, techniques and control systems.

An STC would build on Portland’s solid and growing reputation as a leader in sustainable development where it already houses a leading school of environmental law (Northwest School of Law at Lewis and Clark University), the China-US Center for Sustainable Development, EcoTrust, and the Portland Office of Sustainable Development. The recent $25 million grant from the Miller Foundation is helping to make Portland State University and academic leader in sustainability. The STC would give Portland a downtown sustainability applied development and production facility to complement academic research.

The Coliseum itself can be rehabilitated to be an outstanding example of adaptive re-use according to the best green building techniques. The 130,000 square-foot roof is large enough to become an efficient eco-roof providing insulation reducing cooling loads, absorbing storm water and holding a 3.25-acre array of photovoltaic solar collectors providing power to the building. The large glass walls would provide natural light and, with the addition of another internal glass wall, provide a natural tempering chamber that will either bring heated air into the building or exhaust it from it using relatively simple control systems. By providing counter-cyclical weekday daytime use of an under-utilized historic building and supporting existing city-owned garages, an STC would advance principles of urban density.

This STC project would be economically feasible because the City already owns the land, building, and parking. The total development cost was estimated in 2002 to be $65 million, which included $14 million for tenant improvement allowances at $25 per square foot. At low discounted rents that could then be as low as $9.00 per square foot, averaging industrial and office space, the STC could produce about a $4.5 million net operating income stream that could support about $50 million of the capital costs, using tax-exempt industrial revenue bonds to provide low-cost financing. Students estimated that the project would require only about $15 million in grants, which should be possible to obtain from government economic development funds and foundation sustainability grants.

A Sustainable Technology Center would support multiple goals of job creation, economic development, sustainable development, urban revitalization, reduced commuting, transit-supported development and historic preservation.

**Urban Home Center**

In March 2002, our Development Workshop pointed out that, among other things, the Coliseum is the quintessential big box. At the same time, large format retailers that have
saturated the suburbs were looking to tap into lucrative urban markets but find sites difficult to find or neighborhoods resistant to their entry. The Coliseum could overcome both of these challenges and offers an urban alternative to the single-level behemoth big box in a sea of parking.

While it was clear then that big-box retailers were profitable and that almost any selection of them could succeed at the heart of a regional market of 1.8 million people with over $33 billion of income, students concentrated only on those who were not then represented in the marketplace, would support an urban housing lifestyle and could attract customers also to downtown and to Lloyd Center, as a retail bridge between the two. These objectives excluded retailers who had saturated the region, such as Costco, Home Depot, Lowe’s, Target and Wal-Mart. Should the City decide to approve an Urban Home Center, it should adopt these criteria.

Rather, we looked at international retailer IKEA whose nearest location then in suburban Seattle attracted many Portlanders. IKEA’s typical minimum store size is 260,000 square feet, which is precisely two floors of the Coliseum. IKEA is accustomed to a two-floor concept and many of its stores have glass walls. Moreover, the column-free interior space is ideal for large format retailing. Urban dwellers in smaller apartments and condominiums often use the type of affordable folding and modular furniture in which IKEA specializes.

IKEA would also have been co-located with an Expo Design Center, as it is in Palo Alto, CA. Expo Design Centers were mainly conceived as showrooms with fully furnished lifestyle vignettes featuring the products and design and construction services it provides to customers and their contractors. They occupied about 130,000 square feet, just the size of one floor of the Coliseum. The third major type of retailer appropriate to the Coliseum, and one which would fit nicely into its 40,000+ square-foot exhibition hall, would be a Crate & Barrel outlet store, none of whose 13 outlets is currently in the northwest.

One must recognize that adequate parking must be available to serve this volume of large-scale retail. In order to maintain the transparency of the glass box and reveal the retail activity
within, students located two floors of parking for more than 900 cars within the concrete base of the Coliseum. In addition, the City owns about 2,500 existing spaces in its Rose Garden garages that are under-utilized except during large events. Unlike those events, retail traffic is spread throughout the day and week so more efficient utilization could be expected. Counting all spaces potentially available when no event was held at the Rose Garden, there could be a very high parking supply of over 8 spaces per 1,000 square feet, attractive to retailers.

Some may object to bringing automobile-oriented retailing to an area so well served by transit. Unlike typical retailing, only small furniture is carried home via personal car and all larger items are delivered. Therefore, one might expect that more than normal numbers of customers would come via transit. A large number of employees would also likely use transit.

At an estimated development cost in 2002 of $61 million, and with a net operating income of approximately $7 million, an Urban Home Center should be financed privately and might be expected to return at least about $3 to $4 million annually. Since the city owns the land, the building and the parking, it is reasonable to expect that a substantial portion of that should flow to the city. In addition, the real estate tax revenue on a leasehold interest should be expected to be well in excess of $1 million annually. The City might choose to use some of those funds to support a smaller-scale athletic complex with competition swimming facilities envisioned in other Coliseum plans.

Beyond economic benefits, an Urban Home Center could revitalize the Rose Quarter with non-event activity and act as a retail bridge between downtown and Lloyd Center that complements both and broadens the selection, quantity and price of available goods. It also would support urban housing and could reduce regional auto trips.

[Please note that although each of the four proposals above incorporated a veterans’ memorial as part of the project, this summary excluded consideration here, but one could and should be incorporated in any chosen alternative.]
Coliseum as Coliseum

Strangely, the use for which the Coliseum is most well adapted has received the least attention — as a Coliseum. One must understand the basic deal structure to surmise reasons for the lack of attention.

The Deal Structure

At the time of the construction of the Rose Garden, the City executed an operating agreement providing that the same manager manage both the Coliseum and the Rose Garden. While Paul Allen’s Oregon Arena Corporation (OAC) has the obligation to cover any operating losses at the Coliseum, it must pay 60% of any net income from the Coliseum to the City, retaining 40% of net income as a management fee. Events at the Rose Garden are not so burdened. While the City may have believed that the agreement was favorable to it, one must realize that it is in the economic interest of the manager to hold just enough events at the Coliseum to keep it at a breakeven level, but no more because there is not incentive to exceed that level, especially when all the profit is available for holding the same event in the Rose Garden. The agreement does not address or resolve that conflict of interest.

In addition to receiving 40% of the net income from the Coliseum as a management fee, the OAC passes the full costs of operating the two parking garages owned by the City, including OAC’s management fees, on to the city along with any parking revenues generated by events at the Coliseum. This does not constitute an incentive to hold more events at the Coliseum. The City is obligated to pay for all capital improvements to the Coliseum as well as all major repairs and maintenance. Since the Coliseum has been kept at a breakeven point, the City has had no incentive to repair and improve it.
Development Rights: Public or Private Use Questions

Furthermore, the Oregon Arena Corporation was granted and enjoys development rights for any non-public development that would occur on the Coliseum site but has no such rights for public development. It is in the City's sole discretion to determine that the Coliseum is not needed for any public use. It is in OAC's economic interest for the City to declare there is no public use for the Coliseum, and over the years it has advocated solutions that demolish it.

Can the City truly declare, without a complete professional evaluation and fully open and transparent public process, that no public use exists for the Coliseum? Can the City really prove beyond reasonable doubt that the Coliseum is not a viable public use and, even if so, that no other public use could take its place? Should the City investigate other deal structures to maximize the value of its assets? Should it actually negotiate and try such other deal structures for a reasonable time before it takes the radical step of demolishing an historic icon right before it can be nominated and accepted on the National Register of Historic Places? Why should the same private entity manage both facilities?

Management by Metropolitan Exposition Recreation Commission [MERC]

In 1990, the City transferred management of both the Coliseum and Civic Stadium-(PGE Park) to MERC, which also manages the Oregon Convention Center [OCC], the Portland Center for the Performing Arts [PCPA] and the Portland Metropolitan Exposition Center [EXPO]. That placed in a single public manager all the publicly owned facilities that could accommodate large events. In 1992, the City pulled the Coliseum management from MERC and transferred it to Paul Allen’s Oregon Arena Corporation (OAC). Nine years later, in 2001, the City transferred management of PGE Park to the private sports firm Portland Family Entertainment, which later defaulted on its agreement with the City. In both cases, private management of public facilities has led to adverse economic consequences for the City. Since the Coliseum is only five minutes from the Oregon Convention Center, and since the Coliseum already offers a variety of venues in which to hold public convention and conference events, and could add more as outlined above in the section about the arts center, why should not MERC again manage both facilities to their mutual benefit? Since MERC also operates the performing arts center, including the Keller Civic Auditorium, would it not make more sense for it to have a venue in which to stage
large events, concerts and festivals? Would not Coliseum rock, folk and country music concerts produce additional profits that could offset losses at smaller venues?

As described, the deal structures for both the Coliseum and PGE Park have revealed conflicts between public and private interests that have impeded the success of publicly owned facilities. MERC is subsidiary of Metro, our elected regional government, and MERC’s board members represent Metro, the City of Portland, and Washington, Clackamas and Multnomah counties. It has a professional staff with broad experience in real estate management, entertainment, film and television production, arts administration, marketing and sales. The Coliseum is currently the responsibility of the City’s Office of Management & Finance, which does not have similar experience or transparency.

The City also owns the parking garages for approximately 2500 cars that are mostly empty during the week, during the day. Are there other uses of the Coliseum that could help generate weekday revenue from those parking spaces? Are there ways to amalgamate the best elements of the various elements of the creative proposals that have been made within the context of the existing Coliseum? For example, could a substantial portion of the 80,000 square feet of the lower level be leased as a broadcast center to both facilitate dissemination of events that occur above and generate continuous income to offset operating expenses of the Coliseum?

Could the concourse level be leased for a large restaurant overlooking the Willamette as proposed in the arts solution? Could the east side under the cantilevered bowl be leased for sale of books or other merchandise? Could a portion of the 40,000 square feet in the Exhibition Hall be leased for a fitness center, or classrooms or a myriad of other uses especially during weekdays? Could the concrete bowl, with its stadium seating for 12,000 people and electronic communications equipment, supplement the Convention Center for general sessions for large conferences during weekdays? Are not political conventions held in precisely those kinds of venues?
As noted by Brian Parrott (*Portland Tribune, April 2, 2009*), the head PSU tennis coach, Portland would “give up a significant competitive advantage that the city has in attracting events that other cities cannot accommodate because we have two world-class arenas side by side. Example: The U.S. vs. Russia Davis Cup Final that we won the right to host because we have the Memorial Coliseum that can provide dates that very busy buildings cannot bid for. That event brought an estimated $7 million to $10 million to the city and filled up every hotel room available. Philadelphia is the only other U.S. city that has two such buildings, and they are going to tear down the Spectrum. Portland will become the only U.S. city to be able to host events that cannot find a location in a major metropolitan area.”

Does it make any economic sense to demolish an historic icon for which so many uses have been developed to spend at least $55 million building a new baseball stadium that would operate only six months of the year and house only about 70 home games? What will produce revenue there on the other 295 days of the year? In a rainy area like Portland, why does it make sense to demolish
a covered, enclosed and heated venue usable year-round for a multiplicity of uses with an open one usable only half the year, and then only for a single use? Why try to raise $55 million in new debt when about $28 million still remains of the debt to convert PGE Park for baseball? Why should the City rush to demolish the Coliseum at the end of this year when no public process has considered all the alternatives?

Public Policy Questions
As a matter of public policy, for all the reasons and questions raised in this article, is it difficult to find a logically consistent sustainable public purpose based upon sound economics, rational urban planning and development, conservative architectural historic preservation, progressive transportation planning, environmental integrity, respectful veteran memorial integrity and equitable social policy to justify the demolition of a valuable public asset?

At the height of the deepest recession since the Great Depression, when Oregon’s unemployment rate is the third highest in the nation, when the incomes of those employed are falling with involuntary furloughs, when homelessness is rising and even food banks experience shortages, when school budgets are being cut and tuitions are rising, and when the City cannot even maintain roads without raising parking fees, how would demolition of the public asset of the Coliseum advance public responsibility to protect and enhance public property? Why is the City considering demolishing public assets in such a cavalier fashion, on such a short timeline, before thorough investigation and public evaluation of all alternatives?
In this article alone, we have discussed seven different alternatives, each of which would preserve the Coliseum in whole or in part. The best in terms of preserving the public's economic, historic, civic and public investment may well be the simplest, improving and operating the Coliseum as a Coliseum, under the management of MERC. How can the City decide, in a period of weeks, after private discussions with only two companies owned by wealthy families who each advance their own private interests, to demolish an historic 50-year old public asset that has not only served the community well but also offers a wide array of rehabilitation and reuse options? Would Portland be making the same mistake that New York City did when it demolished the historic Pennsylvania Station?

The Hippocratic Oath to which every doctor swears allegiance is to do no harm. Do not City Commissioners owe the same allegiance to public citizens who elected them? What sense of public priorities and public interests does this course of action reveal and why should the public support any City Commissioner who advances it? When city leaders publicly purport to create “the most sustainable entertainment district in the United States”, is it not incumbent upon them to show how demolition of a complex that can itself be an embodiment of energy efficiency is sustainable? The accepted criteria by which sustainable projects are measured have been the triple bottom line summarized by the three “E”s – economy, ecology and equity. Where are the independent studies by independent experts that show that a single-use, minor league baseball stadium operating for 70 home games can support a $55 million public investment, plus the economic value lost, with an existing venue that can operate 365 days in all weather with a multiplicity of uses? Where are the independent studies showing that the energy to destroy all the materials and embodied energy that comprise the Coliseum, added to all the materials and energy to build a baseball stadium, produce a net positive ecological result? Where are the independent studies to show that social equity is advanced more by 70 baseball games over six months versus admission to graduations, concerts, rallies, conventions, exhibits, festivals, hockey, basketball, tennis, figure skating and other spectator events over an entire year? When a public entity contemplates destroying a public asset, is it incumbent upon
it not only to publicly examine all alternatives, but also to produce a cost benefit analysis showing that all alternatives are inferior to the chosen one? Should the city first do no harm?

Respectfully yours,

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The Credit Crisis in Commercial Real Estate

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It is very difficult to argue with the premise that the current financial turmoil is without modern comparison, or that its impact will be anything less than generational in its severity. The current lack of commercial real estate (CRE) financing is a tremendous challenge confronting both owners and investors and has significant ramifications with respect to underlying property valuations. However, at its core the credit crisis is a lending crisis and as such it does share common elements with past banking failures. While financial markets are experiencing unprecedented disruption, it seems negligent to ignore these commonalities, particularly when trying to understand the impacts on commercial real estate and why the worst may very well be yet to come for this market. The more challenging aspect may be in understanding just how severe it can get for the commercial real estate market as the many underlying causes and fundamental challenges ahead are truly without peer as the market attempts to restore some measure of liquidity.

The Savings & Loan Crisis

The last lending crisis with significant implications to the commercial real estate market was the savings and loan crisis [S&L] of the 1980s. From 1986 to 1995, over 1,600 FDIC-insured institutions were either closed or received federal assistance. Over 1,000 of these institutions
with assets of $500 billion failed. The cost of the S&L crisis is estimated to have totaled approximately $160 billion, of which about $125 billion was directly paid for by US taxpayers. That lending crisis, the recession which accompanied it, and in particular the actions of the Resolution Trust Corporation (RTC), chartered with the directive to liquidate the assets of these failed institutions, defined the commercial real estate industry during the late 1980s and into the early 1990s.

In a 1997 examination of the S&L crisis, the FDIC’s Division of Research and Statistics identified four common elements of recessions associated in large part from bank failures. These common elements were:

1. Recession followed a period of rapid expansion with external factors exacerbating cyclical forces.
2. Speculative activity was prevalent and opinion, rather than fact, supported optimistic expectations.
3. Wide swings in real estate activity contributed to the severity of the recession; and
4. Boom and bust activity in commercial real estate markets was one of the main causes of losses at both failed and surviving banks.

The first three elements are obvious in their relevance to the current financial crisis. However, the parallels to current residential markets are unmistakable. For market participants, these factors most certainly apply as well to the commercial real estate market of 2005 - 2007 which makes the fourth element particularly alarming. By and large, banks have not yet experienced significant losses with respect to their commercial real estate loan portfolios, although the market almost unanimously agrees that these losses are coming and that they will likely be sizeable.

The Credit Cycle

Underlying the business cycle is the credit cycle. Ready access to affordable capital spurs investment and fuels expansion. These periods of liquidity generally lead to periods of excess liquidity followed by contraction and relative drought as the cycle turns downward. Periods where credit flows easily can just as quickly end in periods of excessive tightening before returning to more sensible loan underwriting standards. Where the current crisis deviates from history most profoundly, particularly with respect to CRE lending, is the sheer magnitude of this most recent credit cycle, first on the way up and now in it’s relentless down cycle.

In understanding this credit cycle, it is important to understand the process by which financial institutions extend credit and, for the purposes of this analysis, the focus is specifically on the process by which financial institutions extend credit to the owners of commercial real estate. Within lending institutions, this process is referred to as loan underwriting and encompasses the quantitative and qualitative assessment of relative risk.

Debt is a fixed return vehicle which receives scheduled payments of interest and principal. As a result, when assessing risk from the lender’s perspective, considerable attention is paid to downside underwriting: How much can the asset underperform and still produce the underwritten return? This is a significantly different perspective than that of the equity investor seeking the loan. Investment upside, property performance exceeding expectations, accumulates to the equity interest as the property owner. Better than anticipated property performance for the lender, other than providing for a greater measure of loan safety, does not provide the windfall returns that accrue to the equity holdings. The lender still receives only

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1 Source: FDIC, The S&L Crisis: A Chrono-Bibliography
2 Source: FDIC, History of the 80s: Volume I: An Examination of the Banking Crises of the 1980s and Early 1990s
the scheduled payments of interest and principal, unless the lender has been granted participating income or equity kickers.

**Risk Considerations**

This perspective is particularly evident when discussing the standard risk considerations of commercial real estate loan underwriting which involve loan-to-value ratios, debt service coverage ratios, credit support and loan covenants as outlined in the table which follows.

<table>
<thead>
<tr>
<th>Risk Consideration</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan-to-Value Ratio (LTV)</td>
<td>( \frac{\text{Total Loan Amount}}{\text{Total Property Value}} )</td>
</tr>
<tr>
<td>Debt Service Coverage Ratio (DSCR)</td>
<td>( \frac{\text{Net Operating Income (NOI)}}{\text{Interest and Principal Payments (Debt Service)}} )</td>
</tr>
<tr>
<td>Credit Support</td>
<td>Additional Collateral or Borrower Guaranties</td>
</tr>
<tr>
<td>Loan Covenants</td>
<td>Ongoing Loan Conditions (e.g. minimum levels or cash flow or maximum levels of leverage)</td>
</tr>
</tbody>
</table>

Beyond the standard analysis of the property attributes (age, appearance, local market factors, location, etc.) these considerations define a relative risk tolerance for any loan by framing (1) the lender’s exposure within the context of fair market value, (2) the cash flow available for the payment of debt service, (3) a borrower’s ability to repay the obligation, and (4) the lender’s ability to safeguard its loan.

**Conservative Loan Underwriting Standards**

Immediately following the S&L crisis, CRE lending was governed by a strict adherence to conservative loan underwriting standards characterized by modest LTV ratios, strong DSCR, personal borrower guaranties and a rigorous structure providing for regular loan performance tests. However, beginning in the mid-1990s, the commercial real estate embarked on what would end up being twelve consecutive years of market growth and value increases. During that period, diligent underwriting encountered a record CRE up-cycle. Conscientious lending standards combined with stellar performance of the underlying real estate and provided for record low default rates in loans secured by commercial properties.

In turn, CRE loans established a solid track record of strong returns on investment and appealing risk-adjusted returns. Market participants increased their allocations to CRE-backed assets. Others expanded their investment portfolios then to include investment in CRE loans, attracted by greater income and capital protection than that provided by riskier equity investments. This emergence of a viable investment market for CRE loans, and the seemingly limitless demand which followed, promoted further investment and unprecedented liquidity for commercial property acquisitions. The secondary lending market, as the primary vehicle for these investors seeking to put money to work in commercial real estate, changed the nature of CRE investment in a relatively brief time period.

The secondary lending market, or securitized lending, refers specifically to loans originated and sold, or syndicated, to secondary market participants. Across all real estate lending platforms, this securitization process converts originated whole loans to mortgage-backed securities (MBS) and, specifically for commercial properties, to commercial mortgage-backed securities (CMBS). The dynamics of this market differ greatly from the more traditional commercial real estate lending model, which is referred to as the primary lending market or balance sheet lending.

In its simplest form, the primary lending market can be thought of as a local bank providing a loan for a local property to a neighborhood operator or long-time client. The market relies on relationship lending, as the originating bank or institution will be holding the loan in its
portfolio for the life of the investment. In doing so, the lending institution genuinely becomes a partner with the borrower until loan maturity.

**Securitized Lending Process**

By way of contrast, the securitized lending process relies upon a third party intermediary to aggregate multiple loans and resell a collection of asset pools as individual new securities. An originator is responsible for the initial underwriting and funding of the loan. The originator sells the loan to a third party intermediary, typically an investment bank, referred to as the issuer, who would be responsible for assembling the pools of loans into the CMBS security, which are then sold in the market to individual investors (see figure 1).³ The growth of the CMBS market, and its resulting impact on CRE lending, cannot be understated. The CMBS market, which first emerged in the mid-1990s, rapidly transformed real lending from one centered on local primary lending institutions to a global investment market where investors worldwide could pool funds to lend.

The growth the CMBS market corresponded with, and in large part fueled, the growth of CRE lending in general. In 1995, there were $1.0 trillion in outstanding CRE loans of which 5.4% were CMBS.⁴ By early 2001, the CMBS market supplanted insurance companies and pension funds as the largest holders of CRE debt behind banks.⁵ CMBS issuance swiftly increased as the market demonstrated strong performance and rapidly decreased delinquencies (See figure 2). By 2005, CRE loans outstanding totaled $2.62 trillion and CMBS represented 37% of the market. At the market peak in 2007, roughly half of the new CRE debt originations were intended for the CMBS market, which had a tremendous impact on liquidity and pricing in the commercial real estate market, as will be demonstrated later in this discussion.

³ Source: Federal Reserve Bank of Chicago
⁴ Source: Commercial Mortgage Alert, Wachovia Securities and Mortgage Bankers Association
⁵ Source: Nichols, Joseph; CMBS World, Summer 2007.
CRE lending was seen as providing an appealing risk-weighted return and CMBS were the primary investment vehicle for those outside the primary lending market.

**CMBS Default Rate**

As illustrated in figure 2, the CMBS default rate had historically averaged approximately 5.0%. However, in the periods that followed, delinquencies began declining rapidly, eventually falling to a record low 0.28% at the end of 2007.\(^6\) Loan terms began loosening and underwriting standards eased dramatically. Institutions took larger risks, compounded by the reduction of risk-mitigating covenants and structure.

![Delinquency by Vintage](image)

This easing of credit and the ongoing bull-run of the CRE market, spurred unprecedented investment in commercial properties and demand for CRE loans. In 1988, total commercial mortgage debt outstanding was approximately $1.0 trillion. Over the next ten years, total commercial debt outstanding had expanded to approximately $1.2 trillion, representing a modest market growth rate of approximately 1.5% per year.

The decade which followed experienced much more rapid growth. By 2008, the U.S. market had $3.4 trillion in commercial debt supporting $6.5 trillion in investment-grade, income-producing real estate. From 1998 to 2008, the commercial mortgage debt market had experienced annual compounded growth of almost 11%.

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\(^6\) Source: Business Wire, January 17, 2008
Interestingly, depository institutions were not necessarily crowded-out by the CMBS market and maintained a relatively stable proportion of the overall marketplace. However, the securitized market was leading the way and, in doing so, began to deviate significantly from the lending standards that had been established by the primary lending community. The securitized market had effectively removed the originator as an investment companion of the borrower. The originator and the third-party intermediary securitizing the loan were often the same group. Loans originated and packaged to secondary market participants carried with them no vested interest beyond what could ultimately be sold to the market.

**Credit Rating Agencies**

In turn, the market relied almost exclusively on the credit monitoring by the major credit rating agencies, hired by, and on behalf of, the third-party intermediaries to assess the underlying risk. Loan originators increased maximum leverage ratios, replaced amortizing loans with interest-only ones, and in general began lending more aggressively on more volatile assets such as land and other non-cash flowing investments. In turn, these loans were packaged and sold to the investors of CMBS who, by now, were more than comfortable with the safety of these investments given demonstrated past performance, AAA-credit agency ratings, and a track record of decreasing delinquencies. This is particularly true of loans originated in 2006 and 2007, which are generally considered the worst of the CMBS vintages.

Depository institutions generally followed suit. In order to compete with the secondary market, underwriting standards loosened. Additionally, small to mid-size institutions increased their exposure and concentration to commercial real estate, encouraged by the performance of their
outstanding loan portfolios and low delinquencies. Market participants began to talk of fundamental changes in the commercial real estate markets. Cap rates’ compression was fueled by suggestions that the liquidity premium had been eliminated from the market, given readily available capital for investment. Particularly in the office sector, market participants pointed to the relative lack of new construction as the practicing of a new market discipline that would temper the traditionally cyclical nature of commercial real estate. “This time it’s different” was an expression of the collective market consensus and the only thing better than today were the prospects of tomorrow.

**Commercial Real Estate Market Peak**

In hindsight, with a tremendous amount of money pouring into commercial real estate, and no shortage of available financing, it was only a matter of time before the market overheated. CRE transaction volume increased 233% from $118 billion in 2003, to $276 billion in 2005. In 2007, investors channeled a record $417 billion into commercial real estate in the United States, financed in part by $233 billion in CMBS.8

The market peak did come in early 2007 with the sale of the Equity Office Properties Trust (EOP) portfolio to the Blackstone Group. Blackstone paid $39 billion for 573 properties that EOP had amassed over its thirty-year history to consummate the largest private equity deal in history. Blackstone, in turn, then sold almost 70% of the portfolio within six weeks for $27 billion to 16 different companies. The transactions broke sales volume and cost-per-square foot records in major markets throughout the country, including locally where San Francisco-based Shorenstein Properties purchased 4.0 million square feet of Portland office properties for approximately $1.2 billion, roughly $300 per square foot. In most cases, buyers financed the portfolio purchases aggressively, but none more aggressive than New York investor Harry Macklowe’s purchase of the 6.5 million square feet of New York City properties he purchased from Blackstone for $7.5 billion, or $1,100 per square foot. The entire purchase was financed with short-term debt and only $50 million of cash contributed by Macklowe. Essentially, the entire $7.5 billion purchase was 100% financed through Deutsche Bank and the Fortress Group. Deutsche Bank would later sell some of these buildings, recouped though foreclosure, for $818 per square foot, or almost 26% less than Macklowe’s purchase less than 18 months prior.

In summer of 2007 the subprime mortgage crisis irrevocably changed the financing landscape for commercial real estate. Even though the roots of the crisis were in residential real estate lending practices, the ubiquity of the exposure across most classes of investors was surprising, most of all to investors who were unaware of any such exposure. As described by David Leonhardt in the New York Times, “The American home seemed like such a sure bet that a huge portion of the global financial system ended up owning a piece of it.”10 However most were unaware of the underlying risk of their investments. The secondary market had become so complicated that investors relied almost exclusively on the rating agencies’ evaluation of risk. When massive losses exposed the enormous flaws in relying upon these agencies, the market immediately looked to the CMBS market that functioned under much of the same investment principles. Investors lost complete confidence in the secondary market and liquidity literally vanished almost overnight. The CMBS market, which had provided $605 Billion in commercial real estate financing in the three years prior to 2008, seized. Total CMBS market activity plummeted to $12 billion in total issuance in 2008 with no activity at all in the second half of the year (see figure 4).

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7 Source: CMBS World, Summer 2007
8 Source: NAREIT
9 Source: Sam Zell’s Empire, Underwater in a Big Way: NYTimes February 7, 2009
10 Source: Can’t Grasp Credit Crisis? Join the Club: NYTimes March 19, 2008
As noted, the valuation of the New York City portfolio formerly owned by EOP and later acquired by Macklowe had lost almost 26% of its value in 18 months. To state that Macklowe dramatically miscalculated value oversimplifies the issue. In fact, it can be demonstrated that the change in the lending climate alone can be held responsible for a great deal of the revaluation and with it a corresponding change in market capitalization rates.

**Impact of Leverage**

This demonstration was initially presented in a 2009 CMBS market forecast prepared by Merrill Lynch (See Figure 5). An investor who requires a 10% return on equity (ROE) is presented with the opportunity to purchase a property with an NOI of $6.6 million. The financing market is prepared to provide an 80% LTV interest-only loan at the rate of 5.75%. Given this available financing, the resulting cash flow after debt service would equate to a 10% return on the initial investment equity of $20 million and the investor would be prepared to purchase the property for $100 million equating to a 6.6% cap rate. This fairly simple example is surprising accurate in representing the commercial real estate market dynamics from 2005 - 2007.

Transfer this example with the same property and the same investor return requirements to 2009 and the effects of the change in the lending markets upon property valuation are evident. The assumption for the financing available in today’s market is 60% LTV payable at 7.25%
interest and amortizing on a 30-year schedule. Given the financing now available and the resulting cash flow after debt service that would equate to a 10% return on investment, the investor is no longer able to purchase the property at any price greater than $74 million. With no change other than the financing terms available to the investor, the property has lost 26% of its value and the market capitalization rate has increased 230 basis points.

**The Impact of Leverage on Value**

<table>
<thead>
<tr>
<th></th>
<th>2007 Loan</th>
<th>2009 Loan</th>
<th>2009 Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building Cost</td>
<td>100,000,000</td>
<td>100,000,000</td>
<td>74,000,000</td>
</tr>
<tr>
<td>NOI</td>
<td>6,600,000</td>
<td>6,600,000</td>
<td>6,600,000</td>
</tr>
<tr>
<td>Cap Rate</td>
<td>6.6%</td>
<td>6.6%</td>
<td>8.9%</td>
</tr>
<tr>
<td>LTV</td>
<td>80.0%</td>
<td>60.0%</td>
<td>60.0%</td>
</tr>
<tr>
<td>Loan Amount</td>
<td>80,000,000</td>
<td>60,000,000</td>
<td>44,400,000</td>
</tr>
<tr>
<td>Loan Type</td>
<td>5.75% IO</td>
<td>7.25% Amortizing</td>
<td>7.25% Amortizing</td>
</tr>
<tr>
<td>Annual Debt Service</td>
<td>4,600,000</td>
<td>4,911,669</td>
<td>3,634,635</td>
</tr>
<tr>
<td>DSCR</td>
<td>1.43</td>
<td>1.34</td>
<td>1.82</td>
</tr>
<tr>
<td>Buyer’s Equity</td>
<td>20,000,000</td>
<td>40,000,000</td>
<td>29,600,000</td>
</tr>
<tr>
<td>Annual Cash Flow</td>
<td>2,000,000</td>
<td>1,688,331</td>
<td>2,985,365</td>
</tr>
<tr>
<td>Return on Cash</td>
<td>10.0%</td>
<td>4.2%</td>
<td>10.0%</td>
</tr>
</tbody>
</table>

Figure 5 – Source: Merrill Lynch

Anecdotally, the market consensus among CRE professionals is that property values have fallen 20-30% and cap rates have increased approximately 200 basis points, generally consistent with what is suggested in figure 5. However, the same market participants will also concede that for most properties, NOI is decreasing in the current economic climate and that investors’ required rates of return have increased given the relative scarcity of investment capital available. If this is indeed the case, then the previous example suggests that the impact on value should be even greater.

**Property Value Declines**

The fact that property values may have declined more than 30% is exactly the fear in today’s market climate. With relatively limited financing, there have been very few trades and as a result it has been difficult to assess current market values. The lending community is particularly fearful. Looking once more to the example in figure 5, except this time from the perspective of the lender, and the prospect of significant principal loss on the part of banks and lending institutions becomes increasingly likely.

The lack of affordable, or in some cases any, debt financing is the most significant obstacle currently facing the CRE market. Estimates are that approximately 40% of the $3.4 trillion in commercial mortgages outstanding will reach maturity over the four-year period ending in 2012. During that time, the relative average outstanding loan-to-value ratio of these loans may approach 100% LTV (figure 6). One of the larger issues is that the loans originated after 2005 were provided to investors at extraordinarily low interest rates and with minimal loan covenants. The underlying assets may be expected to generate enough income necessary to cover debt service and avoid default, but lenders are unable to take any action to protect their loan positions even though the prospects of full repayment at maturity are increasingly uncertain.

11 Source: PPR
unlikely. In many instances, these loans will hobble toward default at maturity. Many of the riskiest loans from 2005-2007 were five-year interest-only loans.\textsuperscript{12} This provides for a large segment of the most problematic loans to mature after 2010 and the possibility of a more protracted and distressing resolution. It also raises the risk that many more bank failures may be inevitable.

**Projected CMBS Loan-To-Value by Maturity**

![Projected CMBS Loan-To-Value by Maturity](image)

**National Problems**

What lies next for the CRE market is uncertain. The severity of the current crisis for the commercial real estate market appears highly dependent upon the economy. CRE fundamentals are weak across almost every property category and comparisons are being made to the 1990s in an effort to estimate the extent of the market devaluation. Deutsche Bank recently published its commercial real estate outlook for Q1 2009 in which it estimates that property price declines of up to 35-40\% can be expected. That would not only exceed the declines experienced in the early 1990s, but also push prices to those levels of early 2004. However, where the downturn in the 1990s was the result of over-building and excess supply, the current crisis is one of reduced demand. Rent declines and vacancy rates may approach those of the early 1990s even without the overhang of new inventories, and delinquencies could reach the peak rate of 6-7\% experience during that era by 2010.\textsuperscript{13}

What is certain, however, is that the CRE market will go through a painful but necessary process of delevering over the next several years. Unfortunately, the combination of deteriorating property fundamentals, and the resulting impact on cash flow and value, with more stringent market underwriting standards, increases the likelihood that a high percentage of the loans originated from 2005 – 2007 will not qualify for refinancing. In fact, assuming that the lending market has returned on a more permanent basis to conservative underwriting

\textsuperscript{12} Source: Deutsche Bank

\textsuperscript{13} Ibid
standards (LTV <70%) it is anticipated that approximately two-thirds of loans maturing through 2012 would not qualify for refinancing.  

With greater than $300 billion in CRE loans maturing annually through 2012, it was originally perceived that these loan maturities would fuel forced sales activity. Without question, there will be opportunities for those adequately capitalized to purchase defaulted loans or assets from fallen banks. However, with bank balance sheets precariously weak, many in the lending community are unwilling to book losses or post the increase in reserve requirements associated with foreclosure activity. With the vast majority of loans covering debt service, and banks either unwilling or unable to foreclose, it appears increasingly likely that the market may address the issue in the short term through extending loan maturities. Without additional intervention, however, it doesn’t seem that time alone would be adequate to provide the asset appreciation required to eventually qualify for refinancing.

Portland Prospects

The failure of Pinnacle Bank in February, the first Oregon Bank to close since 1992, is indicative that the local market will also have its share of challenges. However, the outlook for Portland’s commercial real estate market may not be as bleak as other areas of the country. It is not necessarily a result of regional market strength, but rather a combination of extenuating circumstances that may temper the local fallout.

Shorenstein Properties’ Portland portfolio is certainly not nearly worth the $300 per square foot transaction price today. However, Shorenstein’s owner profile has traditionally been that of a durable investor utilizing modest leverage over a long-term investment horizon. There is little probability that the 45 buildings purchased, including the 369,000 square foot Congress Center and the 271,600 square foot Umpqua Bank Plaza will be dumped on the market in the type of distressed sale that may be seen in other localities. In addition, Portland came under the focus of out-of-market investors very late in the cycle. As a result, the market continues to be dominated by local investors and primary lenders generally attracted to the traditional attributes of the slow-growth, high barrier to entry Portland market.

This is not to suggest that Portland will not face significant challenges or declines in value. The prospects of even higher unemployment, higher vacancies, decreased traffic at the Port of Portland and the pressures of significant additions to the Portland office inventory will certainly be a drag on values. However, Portland did not see the extended wave of yield-chasing, high leverage, short-term investors that will feed distressed sales.

Seattle Scenario

Unfortunately, the same may not be said for Seattle, and it is likely that this credit crisis will impact that metropolitan area particularly hard. During the last cycle, Seattle emerged as a viable institutional investor market. The region had been previously bypassed as a market with few institutional quality assets, and a cyclical economy closely linked to the fortunes of Boeing. However the proliferation of a more diversified economic base generated strong outside demand. It was also one of the last markets to exhibit weakness, which many pointed to as proof of the strength of underlying investment fundamentals. Unfortunately, much of that optimism vanished with the collapse of Washington Mutual in February 2008 and, while Seattle burned hotter and longer than many markets, it may also fall harder.

Seattle is also one of the markets that is currently exhibiting some distressed sales activity. Some of the institutions which made market-entry decisions during the last cycle are now

14 Ibid
retrenching to their core markets at the expense of the Puget Sound region. The prospective sale of the recently listed Seattle Tower in downtown Seattle is being closely watched as an indication of market valuations. The property sold in 2004 to Trinity Real Estate for $19.2 million, or roughly $120 per square foot.\textsuperscript{15} In 2006, the property was purchased for $36 million, or approximately $227 per square foot.\textsuperscript{16} Now back on the market, speculation remains that value may revert very close to 2004 levels and could very well define the level of risk and returns that are required of commercial real estate investors in today’s economic climate.

**Federal Intervention**

The government is highly motivated to prevent the damage to banks, insurance companies and other financial institutions that would be caused in the downward spiral of commercial real estate values brought on by the mass sale of distressed assets or foreclosed properties. In exactly what form or fashion the government will intervene is unclear, although it can be anticipated that the government will participate, and likely aggressively, to prevent market deterioration beyond what is necessary. In any event, the credit crisis and its resulting impacts are the defining events of the CRE landscape and will define the industry for at least the next half decade as the S&L crisis defined the markets of the late 1980s and early 1990s.

\textsuperscript{16} Source: Cushman & Wakefield, Marketbeat Snapshot, Third Quarter 2006.
Bursting Bubbles:
Portland’s Distressed Housing Market

Tom Heinicke, Broker, Meadows Group, Inc. ¹

As of mid 2008, essentially all leading home price indexes had been confirming declines for all major U.S. Metropolitan Statistical Areas (MSAs), bringing to an end what economists consider the greatest asset bubble in history². Throughout the nation, these housing bubbles have varied in intensity. Home values almost tripled in a span of a couple of years in places such as Miami or Las Vegas. In Portland, by contrast, price movements reflected a more moderate trajectory, nonetheless producing gains in excess of 90% between 2000 and late 2007³.

Apart from intensity, Portland’s housing bubble also differed markedly with respect to timing. San Diego and Los Angeles, for instance had maintained consistently high appreciation rates since the late 1990s, whereas the Las Vegas and Phoenix bubbles did not develop until 2003 and 2004 respectively. Portland was even later yet, experiencing its highest appreciation in 2005 and parts of 2006.

Home Price Appreciation Index for Selected Metropolitan Areas (S&P/Case-Shiller)

By mid-to-late 2006, at a time when the Portland housing market was in full swing, the bubble had popped in many parts of the country. Portland had been late to the party and would be among the last to leave. Eventually as much as 18 months after the first hot markets had begun to cool down, Portland started showing signs of weariness.

¹ www.agent503.com
² Irrational Exuberance, 2nd edition AND “In come the waves”, Economist, June 16, 2005
³ S&P/Case-Shiller Home Price Indices
Planned Communities, Suburban Developments Take the First Blow

During the boom years, Portland’s urban growth boundary (UGB) served as a means to protect the city against the perils of endless sprawl. The limited space available to developers within the city limits helped to contain the supply of housing inventory and avoid the deep pain found in fast-growing cities in the nation’s southwest.

Nonetheless, recent nearby incorporations and additions to the UGB, such as 800 acres of land on the north side of NW Springville Road in 2002, created potentially lucrative opportunities for developers of master-planned communities. As a result, a record 16,786 building permits were issued in 2005, followed by another 15,325 in 2006.4

In the wake of ever tighter credit markets and an increasingly dismal economic outlook, demand then began to dry up, leaving behind large numbers of desperate sellers and dozens of nearly vacant subdivisions. Happy Valley’s Francesca Lane, in Clackamas County embodied this trend like few other developments in the Portland metropolitan area and soon became the Oregonian’s poster child for developer greed, lofty housing dreams and the inevitable harsh landing5.

“In 2006 young families rolled in to snap up $600,000, stone-fronted homes with Mount Hood views. They came for the country meets cul-de-sac life, solid schools and a 4,000-square-foot edition of the American dream. Speculators trailed on their heels for the next get-rich-quick venture.

One of every five homes or lots on the street has fallen into foreclosure since the neighborhood sprang up three years ago. The street offers a grim picture of how greed dragged Happy Valley, Oregon, and even the world, into financial turmoil. Francesca Lane is where the country’s gamble on high-risk mortgages inflated home values, then crashed down on the freshly manicured lawns”6

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4 Number of Building Permits; Portland-Vancouver-Beaverton, OR-WA; Total, 2005;2006
5 Road to ruin: Happy Valley street embodies national housing bust, Oregonian, Dec 06, 2008
6
1. Buena Vista Custom Homes lot in foreclosure lawsuit
2. Ditto
3. Investment home with no-down payment loan, interest-only option and $5,000 monthly payment; purchased for $633,000, re-sold for $515,000
4. Subprime, no-down loan, two-year adjustable rate and interest only option, resold for $450,000
5. No-down loan, five-year adjustable rate, resold for $450,000
6. Home bought for 638K on no-down loan. Then filed for bankruptcy and reported $35,477 in wages. Resold for $470,000
7. Subprime, no-down loan. Resold: $477,000
8. Subprime loan, 11.75% interest, $6,390 monthly payments. Resold: $435,000
9. Developer deeded home to bank in-lieu of foreclosure
10. Ditto.

With more than 675 empty lots and 35 half-finished homes exposed to the weather, price points soon started to tumble, affecting nearby neighborhoods and eventually leading to one of the highest numbers of foreclosures for any county in the state or Oregon. The Center for Responsible Lending, a North Carolina nonprofit, estimates 50,000 Clackamas County homes will lose an average of $3,200 in value because of neighboring foreclosures.

Subprime-Related Defaults Usher In Initial Wave of Suburban Distress

Spillover effects from neighboring subdivisions contributed to a rising number of distressed property situations throughout the Portland-metro area. However, the bulk of short sales and foreclosures that surfaced in the early stages of the downturn i.e. onwards from Q3/2007, were the result of sub-prime lending practices, particularly prevalent among low-income, high risk borrowers.

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6 Ibid.
7 Ibid.
8 Clackamas Co. among highest foreclosure rates in Oregon, MSNBC, Mar 19, 2009
9 According to the U.S. Dept. of Treasury guideline: “Subprime borrowers typically have weakened credit histories that include payment delinquencies and possibly more severe problems such as charge-offs, judgments, and bankruptcies. They may also display reduced repayment capacity as measured by credit scores, debt-to-income ratios, or other criteria that may encompass borrowers with incomplete credit histories.”
Having largely been priced out of property markets in the urban core, a high-risk demographic group has typically sought more affordable alternatives on the outskirts of Portland, as indicated below.

**Map of Median Household Income for Portland-Metro Areas – Year 2000** (Subprime-Related Default Hotspots Outlined in Red)

![Map of Median Household Income](image)

Source: U.S. Census Bureau, 2000

Therefore, on Portland’s eastside a large proportion of the initial wave of defaults has been concentrated in areas bordering the I-205 corridor as well as North and NE Portland.

**Average # of Notice Of Default Filings Per Week For Eastside Zip Codes, Q4/2007**

![Bar Chart](image)

Source: First American Title Co.
The vast majority of these homes had a market value that was significantly lower than the median sales price ($285,000) for the Portland-metro area at the time. In fact, at the median price sold for both bank-owned and short sales in Q4/2007 for zip codes 97206, 97236 and 97266 was roughly $100,000 less than the median for the city at large.

Profile of Eastside Homes In Subprime Distress (Zip Codes: 97206, 97236, 97266)

<table>
<thead>
<tr>
<th></th>
<th>1,720</th>
<th>1,532</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average Sold Price Of Short Sales:</td>
<td>$195,497</td>
<td></td>
</tr>
<tr>
<td>Median Sold Price Of Short Sales:</td>
<td>$173,250</td>
<td></td>
</tr>
<tr>
<td>Average Sold Price Of Bank-Owned:</td>
<td>$188,338</td>
<td></td>
</tr>
<tr>
<td>Median Sold Price Of Bank-Owned:</td>
<td>$169,205</td>
<td></td>
</tr>
<tr>
<td>Average Sq. Ft:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Median Sq. Ft:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Source: RMLS, Q4/2007</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Gradually, Distress Turns Endemic

Initially a suburban phenomenon, distress soon spread throughout the Portland metropolitan area accelerating as more and more delinquent borrowers were added to the statistics.

Share of Delinquent Loans Increases by 70%, Year-over-Year

Ranked among the top five states for loan performance as recently as Q4/2007, Oregon appeared to remain largely unscathed by the housing downturn. By the fourth quarter of 2008, however, the share of delinquent loans had reached 5%, up more than 70%.

Mortgage delinquencies for the nation as a whole are reported at 7%, influenced to a large extent by foreclosure hot spots such as California, Florida and Nevada. Oregon mortgage troubles have yet to reach levels seen during the 1980s timber recession, but delinquencies clearly exceed the fallout from the dot.com bust.

Source: Mortgage Bankers Association

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10 Median Sales Price for Q4/2007, RMLS
Loans that have been delinquent for more than 90 days are typically subject to a notice of trustee sale and typically scheduled for foreclosure proceedings. This process is referred to as “foreclosure starts”. Tracking foreclosure starts provides additional insight into housing distress.

**Foreclosure Starts Increase 111% From the Same Time Last Year**

Roughly 5,000 foreclosure starts were recorded for Q4/2008 – more than twice as many as in Q4/2007. On average, 55 foreclosure starts were filed each day in the last quarter of 2008 up from 26 per day one year earlier.

Assuming a linear trend over the next couple of months, foreclosure starts will have increased threefold by the mid 2009 over late 2003.

**Number of Foreclosure Starts Fourth Quarter (Oregon)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Foreclosure Starts</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>1,857</td>
</tr>
<tr>
<td>2007</td>
<td>2,339</td>
</tr>
<tr>
<td>2008</td>
<td>4,939</td>
</tr>
</tbody>
</table>

Source: Mortgage Bankers Association

Oregon’s housing distress phenomenon also appears to have closed the gap with many other States. According to RealtyTrac, an online marketplace for foreclosures, the number of properties in Oregon with at least one foreclosure filing (default, auction, repossession) has risen steadily, placing Oregon among some of the most distressed states in the country by some measures.

**Oregon Among Top 5 States For Foreclosure Filings**

A recent RealtyTrac report showed Oregon among the top five states with the most foreclosure filings on a per household basis for the month of January. One in every 357 homes in Oregon received a foreclosure filing, with less densely populated counties such as Deschutes, Jackson and Clackamas at higher levels. Oregon’s February rating improved slightly putting Oregon in 9th place.

**Number of Foreclosure Filings (1/every HH rate), January 2009**

1. Nevada (1 in every 76)
2. California (1 in every 173)
3. Arizona (1 in every 182)
4. Florida (1 in every 214)
5. Oregon (1 in every 357)
24. Washington (1 in every 874)

Source: RealtyTrac

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11 MBA National Delinquency Survey, 4th Quarter 2008, Mortgage Bankers Association
12 The 1/every HH approach is skewed by counties with a large number of foreclosures, but low population density
Alarming Delinquency Trend Similar Across Tri-County Area

Multnomah County, the most populous among the three largest Oregon counties, dominates delinquency filings. In January 2009, roughly 730 Notices of Default were recorded, up 175% from one year ago. Delinquency filings were up threefold for Washington County, Registering 431 filings for the month of January and surpassing Clackamas County, where delinquency grew 118%.

Not every delinquent homeowner suffers foreclosure. As a result, the actual number of foreclosed properties will differ considerably from delinquency rates for a given area. In spite of the fact that trustee/foreclosure sales are open to the public, most foreclosed properties in Oregon currently revert back to the bank. Market inventory for distressed properties typically also consists of short sales.

Largest Inventory of Bank-Owned Short Sales - Multnomah County

Within the tri-county area, Multnomah County currently offers the largest inventory of bank-owned and short sale properties. More than 700 short sales and 250 bank-owned properties are available to buyers in Portland’s most populous county.

Washington County trails Multnomah by some 100 bank-owned properties and reports roughly 100 fewer short sales. Short sales are least common in Clackamas county.

13 A short sale is a sale of real estate in which the proceeds from the sale fall short of the balance owed on the loan.

Source: First American Title Co.

Source: RMLS
Distress Likely Spurred by Delinquencies on Alt-A Mortgages

It would appear that a significant proportion of the most recent rise in housing distress throughout the Portland metropolitan area can be attributed to a phenomenon that is accelerating nationwide. Homeowners with good credit are falling behind on their payments in growing numbers, even as the problems with mortgages made to people with weak, or subprime, credit are showing their first, tentative signs of leveling off. Of particular concern are so-called “Alt-A” mortgages, offered to borrowers in the segment between subprime and prime. This market was created as a means of extending home ownership to those, such as the self-employed, with a reasonable credit standing but unsteady income. Alt-A lenders specialized in loans with limited documentation requirements and exotic features such as negative-amortization mortgages, akin to a credit card, which allow borrowers to pay less than the accrued interest, with the difference added to the loan balance.

Negative-amortization and interest-only mortgages seemed appealing to many borrowers while home prices were still rising and homes could be sold prior to payments on principal being required. After spending several years paying only interest or sometimes even less than that, many Alt-A borrowers are now seeing their payments jump 50% or more. The higher bills come as home prices continue to decline and banks tighten their lending standards, making it harder for people to refinance loans or sell their homes ultimately forcing homeowners into negative equity, under-water positions and pushing up the number of defaults.

Alt-A borrowers typically had a five- or seven-year grace period before payments toward principal were required. By contrast, subprime loans had a two-to-three-year introductory period. That difference partly explains the lag in delinquencies between the two types of loans. Alt-A troubles first made headlines last summer, when IndyMac, the seventh largest mortgage originator in the nation, had to be seized by the FDIC as a result of its over-leveraged Alt-A operations. The speed at which Alt-A mortgages have since soured has taken many by surprise. Moody’s, which had issued a relatively optimistic outlook for Alt-A loans in mid-2008, recently quadrupled its loss projections on bonds backed by such loans. Of the $59 billion of AAA-rated securities on which Moody’s cut ratings in late January, an overwhelming 91% were subsequently downgraded to junk bond status. Moody’s now expects losses for 2006-07 Alt-A securitizations to top 20%, compared with an historical average of well under 1%. The volume of Alt-A debt nationwide is substantial. Currently an estimated $1.3 trillion of total Alt-A debt exists, including both securitized and unsecuritized loans. According to some sources losses could exceed $600 billion, almost as much as expected subprime losses.

An estimated 26,000 Portland-area homeowners currently hold an Alt-A mortgage. Portland residents, facing relatively high-priced homes but not-so-high incomes, resorted to Alt-A mortgages more frequently than residents of most other American cities, while using fewer subprime loans. Much of the recent data would seem to support that Alt-A and prime delinquencies are indeed a serious and growing problem for Portland and beyond.

15 IndyMac Bank seized by federal regulators, LA Times, July 12, 2008
16 Move Over, Subprime, Economist, Feb 5, 2009
17 Shaky loans may spur new foreclosure wave, Portland Tribune, Mar 6, 2009
Prime Foreclosure Starts are Growing Three Times Faster than Subprime

Prime foreclosure starts in Q4/2008 increased by 182% compared to Q4/2007, outpacing subprime foreclosure starts in terms of growth as well as volume. Overall, subprime loans continue to have higher rates of problems than prime loans, as a percentage of loans serviced in the respective category, but the rate of increase in prime problem loans is much higher than for subprime loans. Subprime loans account for 9% of all loans but 40+% of problem loans. However, prime loan problem loans grew by 180% to 240% in several problem loan categories.

Number of Prime vs. Subprime Foreclosure Starts, Fourth Quarter, Oregon

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Subprime</td>
<td>1,360</td>
<td>2,137</td>
</tr>
<tr>
<td>Prime</td>
<td>882</td>
<td>2,485</td>
</tr>
</tbody>
</table>

57% 182%

Prime vs. Subprime Foreclosure Starts, Fourth Quarter, Oregon

Source: Mortgage Bankers Association

Mortgage Resets Likely to Trigger Additional Defaults

Beyond Alt-A and prime mortgages, resets on Option Adjustable Rate Mortgages (Option ARMs) are expected to pose an additional problem for borrowers and lenders alike. The majority of subprime resets has already occurred, resulting in fewer problems than anticipated since many borrowers have been able to refinance at historically low interest rates.

However, as the first wave of Option ARM resets approaches, home prices will have declined even further, reducing the share of homeowners that are likely to qualify to refinance. The situation is considered especially precarious given the widespread use of negative amortization among Option ARMs and could be further exacerbated by rising interest rates.

Monthly Mortgage Rate Resets (U.S.)

In Billions of Dollars

Source: Credit Suisse.
Higher-End Homes Increasingly Affected By Mortgage Crisis

As distressed housing works its way up the food chain, the crisis is spreading from lower-priced neighborhoods to well-heeled parts of town. From high-end downtown condos to 4,000 square foot close-in mansions, distressed properties have become increasingly common.

Delinquency No Longer An Entry-Level Phenomenon

In the Pearl District, borrowers are late on their payments at such high-end condominiums as the Henry or the Waterfront Pearl, where luxury lofts until recently have been selling at a minimum of $500 per square foot. Delinquency has become a regular feature at several South Waterfront developments, notably the John Ross.

Recent Notice Of Default Filings For Multnomah County

<table>
<thead>
<tr>
<th>Location</th>
<th>Purchase Price</th>
<th>Mortgage Amount</th>
<th>Default Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Henry Lofts (Condo)</td>
<td>$490,000</td>
<td>$343,000</td>
<td>$10,565</td>
</tr>
<tr>
<td>Pinnacle (Condo)</td>
<td>$817,500</td>
<td>$613,100</td>
<td>$24,105</td>
</tr>
<tr>
<td>Belmont/Hawthorne (SFH)</td>
<td>$760,000</td>
<td>$608,000</td>
<td>$37,337</td>
</tr>
<tr>
<td>Forest Heights (SFH)</td>
<td>$1,100,000</td>
<td>$715,000</td>
<td>$30,382</td>
</tr>
<tr>
<td>Alameda (SFH)</td>
<td>$875,000</td>
<td>$1,000,000</td>
<td>$45,293</td>
</tr>
</tbody>
</table>

Source: First American Title Co.

High-End Distressed Properties Have Been Selling At Significant Discounts

Roughly 50 distressed condos are currently on the market in downtown Portland. More than half of the resale inventory at the Shoreline townhouses in the Pearl District is bank-owned. Half a dozen ridge-top mansions in Forest Heights have been substantially discounted since banks took them back. Some of the most competitively priced inventory in the Portland-metro area is either a short sale or bank-owned, placing considerable pressure on conventional sales in recent months. In an effort to move large-ticket inventory off their balance sheets, banks have begun to show more flexibility when negotiating with cash buyers.
Recent Sales Of Distressed Property In Multnomah County

<table>
<thead>
<tr>
<th>Location</th>
<th>Sale Price</th>
<th>Sale Date</th>
<th>Previous Sale Price</th>
<th>Previous Sale Date</th>
<th>% Decline</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pearl District</td>
<td>$ 420,000</td>
<td>Mar, 2009</td>
<td>$ 755,000</td>
<td>Jun, 2006</td>
<td>44%</td>
</tr>
<tr>
<td>Sullivan’s Gulch</td>
<td>$ 475,000</td>
<td>Mar, 2009</td>
<td>$ 549,000</td>
<td>Jul, 2005</td>
<td>13%</td>
</tr>
<tr>
<td>West Linn</td>
<td>$ 382,000</td>
<td>Mar, 2009</td>
<td>$ 541,000</td>
<td>Sept, 2006</td>
<td>29%</td>
</tr>
<tr>
<td>Downtown</td>
<td>$ 700,000</td>
<td>Oct, 2008</td>
<td>$ 1,115,000</td>
<td>Dec, 2006</td>
<td>37%</td>
</tr>
<tr>
<td>Forest Heights</td>
<td>$ 800,000</td>
<td>Dec, 2008</td>
<td>$ 1,220,000</td>
<td>July, 2006</td>
<td>34%</td>
</tr>
</tbody>
</table>

Source: RMLS

Liquidation Sales, Auctions and Incentive Programs Sought To Unload Inventory

Liquidation sales and auctions have been a staple method to unload surplus inventory among developers faced with the prospect of bankruptcy since the early days of the housing market downturn.

Buena Vista Custom Homes conducted a well-publicized December 2007 auction that resulted in 141 homes being sold generating over $65 million in sales\(^{18}\). The December sale is believed to be the largest two-day sale of real estate by one seller in Oregon history. In early 2008, another auction followed with 52 homes from nine of Buena Vista’s neighborhoods and 18 buildable lots from three different developments in the Portland metropolitan area. Buyers at the December auction, in particular, were able to purchase homes at significant discounts:

- In Beaverton’s Carson Crest neighborhood, a home previously listed at $624,950 was sold at auction for $475,000, discounted 24 percent.
- In Sandy, a home in Buena Vista’s Hamilton Ridge development sold for $241,500 after being previously listed at $321,950, discounted 25 percent.

Pacific Lifestyle Homes and Legend Homes, two of four local home builders to file for reorganization under Chapter 11 of the U.S. Bankruptcy Code in 2008, had formed a joint marketing venture to sell more than 100 completed homes in the Willamette Valley by the end of March\(^{19}\). List prices ranged between $174,000 and $599,999. The event has been a considerable success, clearing out more than 40% of the available inventory.

\(^{18}\) Oregon Home Builder Announces Second Home Auction, Reuters, Feb 08, 2008
\(^{19}\) Bankrupt home builders form marketing venture..., Portland Business Journal, Jan 22, 2009
Recent Sales at New Home Liquidation Sale

<table>
<thead>
<tr>
<th>Location</th>
<th>Original Price</th>
<th>Sale Price 20</th>
<th>Discount %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hillsboro</td>
<td>$269,900</td>
<td>$209,900</td>
<td>22%</td>
</tr>
<tr>
<td>Happy Valley</td>
<td>$425,200</td>
<td>$368,900</td>
<td>13%</td>
</tr>
<tr>
<td>Wilsonville</td>
<td>$536,962</td>
<td>$469,900</td>
<td>13%</td>
</tr>
<tr>
<td>Tigard</td>
<td>$412,833</td>
<td>$354,900</td>
<td>14%</td>
</tr>
<tr>
<td>Wilsonville</td>
<td>$436,818</td>
<td>$387,900</td>
<td>12%</td>
</tr>
</tbody>
</table>

Source: RMLS, Pacific Lifestyle Homes, Legend Homes

Community Financial Corp., a subsidiary of Banner Bank, recently launched “The Great Northwest Home Rush”, a program that is intended to boost sales for builders who owe the bank millions of dollars, by offering mortgages to new homebuyers at less than four percent interest. Loans are available only for properties purchased from a list of roughly 300 homes and lots in the Portland-metro area developed by numerous builders indebted to Banner Bank.

Although Banner Bank never engaged in subprime lending, it did provide construction and land loans to dozens of builders during the boom. The bank’s publicly traded parent company, Banner Corp., recently reported that it had about $150 million in bad residential construction loans and related lot and land loans on the books at the end of 2008. The program officially ended on Mar 22, 2009 after some 30 homes sold, generating at least $50,000 million in loans for Banner. 21

The Real Estate Disposition Company (REDC), one of the nation’s largest residential real estate auction marketing companies, held its largest auction to date in the Portland-metro area in April. Despite attendance of over 1,000 people, bids were accepted for only 35 of 50 properties, subject to seller confirmation. Auction inventory included a wide range of properties from beach homes in Tillamook County to condominiums in the Pearl District and custom homes in upscale neighborhoods.

3,000 Square Foot Forrest Heights Home Among 50+ Properties at Auction

Source: REDC

20 Sale pending. Final price and additional incentives not confirmed
21 Bank offers home loans below 4%, Inman News, Mar 17, 2009
Outlook: Rapid Recovery Unlikely

Much of outlook for the Portland real estate market will depend on how unemployment is affected by the economic downturn in the months ahead. Recent trends have not been very encouraging. So far, lay-off announcements by Oregon’s most prominent and significant employers have been fairly moderate.

- OHSU, Portland largest employer with 12,700 staff, suffered substantial investment losses in 2008 and now needs to reduce expenses by about $30 million, approximately 4 percent of payroll\(^\text{22}\).

- In February, Nike, the state’s largest publicly traded company announced that it intends to cut its workforce by 4% as part of restructuring efforts\(^\text{23}\).

- Portland’s PCC Structural, Inc., a division of Precision Castparts Corp., the second-largest publicly traded company based in Oregon, will cut 10 percent of its salaried workers\(^\text{24}\).

Nonetheless Oregon’s downward employment trend is well underway. According to Oregon Employment Department officials, the state lost 81,800 jobs in the past 12 months, far exceeding the 64,500 jobs lost between 2001 and 2003 during the previous recession\(^\text{25}\). The number of unemployed Oregonians jumped to 236,286 in February, more than doubling over the past 12 months. The state’s total nonfarm payroll employment fell to 1,636,400. Experts were particularly concerned by February numbers which revealed a one-month loss of 21,700 jobs, seasonally adjusted, the largest since the state began keeping records in 1977. On average, 775 jobs Oregon were lost each day in February.

Oregon Loses 21,7000 Jobs in February, Now #3 In The Nation For Unemployment

As a result of February’s steep drop, unemployment in Oregon jumped a full percentage point - up from January’s rate of 9.8 percent. According to David Cooke, a state labor economist,

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\(^\text{22}\) OHSU freezes salaries, plans layoffs, Oregonian, Dec 01, 2008
\(^\text{23}\) Nike may cut workforce by up to 4% as part of restructuring; MarketWatch, Feb 10, 2009
\(^\text{24}\) Precision Castparts plans 10% layoffs, DJC, Jan 13, 2009
\(^\text{25}\) Oregon jobless rate hits 10.8%, Oregonian, Mar 16, 2009
Oregon hasn’t had 10.8 percent unemployment since July 1983. By the end of March, Oregon’s unemployment reached 12.1%. Oregon now has the second-highest unemployment rate in the country, behind only Michigan at 12.6%.

The administration’s Homeowner Affordability and Stability Plan is expected to bring some temporary relief for housing markets as banks suspend foreclosures, while some debt situations are worked out with delinquent borrowers. However, considerable doubt remains as to how the plan will be perceived by lenders, the entities charged with implementing the plan. If billion-dollar bailout funds are not encouraging banks to increase lending, it remains questionable how much can be expected from yet another set of incentives, well intentioned though they might be. Action on behalf of lenders is furthermore impeded by the complexity of the plan with multiple programs, federal and state bureaucracies, conditions and caveats. The four-page White House executive summary is confusing to many. How well it may be digested by the average bank officer or low-income subprime borrower is open to question.

Assuming distressed property inventory does indeed level-off, Multnomah County would still face at least another 10-12 months to clear out its share of distressed property, based on the current rate of sales for this category. That’s assuming demand continues at current levels, in spite of a worsened economic outlook in recent months. It may be more likely that inventory will increase as banks are not inclined to suspend foreclosures indefinitely and many borrowers face increasing pressures to meet payments in a harsh economic climate.

26 Gov’t: Bailed-Out Banks Still Not Lending, USA Today, Mar 17, 2009
27 Number of distressed property sales for the month of February 2009 divided by total amount of available distressed inventory for that month. Source: RMLS
Housing Market Analysis
Elizabeth Warren, Certificate of Real Estate Development Graduate Student & Oregon Association of Realtors [OAR] Fellow

The close of the 1st quarter in 2009 marks the continuation of last year’s trend as housing prices across the nation continue to depreciate. Median U.S. home values were down -15% annually in February, and -30% for the western part of the nation. According to February’s Standard & Poor’s Case-Shiller index, home prices fell a record 18.5% in 2008, with the biggest downturns in Phoenix (34%), Las Vegas (33%), and Miami (28.8%). For Portland, the index valued a $100,000 home in 2000 at $158,500 for the end of 2008. RealtyTrac’s January foreclosure report put Oregon at fifth in the nation for notices of default, auctions, and other forms of foreclosure action. In 2008, 12.2% of all transactions involved foreclosed real estate. The number of permits issued nationally was down 50% and reduced by 58% in Oregon.

Median Home Values of Existing Detached Homes

<table>
<thead>
<tr>
<th></th>
<th>U.S.</th>
<th>West</th>
<th>Portland Metro Area</th>
</tr>
</thead>
<tbody>
<tr>
<td>February 2008 Median Sales Price</td>
<td>$193,600</td>
<td>$296,600</td>
<td>$287,550</td>
</tr>
<tr>
<td>February 2009 Median Sales Price</td>
<td>$164,600</td>
<td>$207,700</td>
<td>$256,950</td>
</tr>
<tr>
<td>% Change in Median Sales Price</td>
<td>-15.0%</td>
<td>-30.0%</td>
<td>-11.0%</td>
</tr>
<tr>
<td>% Change in Number of Sales February 2008-2009</td>
<td>-3.6%</td>
<td>30.6%</td>
<td>-21.0%</td>
</tr>
</tbody>
</table>

Source: National Association of Realtors (February 2009) and RMLS (February 2009)

Median Sales Prices of Existing Single Family Homes By Metropolitan Area

Source: http://www.realtor.org/Research.nsf/Pages/MetroPrice

1 Portland Business Journal. “Home Prices Tumble by Record 18.5 Percent”. Tuesday, February 24, 2009
Portland was no exception to the national trend. By the end of 2008, 18.9% of all home sales in Portland resulted in a loss to the seller, and 21.2% of all homeowners statistically owed more on their homes than they were worth.\(^2\) In March, buyers closed on 1,184 homes, dropping over -30% from a year ago.\(^4\) The level of unsold homes in March decreased to a 12 month supply, well below the 16.6 month supply level of February, and the 19.2 month supply of January. Median prices for the first quarter were down –7.24% to $255,000 for the collective Portland market, resulting in a -13% annual depreciation. Existing home sellers continue to mark down their prices, collecting an average of 90.05% of the original list price, with hopes that the three month wait on the market will decline as prices are lowered. The number of transactions fell 16% from last quarter, and 28% from the previous year. An emphasis on the longer-term outlook of price per square foot puts the recent depreciation into perspective. Portland’s existing single-family home values are still slightly above the median price per square foot values of the 2005 pre-bubble market.

\(^3\) First Quarter denotes aggregate data for January 1 – March 31, 2009. Data compiled from RMLS [March 2009]

Median Sales Price & Number of Homes Sales per Quarter - Existing Detached Homes

Portland Metro (Excluding Clark County)

8-Year outlook for Median Sales Price & Number of Transactions

1st Quarter Median Price: $255,000
Quarterly % Change: -7.24%
Annual % Change: -26.35%

Number of Transactions: 1,996
Quarterly % Change: -16.10%
Annual % Change: -28.56%

Sale Price/Original List Price & Average Days on Market – Existing Detached Homes

Portland Metro (Excluding Clark County)

2-Year Outlook for Average Days on Market & Sales Price/Original List Price Ratio

1st Quarter Sale/Original ratio: 90.05
Quarterly % Change: -0.60%
Annual % Change: 0.55%

Days on Market: 87
Quarterly % Change: 14.47%
Annual % Change: 20.83%

Median Sales Price & Number of Transactions – New Detached Homes

Portland Metro (Excluding Clark County)

8-Year Outlook for New Construction Single-Family Home Sales

1st Quarter Median Price: $357,450
Quarterly % Change: -0.68%
Annual % Change: -5.31%

Number of Transactions: 262
Quarterly % Change: -30.87%
Broken down by sub-market, we can see where the single-family home activity took place in the 1st quarter. In the 4th quarter breakdown, Mt. Hood and Columbia County experienced over 12% appreciation for single-family homes.5

This quarter, the appreciation rates have moved toward Wilsonville and Yamhill County where home sales were up 16%. An annual outlook puts all submarkets into the negative, with Lake Oswego again at the highest depreciation (-20.63%). However, a few markets encountered slightly less stark annual depreciation rates. The Tigard/Wilsonville and Mt. Hood markets depreciated -5% annually; Yamhill County values depreciated -6.5%.

5 Appreciation is based on the 17 home sales in Mt. Hood, and the 80 home sales in Columbia County.
Vancouver

For Clark County, the story is similar to that in Portland. In February, the Portland Business Journal reported that there were 225 total sales, down 23.5% from last year. Pending sales decreased 15.7%. The end of the first quarter showed that existing home prices for the downtown area of Vancouver dropped 5.75% from last quarter to $205,000. This marks a 13.1% annual decrease. The number of downtown transactions fell -10% quarterly and -14% annually to 379. The number of days on the market surpassed 100 for the first time in 5 years, with an average total of 105 days.
In the suburbs of Clark County, the median price of existing detached homes hit $245,500 – up 2.29% from 4th quarter's $240,000, but still -11.1% below last year's values. The number of transactions fell -9% quarterly, but enjoyed a small 2% upturn annually. The average number of days on the market increased by about 9% quarterly and annually to 112 days.
For the Vancouver and Clark County submarket, the first quarter followed Portland’s submarket. Fourth quarter 2008 showed sales appreciating in Battleground, N. Felida, and Washougal.

This quarter, appreciation rates are found in a handful of markets. However, none surpassed the 5% wall seen for the past few quarters. Like Portland, annual median value rates for existing single-family homes for all markets were depreciating. East Heights and North Felida take the lead with –36% annual depreciation. Cascade Park maintained an almost stationary position through the real estate turmoil of the past year, with only a slight depreciation of 0.3% in existing home sales. The Lincoln/Hazel Dell market experienced a -3% annual depreciation.
Condominium and Attached Market

Condominium sales are significantly down from both the last quarter and the previous year numbers. Across the metropolitan area, sales were down -36% from Portland's 4th quarter transactions, and -50% for Vancouver. Decreases in the price per square foot were not as dramatic, but still confirmed that the 2008 bubble is still deflating. For Portland, the price per square foot hit $192.96, with a median home value of $200,000. The central city of Vancouver's price per square foot for condominiums fell -25% from last year. Sellers in the condominium market are receiving a median of $115.85/square foot and a median value of $123,950. As seen in the graphs below, the Portland submarket follows a path which is similar to the larger central city areas.

---

6 RMLS defines attached as "an element of the residence construction is shared with another property. Condominiums are excluded. Condominiums are defined as an attached or stand-alone residence for which the owner has title to the space inside the unit and shares common spaces with other unit owners in accordance with specific legal guidelines."
For the single-family attached market, nearly all markets have fallen back to 2005 price/square foot values. However, for Vancouver, attached home values match more closely to the price/square foot values of 2002. The longer time span outlook for the Portland market reveals substantial volatility, with the number of transactions down -27% quarterly and a slight 16% increase annually from 145 to 168. Analysis of price per square foot appears less dramatic with -4% depreciation quarterly, and -7% annually to $138.58/square foot. The first quarter median home value was $220,250. For central Vancouver, there were 19 total transactions, a decline of -24% from 4th quarter, and a dramatic -62% annually. Attached home values were largely impacted by the current economic downturn, depreciating by -22% quarterly, and -28% annually. Median prices fell to $150,000, with a $96.40/square foot value.
Central Oregon

For the cities of Bend and Redmond, the first quarter median price and the number of transactions continued their slow decline while the average number of days on the market increased moderately. In Bend, median single family home values fell -21% quarterly and -28% annually to $221,250. The number of transactions was down -31%, and the average number of days on the market reached 191, a 3% increase from this time last year. Redmond is similar, with the number of transactions down -17% annually, -33% quarterly, and median values falling -25% annually to $165,000. Residents looking to sell experienced a -20% decline in the number of days on the market. Homes remained on the market for an average of 143 days.
As it is commonly reported in Central Oregon, the housing stock is separated by lot size – properties under one acre and those between one and five acres. Price per square foot is provided to control for lot size between both categories. Here we see the continuing trend of declining prices after the peak in 2006. For Bend, this quarter marks the first time median home prices have fallen below 1st quarter 2005 values, translating to a decline of -17% quarterly, -34% annual depreciation and a $347,500 median price for large lot homes. Price per square foot followed suit, falling to a -27% annual depreciation of 167$/square foot. The number of transactions was up 22% and the average days on the market fell -9%. In Redmond, the first quarter was the second quarter in a row that median values for large lot homes fell below 2005 prices. Although it was a 7% jump from last quarter, the $299,000 median price marks a -15% annual depreciation for homeowners. Redmond’s average price per square foot of $149/sq.ft revealed a -7% quarterly and a -28% annual depreciation. The number of transactions remained steadily low at 11, while the number of days on the marked decreased dramatically from 264 to 195.
The housing trends found in the northern parts of Oregon continue down the valley and into the southern counties. Lane County has been hit the hardest by the housing crunch, with a -10.5% depreciation quarterly, and a -17.1% annual depreciation of existing homes. However, with such a decline in prices, the average number of days a house remained on the market fell -21% from last year, and the number of transactions rose 212% to 278 transactions. This could be due to sellers lowering their prices, and accepting 85% of their original list price to get the sale. For the other four counties recording an annual depreciation, the number of days on the market rose dramatically and the number of transactions was far lower than the previous year. Linn County’s housing market is relatively strong. Median home values are up 10% annually to $155,000, and the number of transactions rose 4.8%. However, in the longer term perspective, median values are still below 2007 prices, as are the number of days on the market (a 35% increase since 2007). The county’s number of transactions is half what it was two years ago.
The Salem housing downturn continues. Homeowners are waiting an average of four months before their homes sell, resulting in a -23% annual decline in the number of sales for the area. Median home values remain stable, falling less than one percent annually. As stressed in previous sections, a longer term outlook shows the median price of a single family home is still considerably higher than three years ago.
In the joint cities of Eugene/Springfield, median home values were down, the number of transactions fell, and the number of days on the market rose. Homeowners are waiting three months to sell their homes, accepting a sale price averaging 88.8% under their original list price to get the property sold. Median home values remained at the previous quarter’s price of $220,000, and the annual depreciation hovered around a relatively moderate -5%.
Portland Office Market

Overall the office market has performed as anticipated this first quarter of 2009. Overall vacancy is up, absorption is negative, sublease space has increased and most submarkets have seen a decrease in rents. However, it seems that some companies are taking advantage of the downturn to move to more favorable locations. The CBD is faring better than other areas, and actually saw an increase in asking rents. Suburban vacancy rates are double those of the CBD. While the CBD has experienced an increase in vacancy, the median vacancy rate is now equal to what it was in the first quarter of 2008, which is still lower than the first quarter of 2009 by eight tenths of a percentage point. CBD class A vacancy rates remain low at a 6.3% median rate and asking rents have actually increased $0.22 since last quarter, to $27.02 per square foot. The suburban Class A median rent has decreased by $1.01 since last quarter, and the median vacancy rate has increased 1.2 percentage points since last quarter to 17.5%.

Most are still positive about Portland’s ability to hold its own during the downtown. CB Richard Ellis points to the Forbes ranking of Portland 26th out of 200 largest metro areas, as a good place to do business. They also mention that Element Power, a renewable energy company has decided to locate in Portland. CBRE states that nearly 933,966 SF of office space is under construction, but makes a note that TMT Development plans to halt construction on Park Avenue West. According to Norris, Beggs and Simpson, OHSU and Intel both laid off up to 1,000 people this quarter, but Intel is still planning to invest $1.5 billion through 2010.

Overall Net Absorption (sq. ft.) and Vacancy (%) for Portland Market

Source: Grubb & Ellis, Co., Office Quarterly Report, First Quarter 2009 Statistics
### OFFICE Q1-09

<table>
<thead>
<tr>
<th></th>
<th>CB Richard Ellis</th>
<th>Cushman &amp; Wakefield</th>
<th>Grubb &amp; Ellis</th>
<th>Norris, Beggs &amp; Simpson</th>
<th>Median</th>
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<td></td>
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<td></td>
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<tr>
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<table>
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<th>17%</th>
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<td>16.2%</td>
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<table>
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<th>17%</th>
<th>18%</th>
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<tbody>
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<td>16.3%</td>
<td>15.2%</td>
<td>17.0%</td>
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<tr>
<td>First Quarter 2008</td>
<td>N/A</td>
<td>13.9%</td>
<td>12.7%</td>
<td>N/A</td>
</tr>
<tr>
<td>First Quarter 2007</td>
<td>N/A</td>
<td>13.7%</td>
<td>10.5%</td>
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<tr>
<th><strong>Suburban Class A Asking Rents</strong></th>
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<th>$22.95</th>
<th>$23.20</th>
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<tr>
<td>Previous Quarter</td>
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<td>$24.48</td>
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**Source:** CB Richard Ellis, Cushman & Wakefield, Grubb & Ellis, Norris, Beggs & Simpson Quarterly Reports and Statistical Reports, First Quarter 2009.

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1. Vacancy rates above include subleases except those reported by CBRE. CBD figures include close-in neighborhoods, except Class A figures reported by CBRE. All rents are full service. All other suburban figures include Vancouver.
Office Absorption for Class A, B & C

CBD Direct Rental Asking Rates (sq.ft.)
Metro Wide All Classes v. CBD Class A

Source: Grubb & Ellis, Co., Office Quarterly Report, First Quarter 2009 Statistics

Source: Cushman & Wakefield, Portland First Quarter 2009, Overall Office Summary.
CBD Trends

Norris, Beggs and Simpson noted that, “sublease space is becoming more prevalent”, which can be seen in the following graph based on the report by Cushman and Wakefield. Sublease availability increased in the CBD, with 237,907 square feet available at quarter’s end. Not surprisingly, subleases as a percentage of the direct vacancy also increased, up to 39.2% in this first quarter of 2009. However, it is still well below the peak seen in the fourth quarter of 2002 when it reached 49.3%. The CBD saw an increase in asking rents, which may mean that landlords are offering more concessions to lure tenants. Absorption is negative with more office space coming on line than was absorbed by the market.

Office CBD Class A Direct v. Sublease Availability

Source: Cushman & Wakefield, Portland First Quarter 2009, Overall Office Summary.

CBD Direct Rental Asking Rates/sq.ft.

Source: Cushman & Wakefield, Portland First Quarter 2009, Overall Office Summary.
Office CBD Class A Direct v. Sublease Availability (Sq. Ft.)

Source: Cushman & Wakefield, Portland First Quarter 2009, Overall Office Summary.

CBD Net Absorption (sq. ft.) and Vacancy (%)

Source: Grubb & Ellis, Co., Office Quarterly Report, First Quarter 2009 Statistics
Suburbs:

Most vacancies have been felt in the suburbs, especially southwest. Kruse Way was hit hard, but has seen some leasing activity. According to Norris, Beggs and Simpson, Kruse Way vacancy fell as EthicsPoint leased 22,654 SF at 6000 Meadows. It may be offset by the completion of Kruse Oaks III which will soon add 110,000 SF in the second quarter of 2009. The Tualatin/Wilsonville submarket shows the greatest vacancy rate of 26.1%, although its current vacant square footage of 417,523 SF equals less than half the vacant square footage found in The Sunset Corridor, which had the highest total vacant square footage with 1,062,048 SF currently vacant.

*Source: Grubb & Ellis, Co., Office Quarterly Report, First Quarter 2009 Statistics

<table>
<thead>
<tr>
<th>Submarket</th>
<th>Rank</th>
<th>Vacancy Rate</th>
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<tbody>
<tr>
<td>Camas</td>
<td>2</td>
<td>25%</td>
</tr>
<tr>
<td>Cascade Park</td>
<td>4</td>
<td>18.8%</td>
</tr>
<tr>
<td>Vancouver</td>
<td>9</td>
<td>13.2%</td>
</tr>
<tr>
<td>Clackamas Sunnyside</td>
<td>12</td>
<td>9.30%</td>
</tr>
<tr>
<td>Clark Co. Outlying</td>
<td>7</td>
<td>14.1%</td>
</tr>
<tr>
<td>Columbia Corridor</td>
<td>10</td>
<td>12.8%</td>
</tr>
<tr>
<td>Eastside</td>
<td>15</td>
<td>7.6%</td>
</tr>
<tr>
<td>Hazel Dell/Salmon Creek</td>
<td>17</td>
<td>5.1%</td>
</tr>
<tr>
<td>Johns Landing/Barbur Blvd</td>
<td>8</td>
<td>13.9%</td>
</tr>
<tr>
<td>Northwest</td>
<td>16</td>
<td>6.7%</td>
</tr>
<tr>
<td>Orchards</td>
<td>14</td>
<td>8.4%</td>
</tr>
<tr>
<td>St. Johns/Central Vancouver</td>
<td>11</td>
<td>11.6%</td>
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<tr>
<td>Sunset Corridor</td>
<td>2</td>
<td>25.3%</td>
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<tr>
<td>SW/Beaverton/Sylvan</td>
<td>5</td>
<td>16.5%</td>
</tr>
<tr>
<td>Tualatin/Wilsonville</td>
<td>1</td>
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<td>Vancouver Mall</td>
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<tr>
<td>Washington Sq/Kruse Way</td>
<td>6</td>
<td>16.3%</td>
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*Source: Grubb & Ellis, Co., Office Quarterly Report, First Quarter 2009 Statistics

Vacant and Occupied SF as Part of Total SF Available for Suburban Submarkets

*Source: Grubb & Ellis, Co., Office Quarterly Report, First Quarter 2009 Statistics
### Major Lease Transactions Q1 2009

<table>
<thead>
<tr>
<th>Lessee</th>
<th>Property</th>
<th>Submarket</th>
<th>Size (SF)</th>
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<tr>
<td>Comcast of Tualatin Valley Northwest Evaluation</td>
<td>Tektronix Building 48, BVrttn</td>
<td>Sunset Corridor</td>
<td>118,612</td>
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<tr>
<td>Allstate Corp</td>
<td>121 SW Everett St.</td>
<td>Northwest</td>
<td>104,000</td>
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<tr>
<td>EthicsPoint</td>
<td>Southwest Center</td>
<td>I-5 South</td>
<td>36,912</td>
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<td>Tonkon Torp LLP</td>
<td>6000 Meadows</td>
<td>Kruse Way</td>
<td>22,654</td>
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<tr>
<td>Markowitz, Herbold, Glade &amp; Mehlhaf</td>
<td>Pioneer Tower</td>
<td>CBD</td>
<td>62,813</td>
</tr>
<tr>
<td>Vestas America</td>
<td>Harrison Square</td>
<td>CBD</td>
<td>18,748</td>
</tr>
</tbody>
</table>

Source: Grubb & Ellis, MarketView First Quarter 2009, Norris, Beggs & Simpson, "Market Summaries, Office Report 1Q09"
Portland Industrial Market

The industrial sector has been hit hard by the recent spike in unemployment, which reached 12.1% in March. Overall median vacancy rates jumped to 7.8% compared to 5.5% in the first quarter of last year. Grubb & Ellis note that the Portland Metro area delivered just over 527,000 square feet this quarter with construction projects under way totaling 741,000 square feet, 415,000 of which will be occupied by FedEx in 2010. Sublease space is becoming an important factor in the market as companies are unable to use all of the space they have leased. Asking rates are holding steady, but as with the office and multifamily markets, brokers report that landlords are starting to give more concessions in response to market conditions. Tenants have more options available to them. Leasing agents also report having to pass on potential leases because of a lack of funding needed to provide requested tenant improvements, due to the tight credit market.

<table>
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<tr>
<th>INDUSTRIAL</th>
<th>Q1-09</th>
<th>CB Richard Ellis</th>
<th>Cushman &amp; Wakefield</th>
<th>Grubb &amp; Ellis</th>
<th>Norris, Beggs &amp; Simpson</th>
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<tr>
<td>Market-wide Vacancy</td>
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<td>13.0%</td>
<td>7.8%</td>
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<tr>
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<td>6.4%</td>
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<td>6.9%</td>
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<td>First Quarter 2008</td>
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<td>9.4%</td>
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<td>$0.81</td>
<td>N/A</td>
<td>$0.81</td>
<td></td>
</tr>
<tr>
<td>First Quarter 2008</td>
<td>$0.85-$1.05</td>
<td>N/A</td>
<td>$0.81</td>
<td>N/A</td>
<td>$0.81</td>
<td></td>
</tr>
<tr>
<td>First Quarter 2007</td>
<td>$0.85-$1.05</td>
<td>N/A</td>
<td>$0.80</td>
<td>N/A</td>
<td>$0.80</td>
<td></td>
</tr>
</tbody>
</table>

Source: Grubb & Ellis, Cushman and Wakefield, Norris, Beggs & Simpson, Quarterly Reports
Cushman & Wakefield report a negative absorption for all submarkets this quarter, except for the North/Northeast Portland. Grubb & Ellis point out Rivergate as the submarket with the highest vacancy rate, currently at 11.4%, and the I-5 Corridor with the highest negative net absorption with just over 960,000 square feet, due at least in part to the 500,000 square feet Nike returned to the market.

**Submarket Vacancy and Absorption First Quarter 2009**

![Graph showing submarket vacancy and absorption for the first quarter of 2009.]

Source: Cushman & Wakefield Industrial Quarterly Summary, 1Q09

**Overall Industrial Net Absorption (sq. ft.) and Vacancy (%) for Portland Market**

![Graph showing overall industrial net absorption and vacancy for Portland Market from 2000 to 2009.]

Source: Grubb & Ellis Co., Industrial Quarterly Report, First Quarter 2009
Again this quarter, new construction outpaced absorption reversing a trend that started in 2004. Grubb & Ellis report a negative absorption of <22,187> square feet in the fourth quarter, with 527,984 square feet of new construction delivered to the market. The nine year period spanning 2000-2008 averaged 2.8 million square feet per year absorption into the market. The first quarter vacancy rate of 8% just surpasses the nine year average of 7.9%, and well below the low-point in 2003 of 11.6%.

Norris, Beggs & Simpson report that SolarWorld plans to expand their solar facility in Hillsboro, adding a 210,000 square feet building, which may reflect the tax incentives Oregon provides to solar companies. According to CB Richard Ellis, SolarWorld willemploy 200 construction workers during construction, and employ up to 1,000 people by the year 2011.

**Major Lease Transactions Q1 09**

<table>
<thead>
<tr>
<th>Tenant</th>
<th>Building</th>
<th>(Sq. Ft.)</th>
<th>Submarket</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wymore Transfer</td>
<td>Wilhelm Distribution Center</td>
<td>170,000</td>
<td>Central 205</td>
</tr>
<tr>
<td>OIA Global Logistics</td>
<td>Bybee Lake Logistics Center</td>
<td>60,102</td>
<td>North/Northeast</td>
</tr>
<tr>
<td>Apex</td>
<td>Tigard Central Industrial Park</td>
<td>40,000</td>
<td>Southwest I-5</td>
</tr>
<tr>
<td>Ernest Packaging Solutions</td>
<td>PDX Corp Center South</td>
<td>62,150</td>
<td>North/Northeast</td>
</tr>
<tr>
<td>O’Neill Transfer and Storage</td>
<td>2455 NW Nicolai</td>
<td>58,008</td>
<td>Northwest</td>
</tr>
<tr>
<td>Leif’s Auto Collision</td>
<td>Nelson Business Center</td>
<td>49,900</td>
<td>Tigard/Southwest</td>
</tr>
<tr>
<td>Mariner Productions</td>
<td>2811 NE Riverside Way</td>
<td>46,800</td>
<td>North/Northeast</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>486,960</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: NAI Norris Beggs & Simpson, CB Richard Ellis, and Cushman & Wakefield, Industrial Quarterly Reports*
Portland Multifamily Market

According to Norris, Beggs & Simpson’s First Quarter 2009 Multifamily Report, the overall multifamily vacancy rate has increased in the first quarter to 4.96% compared to 3.80% this time last year, which is still much lower than other markets. It reports a total overall average rent of all apartments in the Portland metro area, from studios to 3BR/2BA, both new and seasoned units, to be $773 per unit or $0.89 per square foot. Average 2BR/2BA new units rent for $1,179 per unit, an increase of $105 over last quarter. Seasoned 2BR/2BA units rent for an average $822 per unit, which is an increase of only $2 over last quarter.

**Metro-Wide Average Rents First Quarter 2009**

<table>
<thead>
<tr>
<th>Price per unit ($)</th>
<th>Studio</th>
<th>1BR/1BA</th>
<th>2BR/1BA</th>
<th>2BR/2BA</th>
<th>3BR/1BA</th>
<th>3BR/2BA</th>
<th>Overall Average</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$574</td>
<td>$677</td>
<td>$718</td>
<td>$870</td>
<td>$722</td>
<td>$970</td>
<td>$773</td>
</tr>
</tbody>
</table>

Average Portland Metro Rents

<table>
<thead>
<tr>
<th>Price per unit ($)</th>
<th>1998</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>1Q 09</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$726</td>
<td>$739</td>
<td>$747</td>
<td>$761</td>
<td>$774</td>
<td>$738</td>
<td>$740</td>
<td>$756</td>
<td>$783</td>
<td>$865</td>
<td>$820</td>
<td>$822</td>
</tr>
</tbody>
</table>

Source: Norris, Beggs & Simpson "Portland Area Multifamily Report First Quarter, 2009,
*Price per square foot shown in white

Source: Norris, Beggs & Simpson "Portland Area Multifamily Report First Quarter, 2009"
Average Historical Rents & Rent Growth

*Based on 1BR rate
**2009 estimated.
Source: Brokers, Gary Winkler, and Beth DuPont, Colliers multifamily investment team, "Portland Multifamily Private Capital News, Year End 2008"

The Clackamas/OR City/Milwaukie submarket shows the highest total vacancy rate at 6%, while SW Portland has the lowest submarket vacancy at 4.28%.
Most sources agree that the single-family market continues to affect the multi-family market, as the “shadow inventory”, or the amount of available single family rentals as well as the rental of unsold condominiums, increased due to problems in those markets. Mark Barry estimates a current 2.5 to 3.5 years of inventory in the condominium market. He expects to see between 2,500 and 3,500 new apartment units in 2009 as some investors take advantage of lower labor and material prices and less competition for high density sites from the condo and row house developers.

As in other markets, landlords are starting to make concessions to attract and keep renters. Brokers from the Colliers Portland office, released results from a recent survey of advertised rental units, noting that “landlords are offering aggressive incentives, including free rent, favorable lease terms, free parking, and lower monthly rental rates to fill vacancy”. The total discount of the net effective rent with parking and concessions in select buildings downtown range from 11% to 25%. Suburban/Outer Portland survey results show lower discounts, in the 4% to 12% range. As the chart below shows, rents have increased significantly since 2005 while vacancy decreased. Brokers at Colliers expect this trend to change in the coming year.

Most experts forecast an increase in cap rates, which will decrease the market value of apartment buildings, especially those that were recently purchased. Another challenge that investors face, as noted by Mark Barry, is an increase in utility costs of 11% for water and sewer, 14% for electric and natural gas, and 10% for garbage, which will increase operating costs.
The above graph based on the figures reported by Mark Barry, shows the inverse relationship between the median sales price and the cap rate of sales from 2002 to 2008, which illustrates how big the bubble has been. The following graph produced by Colliers gives an example of how a rising cap rate will affect property values, and gives an indication of the expected trend reversal, until we reach the historical average 7% to 9% cap rate. With lower property values as a result of increasing cap rates owners may be reluctant to sell and buyers may wait for further declines, which will reduce the number of transactions in the coming year. Norris, Beggs & Simpson note that “cap rates will be calculated more conservatively with much more scrutiny on underwriting, in-place income, historic performance, cost of capital and market stability.”

Source: Colliers, “Portland Multifamily Private Capital News, Year End 2008”
### MAJOR SALE TRANSACTIONS

<table>
<thead>
<tr>
<th>Buyer</th>
<th>Building</th>
<th>Price</th>
<th>Units</th>
<th>Submarket</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dan Piantanida</td>
<td>Las Brisas</td>
<td>$4,815,000</td>
<td>48</td>
<td>North/NE Portland</td>
</tr>
<tr>
<td>David Kornblum</td>
<td>The Village Apartments</td>
<td>$4,700,000</td>
<td>60</td>
<td>Gresham/Troutdale</td>
</tr>
<tr>
<td>Bristol Court Apt.</td>
<td>Bristol Court Apartments</td>
<td>$3,850,000</td>
<td>48</td>
<td>Clackamas/Milwaukie</td>
</tr>
<tr>
<td>RDC Acquisitions</td>
<td>Apartments</td>
<td>$2,600,000</td>
<td>39</td>
<td>North/NE Portland</td>
</tr>
<tr>
<td>Stewart Terrace</td>
<td>21754&amp;21766 SW Apartments</td>
<td>$2,050,000</td>
<td>29</td>
<td>Sherwood</td>
</tr>
<tr>
<td>Bannon Land 2</td>
<td>Midtown Apartments</td>
<td>$1,630,000</td>
<td>22</td>
<td>Downtown</td>
</tr>
<tr>
<td>Ivy Tree</td>
<td>Ivy Tree Apartments</td>
<td>$1,580,000</td>
<td>24</td>
<td>Southwest Portland</td>
</tr>
</tbody>
</table>

Source: Norris, Beggs & Simpson "Portland Area Multifamily Report First Quarter, 2009"