RETAIL MARKET ANALYSIS:

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Amid dire circumstances for the US consumer, retail real estate in the Portland metro is showing new and encouraging signs of life. Despite a number of clear challenges from the closing of regional Border's bookstores to continued high energy prices and unemployment, brokerages concur on an upswing in overall leasing activity, positive year-over-year same-store sales data for the back to school season, and stable or falling rates of vacancy. While progress and activity remain moderate by pre-recession standards, most analysts are predicting continued gains and stabilization through the coming year.

Any progress seen has taken place against a backdrop of conflicting economic news including positive moves in employment, high prices at the pump, continuous declines in housing prices, poor income performance, and sluggish but consistent growth in GDP. These factors have combined to slow progress in consumer confidence and retail sales, and have led many to worry about the imminence of a national double-dip recession. Locally, however, signs are more positive, with an unemployment rate dropping to a seasonally adjusted 9.1 percent in September, below or on par with national and state numbers. State projections have Portland's economy continuing to grow at above 2 percent for 2011 and 2012.

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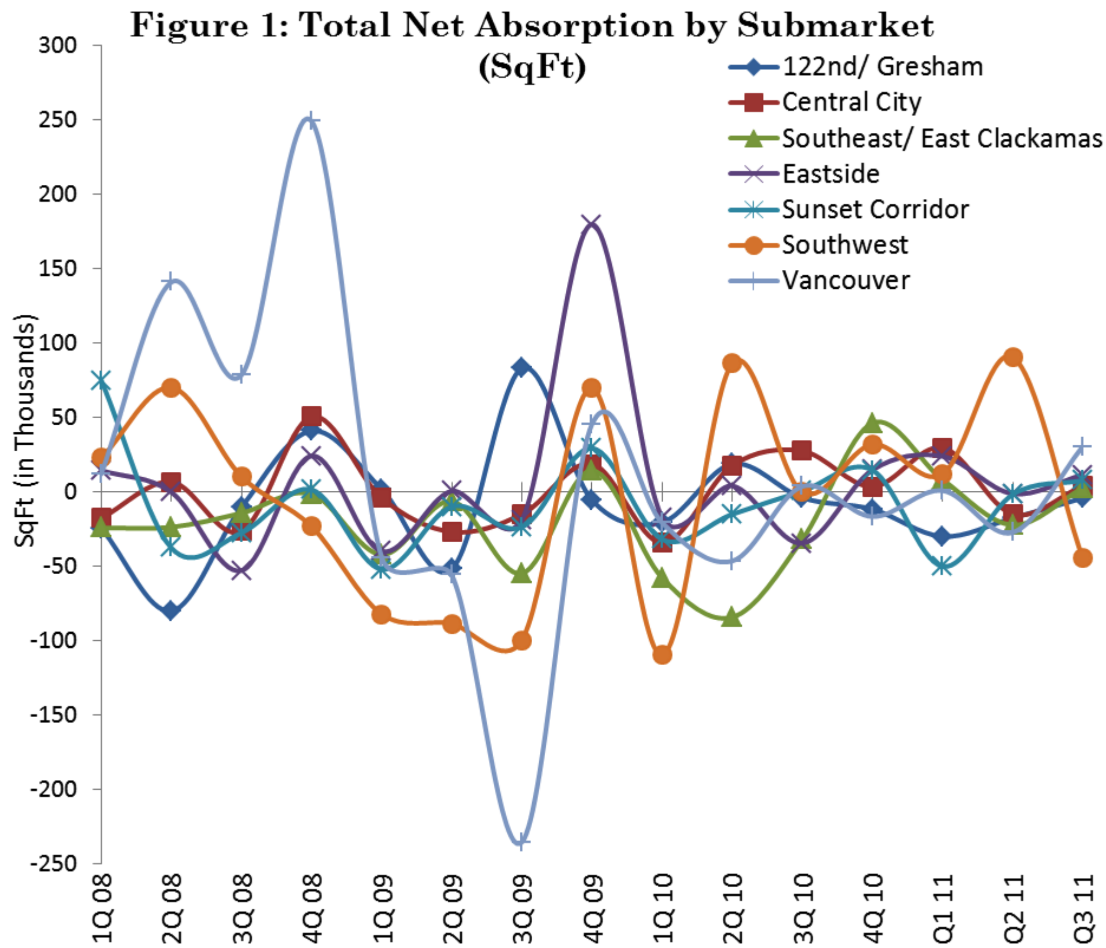
Table 1: Major Retail Lease Transactions, 3nd Quarter, 2011

Tenant	Property	SqFt	Submarket
New Seasons	2100 SE 164th	40,000	Vancouver
Walmart	Robinwood Shopping Center	40,000	Southeast
Salvation Army	San Rafael Shopping Center	23,695	Gresham
DSW	1981 NW 185th	20,000	Sunset Corridor
Concentra	2225 NW Town Center Drive	8,000	Sunset Corridor

*Source: Portland Business Journal, Norris, Beggs & Simpson, and Cushman Wakefield Q3 2011 Reports

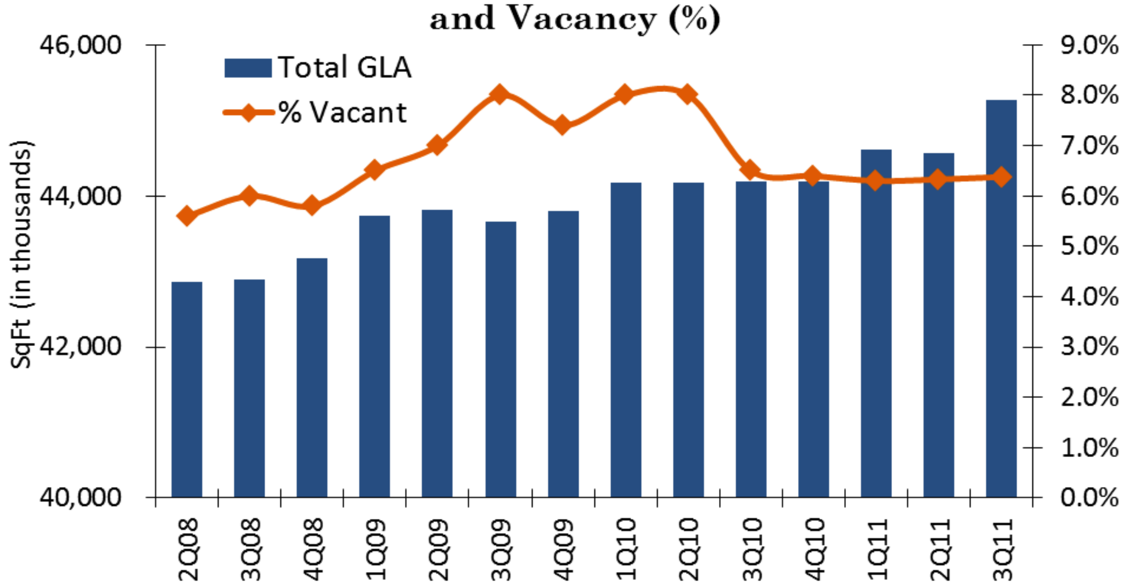


Source: Norris, Beggs, & Simpson Retail Reports

Norris, Beggs and Simpson reports that retail vacancy has remained stable since the first quarter at 6.4 percent, alongside a positive but negligible net absorption of 6,000 square feet. This coincides with Kidder Matthews reports of a 10 basis point drop to 5.9 percent vacancy in the metro area, though Kidder Matthews reports a more robust absorption of 436,000 square feet following a gain of 299,000 square feet in the second quarter and a net loss of 293,000 square feet in the first.

The Gresham submarket continues to carry the highest vacancy rate according to Norris, Beggs & Simpson, up 10 basis points to 9.0 percent in the third quarter. Central City carries the next highest vacancy rate at 8.4 percent, down 20 points from the second quarter. Eastside remains well below all other submarkets, dropping 20 basis points in the third quarter to a very strong 3.4 percent, according to Norris, Beggs & Simpson. Following a string of positive quarters, the Southwest submarket experienced a net loss of 45,000 square feet in the third quarter, driving the vacancy rate up 70 basis points to 5.0 percent. Store losses at Bridgeport Village reportedly account for a significant portion of Southwest's negative absorption and vacancy. This adjustment returns the Southwest submarket to a 5.0% vacancy, similar to its rate at the outset of 2011.

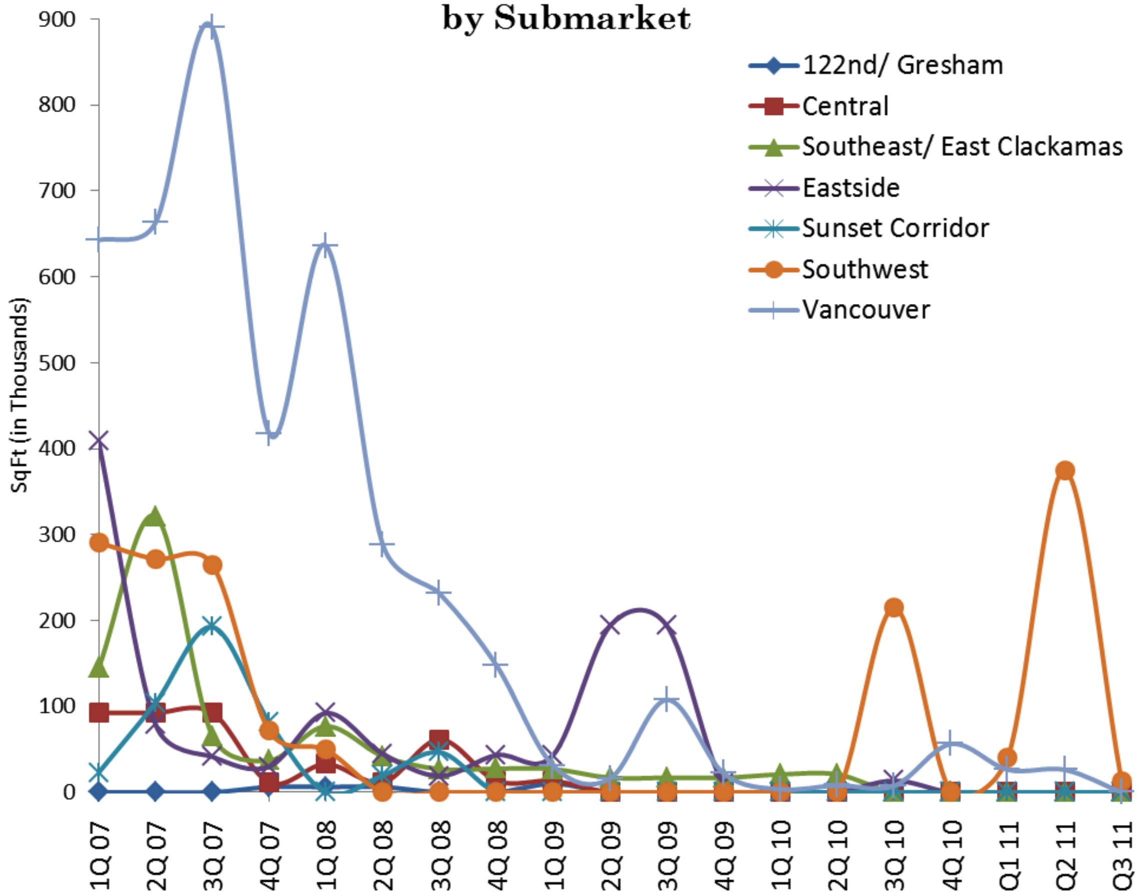
Figure 2: Total Gross Leasable Area (GLA) and Vacancy (%)



Source: Norris, Beggs, & Simpson Retail Reports

Kidder Matthews reports that average retail quoted rents for the Portland market currently sit at $16.14/square foot (triple net), a rate that has been steadily dropping since a peak of $18.14 in Q4 2008, and down nearly $0.80 from the first quarter. Kidder Matthews' forecasts continues to suggest that that this rate will stabilize through the coming year based on high rates of concession currently being offered by landlords. The report suggests that concessions will be a key indicator in future quarters, with a decrease in concessions signifying imminent rental rate increases. A rise in rates is not expected in the coming quarters, however. Brokerages are consistent in comments that most leasing activity is currently taking place in small spaces, with little activity among larger retailers. As the Kidder Matthews report discusses, "There are a lot of small deals getting done but it's pretty slow in the 4,000 to 15,000 s.f. range."

Figure 4: Total Retail SqFt Under Construction by Submarket



Source: Norris, Beggs, & Simpson Retail Reports

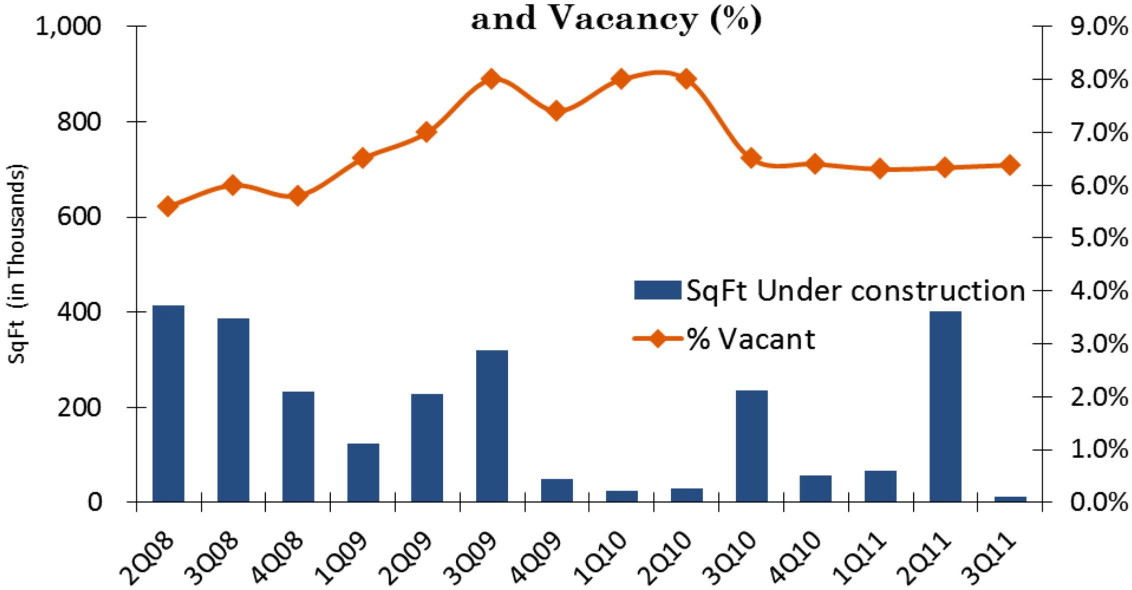
Norris, Beggs, & Simpson reports that much of the negative absorption in the third quarter is due to the bankruptcy filing and national closures of Borders Bookstores retail locations. According to a KGW report on the topic, Borders had 11 stores in Oregon and Southwest Washington prior to the closure.[1] With the average Borders store at 25,000 square feet, the closure of 11 stores has made a significant dent in overall retail absorption, and could be interpreted as good news that overall vacancy and absorption remain stable after the shock of the loss of a major chain. It is reported that Borders was slower to react to consumer trends in the book marketplace than rivals Barnes & Noble, most notably through the late adoption of electronic books.[2] Borders peaked in 2003 with 1,249 stores nationwide, but had dropped to 642 stores and 19,500 employees by the second quarter of 2010. The

[1] D'Innocenzio, Anne. "Borders Closing 11 Stores in OR & SW WA", *KGW.com News*, July 19, 2011. Accessed November 2, 2011. http://www.kgw.com/news/local/Borders-seeks-to-close-nationwide-including-11-SW-Wash-Ore-stores--125810843.html

[2] Sewell, Dan. "Last Borders shoppers wistful, looking for deals", *Wall Street Journal*, September 18, 2011.

closing of the remaining stores opens up significant inventory in retail markets nationwide.

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



Source: Norris, Beggs, & Simpson Retail Reports

Nike's recent opening of its 26,000 square foot flagship store in downtown Portland was hailed by Elliot Hill, a Nike vice president and general manager for North America as "a catalyst for the overall marketplace and the sports retail industry". [3] The new location at SW 5th & Morrison was designed with a focus on sustainable practices, and the developers are seeking a platinum LEED (Leadership in Energy and Environmental Design) rating from the US Green Building Council. The new store is planned to be one of seven of Nike stores with a LEED rating, and the company credits initiatives like recycling of 93 percent of renovation waste and local sourcing for 30 percent of construction materials along with on-time, under-budget development with setting an example for the industry. Built as a "brand experience store", the new location includes large touch-screen displays with information on the history of the company and an open footprint with elements resembling both a museum and retail store.[4]

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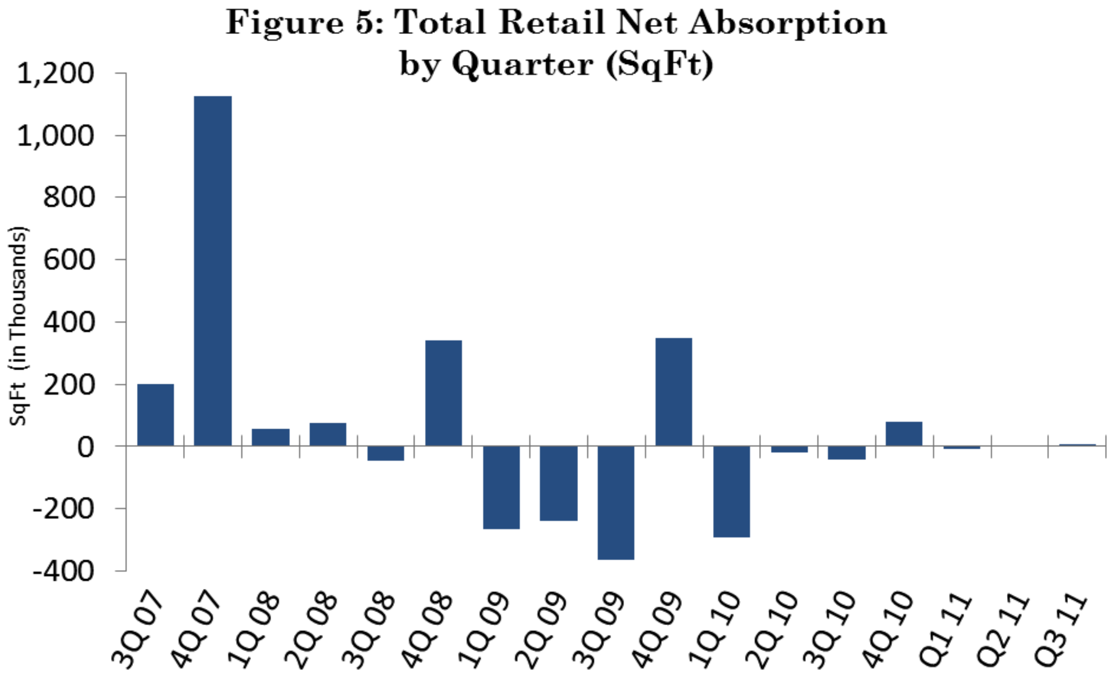
[3] Siemers, Erik. "Nike Portland store enters 'new evolution of retail'", *Portland Business Journal,* November 4, 2011.

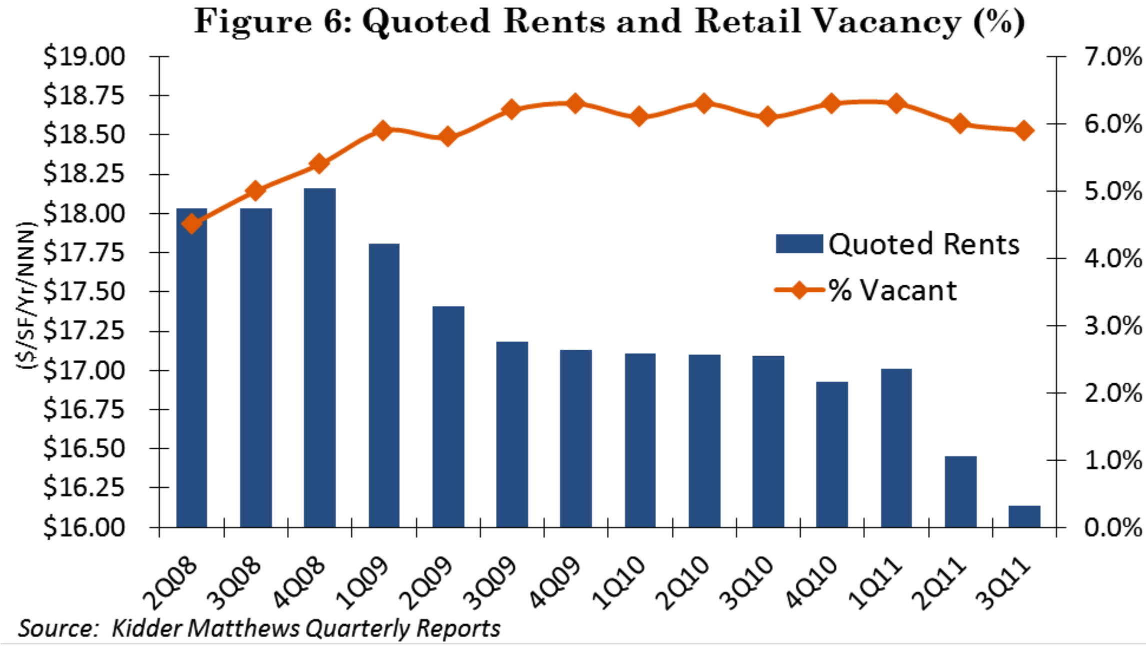
[4] Brettman, Allan. "Nike Portland opens downtown store that's half museum, half marketing", *The Oregonian*, November 3, 2011.



Source: Norris, Beggs, & Simpson Retail Reports

Two major grocery store-anchored strip malls have opened in the Portland metro region this year. First, Wilsonville Old Town Square, opened in July, surrounds a new Fred Meyer store and includes a McMenamin's restaurant and a range of other eateries and attractions. Also, Progress Ridge in Beaverton opened in September, anchored by New Seasons and is set to include a luxury theater (Cinetopia), high end bowling alley (Big Al's) and a set of bars, restaurants and service businesses. These ambitious projects, both developed by Tualatin's Gramor Development are in striking contrast to national retail building trends. Taken together, the two Portland strip mall developments constitute 460,000 square feet of new retail. According to numbers compiled by Reis and reported by the Oregonian, only 721,000 square feet of "new community shopping centers and strip malls" were developed in the first half of 2011 in the US as a whole.[5]

[5] Gunderson, Laura. "Two new Portland area shopping centers may provide glimpse into the future", *The Oregonian*, July 23, 2011.



A string of box store development sites are also moving forward locally, as WalMart continues with its planning for new store locations and Target is said to be eyeing space at both Jantzen Beach and the downtown Galleria. In October, PDC voted unanimously to drop its plans for a parking garage at SW 10th and Yamhill in support of the Galleria ownership's bid to attract a large-format retailer, rumored to be Target.[6] The Daily Journal of Commerce reports that the Galleria location for Target is expected to use approximately 60,000 square feet, as compared with Target's more typical 125,000 square foot footprint.[7] The WalMart stores reportedly being considered are also significantly smaller than their traditional format, as they adopt an "urban approach" to retailing. WalMart has quietly pushed forward with expansion plans in the Portland metropolitan area, having progressed in the design and permitting process in the past year for 17 of their 40,000 square foot "neighborhood market" stores.[8]

[6] Giegerich, Andy. "PDC gives go ahead to Galleria deal", *The Portland Business Journal*, October 26, 2011.

[7] Bjork, Nick. "Target gets serious about downtown Galleria space", *Oregon Daily Journal of Commerce*, April 27, 2011.

[8] Swart, Cornelius. "Walmart's North Portland plans draw little opposition, unlike in 2006", *The Oregonian*, September 22, 2011.