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Gerard C.S. Mildner, Director, PSU Center for Real Estate

Welcome to the July 2007 edition of the PSU Center for Real Estate's Quarterly Real Estate Report.

This issue of the Quarterly Report has been developed with the assistance of several supporters of the Center for Real Estate, including the Oregon Association of Realtors, the Regional Multiple Listing Service, PGP Valuation and PSU's Institute of Portland Metropolitan Studies.

We see the role of the Quarterly Report as a place to publish unbiased analyses of local and national real estate trends and policy issues. As a quarterly publication, we take a longer view, rather than repeating the function of a daily newspaper or a weekly magazine. While the publication is timed so that we can report quarterly economic data (such as the National Economy Report), we try to consider longer term issues.

Among local topics, the most pressing real estate issue is the debate surrounding growth management, Measure 37, and the proposed reform of Measure 37, known either as House Bill 3540 or Measure 49. As most of you know, Measure 37 extended rights to long-time property owners to challenge land use planning regulations, or to seek compensation from local or state government. We felt it was important to get some information about the impacts of the two referenda before members of the real estate community. And we decided to present that in this issue, rather than the October issue, so that people can more fully debate the implications.

In our feature article, Dr. Sheila Martin of PSU's Institute of Portland Metropolitan Studies presents her analysis of the claims made under Measure 37 and how the legislation is being implemented. The staff at Dr. Martin's Institute has studiously collected data on each claim, including acreage, zoning, dollar amount and other variables. The Institute's research is widely used by advocates on both sides of the debate, and I think you will find the results most interesting.

In a follow-up article, I present a longer term view of Measure 37 and House Bill 3540 and how they fit into the debate regarding Oregon's land use planning system. I confess to not being much of a fan of legislating by referendum, but if we must have such a system, voters need good information to make rational choices. Decisions should not be made based upon anecdotes or extreme cases. And unfortunately much of the previous debate has focused exclusively on issues of fairness and rights. In my article, I try to offer some perspective on the question of efficiency and the impact on real estate markets.

Among national topics, nothing seems more important than the rapid appreciation of housing prices in the last seven years, what some call the housing bubble. The more recent decline in housing prices has seriously implications for our financial system and the health of our economy.

In the previous issue, we discussed some of the factors that lead to housing price appreciation. In this issue, we decided to treat the increase in housing prices as a potential risk for future real estate investors and examine the longer term in housing prices by regional submarket. As you will see, we find that the trend for inner city living is alive and well in the Portland market, particularly in North Portland, which has been the fastest appreciating market in the last five years. And we find that prices in Northeast Portland, traditionally one of the lowest cost submarkets in the region, have equaled or exceeded prices in some of Portland's suburban markets, something unimaginable five or ten years ago.

And in our final feature column, Grant Norling, Managing Director with PGP Valuation, reviews the retail market in the Portland Metropolitan area. Norling also finds evidence of a retail revival in Portland's east side, and presents evidence that Portland's retail market is one of the strongest among metropolitan areas in the United States.

We hope that you find these feature articles as well as our regular columns in this edition of the Quarterly Real Estate Report both interesting and useful. We continue to welcome your feedback on our articles, as well as on our mission to provide unbiased and longer term perspectives on the real estate industry. ■

The US Economy and Housing Market

Gerard C.S. Mildner, Director, PSU Center for Real Estate

The first half of 2007 saw continued economic growth in the US economy, although the rate of expansion is some of the slowest that we've seen for the past few years and the slowest among the major industrialized countries. In the 12 months ending with the first quarter, the Gross Domestic Product (GDP) rose by 1.9%, a rate that's below Japan (2.6%), Great Britain (3.0%), Germany (3.6%), or the entire Euro-area (3.0%). For 2007, the US economy is expected to grow at a 2.0% rate, considerably slower than the 3.3% rate for 2006.[1]

In some respects, the relative growth of the US versus other countries shouldn't really matter, except that a strong world economy can keep a slowing economy from outright recession. The strong economic performance of China (+11.0%) and India (+9.1%) mean that the global economy has multiple sources of growth.

The vigorous global expansion, combined with the decline in the dollar over the last three years, explains why this has been a good time for exporting firms like Boeing and Weyerhaeuser. US exports have grown by 8% per year for the past three years and are a major source of GDP growth, despite the weaknesses in personal consumption and housing investment.

Looking forward, most economists expect the US economy to rebound, rather than continue downward. A panel of economists for *The Economist* magazine projects growth for 2007 at 2.1% and for 2008 at 2.7%, while the economies in Japan and Europe are expected to cool.

In terms of inflation, the latest survey released in May indicated 2.7% inflation in the US economy, which is one of the highest rates in the industrialized world. That has prevented the Federal Reserve from easing on the money supply. The Fed has kept the short-term fed funds rate at 5.25% for the past year. Perhaps more importantly, long term interest rates have risen sharply in the past two months. The average rate on 30-year mortgages has risen by more than 50 basis points to 6.7% in the latest survey by Freddie Mac.[2]

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[1] Much of the data for this section comes from *The Economist*, www.economist.com.
[2] Freddie Mac (2007)

Some of the increase in interest rates results from investor wariness about the mortgage markets and the extent of subprime lending. As I discussed in the previous Quarterly Real Estate Report, banks expanded their lending in recent years to borrowers with weak credit histories and employment patterns, driven in part by their Federal Community Reinvestment Act responsibilities. In the drive to bring more households to homeownership, banks pioneered the development of low-documentation or so-called "NINJA loans" (no income, no jobs, or assets required).

These high risk, high return mortgages were bundled and sold to investors as mortgage-backed securities (MBS) and collateralized debt obligations. As rates have risen and more of these borrowers have become delinquent on their mortgages, many of these securities have declined in price. As a result of the greater perceived risk, investors insisted upon higher returns.

Given this rise in rates, many holders of hybrid and adjustable mortgages will see their rates adjusted upwards. Combined with the delinquency problem in the subprime lending market, these rate increases put a serious damper on housing demand. Nationwide, the sales of existing homes are estimated to have fallen by 10%, and sales of new homes have declined by 16% over the last year.[1]

The decline in demand has led to declines in prices. The National Association of Realtors (NAR) expects existing home prices to decline by 1.4% and new home prices to decline by 2.6% for 2007. The amount of new housing for sale remains relatively high at seven months of inventory. Homebuilders reduced the number of housing starts by 22% in the last year, but many housing units remained in the development pipeline.[2]

Given the slowdown in US economic growth and the national decline in US housing prices, why hasn't the same decline shown in the Portland region? The first reason is that Oregon is a state whose economy is highly driven by exports, whether in agriculture, high tech, or aircraft manufacturing. As a result, Portland's regional job growth has outstripped the national economy in each of the last three years.

Second, growth constraints in the Oregon land use planning system have prevented the over-building experienced in many of the other US metropolitan housing markets. Instead, housing demand led to

[1] National Association of Realtors® (July 2007)
[2] National Association of Realtors® (July 2007)

increases in housing prices and land costs, as builders bid up the price of scarce developable land. While inventory and the average days-on-market have risen, there hasn't been a huge overhang of housing on the market.

Finally, Portland was less susceptible to the problems in the mortgage market than other regions in the United States. In a report released last year, the NAR found that Portland area buyers had nearly half the national rate of subprime mortgages issued and over half the national rate of loans issued with more than 90% of loan to value. Those conservative lending conditions led Oregon to have only half of the national loan delinquency rate. Portland area homebuyers did have a higher adoption of adjustable mortgages than the nation as a whole (38% vs. 28%), but given low loan-to-value ratios, these loans create more risk of a housing payment burden than delinquencies.[1]

In conclusion, the US economy is growing at a slow rate for 2007 but is expected to rebound in 2008. The housing economy remains a drag on the overall economy in terms of construction employment and consumer confidence. However, whether due to conservative borrower and lender behavior or the state's "conservative" planning system, the Oregon economy seems insulated for the moment from those national trends ■

[1] National Association of Realtors® (July 2006)

How Will Measure 37 Affect Real Estate Markets in Oregon?

Sheila Martin, PSU Institute of Portland Metropolitan Studies

On November 2, 2004, Oregon voters passed Measure 37 by a margin of 61 to 39 percent. Of Oregon's 36 counties, only one—Benton County, home of Corvallis and Oregon State University—failed to pass the measure. Even in the Portland metropolitan region, the measure passed in all but the districts closest to the central city. In October of 2005, a Marion County trial court judge struck down the measure, but it was reinstated by the Oregon Supreme Court on February 21, 2006. Thus, the measure once again was effective on March 31, 2006.

Since the reinstatement, claims have come pouring in to county, city, and state planning offices. As of December 4, 2006 (the last day on which to file a claim on a past land use action) cities, counties, and the State have received claims for over 7,500 properties covering over 750,000 acres. The overwhelming majority of the land subject to claim is resource land, and most claimants seek residential development. This article provides a brief discussion of the extent and type of potential claims under measure 37 and the potential impact on the real estate market.

Measure 37 Basics

Simply put, the Measure states that if a land use regulation restricts the use of private property and thereby reduces the value of property, the property owner is entitled to compensation from the government that enacts or enforces the regulation.[1] If the government continues to apply the subject regulation 180 days from the date of written demand for compensation, the landowner has a right to sue for compensation in circuit court, and is entitled to attorney fees on top of the compensation awarded. Facing the threat of significant liability for legal fees, and with neither a fund available for compensation, nor a clear procedure for determining the value of the loss, most local governments have proceeded to waive regulations. In fact, of the over 7,500 claims that have been filed, we know of only one claim that has been awarded compensation; because they were unhappy with the award, the claimants have withdrawn the original claim and filed a new claim for additional development and greater compensation.[2]

[1] State of Oregon (2003)
[2] Central Oregonian (December, 2006)

Oregon’s Measure 37 was not the first attempt to reduce the authority of Oregon’s land use regulation. Since the State’s first attempts at statewide planning in 1969, Oregonians have defeated ballot measures to eliminate statewide planning on four occasions—each by a fairly comfortable margin. However, the notion of compensation for lost value appealed to voters, and in 2000, they passed Measure 7, which was similar to Measure 37, by a 53 to 47 margin. Although Measure 7 was declared unconstitutional, its proponents revived the concept using a slightly different legal strategy: a statutory measure rather than a Constitutional amendment. The revised approach was successful, and Measure 37 passed with 61% of the statewide vote. With the passage of Measure 37, Oregon’s planners and realtors now face a regulatory environment in which any new land use regulation, as well as the enforcement of existing land use regulations, will force a decision about whether to pay the claimant for lost value, or allow the landowner to develop the land as he or she could when the land was acquired.[1]

Statewide Distribution of Claims

The claim information presented in this article was gathered by the Institute of Portland Metropolitan Studies from publicly available documents, including claim forms filed with the counties; state and county claim web sites; and staff reports filed by state and county planning staff.[2] The Measure itself included little clear direction about claim form and procedures; in the absence of any clear direction from the State, forms and procedures of local governments varied widely. This has led to a number of difficulties regarding the collection, analysis, and mapping of Measure 37 data. The most important of these is inconsistency in the availability of some of the key variables needed for analysis. We overcame some of these problems by pursuing data from multiple data sources. Nevertheless, the data are incomplete for some variables, as indicated in the discussion below.

Figure 1 (see accompanying map) shows the density of Measure 37 claim acreage throughout the state of Oregon. Table 1 shows the number of claims and acreage by county. Almost 65% of the claims and 40% of the claim acreage is located in the 11 counties of the Northwest and Willamette Valley, including Hood River County.

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[1] There is much debate over whether waivers must allow a landowner to develop as he could when he first acquired his property, or whether the waiver must only allow the landowner sufficient development to compensate for the documented value of the loss. A recent set of recommendations to the legislature from former Governors Atiyeh and Roberts and John Gray to the legislature (Atiyeh, et al, 2007) summarizes these issues. A recent paper by Bill Jaeger offers a general discussion of compensation valuation (Jaeger, 2006)

[2] Additional details about the Measure 37 database can be found on the IMS website: http://www.pdx.edu/ims/m37database.html

Even at Figure 1's course level of spatial resolution (percent of claim acres per township), we can see that Measure 37 claims are clustered proximate to the urban growth boundaries that surround every municipality in Oregon; they are also bounded by the presence of public land (federal, state, and county). Claims are, not surprisingly, especially concentrated in the Portland tri-county area. Elsewhere in the state, a relatively large number of claims are found in the Grants Pass and Medford-Ashland urbanized areas. The map also reveals significant claim acreages in relatively remote areas east of Depoe Bay at the coast, southwest of Prineville in central Oregon, northwest of La Grande, and just north of Halfway at the eastern edge of the state. The distribution of claims by size is shown in Figure 2. While just over 1% of the claims are for tracts of land larger than 1,000 acres, these very large claims comprise one-third of the total claim acreage.

The Oregon land use system was designed to limit urbanization on resource lands. Not surprisingly, the majority of the claim acreage is on land that is currently zoned for either farm or forest land. Table 2 shows the distribution of claims and claim acreage by current zoning. We know current zoning for about 72% of the claims. Only 11% of the claims and 1% of the claim acreage is for land that is not currently in resource use. The claims are overwhelmingly requesting residential development; of the 52% of claims for which we have data on the proposed development, 92% of the claims and 86% of the acres are for residential development. The next largest category of proposed development is for mixed-use development. Figure 3 shows how the residential development proposals break down in terms of the number of residential lots requested. We have data on this variable for 42% of the claims, comprising 58,745 lots. Of the claims for which we have data, 1,288 claims, or 40%, are requesting one to three lots. Another 30% are requesting four to nine lots. About 20% of the total number of lots requested is from claimants that are developing very large residential developments of over 500 lots. The land division requested by claimants may become a key factor in claim viability if HB 3540 (which was referred to voters by the 2007 Oregon Legislature) passes in November.

Willamette Valley Claims

Figure 4 (see accompanying map) shows the distribution of claims in most of the Willamette Valley, and also indicates land division requested. Within these nine counties, there are 4,168 claims comprising just over 243,000 acres. We have information on the type of development requested for 60% of those claims. Of those, the overwhelming majority (96%) are for residential development. Similarly, we know the proposed land division for about 67% of the claims. Of these, about 57% of the claims are requesting subdivision (four or more lots), and about 28% are requesting partitions (one to three lots).

Potential Impact on Oregon's Real Estate Market

While the total acreage of Measure 37 claims is small compared to the total land area of the state, in some counties, claim acreage comprises a significant share of the total private land area. As shown in Table 1, the most significant of these is in Washington County, where claim acreage comprises over 16% of the private land in the area. The potential conversion of hundreds of thousands of acres of resource land to developable land area could have a significant impact on the residential real estate market in Washington County and in other counties such as Hood River County, where development is constrained by a significant amount of public land and private land currently zoned for resource use.

Uncertainties and Constraints on Measure 37 Development

But will these claims ever lead to development? Not necessarily. There are a number of uncertainties facing landowners who have filed or plan to file Measure 37 claims. These sources of uncertainty include:

1. Unresolved legal issues;
2. Barriers to development even after regulations are waived;
3. A pending revision of Measure 37 that will be on the ballot in November.

Legal issues

The Department of Land Conservation and Development is involved in over 250 lawsuits involving Measure 37.[1] The issues discussed in these lawsuits include subjects as diverse as the federal requirements exception, the transferability of waivers, the evidence required to demonstrate loss, the definition of an "owner," and the necessity of a state waiver. Many of these cases and the legal issues they represent are still unresolved. Of particular interest is the transferability issue. The Office of the Oregon Attorney General has taken the official position that waivers granted by state and local governments under Measure 37 apply to the owner only, and cannot be transferred to a new owner unless the new use is established by the owner to which the waiver is awarded.[2] This interpretation, as well as other legal uncertainties, may limit development of Measure 37 properties because it will not allow the claimants to simply sell the property to another for the purpose of development.

[1] For a list of pending Measure 37 Litigation, including the state's briefings and any court decisions, see www.doj.state.or.us/hot_topics/measure37litigation.shtml.
[2]See http://www.oregon.gov/LCD/docs/measure37/m37dojadvice.pdf

Other Barriers

Even after obtaining a waiver, Measure 37 claimants must still follow the normal procedures required to develop their property. Thus, claimants may be subject to typical procedures and approvals regarding subdivisions.

Furthermore, we might question how quickly Oregon's land market would be able to absorb hundreds of thousands of acres of new developable land. While much of this land is near metropolitan areas with unmet demand for large developable lots, other claims are in relatively remote areas that may harbor a limited market for development. Thus, one barrier to the outright development of Measure 37 claims may be simply the limits to the market's appetite for rural development.

Pending Revision of Measure 37

Finally, the 2007 Oregon Legislature passed House Bill 3540, which refers to the voters a revision of Measure 37.[1] If passed, this Measure would ease the approval process for claimants wanting to develop up to three home sites, and would make the waivers secured through this process transferable to new owners. For claimants pursuing developments of four to ten home sites, a more rigorous process of demonstrating loss would be require and locations would be restricted. However, once secured, these waivers would also be transferable to new owners. Development of greater than ten home sites would not be allowed under the new provisions.

Summary

Measure 37 has the potential to affect the state's real estate market by adding thousands of acres to the supply of developable land, much of it on land that is currently zoned for resource use near existing urban growth boundaries. However, the continuing uncertainty surrounding the implementation of the measure has, up to now, limited its impact. That uncertainty will continue, at least until voters act on Measure 49.

[1] A governor's office summary of HB 3540 is available at http://www.friends.org/issues/M37/documents/hb3540C_summary_6-4-07.pdf

Table 1. Claims, Acreage, and Claim Density by County

County	Claims	Claim Acres	Claim area, % private land area	County	Claims	Claim Acres	Claim area, % private land area
Baker	139	56,945	4.42	Lane	412	34,857	2.89
Benton	140	11,765	3.57	Lincoln	198	43,314	10.44
Clackamas	1049	33,121	5.84	Linn	494	39,927	4.45
Clatsop	109	5,180	1.43	Malheur	13	976	0.07
Columbia	182	10,673	2.71	Marion	489	24,836	4.98
Coos	230	38,185	5.54	Morrow	0	0	0.00
Crook	66	41,349	4.29	Multnomah	187	4,024	2.09
Curry	117	22,873	6.61	Polk	270	18,803	4.45
Deschutes	185	15,248	3.25	Sherman	0	0	0.00
Douglas	258	17,479	1.16	Tillamook	88	12,710	5.28
Gilliam	1	7	0.00	Umatilla	47	29,302	1.87
Grant	16	6,725	0.55	Union	62	20,054	2.03
Harney	1	40	0.00	Wallowa	31	4,748	0.55
Hood River	233	13,786	11.34	Wasco	49	15,608	1.71
Jackson	574	59,406	6.85	Washington	902	64,246	16.11
Jefferson	138	26,427	4.69	Wheeler	2	1,608	0.21
Josephine	319	17,396	5.80	Yamhill	454	36,447	9.50
Klamath	103	21,248	1.27	**Total**	**7563**	**750,530**	**2.69**
Lake	5	1,217	0.09				

Although the total claim density is low overall, in some counties such as Hood River and Washington, claim density is very high.

Table 2. Claims and Acreage by Current Zoning

The majority of claim acreage is on land currently zoned for farm or forest use.

Current Zoning	Claims	Acres	Percent Claims	Percent Acres
Unknown	2,147	250,650	28.4%	33.4%
Exclusive Farm Use**	2,771	305,986	36.6%	40.8%
Farm/Forest Use	805	36,563	10.6%	4.9%
Forest Use	1,004	145,399	13.3%	19.4%
Residential	687	8,329	9.1%	1.1%
Industrial	28	256	0.4%	0.0%
Mixed Use	9	80	0.1%	0.0%
Open Space	21	770	0.3%	0.1%
Commercial	41	184	0.5%	0.0%
All other	50	2,313	0.7%	0.3%
All Claims	7,563	750,529	100.0%	100%

***Includes claims that have multiple zonings including EFU.*

Figure 1. Statewide measure 37 Claims: Percent of Acreage of Township

(See attached map)

Figure 2. Number of Claims and Percent Acres by Claim Size

While a very small share of the claims are for tracts of land of larger than 1000 acres, these very large claims comprise one-third of the total claim acreage.

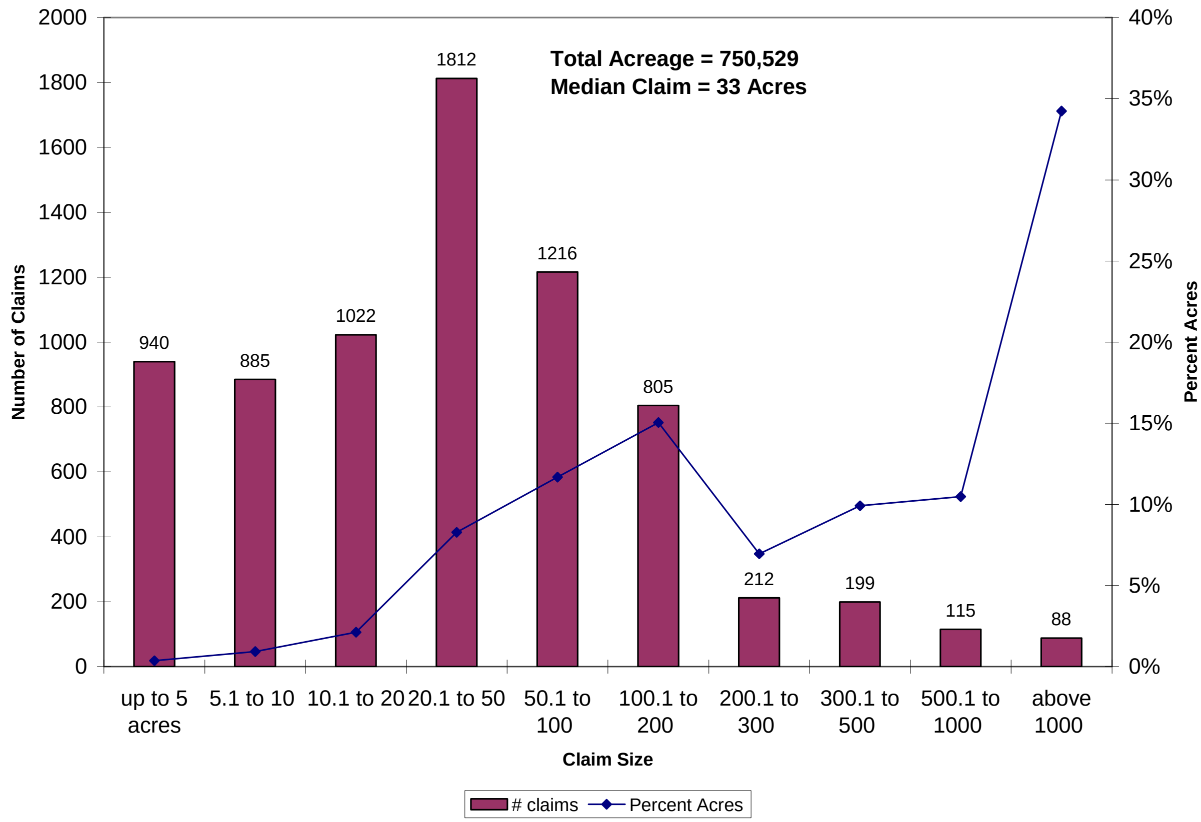


Figure 3. Total lots requested and Percent Lots by Size

About 20% of the total number of lots requested for very large residential developments of over 500 lots.

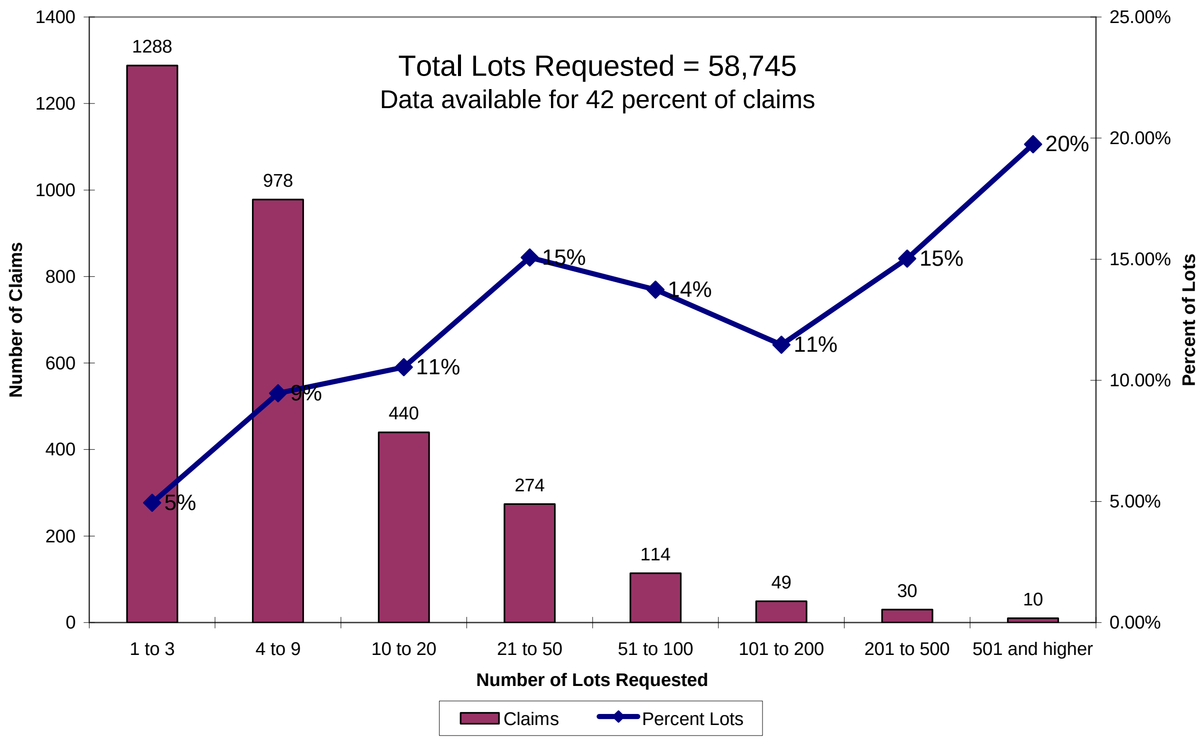


Figure 4. Willamette Valley Measure 37 Claims: Desired Action

(*See attached map*) ■

Economic Analysis of Oregon's Measure 37 and its Reform

Gerard C.S. Mildner, Director, PSU Center for Real Estate

The accompanying article by Dr. Sheila Martin describes the history of Measure 37 and the status of the claims by property owners. In this article, I present some background to the Measure 37 discussion and consider the economic impacts of the two pieces of legislation.

That background begins with Oregon's 30-year history with statewide land use planning. Developed in a period of high economic growth for the state, the land use planning system was implemented to protect rural areas from urbanization and had the effect of reducing the number of building permits on agricultural land. All urban areas of the state were required to establish urban growth boundaries, within which higher density development was encouraged.

While the full effects of this system were not immediately apparent, the last 15 years of vigorous economic growth have led to substantial differentials in land prices inside and outside the urban growth boundaries, both in the Portland area and elsewhere in the state, with a more than 10:1 ratio of land prices on either side of the growth boundary in the Portland area. Inside the growth boundary, land prices have risen 500% in the last 15 years.[1] Outside the growth boundary, residential settlement has been restricted and many rural towns near metropolitan areas have seen vigorous growth as commuting households have bid up the price of rural homes close to the price of homes in urban areas.

That incentive to convert to urban use is tempered by rural property owners who want to remain in the farming business or have significant farming investments that would be at risk should they be surrounded by a cluster of residential settlements. New suburban residents might object to farming practices like manure laying or pesticide spraying and limit farm operations.

However, unlike the land use planning system in Great Britain, which is probably the closest to the Oregon system, the state did not buy the development rights from rural landowners to create a greenbelt. Instead, the state restricted property owners' development rights through the Constitution's police power. The use of the police power, rather than compensation, means that rural

[1] Hall and Mildner (2006).

property owners have a tremendous economic incentive to overturn these rules, whether through the legislature, the initiative system, or the urban growth boundary expansion process.

Moreover, unlike Great Britain, which actively promoted “new town” development for commuters to live beyond or within the greenbelt surrounding London, the Oregon system encourages small rural towns to remain small. Towns are required to estimate a 20-year land supply for future housing development, which often fails to account for the increasing housing demand of commuters to Portland, Hillsboro, Salem, and other urban communities, further exacerbating the housing shortage throughout the state.

Seen from this perspective, Measure 37 reflects an opportunity for rural landowners to capture the price differential between land zones exclusively for agricultural purposes and land developable for residential settlement. However, that is only half the story.

While the direct benefits of Measure 37 will accrue to the property owners, implementation of the Measure will allow land to be allocated to higher valued use, increase the housing supply in the state, and moderate the high cost of housing. In economic terms, new housing supply enhances both producer and consumer welfare. However these potential benefits to homeowners and renters and the improvements in economic efficiency from Measure 37 have largely been ignored by the public debate.

A significant barrier to the efficiency benefits described above has been how development rights enhanced by Measure 37 have been allocated, both by the supporters and opponents of the Measure.

Recognizing the political appeal of older residents and widows (and the lack of sympathy for buyers who purchased property at depressed prices after regulations had been imposed), the backers of Measure 37 required that property owners demonstrate continuous ownership of the property prior to the imposition of the regulation being challenged. As a result, two adjacent parcels may have completely different Measure 37 rights, depending upon the transaction history or longevity of the owner, as opposed to principles regarding land conservation, the efficiency of zoning, the need for housing, or the availability of infrastructure. Rather than promoting the development of rural new towns or the expansion of urban development at the fringe (which is closest to employment sites and creates the most value), Measure 37 would likely create large numbers of dispersed, semi-rural settlements.

However, as noted by Dr. Martin in the previous article, many of the Measure 37 claims are located in Washington County, the fastest developing country in the Portland metropolitan area. Within Washington County, 16% of the private land area in this county is subject to Measure 37 claims.[1] Despite the high demand for housing in Washington County, Metro has avoided urban growth boundary expansions in favor of expansions in Clackamas County, where housing demand has been weaker. As a result, claims next to the western edge of Portland's urban growth boundary would very likely lead to development. And even for sites distant to the UGB, as long as commuting times were tolerable, development would likely occur.

A major problem with the administration of Measure 37 have been rulings by agencies and the court system that development rights permitted under Measure 37 can only be exercised by the historic property owner and cannot be transferred to professional developers who have the necessary resources and expertise. The failure to make property rights transferable creates risk as well as raises the cost of development, thereby reducing the potential benefits of the Measure.

Finally, the level of compensation required under Measure 37 is very difficult to determine and poses significant methodological problems. As researchers Bill Jaeger and Andrew Plantinga at Oregon State University have demonstrated, there's an important difference between changing the zoning of a single property and changing the zoning for an entire area.[2] Restricting development in an entire area creates a scarcity value for the development right being restricted. If a single landowner is relieved of that restriction, they hold a monopoly position, which has great value. The appraisal profession is professionally equipped to estimate that value. However, if a large group of claims are made, the monopoly value of the each claim is reduced. In many of the areas with a large number of claims, the traditional appraisal estimate will be an overestimate. These methodological issues have not yet been litigated, and currently, only one government agency has offered to pay a claim.

[1] Martin (2007)
[2] Jaeger and Plantinga (2007)

In the same article, Jaeger and Plantinga argue less convincingly that the land use planning system has raised rural land values throughout the state. While growth restrictions may enhance some property values, that argument is less plausible given the order of magnitude differentials in land prices inside and outside the urban growth boundaries. Moreover, their study relies entirely upon tax assessor measures of market land prices, which are notoriously inaccurate, particularly after the Measure 5 property tax limitation.

Measure by Measure

Given this analysis, what will be the impact of House Bill 3540, which Oregon voters will determine in a referendum in November?

The main features of this bill are (1) to prevent commercial or industrial development under Measure 37, (2) to create “express lane” approval by Measure 37 claimants for up three housing units, (3) to restrict development on any single parcel to no more than ten housing units, (4) to limit the total development by any single property owner to 20 units, (5) to require the hiring of an appraiser for estimating potential compensation, (6) to limit potential compensation of damages to those suffered in the immediate year before and after the regulation was imposed (plus interest), (7) to limit potential compensation by the value of past special property assessments, (8) to allow transferability of development rights for up to ten years, and (9) to create additional protections (i.e., barriers to development) on high valued farm and forest land.

The “express lane” approval and transferability of development rights is clearly an important benefit to seeing additional development and housing built. Presumably, much of the debate this summer and fall will concern the details of each of the provisions.

However, the features of the legislation to prevent a single property owner from developing more than 20 housing units and the restrictions on “high valued” farm and forest land are significant barriers to additional housing production. Since 98% of the claims occur on land zoned exclusively for farm and forest use, these additional restrictions are important and should be studied carefully.[1] And while the requirement that real estate appraisers be hired to estimate loss of value and potential compensation appears to offer better information, since few compensation claims are likely to paid,

[1] Martin, Sheila (2007)

this appears to be a financial barrier to property owners pursuing a claim, thereby reducing the development impact.

New Housing Production

It is beyond the scope of this paper to assess how many housing units will be created under Measure 37 versus House Bill 3540, even though that is probably the most critical figure to obtain from the point of view of housing market benefits and economic efficiency. Sightline Institute, an environmental organization, estimates that Measure 37 might result in 14,500 additional housing units in Washington, Multnomah, Clackamas, Yamhill, and Marion counties.[1] That represents roughly 6% of the current metropolitan housing stock (or about three years of normal development). That's probably an over estimate, given that some property owners made claims beyond the current financial feasibility of what could be developed. However, if the legal and administrative barriers to transferability reduced that total, such an increase in land availability would lead to a significant burst of economic activity in the state and likely reduce land costs and housing costs in the region.

Regarding House Bill 3540, an overall assessment of the housing production that would occur requires an assessment of the pro-development impacts of the "express lane" approval process and transferability versus the anti-development impacts of the restrictions on the number of units per parcel and per owner. The intended consequence of the supporters of the legislation is to reduce the development impact, so it's probably correct to assume that less housing production will occur under House Bill 3540 than under Measure 37.

Estimating Value versus Cost

Finally, the new requirement that Measure 37 compensation be estimated based upon the immediate before-and-after impact of the legislation will complicate the estimation process and reduce the claim amounts. Compliance costs will certainly rise. The appraisal profession is trained to estimate values under current market conditions, whereas estimates in distant time periods are more difficult. Much of the data from those periods is no longer available. Both Measure 37 and House Bill 3540 have created a burst of employment for "forensic" appraisers.

Moreover, the forensic appraisal method proposed by House Bill 3540 will miss much of lost economic value created by land use regulations. Many of the regulations in question have persistent

[1] Sightline Institute (2007) and Core GIS (2007)

impacts, not immediate ones. A regulation like Portland’s urban growth boundary had little impact in the 1980’s when housing development rarely pressed up against the boundary. The real problem is today, after 15 years of steady population growth and the growing scarcity of land available for residential development.

In a similar way, House Bill 3540’s proposed estimation of the current value of Measure 37 claims using Treasury Bill interest rates confuses cost and value. As any Oregon homeowner can attest, the value of real estate has grown much faster than tax-exempt interest rates. Therefore, the lost economic benefits to society of reduced development will be much greater than the claim amounts permitted under House Bill 3540.

Finally, the provision seeking recapture of past special farmland assessments seems more focused to limit the value of claims than an attempt to address a legitimate public finance purpose. Farm use requires fewer public infrastructure costs than non-farm use, so allowing lower rates of farmland assessment matches the benefit principle of public finance. And since new residential development will be assessed at ordinary property tax rates in the future, that stream of higher taxes (plus the system development charges associated with the development) should support the needed infrastructure in the future.

As a result, these features of HB 3540 will likely reduce the potential value of Measure 37 compensation claims and raise the compliance or transaction cost of making a claim. This should lead to fewer claims and smaller compensation amounts. This might lead to the unintended consequence of more compensation dollars paid by local governments to settle claims (since the current amount is zero). Whether they choose to compensate depends upon how much they value the negative impacts of the development. Therefore, on balance, the compensation limits in HB 3540 would result in fewer housing units being built and few, if any, large subdivisions.

Unfortunately, neither Measure 37 nor House Bill 3540 was written to address the needs of homebuyers and renters nor were they written from the perspective of economic efficiency. While Measure 37 seems to offer the potential for greater housing production and greater development impact, both options create considerable uncertainty for property owners and high transaction costs. The one certainty is the structure of the Oregon initiative and referral system will give voters an all-or-nothing choice in November. ■

Housing Price Appreciation in the Portland Region: A 25-Year Retrospective

PSU Center for Real Estate

The last five years have seen extraordinary appreciation of housing in the United States, including the Portland metropolitan area. As we discussed in April, the rapid appreciation in the United States has several sources: historically low interest rates, positive demographics, strong macroeconomic performance, household income growth, and lenient lending policies by financial institutions. Added to that, the decline in the stock market from 2000 to 2002 made investors receptive to real estate as an alternative investment. Moreover, the appreciation of the real estate market led new investors to purchase properties based upon their expected future appreciation, rather than their real estate fundamentals.

This last factor creates the potential for housing markets (or any market) to suffer from a speculative bubble. The value of any financial asset can be seen as the sum of the discounted cash flows. When the rate of discounting declines (i.e., interest rates) and expected cash flows rise (i.e., future selling prices), demand will increase and prices will rise. But since part of that demand is based only upon expectation, we have the recipe for a bubble.

If the risk of a bubble is important, where in the Portland metropolitan are housing market are those risks the greatest? Which neighborhoods or submarkets have been appreciating faster than others?

Using the familiar RMLS submarket areas, the following table presents data from the Regional Multiple Listing Service and its predecessor, the Oregon Multiple Listing Service. The table is sorted by submarket in order of the median price for an existing home in 2006.

Median Existing Home Price Portland Area Submarkets	1982	1990	2000	2006
Lake Oswego/West Linn	$119,100	$183,600	$325,700	$500,000
West Portland	$97,100	$143,400	$293,300	$430,500
Northwest Portland	$99,100	$144,200	$262,200	$383,400
Tigard/Wilsonville	$86,200	$125,600	$211,900	$343,500
Milwaukie/Gladstone	$68,900	$94,000	$189,200	$290,000
Metro Portland	$73,500	$96,000	$198,600	$289,000
Oregon City/Mollala	$58,500	$89,200	$188,700	$284,700
Beaverton/Aloha	$75,300	$105,500	$182,500	$276,000
Northeast Portland	$56,800	$64,200	$169,800	$275,000
Hillsboro/Forest Grove	$69,500	$87,000	$172,600	$263,700
Gresham/Troutdale	$70,300	$88,900	$174,500	$257,500
North Portland	$42,900	$41,300	$124,500	$240,000
Southeast Portland	$53,200	$59,200	$153,900	$235,300

Source: RMLS™ (July 2007)

As housing economists tend to note, housing prices are really housing expenditures. They view a home as a bundle of amenities, each with a "shadow price". Thus, a house may sell for a high price because it is large or has high level of amenities or because buyers put a high price on the neighborhood location.

As one would expect, the highest priced submarkets in the metropolitan area are those in the high-income sectors of the region, such as Lake Oswego, West Linn and West Portland. The high level of prices reflects the high income of residents, higher quality of housing and larger lot and house sizes, and the central location of those communities. Higher income households purchase larger homes on bigger lots. And since those areas are more recently settled, the more recent construction leads to more amenities (e.g., better insulation, garages, more built-in appliances), leading to higher prices.

The lower priced submarkets in the region tend to be the inner city areas of North, Northeast, and Southeast Portland, as well as the less affluent suburbs like Gresham/Troutdale and Hillsboro/Forest Grove. While land prices tend to be higher in the center of the metropolitan area, the smaller lot sizes and older and smaller homes in North, Northeast and Southeast Portland pull the average home price below the metropolitan area average. While some older homes have been restored and have high prices, older homes tend to have depreciated and be lower priced than new homes. For the suburban communities, their lower prices may reflect lower land prices (due to their less central location) or structures and neighborhoods with fewer amenities.

Median Existing Home Price Index
Portland Region = 100

	1982	1990	2000	2006
Lake Oswego/West Linn	162	191	164	173
West Portland	132	149	148	149
Northwest Portland	135	150	132	133
Tigard/Wilsonville	117	131	107	119
Milwaukie/Gladstone	94	98	95	100
Metro Portland	100	100	100	100
Oregon City/Mollala	80	93	95	99
Beaverton/Aloha	102	110	92	96
Northeast Portland	77	67	85	95
Hillsboro/Forest Grove	95	91	87	91
Gresham/Troutdale	96	93	88	89
North Portland	58	43	63	83
Southeast Portland	72	62	77	81

Source: RMLS™ (July 2007)

A slightly different way to represent the same data is to express the median price in each submarket relative to an index value of 100 for the region as a whole. For example, Lake Oswego/West Linn has a median house price index of 173 in 2006, which means that the typical home in that submarket is 73% more expensive than the metropolitan average.

This table shows how the region has experienced greater housing price disparity among the submarkets prior to 1990 and a narrowing of house price differentials after 1990. The early and mid-1980's were a tough economic period and many inner city neighborhoods saw declining prices, while suburban housing prices tended to rise faster. Communities like Lake Oswego and Northwest Portland saw much higher appreciation than the region as a whole, while prices in North, Northeast, and Southeast Portland stagnated or declined in inflation adjusted terms.

Median Existing Home Price Annual Appreciation Rates Portland Area Submarkets			
	1982-1990	**1990-2000**	**2000-2006**
Lake Oswego/West Linn	5.6%	5.9%	7.4%
West Portland	5.0%	7.4%	6.6%
Northwest Portland	4.8%	6.2%	6.5%
Tigard/Wilsonville	4.8%	5.4%	8.4%
Milwaukie/Gladstone	4.0%	7.2%	7.4%
Metro Portland	3.4%	7.5%	6.5%
Oregon City/Mollala	5.4%	7.8%	7.1%
Beaverton/Aloha	4.3%	5.6%	7.1%
Northeast Portland	1.5%	10.2%	8.4%
Hillsboro/Forest Grove	2.8%	7.1%	7.3%
Gresham/Troutdale	3.0%	7.0%	6.7%
North Portland	-0.5%	11.7%	11.6%
Southeast Portland	1.3%	10.0%	7.3%

Source: RMLS™ (July 2007)

Since 1990, that pattern has reversed. Median home prices in older, lower income areas like North, Northeast, and Southeast Portland appreciated by double-digit rates for over a decade. For North Portland, this pattern continued after 2000, making it the hottest market in the region. The rising median home price in the inner city has created significant burdens on inner city renters, while at the same time causing wealth increases for inner city homeowners. By 2006, the median home price in Northeast Portland had equaled the median home price in Beaverton/Aloha, whereas 25 years ago, there was a 25% discount in price. This reversal of fortunes has several sources.

First, improving social conditions, public infrastructure, and remodeling activity in the east side of Portland during the 1990's may have played an important role. Crime and other measures of social disorder tend to be negatively capitalized in home prices, so improvements in those conditions likely contributed to increased home prices. The infrastructure improvements include completion of the Convention Center, the Rose Garden, light rail lines, and various urban renewal projects.

Note that new housing construction or condominium construction would have minimal or only indirect effects on this indicator. "Existing Housing" doesn't include new home sales so the effect of new housing won't show up until the house is re-sold, which typically is seven to ten years later.

Condominiums are also excluded in this sample. On the other hand, home remodeling activity will increase home quality and sales price, since RMLS data treats a remodeled home as an existing home. Since a remodeled home is a “different” home, price increases partly reflect quality improvement, rather than a true price increase of the product.

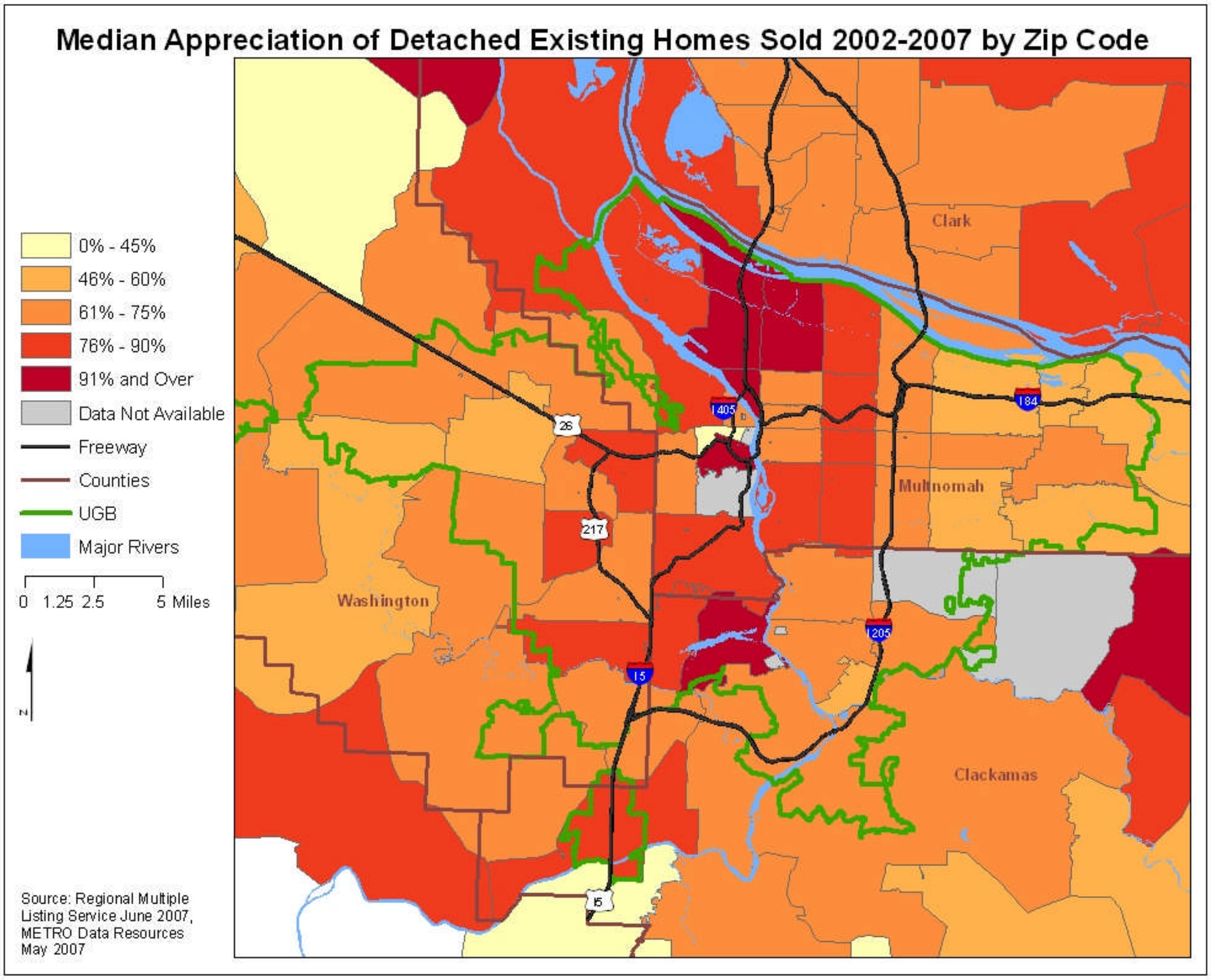
The second major influence on inner city home prices is the disproportionate impact of land prices. Land prices throughout the region rose rapidly, partly in response to the relatively tight urban growth boundary. With land supplies restricted, developers bid up the price of developable land, which impacts home prices. According to a recent study by the PSU Center for Urban Studies, land prices rose by 500% in 15 years, or more than 11% per year.[1]

Since land prices tend to be higher at the center of metropolitan areas and inner city houses tend to be older and more depreciated, land prices are a bigger factor with inner city home prices than suburban home prices. As land prices rose, inner city housing appreciated faster than suburban housing.

Also, rising prices contributed to population shifts or gentrification. As higher income households move to inner city neighborhoods, they bid up the price of those homes as well as participate in remodeling.

A more dramatic representation of the appreciation story can be seen in the map below, which shows the appreciation rates for 2002-2007 for the various zip codes in the Portland metropolitan region. As before, the areas of greatest appreciation are in North and Northeast Portland, along with the Lake Oswego area. However, the map demonstrates that the greatest appreciation occurred in the areas closest to downtown Portland, within North and Northeast Portland. On the east side, areas to the west of 82nd Avenue appreciated faster than those to the east. Portland neighborhoods tended to appreciate faster than nearby neighborhoods in Washington County or Clackamas County.

[1] Hall and Mildner (2007)



Source: RMLS™ (July 2007)

In summary, metropolitan area home prices have continued to appreciate in the past five years, almost as rapidly as they did in the 1990's. The highest appreciation rates in the 1990's were concentrated in neighborhoods closest to downtown Portland, whether measured at the scale of RMLS submarkets or zip codes. The interaction of buyer demand, rising land costs, population movement, remodeling activity, and public improvements make the overall assessment of these price changes quite complex.

Since 2000, the rate of appreciation in Portland has remained high, rising at 6.5% annually, slightly lower than the 7.5% rate in the 1990's. And with the exception of North Portland, the appreciation rates from 2000 to 2006 have been relatively constant across the region. Nevertheless, a 6.5% annual appreciation suggests that home prices will double in 11 years. Since home prices are ultimately bound by population, income, and interest rates, that pattern will not continue forever.

Local Housing Market Update

PSU Center for Real Estate

While national trends continue to demonstrate a decline in the median sales price of single family homes, the Portland metropolitan area continues to appreciate. The following chart shows how the Portland-Vancouver MSA ranks among other US cities in median sales price of existing homes for the first Quarter 2007. Both Portland and Seattle housing markets continue to defy the national trend of slow but steady depreciation.

Median Sales Prices of Existing Single Family Homes by Metropolitan Area

	Q1 2007 Median Sales Price	%Change Q4 2006 to Q1 2007	% Change Q1 2006 to Q1 2007
U.S. Average	$212,300	-1.8%	-3.1%
Salt Lake City, UT	$206,900	12.3%	-7.5%
Spokane, WA	$181,800	5.6%	-3.9%
Denver-Aurora, CO	$239,400	-2.0%	-2.5%
Cincinnati-Middletown, OH-KY-IN	$136,800	-0.7%	-1.4%
Las Vegas-Paradise, NV	$310,100	-2.5%	-1.1%
Salem, OR	$221,600	15.6%	-0.7%
Chicago-Naperville-Joliet, IL	$267,300	1.4%	-0.3%
Boston-Cambridge-Quincy, MA-NH	$387,400	-1.0%	-0.2%
Sacramento--Arden-Arcade--Roseville, CA	$365,500	-2.8%	0.1%
Phoenix-Mesa-Scottsdale, AZ	$262,500	-2.2%	0.1%
Austin-Round Rock, TX	$176,200	5.4%	0.6%
Portland-Vancouver-Beaverton, OR-WA	$289,900	8.9%	1.6%
San Francisco-Oakland-Fremont, CA	$748,100	2.2%	1.9%
Seattle-Tacoma-Bellevue, WA	$380,200	12.3%	2.0%
San Diego-Carlsbad-San Marcos, CA	$595,200	-2.0%	2.7%
Albuquerque, NM	$193,700	12.7%	3.3%

Source: National Association of Realtors® (2007) Based on preliminary data.

Another indicator of the local housing market is the number of building permits issued. In Portland, the number of permits issued so far this year is down 17%. However, Stumptown fared better than the nation which saw a 29% decrease in permit activity. Bend experienced the sharpest decrease in single family home construction with a 45% decline, indicating that the Bend market may have finally hit the end of its housing boom. Both Portland and Bend have experienced a 13% increase in multi-family building permits, although in the case of Bend, that represents a small percentage of total housing units.

Building Permits Issued
Year-to-Date (thousands)

	Single-Family			Multi Family		
	May-06	**May-07**	**% Change**	**May-06**	**May-07**	**% Change**
UNITED STATES	**652.2**	**466.0**	**-29%**	**198.3**	**170.6**	**-14.0%**
OREGON	9.47	7.80	-18%	3.12	3.20	3%
Bend	1.58	0.87	-45%	0.11	0.12	13%
Eugene-Springfield	0.58	0.52	-11%	0.29	0.24	-17%
Medford	0.55	0.49	-12%	0.09	0.09	-4%
Portland-Vancouver-Beaverton	4.95	4.11	-17%	2.39	2.69	13%

National Association of Home Builders (July 2007)

Second Quarter Recovery in Portland[1]

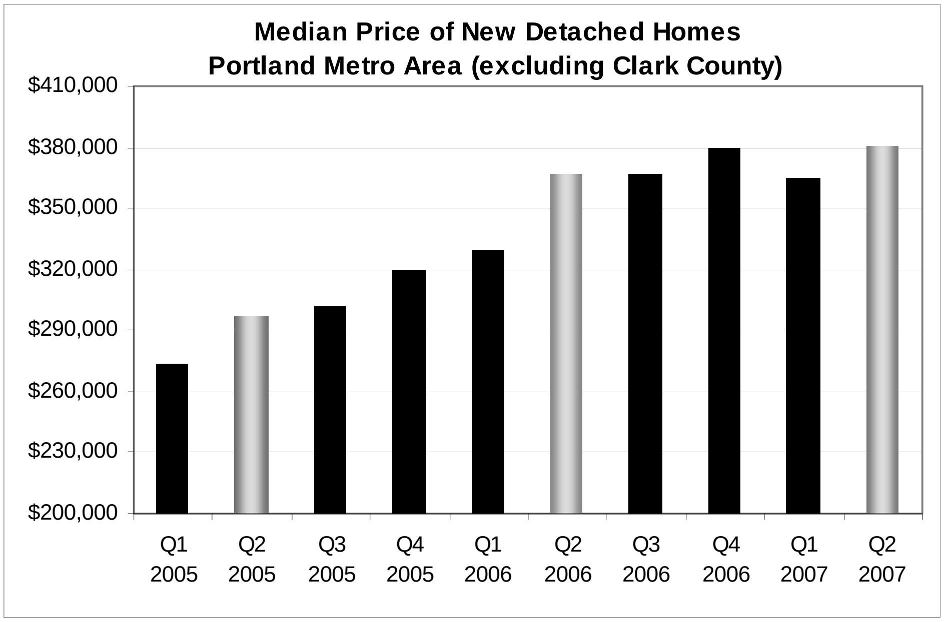
The median price of existing detached homes in the Portland metropolitan area (excluding Vancouver) continues to rise. The median home price increased by 5% from $294,000 in the first quarter of 2007 to $308,000 in the second quarter. Over the entire year, the median price increased by 7%, which is a sharp decline in appreciation when compared to a 20% increase between the second quarter of 2005 and the second quarter of 2006.[2] While the Portland housing market has cooled off from last year's feverish pace, it continues to experience shows healthy appreciation.

[1] Data for all charts and tables in this section and the following section on Vancouver were retrieved July 2007 from the RMLS™ database.
[2] Please note that figures here may differ from previous reports due to a change in how new and existing homes have been defined.

Median Price of Detached Homes
Portland Metro Area (excluding Clark County)

	Q2 2005	Q2 2006	Q2 2007	% Change Q2 2005 -Q2 2006	% Change Q2 2006 - Q2 2007
Existing	$239,000	$286,000	$307,500	19.8%	7.42%
New	$297,000	$367,000	$380,500	23.4%	3.81%

New home sale prices rebounded after a decline during the first quarter of 2007. While the median price for new detached homes dipped down to $365,000 in the first Quarter of 2007, this past quarter the median price returned to $380,500. Similar to existing homes, new homes also experienced a sharp decrease in appreciation when compared to the previous year. Prices of new detached homes increased only 4% from the second quarter of 2006 to the second quarter in 2007 compared to 23% in the previous year.



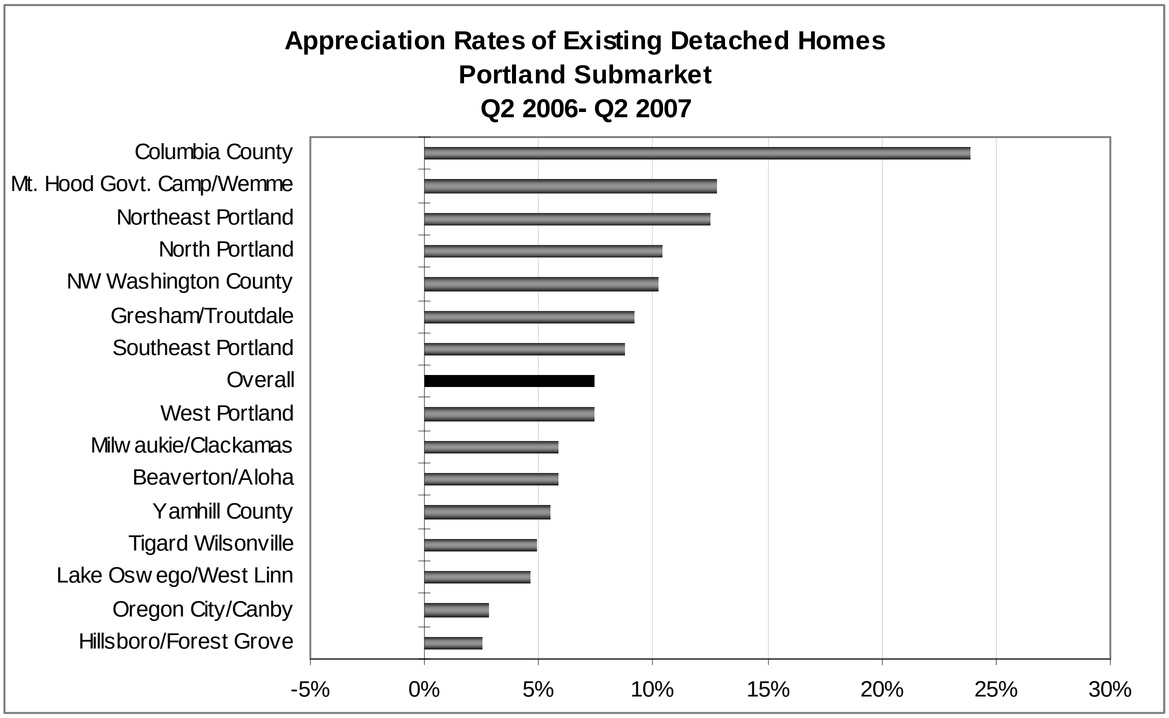
Disaggregating the housing data by month and housing type suggests that the Portland housing market may be softer than the quarterly numbers indicate. While home prices rose in the second quarter, much of that rise occurred in April and May, with prices essentially flat in June. Including all home sales in Portland (new, existing, attached and detached) the median home price declined in June after a $12,000 increase in May. Looking only at detached homes, the median price of new homes declined sharply in June. These changes may simply reflect the volatility of new home prices since an entire subdivision with one product type may come on the market at once and skew the data. As a general rule, new housing production is an important indicator for the health of the economy, but focusing on existing sales price data gives a more reliable picture of the trend in housing prices.

Median Sales Price
Portland Metro Area (excluding Clark County)
2007

	April	May	June
Portland Metro All	$285,000	$297,500	$295,000
Portland Metro Detached Existing	$298,500	$310,000	$312,500
Portland Metro Detached New	$379,000	$392,500	$372,000

A closer look at the neighborhoods in the Portland region shows appreciation of existing homes across the board over the past year. The areas with the greatest increase were the inner city neighborhoods and the exurban areas of Columbia County, NW Washington, and Mt. Hood. The 17-

year trend of fast appreciation in Portland's inner city continued into 2006 to 2007. When looking at the areas in between, i.e., the suburbs of Gresham, Milwaukie, Beaverton, Tigard, and Hillsboro over the past year, only Gresham outpaced the regional average.



When comparing year-over-year appreciation over the past two years, only two exurban submarkets (Columbia County and Mt. Hood) show faster appreciation in the last 12 months versus the previous 12 months. The regional slowdown was felt in almost all the submarkets.

Appreciation Rates of Existing Detached Homes by Submarket		
	Q2 2005-Q2 2006	Q2 2006-Q2 2007
Columbia County	11.8%	23.84%
Mt. Hood Govt. Camp/Wemme	4.3%	12.73%
Northeast Portland	18.6%	12.50%
North Portland	25.4%	10.43%
NW Washington County	16.7%	10.20%
Gresham/Troutdale	16.3%	9.20%
Southeast Portland	24.6%	8.77%
Overall	**19.8%**	**7.42%**
West Portland	22.0%	7.42%
Milwaukie/Clackamas	23.0%	5.85%
Beaverton/Aloha	18.0%	5.82%
Yamhill County	20.4%	5.52%
Tigard Wilsonville	19.0%	4.93%
Lake Oswego/West Linn	15.8%	4.63%
Oregon City/Canby	16.5%	2.79%
Hillsboro/Forest Grove	23.8%	2.54%

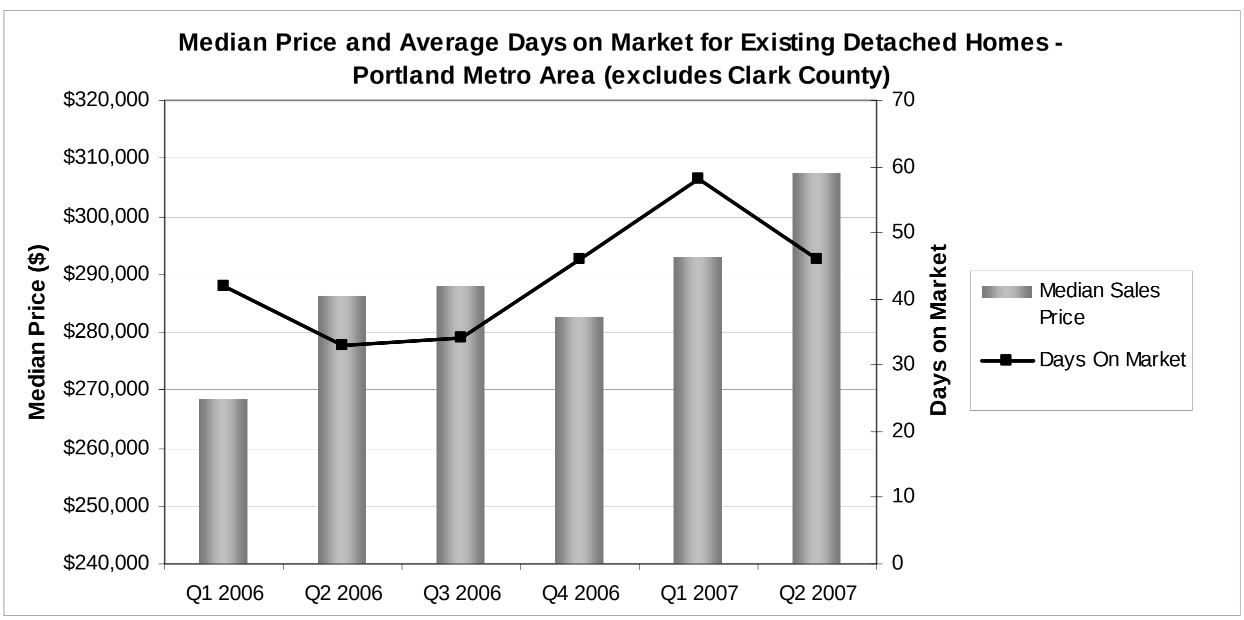
As we indicated before, new home sales have appreciated more slowly than existing homes. The overall median price of new detached homes sales increased by only 4% between 2006 and 2007, down from 23% the previous year. Median new home prices actually decreased this past year in Northeast Portland, Milwaukie/Clackamas, and Beaverton/Aloha.

New Detached Home Median Sales Price Portland by Submarket		
	Q2 2006	Q2 2007
North Portland	$248,000	$254,000
Northeast Portland	$265,000	$262,000
Southeast Portland	$271,000	$301,500
Gresham/Troutdale	$280,000	$315,000
Columbia County	$245,000	$316,000
Yamhill County	$299,000	$321,500
Beaverton/Aloha	$440,000	$349,000
Oregon City/Canby	$288,000	$362,000
Overall	**$366,688**	**$380,671**
Hillsboro/Forest Grove	$319,000	$388,500
Milwaukie/Clackamas	$529,000	$495,000
Tigard Wilsonville	$515,000	$527,000
NW Washington County	$482,000	$560,000
West Portland	$589,000	$616,000
Lake Oswego/West Linn	$796,000	$1,185,500

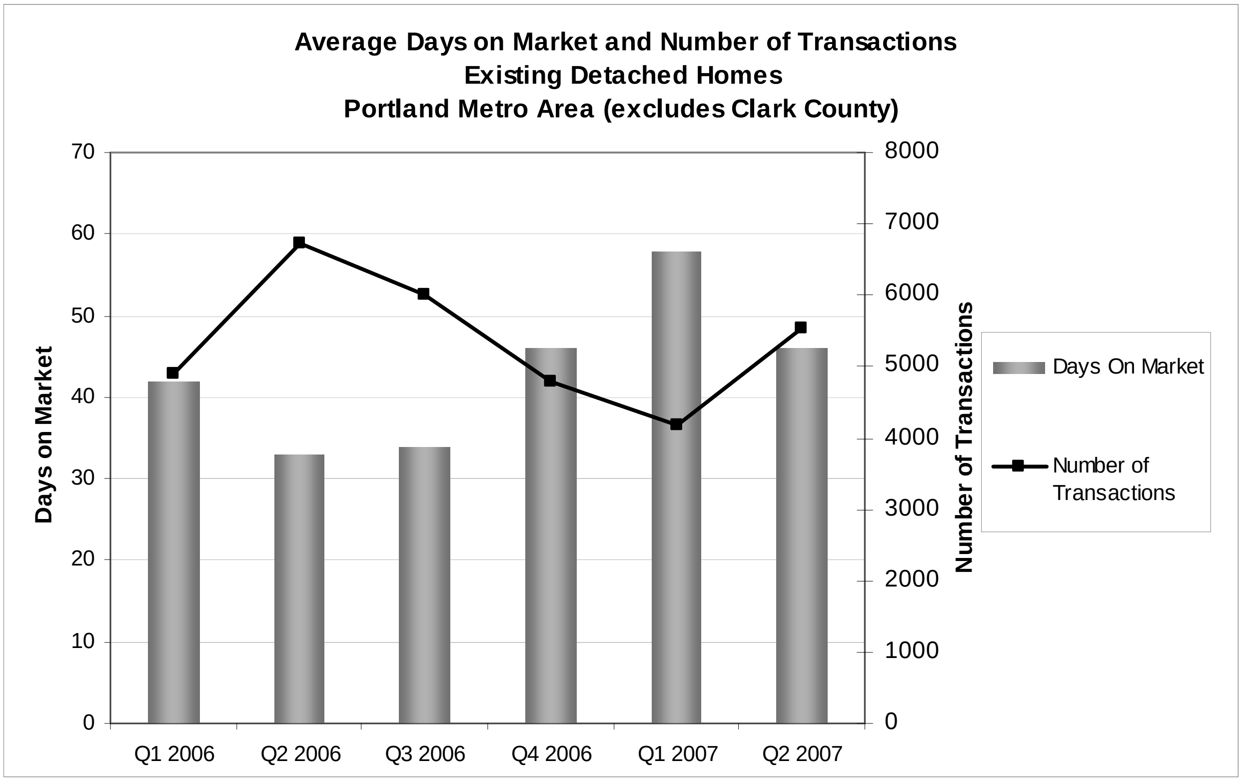
Two standard measures for tightness in the local housing market are the average number of days that homes are on the market and the difference between the original listing price and the sale price. The difference between list price and sale price also reflects the discrepancy between the market and sellers' expectations of the market.

The following chart shows a steady increase in the days on market that has surprisingly followed the increase in median price of existing homes. Perhaps homeowners who have been watching Portland's sharp appreciation mistakenly anticipated the same high appreciation this past year, and thus, homeowners held on to their properties longer waiting for higher prices. During the same period, homeowners gradually accepted lower final prices than the original sales price. In the first quarter of 2007, homeowners were only receiving 93% of original list price, compared to 97% a year previous.

However, as a sign of recovery from this trend, the past quarter saw a 12 day decrease average days on market. Days on market decreased from 58 days in the first quarter of 2007 to 46 days in the second quarter.



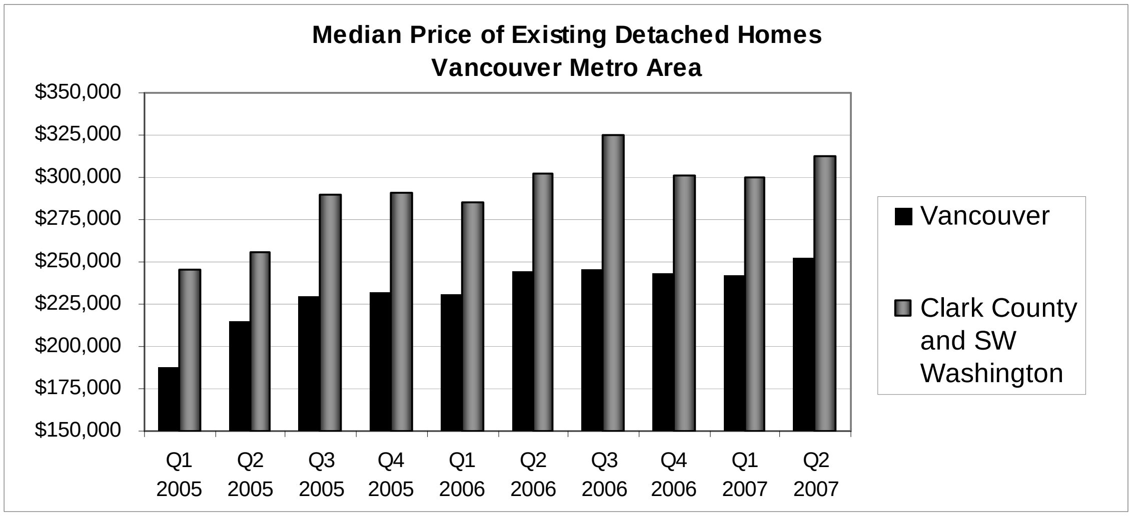
Another indication of recovery is the increase in the number of transactions. Last quarter there were 5,500 transactions, a 32% increase from 4,200 transactions in the first quarter. However part of this reflects the seasonality of the housing market as sales usually pick up in the second quarter. By comparison over 6,700 transactions occurred in the second quarter last year.

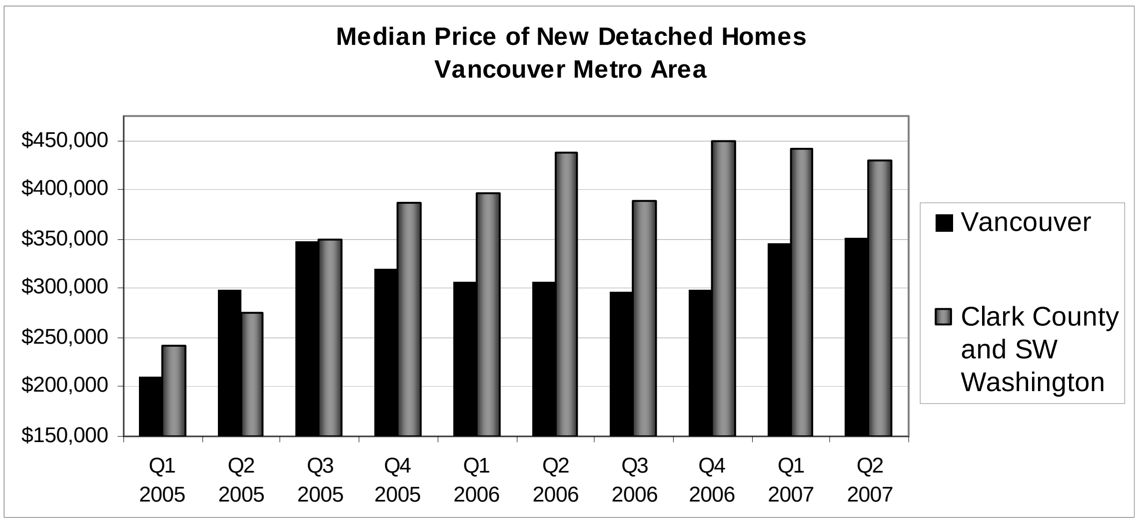


To summarize, Portland defies the national trend with continued modest appreciation. Although appreciation is much slower then the double digits experienced last year, Portland remains healthy compared to the national housing market. While there were some warning signs during the first quarter of 2007, including increasing days on market and declining number of transactions, the area rebounded in the second quarter. The median price of existing homes increased, the number of transactions increased, and days on market fell—all indicating a recovery. But, how long will it last?

Similar Patterns in Vancouver

The recent housing market in Vancouver and Clark County follows Portland's pattern. After two quarters of declining median prices in Vancouver and Clark County, the area experienced modest appreciation this spring. Both close-in Vancouver and the outlying areas in Clark County and SW Washington experienced 4% appreciation of existing detached homes over the past quarter. New detached homes prices dropped 3% in the suburbs and increased 2% in close-in Vancouver.





Measured on an annual basis, however, the appreciation trends in Vancouver and Clark County are much slower this year than last year. After median existing home prices increased by 14% in Vancouver and 19% in Clark County in 2005 to2006, both markets slowed to 3% in 2006-07.

Median Price of Existing Detached Homes
Vancouver Metropolitan Area

	Q2 2005	Q2 2006	Q2 2007	% Change Q2 05-Q2 06	% Change Q2 06-Q2 07
Downtown/Close-in	$215,000	$244,000	$252,500	13.5%	3.5%
Suburbs/outlying	$255,450	$302,825	$312,500	18.5%	3.2%

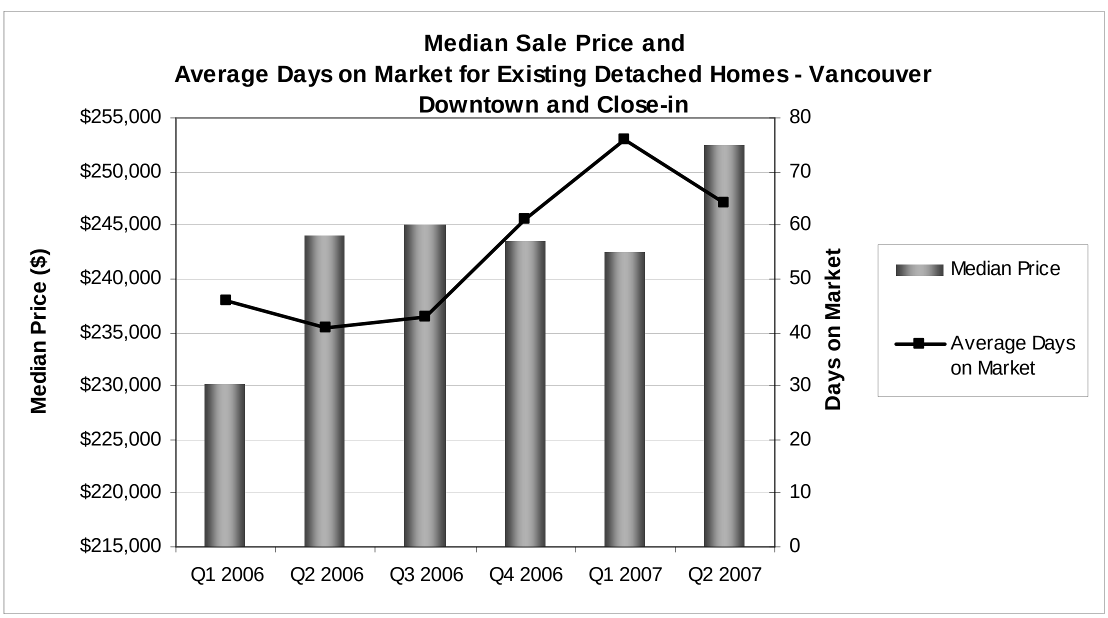
Turning to the new home market, the median price for new homes experienced a sharp increase for inner Vancouver neighborhoods. While they have been relatively stable in the suburbs of SW

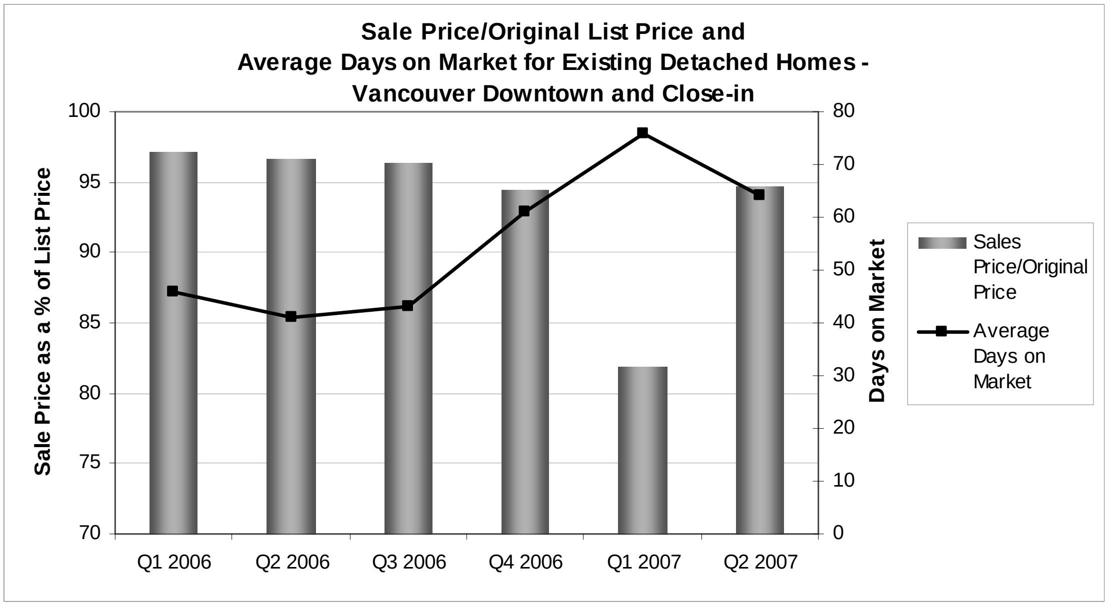
Washington, this is a dramatic change from the prior year when suburban Clark County experienced a rise of more than 50%. Overall, the sales of the last two years suggest that new home builders in Vancouver and Clark County have been able to price their product close to levels in comparable markets on the Oregon side of the river. The Vancouver median price is higher than the submarkets in North, Northeast, and Southeast Portland. And the median price in Clark County is higher than those in Beaverton/Aloha, Hillsboro/Forest Grove, and Oregon City/Canby (although well below the higher priced suburban markets).

Median Price of New Detached Homes
Vancouver Metropolitan Area

	Q2 2005	Q2 2006	Q2 2007	% Change Q2 05-Q2 06	% Change Q2 06-Q2 07
Downtown/Close-in	$297,817	$306,450	$352,500	2.9%	15.0%
Suburbs/outlying	$274,950	$436,950	$430,051	58.9%	-1.6%

Similar to Portland, the average number of days on market for existing homes in close-in Vancouver increased for three quarters before decreasing this past quarter. The average number of days on market decreased by twelve days this past quarter to 64 days. However, Vancouver is different from Portland because the ratio of final sales price to original list price recovered this past quarter. In the first quarter of 2007, the ratio plummeted to 82%, but this past quarter the ratio returned to previous levels that have hovered around 95%.





Willamette Valley Catching Up

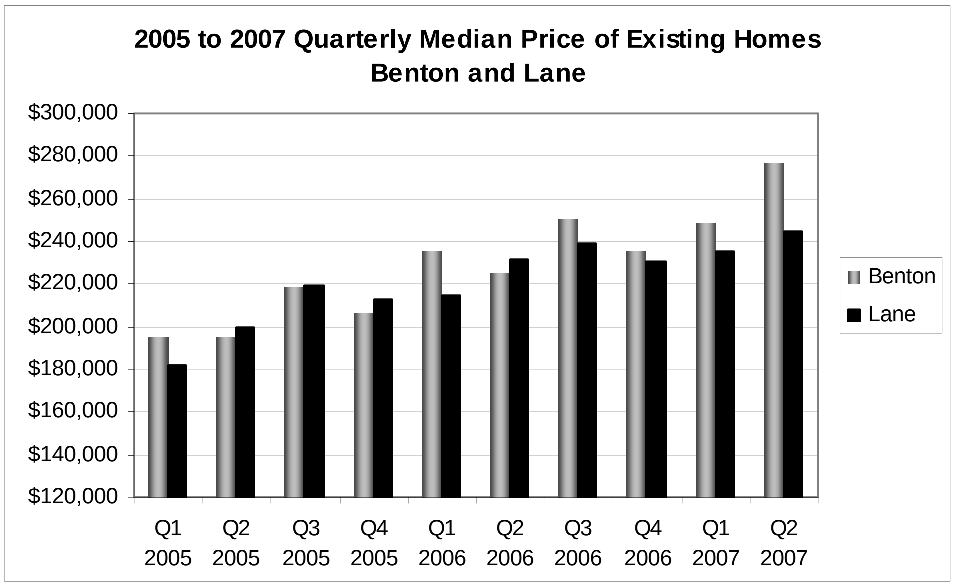
Willamette Valley experienced year-over-year appreciation in first quarter sales in all its markets.[1] Benton County had the fastest appreciation rate and the highest median home price among markets in the Willamette Valley in 2007. The second highest priced market, Lane County saw a 6% increase from 2006 to 2007, with the median home price reaching $245,000. Among the other markets, suburban Marion County market saw a 22% rise, with the median home price reaching $206,000. The data identified as Marion County and Polk County excludes the cities of Salem and Kaiser.

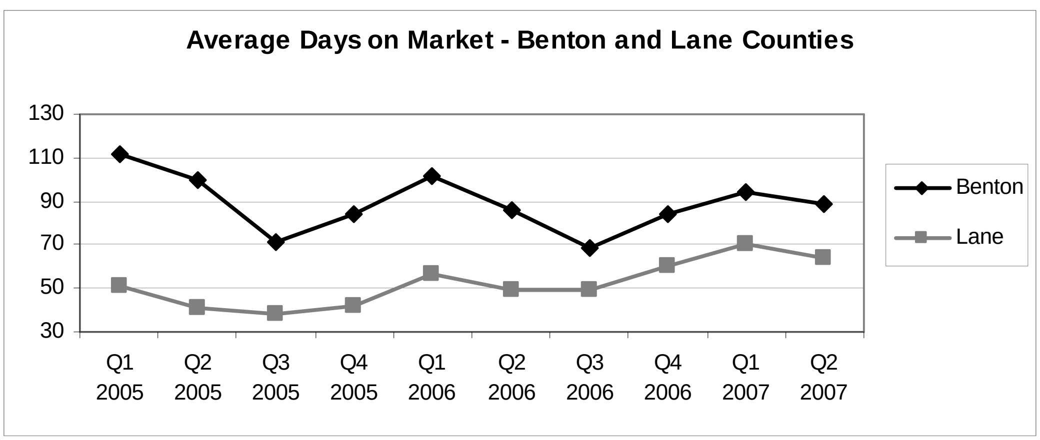
Median Price of Existing Detached Homes Willamette Valley

	Q2 2006	Q2 2007	06-07 % Change
Salem	$188,000	$199,500	6.1%
Marion	$169,494	$206,000	21.5%
Polk	$167,225	$178,900	7.0%
Benton	$224,750	$276,650	23.1%
Lane	$232,000	$245,000	5.6%
Linn	$144,300	$162,500	12.6%

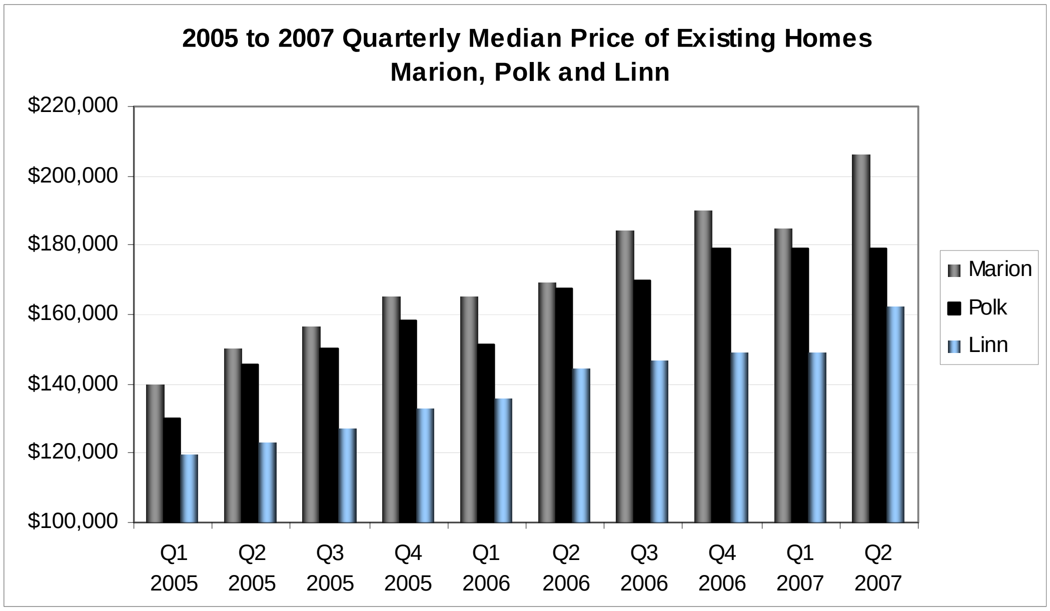
[1] This section uses data from WVMLS for Benton, Linn, Marion and Polk counties and RMLS™ for Lane County retrieved July 2007. Data from WVMLS excludes new homes as well as homes built within the calendar year prior to the year sold.

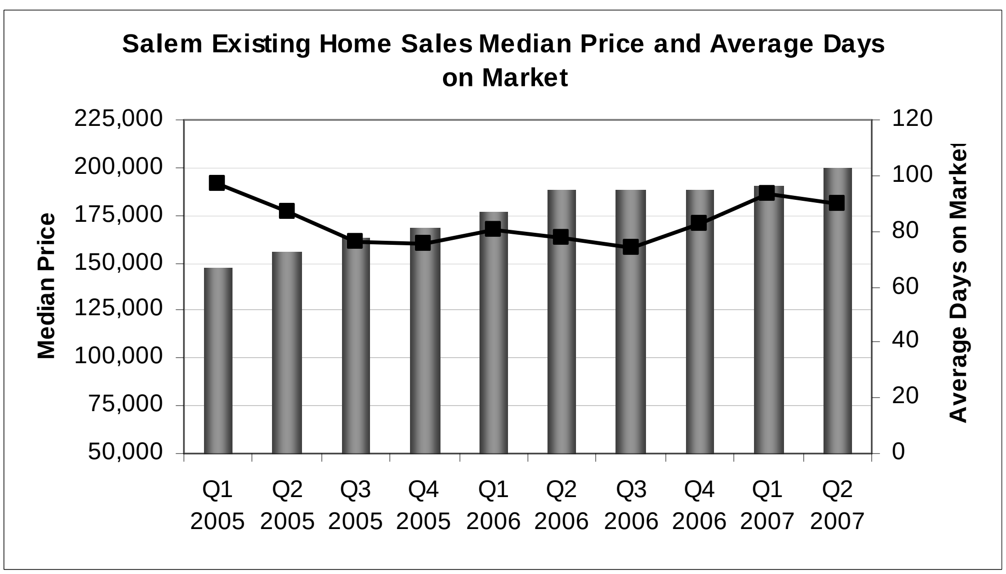
Lane and Benton Counties have been experiencing rising median prices quarter over quarter for the past three quarters. Median home prices rose 11% this past quarter in Benton and 4% in Lane County. While in the fourth quarter of 2006, Lane and Benton County had nearly equally median values, Benton County homes have appreciated at a much greater rate over the past two quarters. Appreciation rates in both markets were accompanied by a decline in the average days on market as well.



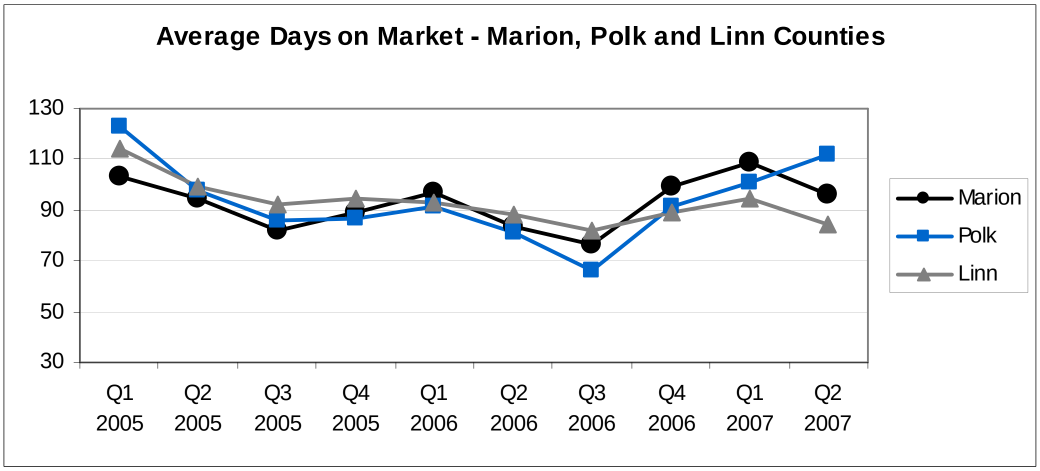


Signs of revival appear in the quarterly data for most of the Mid-Willamette Valley communities. Marion (excluding Salem and Kaiser) and Linn County experienced an increase in median sales price over the past quarter of 11% and 4% respectively, with Marion County recently surpassing the $200,000 median price benchmark. After nearly a year of level median home sales, Salem had its first quarter of appreciation this spring. Existing home sales increased 5% to $200,000. The one weak market in this region has been Polk County. For the past three quarters, Polk County has hit a plateau with home prices hovering around $180,000.



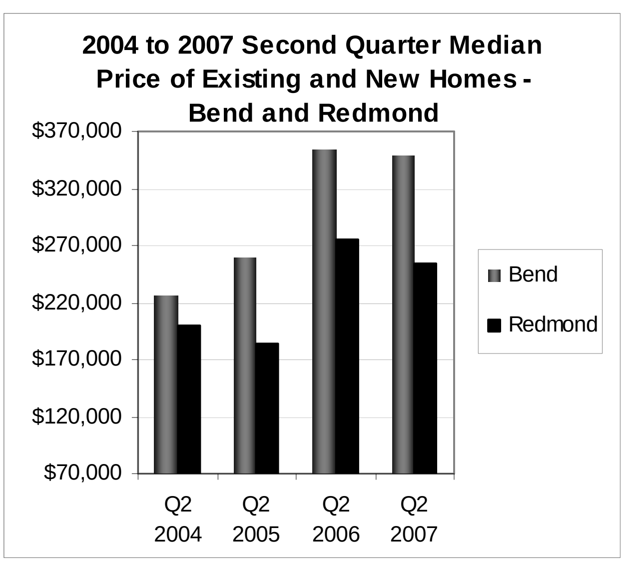


Turning to our measure of market tightness, Salem, Marion, and Linn all experienced a slight decrease in the number of days on market the past quarter after two straight quarters of increase. Marion and Linn experienced a decline in the days on market by ten days, while Salem experienced a decline of three days. As was true in pricing, Polk County was the weakest market, with an increase in days on market from 11 days to 112 days in the last quarter.



Bust in Bend

The Central Oregon markets of Bend and Redmond have been two of the hottest housing markets in the United States in the last five years, with homebuilders struggling to keep up with demand and lower income workers having to commute long distances to find affordable housing. However, the housing boom has finally leveled off. In the last quarter, the median existing home price decreased by 1% in Bend and by 7% in Redmond. In addition, homebuilders have greatly reduced their activity in these towns. A typical house in Bend now commands nearly $100,000 more in price than a typical home in Redmond. Nevertheless, the median price of homes in Bend in the last quarter was $349,500 and in Redmond $255,000, levels unimaginable two or three years ago. The glut of housing may take quite a while to be eliminated. The average days on market jumped this past quarter in both Bend and Redmond by 40 days to 160 days. The dramatic decrease in building permits, down 49%, provides further evidence that Bend has been over built.



Central Oregon Association of Realtors® (June 2007)

Portland Area Retail Market Overview

W. Grant Norling, PGP Valuation

The Portland Metropolitan area retail market continues to demonstrate strong performance into the 2nd quarter of 2007, with no indications of cooling. While outlying locations remained priorities for developers with projects including the highly publicized opening of IKEA within Cascade Station; there is a refreshed interest for the Central Business District as well. In addition to the construction of the new transit mall, large anchor tenants, including Macy's and Nordstrom, are investing in extensive interior renovations of existing spaces, solidifying their position in the downtown core retail area.

Land sales and lease rates continue to rise as the availability of large parcels suitable for the construction of shopping centers dwindles. Anchor spaces in suburban markets are commanding triple net rents in the $14 to $25 per square foot range, while shop retail spaces are achieving robust rents from $25 to $40 per square foot; shop retail spaces with prime exposure within trendy lifestyle centers can lease for a premium beyond this range.

Meanwhile, developers are targeting educated young professionals by picking redevelopment and mixed-use retail projects in the close-in Portland neighborhoods. Common tenants in these new and renovated projects include: specialty grocers, local banks, restaurants and hip art, furniture, national fitness centers and home décor stores. Eastside spots include: Alberta Arts District, Mississippi Avenue, MLK Jr. Boulevard in N/NE Portland, Belmont Street and Hawthorne Street in SE Portland. Local companies paying moderate rents in the $12 to $18 per square foot range are typical tenants in this trendy area, with some regional and national tenants paying in excess of $20 per square foot.

Over on the west side, the Pearl District is rolling with new mixed-use projects coming online as ground is being broken for others. This area continues to attract national and regional retailers, including REI (completed), Eddie Bauer (under construction) and LA Fitness (planned). Ground floor retail spaces within these developments are commanding triple net rents in the $20 to $35 per square foot range, depending on tenant credit and build-out. Large retail spaces (10,000+ square feet) are scarce, so don't expect much of a discount. Overall, the retail market throughout the

Portland area appears strong; however, the true determinants of a retail market's health are the supply/demand conditions.

Supply, Vacancy, Absorption

Retail supply, vacancy and absorption are analyzed using the Norris, Beggs and Simpson Retail Market Report: First Quarter 2007. The total retail supply in the Portland market for first quarter 2007 was 40,037,614 square feet of which 1,821,990 square feet were vacant, indicating a vacancy rate of 4.6%, down from 4.8% in the fourth quarter of 2006. This follows the downward trend in the overall retail vacancy rate since the second quarter of 2001 when the vacancy peaked at 7.3%. Currently, the Portland market is experiencing a retail vacancy rate that is within the range typically exhibited by healthy markets of 4 to 5%.

The following chart details changes in retail supply and year-end vacancy over the last five years:

Retail Growth and Absorption		
Year	**Net Absorption**	**Vacancy (%)**
2002	375,920	5.4
2003	242,709	4.3
2004	2,461,489	4.3
2005	808,981	4.7
2006	43,928	4.9
2007 (1st Q)	261,537	4.6
Average	**699,094**	**4.7**

Source: NBS Quarterly Retail Reports

The Portland retail market has achieved positive absorption each of these years, which indicates relatively strong demand, as more tenants are expanding or entering the market than leaving the market. After several years of strong growth, new construction fell off steeply in 2002 in response to economic uncertainty and the perception of a softening retail market. However, this hiccup in expansion allowed demand to catch up to supply as is depicted in the 2,461,489 square feet absorbed in 2004. Overall, strong growth and low vacancy rates suggest that the Portland retail market is functioning efficiently with average vacancy rates less than 5% and net absorption exceeding 650,000 square feet per year.

As defined by the NBS Market Report, the Portland market consists of seven general submarkets including: Central City, Sunset Corridor, Southwest, Eastside, 122^{nd}/Gresham, East Clackamas, and Vancouver. Four out of the seven submarkets achieved positive year-end absorption. Particularly strong sub markets include the Sunset Corridor and East Clackamas, which have retail vacancy rates of 2.7 and 2% respectively.

Sales of Retail Properties

While vacancy rates are low and absorption numbers are strong, these figure give us little indication of what is happening to improved land sale prices in the Portland area. The charts below summarize the primary retail center sales (10,000+ square feet) in the Portland market for 2006 and 2007 through 2nd quarter:

Primary Retail Center Sales (2006)					
Name/Address	**Sale Date**	**Center Type**	**Price**	**Size (SF)**	**Price/SF**
Meadowland Shopping Ctr Lot 3	December	Strip	$2,855,877	15,257	$187
Meadowland Shopping Ctr: Lot 5	December	Strip	$2,139,370	11,101	$193
Talbert Center	December	Strip	$14,392,500	35,650	$404
Trails End Marketplace	July	Neighborhood	$30,550,000	102,395	$298
The Shops at Griffith Park	July	Strip	$8,854,340	18,884	$466
Oregon City Antique Building	June	Neighborhood	$1,400,000	16,030	$87
Langer Farms Shopping Ctr 2	May	Strip	$10,890,517	27,723	$393
Langer Farms Shopping Ctr	May	Strip	$10,970,000	27,723	$396
Universal Center	May	Strip	$5,550,000	23,254	$239
Division Retail Plaza	May	Strip	$1,000,000	11,500	$87
Retail Brewery	April	Specialty	$1,836,900	16,880	$109
Freestanding Retail	March	Neighborhood	$12,000,000	75,040	$160
Farmington Village Shopping Ctr	February	Neighborhood	$6,490,000	32,649	$199
Sunnyside Town Center	January	Strip	$5,600,000	17,950	$319
Hollywood Plaza Retail Center	January	Strip	$3,050,000	19,687	$155
Washington Green	January	Neighborhood	$23,450,000	79,378	$295
Average Sale			**$8,814,344**	**33,194**	**$249**

Source: Data retrieved from PGP Valuation, Inc. database

Primary Retail Center Sales (2007)					
Center Name	**Sale Date**	**Center Type**	**Sale Price**	**Size**	**$/SF**
Esquire Building	May	Neighborhood	$1,500,000	29,780	$50
NW Flanders Shell Building	May	Neighborhood	$3,250,000	25,000	$130
Southgate Shopping Center	May	Strip	$11,500,000	53,883	$213
Patrick & Poppelton Building	May	Neighborhood	$2,600,000	19,460	$134
Average Sale			**$4,712,500**	**32,031**	**$132**

Source: Data retrieved from PGP Valuation, Inc. database

Based on our research, primary retail center sales ranged in size from 11,101 to 102,395 square feet and from $50 to $466 per square foot. While the majority of these sales were of properties 10,000 to 30,000 square feet and smaller, two premier properties ($20+ million) were traded in 2006, namely

Trails End Market Place and Washington Green. Conversations with brokers revealed that 2006 was largely a seller's market, with demand significantly outweighing supply. Interest rate increases throughout 2006 and into 2007 substantially subdued the refinancing craze market-wide, but demand for all primary retail continues to remain strong.

Sellers are commanding higher prices as they cash out their investments as prospective buyers continue to favor real estate investments over stock and bond markets. Ivana Trump has been famously quoted as saying "I made a tremendous amount of money on real estate. I'll take real estate rather than go to Wall Street and get 2.8%". Shrewd investors are beginning to see investment from Ivana's perspective and are jumping on the real estate band wagon preferring the larger payoffs in a shorter amount of time when compared with recent Wall Street trends.

Capitalization Rates

Historically low interest rates, increased demand for primary commercial real estate and decreased returns on alternative investments have put considerable downward pressure on capitalization rates in the past year. In fact, prime commercial properties with strong tenants and long-term leases have sold at cap rates below 6.0%. The following table compares cap rates for 2006 and first quarter 2007 retail center sales with those of the preceding six years:

CAP Rate Analysis

Year	No. of Sales	Center Type	CAP Rate Range	Average CAP Rate
2001-02	7	Strip	8.3 - 10.8%	9.6%
	11	Anchored	7.9 - 9.5%	8.9%
	18	**All Centers**	**7.9 - 10.8%**	**9.2%**
2003	9	Strip	8.0 - 9.6%	8.8%
	9	Anchored	7.0 - 9.5%	8.7%
	18	**All Centers**	**7.9 - 9.6%**	**8.7%**
2004	11	Strip	6.5 - 8.9%	7.6%
	9	Anchored	7.0 - 9.4%	7.6%
	20	**All Centers**	**6.5 - 9.4%**	**7.6%**
2005	17	Strip	6.4 - 7.8%	7.1%
	9	Anchored	5.9 - 8.6%	7.2%
	26	**All Centers**	**5.9 - 8.6%**	**7.1%**
2006				
	20	Strip	5.5-8.75%	6.9%
	5	Anchored	5.9-8.4%	7.0%
	25	**All Centers**	**5.5-8.75%**	**6.9%**
2007*	7	Strip	5.5-7.0%	6.1%
	1	Anchored	6.5%	6.5%
	8	**All Centers**	**5.5-7.0%**	**6.3%**

Source: Data retrieved from PGP Valuation, Inc. database

The average cap rate for all centers declined from 7.1% during 2005 to 6.9% in 2006. This gradual decline from year to year is promising to repeat itself for 2007 based on the latest cap rate trends we have observed.

Destined for Development

While the retail sales market remains strong, there is new activity on the development front. Claritas National Research Bureau just recently named Portland the most promising US market for retail developers. Portland found its place on the top of the list for a variety of reasons. First and foremost, it has the smallest Gross Leaseable Area (GLA) per capita of all major US cities with approximately 15.61 square feet of developed retail area per person in Portland compared to the national average of 18.19 square feet. Also factored into the ranking is Portland's stronger than average (1.10%) projected yearly population growth of 1.56% through 2010. Additionally, over the next five years, household income in Portland is expected to increase by almost 4.3%, exceeding the national average of 3.81%.

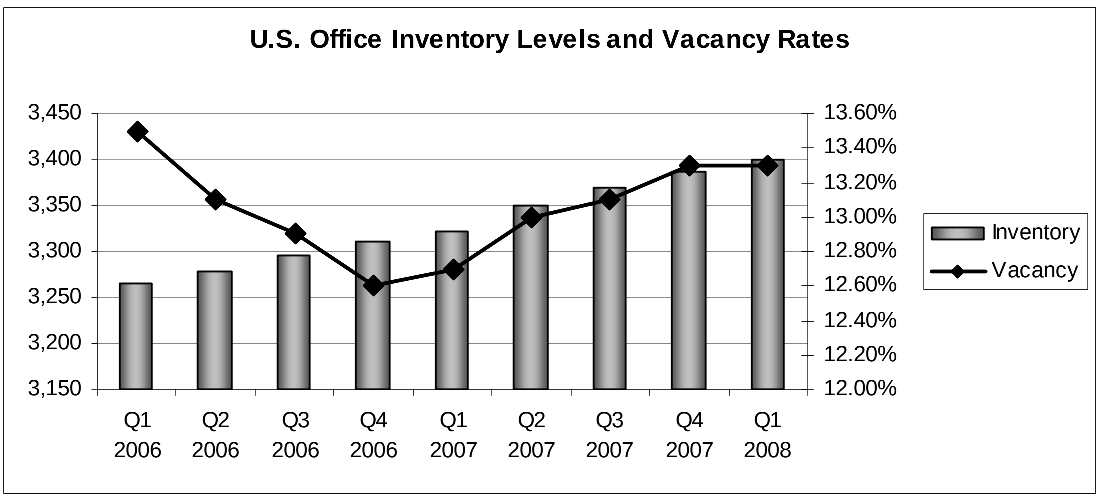
What does the future hold for Portland's retail market? Lower than average retail development per capita and stronger than average population growth estimates as well as improving demographics hint at increasing land prices and contract rents as developers attempt to turn speculations into successful investments. Consumer prices are likely to increase as businesses confront inflating lease rates, and increasing competition. Watch cap rates to signal changing market conditions as interest rates increase and once marginal projects become less than profitable ■

Portland Office and Industrial Update

PSU Center for Real Estate

National Market

Office and industrial rents continue to rise nationwide as the average vacancy rate drops. Office rents saw a record 5.6% growth last year according to the National Association of Realtors (NAR), although that growth is projected to slow to 4.1% this year.[1] NAR forecasts a softening of the market with a steady increase in office vacancy rates due primarily to the predicted 78 million square feet of new construction in 2007 (almost twice the amount in 2005) and a cooling economy. The following chart shows the quarterly average national vacancy rate as well as quarterly inventory levels from 2006 through 2008.



Source: National Association of Realtors® (June 2007)

In many cities, the economics of supply and demand are driving up rents, particularly in coastal markets, many of which are experiencing historically low vacancy rates. In markets lacking this tightness, rents are still increasing due to heavy sales activity at high premiums, which are then being passed on to tenants. NAR reports $95 billion in office trades in the first four months of 2007 as well as increasing prices per square foot and decreasing cap rates. The average price per square foot increased from $160 in 2004 to $250 today. Currently, national average cap rates for Central

[1] National Association of Realtors® (June 2007). These figures do not reflect changes in effective rents, which include concessions made by landlords.

Business Districts are approximately 5.5% and for suburban markets, 7.0%, compared with cap rates in the 8-9% range seen in 2004.[1]

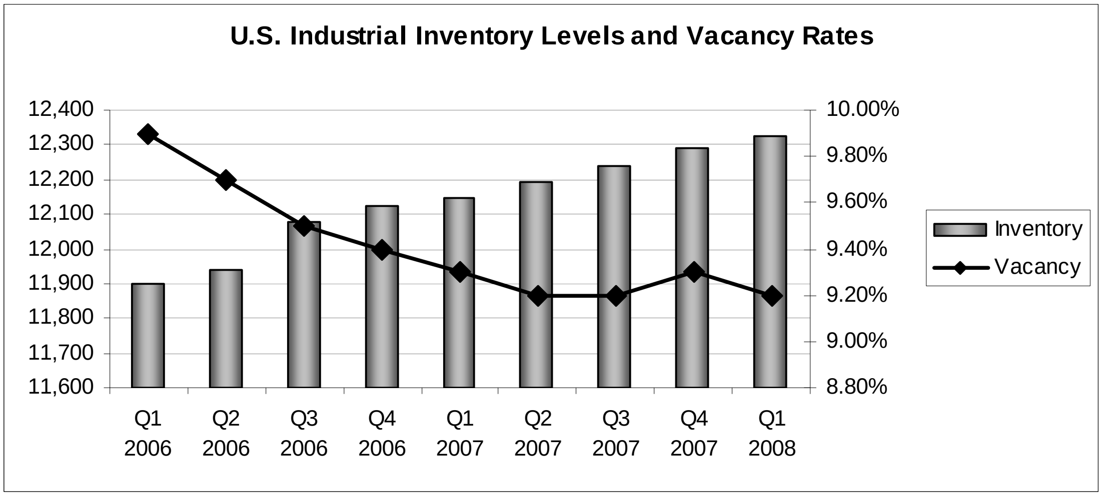
These figures show that investors are willing to pay more for less current income, banking on their ability to pass the premium on to tenants through future rental increases. As a result, many tenants are choosing to relocate to suburban and secondary markets, driving up rents there. Landlords, many of which are now private equity firms, are choosing to endure higher vacancies in order to wait for premium-paying tenants. Unlike their public counterparts, REITS, private equity firms are cash-heavy and unburdened by obligations to report their building vacancy rates to investors.[2]

While 2006 and the first part of 2007 saw a flurry of commercial real estate sales, most notably the sale of the office portfolio of Equity Office Properties Trust, the spate of deals could slow as the cost of debt increases. Although recently the 10-year Treasury yield fell, spreads between commercial mortgage backed securities (CMBS) and the 10-year Treasury continue to increase. The ratings firm, Moody's, further sounded alarms when it decided to increase subordination levels required of riskier bonds in order to receive investment-grade ratings and thus raising the cost of debt even more for riskier loans. The troubles in the residential subprime mortgage market is making commercial lenders skittish—a phenomenon that could dampen the sales pipeline as the cost of debt increases.

Unlike the office market, the industrial market has remained relatively stable with steady growth. In many cities, construction has kept pace with demand without superseding it. The thriving foreign trade sector benefited coastal ports, particularly those with land constraints. The estimated national vacancy rate for industrial space decreased from 9.3% to 9.2% in the second quarter. Rent is projected to grow 3% this year. (However, predictions of slower economic growth and decreased consumer spending will likely soften this market.)

The following chart shows the national industrial vacancy rate falling even as inventory grows reflecting the impact of markets such as the Inland Empire in southern California where demand far outstrips supply.

[1] National Association of Realtors® (June 2007)
[2] Forsyth, Jennifer (July 2007)



Source: National Association of Realtors® (June 2007)

NAR forecasts delivery of more than 165 million square feet of industrial supply this year pointing out that many of these new facilities are replacing older obsolete buildings that have been converted to other uses.[1] In some areas, the tightness in the office market is prompting some office tenants in class B and C space to move into the flex market, pushing vacancies lower in that market as well.[2]

While the industrial market appears to be in equilibrium nationally, there are concerns of over supply in certain markets that have seen large amounts of speculative space, particularly in inland distribution hubs like Chicago, which have ample suburban land and few development restrictions. As mentioned above, the big concern is a slack in trade activity. National Real Estate Investors points out that "a global economy creates both opportunity and risk." The opportunity to construct new facilities to service growing trade volumes always creates the risk of oversupply and vacancy when trade turns sluggish.[3]

Portland Office Market

The pace of office construction in the Portland market quickened this year, with almost 300,000 square feet of office space completed.[4] However, one-third of this space was the built-to-suit RiverEast Center and another one-third fits the classification of 'creative space' as opposed to traditional office space that serves the financial, legal and related industries. Thus, even with

[1] National Association of Realtors® (June 2007)
[2] Flex buildings are typically one to two stories and are versatile enough to be used as office space in combination with light industrial and high tech research and development.
[3] NREI (April 2007)
[4] Grubb & Ellis (July 2007)

significant new deliveries, the choice of office space remains minimal for core office users particularly in the CBD.

This dearth of office space resulted in a low market-wide vacancy rate shown in the table below (although the three brokerage firms represented here show the vacancy rate moving in different directions). The central business district (CBD) remains bullish as downtown Portland has yet to see new office completions. Class A space remains particularly tight and landlords are taking advantage of this by increasing the average asking rental rates to almost $25 per square foot full service, approaching levels seen in 2002.[1] However, approximately 80,000 square feet of space is under construction in close-in northwest, which should alleviate some of the demand pressure in the CBD, although not a significant amount. The most desirable newer spaces city-wide are expected to command rents in the $33 to $36 per square foot range full service.[2]

Office	CB Richard Ellis	Cushman & Wakefield	Grubb & Ellis
Market-Wide Vacancy	11.6%	11.3%	12.3%
Previous Quarter	11.5%	11.9%	12.5%
Second Quarter 2006	11.8%	13.0%	11.9%
CBD and Downtown Vacancy	8.5%	9.5%	9.1%
Previous Quarter	8.9%	10.1%	9.5%
Second Quarter 2006	9.5%	11.5%	10.0%
CBD Class A	4.7%	6.8%	5.6%
Previous Quarter	5.3%	7.1%	6.4%
Second Quarter 2006	6.0%	7.0%	6.7%
CBD Class A Asking Rents	$23.42	$24.75	$24.76
Previous Quarter	$23.38	$23.87	$24.31
Second Quarter 2006	$22.03	$23.06	$22.97
Suburban Vacancy	14.4%	13.2%	14.2%
Previous Quarter	13.8%	13.7%	14.3%
Second Quarter 2006	14.1%	14.5%	13.2%
Suburban Class A Vacancy	N/A	12.6%	10.5%
Previous Quarter	N/A	14.1%	10.5%
Second Quarter 2006	N/A	12.6%	7.8%
Suburban Class A Asking Rents	N/A	$23.38	$25.99
Previous Quarter	N/A	$23.36	$25.50
Second Quarter 2006	N/A	$21.33	$23.33

Source: CB Richard Ellis (CBRE), Cushman & Wakefield and Grubb & Ellis (July 2007). Vacancy rates above include subleases except those reported by CBRE. CBD figures include close-in neighborhoods, except Class A figures reported by CBRE. Class A suburban figures reported by Grubb & Ellis reflect Kruse Way and Washington Square only. All rents are full service. All other suburban figures include Vancouver.

[1] Data from Cushman & Wakefield
[2] Cushman & Wakefield (July 2007)

As a whole, the suburban rental market is lackluster compared with the CBD. The Sunset Corridor is the slowest submarket to recover from the real estate recession in 2001, with a vacancy rate in the low 20's. Grubb and Ellis even report a softening in the suburban market in both quarter-to-quarter as well as second quarter 2006 to second quarter 2007 figures. This difference is due primarily to differences among firms in categorizing the product type of new construction completed.

Some suburban submarkets such as Tigard and Kruse Way mirror the bullish trends in the CBD. Rents in Kruse Way top those of any other submarket at almost $29 per square foot.[1] Whereas Hillsboro and Beaverton primarily serve information and technology firms, the Kruse Way submarket attracts a cluster of financial and real estate firms, with many tenants seeing it as an alternative to the CBD.

Portland Industrial Market

The Portland industrial market is experiencing similar supply and demand trends seen in the CBD office market—land constraints and historically low vacancy rates. Portland's current industrial vacancy rate is the lowest seen in twenty years.[2] The warehouse/distribution market, by far the largest industrial market with over 100 million square feet of inventory, is also the tightest with vacancy in the 4% to 5% range.[3] With average footprints of approximately 100,000 square feet, warehouse/distribution construction requires large contiguous space to accommodate both facilities and truck bays—a resource that is quickly dwindling within the Urban Growth Boundary.

Still, there are several significant speculative construction projects that may address this shortage. An estimated 1.5 to 2.0 million square feet of construction will be completed in 2008, primarily in the Northeast Rivergate submarket.[4] While these new projects will likely be quickly absorbed without significantly impacting the industrial vacancy rate, they will provide tenants and owner-users with more choices.

[1] Cushman & Wakefield (July 2007)
[2] Grubb & Ellis (July 2007)
[3] Based on figures from Cushman & Wakefield and Grubb & Ellis
[4] CB Richard Ellis (July 2007)

Industrial	CB Richard Ellis	Cushman & Wakefield	Grubb & Ellis
Market-wide Vacancy	5.1%	4.9%	5.6%
Previous Quarter	5.2%	5.4%	6.1%
Second Quarter 2006	6.1%	6.5%	7.4%
Warehouse/Distribution	N/A	3.8%	5.1%
Previous Quarter	N/A	4.6%	5.7%
Second Quarter 2006	N/A	5.5%	6.4%
R&D/Flex Vacancy	N/A	9.5%	7.3%
Previous Quarter	N/A	9.2%	7.4%
Second Quarter 2006	N/A	11.4%	10.3%
Asking Monthly Shell Rates	$0.36 to $0.40	N/A	$0.39
Previous Quarter	$0.36 to $0.40	N/A	$0.38
Second Quarter 2006	$0.32 to $0.40	N/A	$0.36
Asking Monthly Flex Rates	$0.85 to $0.95	N/A	$0.81
Previous Quarter	$0.75 to $0.85	N/A	$0.80
Second Quarter 2006	$0.75 to $0.85	N/A	$0.72

Source: CB Richard Ellis, Cushman & Wakefield and Grubb & Ellis (July 2007) Warehouse/Distribution figures for Cushman & Wakefield include manufacturing space, which represents one-fifth of warehouse/distribution space. All rents are NNN.

Leasing in the flex market, concentrated on the west side is still not as strong as the warehouse/distribution market. However, the vacancy rate fell into the single digits, a point where rents begin to accelerate as evidenced by the increases shown in the table above. Most of the improvement in the flex market is due to the recent purchase of the former Komatsu silicon chip plant by Solarworld, taking 470,000 square feet off of the market. Very little in new construction is underway in the flex market and any continued improvement in the office market should spill over into the flex market. Both of these trends should help the feeble flex market which is enduring lukewarm employment growth in the high tech sectors.

Activity at the Port of Portland, which drives a majority of the warehouse/distribution market, started the year with a robust 58% increase in cargo over last year before the surprising news that its largest carrier, the Israeli-based Zim, will no longer be docking at Portland.[1] While a significant blow, the Port continues to show healthy year-over-year growth. Each month from January to June shows an increase, in total tonnage, in TEU's or twenty-foot equivalent units and in the number of vessels that docked at the Port.[2]

[1] Portland Business Journal (July 2007)
[2] Port of Portland (June 2007)

Other significant developments at the port include the expected arrival of the 4th post-Panamax crane in early 2008, which will cater to larger ships and make Portland a more attractive port. In addition, one shipping line, the Yang Ming, is now using ships with double the previous capacity for their Portland shipments. Since they will continue using the same number of ships, the larger capacity is expected to result in a volume increase of 1,700 TEUs.[1]

The industrial market is closely linked to the broader US and global economy, given its heavy reliance on trade activity and consumer demand for goods. With expectations of a slowdown in the economy, the broader US industrial market will be adversely impacted. However, in Portland, where the market has remained tight for so long with little supply to alleviate pressure, there will be a lag between any slowdown in the broader economy and a subsequent impact on industrial vacancy and rents ■

[1] Port of Portland (May 2007)

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