SOUTHWEST MARKETS NEWSLETTER

Sherwood Commerce Center- Phase I - FOR LEASE

JANUARY 2025

As we move into 2025, the Southwest Industrial and Office markets are headed into their third year of slowdown/lackluster performance. That said, this market still has a lot more luster than its surrounding submarkets, which have a lot more of the lack. According to Costar's research, the Portland Metro Industrial Market occupancy declined by 2.9 million square feet, and the office market declined by approximately 1.5 million square feet. This decline only represent 1.5% of the space tracked for the industrial markets. For the office market, this marks the fourth straight year of retreat. In relative terms, the Metros industrial vacancy is approximately 6%, while the punched-in-the-gut office market is approaching 14%.

This macro data hides more ominous tides in the various submarkets. The most eye-opening trend is that Clark County is the only submarket to escape these negative numbers. It registered gains in both sectors. Likewise, Kruse Way was the only office submarket in the Portland area to show positive growth.

The reason for this migration is no secret. Companies are fleeing Multnomah County and its crime and punitive taxing structure. Clark, Washington, and Clackamas County are favorite landing spots for these relocations.

INDUSTRIAL MARKETS

Vacancies in Southwest Industrial space are far less than the vacancies in comparable space in Multnomah County. The disease that began in Multnomah County office space during the 100 nights of riots, combined with the remote work evolution, devastated the CBD office market. The same symptoms caused by many of the same issues have sprung up in the industrial marketplace in Multnomah County.

The vacancy statistics illustrated below highlight this disparity. The industrial vacancies in Portland are generally twice as high as the SW and SE markets. More alarming and illustrative of the disparity is the rental rates. While SW is modestly trending upward, rents in Portland/Multnomah County are reeling. The table shows asking rents, but real-deal rental rates tell a more sinister story. Rents in the Southwest Industrial markets are steady and, if anything, are trending upward. Recent transactions in Multnomah County have been completed at rates 15-20% below those in the Southern markets, and the higher vacancy and lower absorption rates in Multnomah County portend greater disparity to follow.

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For example, a large lease was recently done in the Rivergate area of Portland in a very functional warehouse space with a "shell" rent of $0.65/SF/mo. Conversely, the Sherwood Industrial Park I represent (see back page) is obtaining shell rents in the upper $0.90/SF/mo range. New projects under construction in Hillsboro and Sherwood will be higher still.

The Southwest I-5 corridor and Washington County have generally held up better than their northern neighbor for many reasons: a safer work environment, more local ownership basis, and strong manufacturing/tech companies that have continued to thrive. The Southwest jurisdictions are less hostile to business and boast an excellent employment base augmented by outlying cities.

There is a service in Portland where commercial brokers post requirements for facilities their clients need in specific terms. Often, the post begins with a description of a desired location with the term "No Multnomah County." This trend has measuredly helped buoy Washington, Clackamas, and Clark County's commercial real estate. However, not all the news for the southwest submarket is good. Nike and Intel, the two bulwarks of growth for decades in this region, face significant headwinds, sending a chill through the Beaverton and Hillsboro flex and office spaces.

Notable trends in Southwest Industrial Markets during 2024 were the slowdown in new construction compared to the 2021-22 period, during which, following a nationwide trend, a flurry of new warehouse buildings were brought to market and quickly absorbed by manufacturing and wholesale tenants in Tualatin and Sherwood. The slowdown in overall industrial demand nationwide precipitated this slowdown in new construction. The new space slowdown will continue in 2025, with only three new projects available in Sherwood, Hillsboro, and Tualatin. Together, they will account for approximately 1.2 million square feet of large warehouse space. Demand will need to increase substantially to fill these spaces.

Warehouse Buildings

Overall, The Industrial market is the healthiest of all the commercial real estate sectors, and its future is bright. Specifically, new modern warehouses are still in demand from tenants and investors. A new leased warehouse will command a cap rate (return on investment) of 200 basis points less compared to other product types. Online sales are still increasing; by some estimates, they are now moving towards 20% of all consumer sales. This statistic bodes well for the future of the industrial segment as goods move off the shelves of retail space and into warehouses. Warehouse buildings are by far the most flexible of all space and increasingly house many manufacturing companies; this is especially evident in Washington County, where warehouse buildings provide millions of square feet of facilities for advanced manufacturing/tech companies.

INDUSTRIAL (5K+ SF)

Submarket	Inventory SF	Under Construction	12 Mo NET Absorption SF	Vacancy Rate	Market Asking Rent/SF
I-5 Corridor	31.1M	407K	253K	4.1%	$10.87
Westside, Washington County	24.4M	396K	177K	1.9%	$13.00
Close-In, PDX	20.4M	0	553K	9.5%	$11.80
Clark County	29.5M	1.1M	485K	7.3%	$11.36
N/NE, PDX	81.4M	793K	1M	7.5%	$10.49
Southeast, Clackamas County	28M	0	939K	5.3%	$10.96

Data sourced from CoStar

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Office Markets

The overall office market nationwide is still in a tailspin due to the rise in remote work. It seems like every 90 days, I see an article in some publication saying this trend is going to reverse itself. Examples of CEOs threatening the company's employees with an ultimatum to return to the office are given, and market statistics continue to dispel these headlines.

Every month, office leases expire, and the company renews for a smaller footprint in their existing space or elsewhere. In some cases, the reductions are dramatic. Liberty Mutual Insurance came to mind when it migrated from the Lloyd District to Lake Oswego and reduced its space need from 90,000 SF to 10,000 SF. Some smaller companies even go "virtual," meaning they only work remotely and interface via videoconferencing. Some services have estimated that 30% of office leases signed before this trend have yet to expire, so expect the office market to continue to worsen before it stabilizes.

While office space occupancy, in general, is declining, the effect on our market is much more acute in Portland than in the surrounding suburbs. Like Portland's industrial tenants, office tenants, especially professional firms, flee Portland for the more friendly confines of Lake Oswego, Tigard, and Beaverton. While rents are generally declining in these areas as well, the effect is much less dire than in the Portland office markets. Recently, a well-known Portland building offered $6.00/SF full-service rent as an incentive to locate there. Office vacancies are about twice as high in Portland than in the surrounding suburbs. Major tenants scheduled to depart the CBD in early 2025 are US Bank and Hoffman Construction, leaving behind gaping holes.

If Portland is going to improve, it will need help from the courts, the legislature, and the new city government, which, based on the makeup of the commissioners, seems anything but business-friendly. As I was finishing this letter the newly elected commissioners announced a budget increase to provide for more personal staff for themselves in the face of the city facing a $100,000,000 dollar deficit. The city of Portland is facing an unprecedented crises of its own making.

If you have been downtown in the Portland Central Business District, you will notice a change for the better. There are fewer tents and very little evidence of drug abuse or threatening individuals due to the significant presence of private security hired by businesses and landlords. There is still a shortage of police officers in Portland and Multnomah County. Solving this issue will rectify many of the city and county commercial vacancy problems. In Southwest, the situation is somewhat better, but work-from-home is still an issue that shows no signs of improving. With the exception of Kruse Way, which has proven to be the favored landing spot for companies moving from the core, vacancies are still increasing.

Office space in West Beaverton and Hillsboro, especially, will be walloped in 2025 by the Nike meltdown and Intel's struggles. Nike left nearly a million square feet behind in its contraction.

OFFICE (10K+ SF)

Submarket	Inventory SF	Under Construction	12 Mo NET Absorption SF	Vacancy Rate	Market Asking Rent/SF	Market CAP Rate
I-5 South	8.1M	0	336K	18.2%	$33.50	8.6%
Hwy 217	7.7M	0	155K	17.6%	$29.20	8.5%
Kruse Way	2.5M	0	11.7K	25.3%	$39.97	8.2%
Westside	22.2M	0	133K	6.5%	$31.86	8.6%
CBD	26M	0	355K	33%	$34.50	7.5%
Close-in NW	9.7M	109K	67K	26.8%	$33.13	8.2%
Clark County	10.6M	165K	284K	7.3%	$31.98	8.5%
Close-in Eastside	8.2M	0	25.6K	15.4%	$31.32	8.0%
Eastside	5.1M	0	70.1K	6.8%	$28.52	8.7%
Milwaukie/Clackamas	2M	0	14.2K	9.6%	$31.91	8.7%

Data sourced from CoStar

2025

As I look forward to the new year, optimism reigns in many of the observers I speak to. I wish I could say I feel the same way. The region's headwinds remain: the contraction in two of our largest and most important private employers, stagnant migration patterns (first time in decades), and general leadership and a body politic with business interests far down their list of priorities damper my enthusiasm. Portland and Multnomah County are our two largest markets for office and industrial space, and the value of properties in this area continues to decline as we enter the new year. In addition, the long-hoped-for decline in interest rates seems to be fading.

What perplexes me as I head into my 43rd year as a broker is that the national economy continues to show health in all economic measurements. Yet, this is undoubtedly the worst local market I have experienced during national economic expansion. It resembles a recession in demand for commercial space that runs counter to the robust numbers in the economic indicators.

The good news is that I envision the SW I-5 corridor, including Washington County and large swaths of Clackamas County, will continue to grow, albeit slowly. I see no decline in industrial rents there in the coming year. Likewise, while office rents and occupancy may decline, it will be far less precipitous than its larger neighboring market to the north.

Featured Listings

27100 SW Parkway Avenue, W3

4405 Turner Road

21600 SW Oregon Street

2187 Reed Street

Significant Completed Transactions in 2024 By Stu Peterson

1980 SE 4th Avenue, Suite B
Braber Equipment Building, Canby OR
SF Leased: 37,500 SF

11555 SW Leveton Drive, Tualatin OR
Industrial Land Sold to LAM Research
Acres Sold: 19 AC

SW Hunziker St & SW Wall St, Tigard OR
Industrial Land Sold to the City of Tigard
Acres Sold: 11 AC

18280 SW 108th Avenue
Sold to Lam Research
SF Sold: 40,000 SF