

DUNCAN & BROWN WEST EUGENE INDUSTRIAL REPORT

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In an effort to document market trends with respect to industrial properties, approximately 4.2 million square feet of industrial space located in the West Eugene industrial area was surveyed during October 2006.

This survey is to report long-term vacancy in industrial properties without affecting the measurement by including newly developed buildings that are still in their absorption. All the buildings surveyed are typical industrial structures, rather than specialized buildings.

The general boundaries of the survey are West 11th Avenue to the south, Garfield Street to the east, Belt Line Road to the west, and the Southern Pacific Railroad Line to the north.

The Lane County Assessor's records were relied upon for estimates of building size. The area surveyed represents the heaviest concentration of industrial development in the greater Eugene/Springfield metropolitan area.

The survey is intended to offer a perspective of overall market conditions for the entire metropolitan area. The survey was conducted with a variety of parameters, including building construction type, type of tenancy, and overall building size.

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The 2006 Industrial Survey shows the continued strength of the market indicated by the last several surveys: vacancy rates have decreased across all categories (*All Structures*, *Single-Tenant* and *Multi-Tenant*). The vacancy rate for the *All Structures* category decreased slightly to 2.84% from the 2005 survey rate of 3.04%, which had declined from a 10-year high of 8.53% in 2002. The 2006 survey reflects the continued stable occupancy level of the market prior to September 11 and the recession of the early 2000s. A return to a stable industrial market began five years ago, with this recent study confirming that a strong market is continuing.

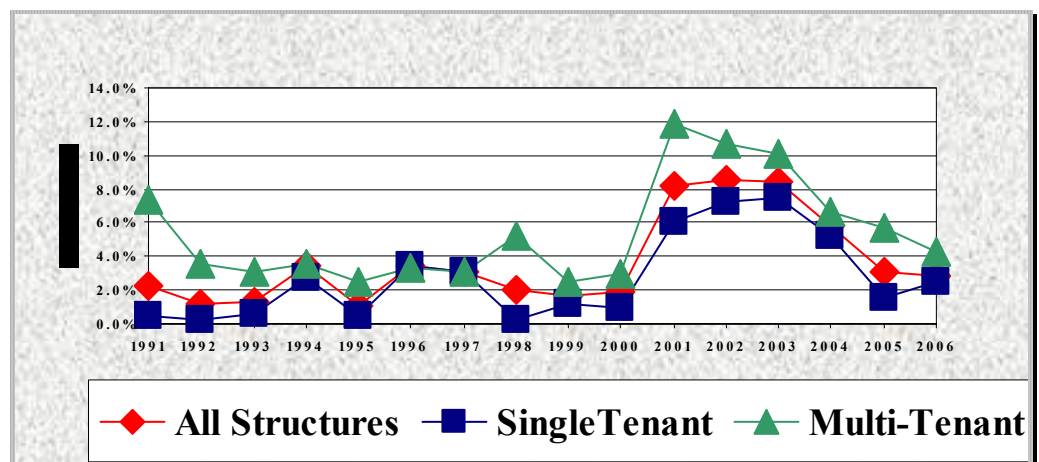
The industrial market in Eugene has had a vacancy rate of 5% or less for the last 15 years, except for a short period, which began in 2001, when industrial vacancy rates increased dramatically. Since vacancy peaked in 2001, there has been a steady decline in vacancy rates to a new historical low for the last 2 to 3 years. There has been a substantial

increase in demand within the industrial market for rentable and owned space.

As was true throughout most of the 1990s, the Eugene/Springfield market experienced considerable construction of new multi-tenant buildings, as well as owner-occupied properties. As vacancy rates increased in 2001 and 2002, this type of construction stopped. Over the last couple of years, there has been a resurgence of new construction. Many newer, better quality industrial buildings were developed throughout the entire market but particularly within the west Eugene area. There are several projects in the pipeline and the trend of low vacancy rates is expected to continue. New construction has been limited in this market because of the high cost of construction, which is not supported by current rent levels in Eugene. Many of the construction projects are for owner/users, who recognize the benefit of ownership versus leasing and show a willingness to accept the

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West Eugene Industrial Vacancy Rates Fall 1991-Fall 2006



Market Analysis (Continued from page 1)

higher cost of ownership. The 2004 survey forecasted that vacancy rates were stabilizing, and the outlook for 2005 was a continued decrease in the vacancy levels. These predictions were confirmed and Eugene has returned to a strong industrial market. The outlook for 2006 was a continued strong industrial market with the beginning of strengthening rent levels. The 2006 study confirms the earlier forecasts: vacancy rates have stayed low.

The surveyed properties are categorized by size and tenancy type — under and over 20,000 square feet and single- or multi-tenant — and vacancy rates are further analyzed.

The vacancy rate for *Single-Tenant* spaces decreased dramatically from 5.25% to 2.49%. The main reason for this large change is the sale of the HMT property on West Third Avenue in Eugene. This vacancy rate has moved up slightly to 2.49% with a newly available 48,000-square-foot building. This category has historically shown a very low vacancy rate, because the tenants in this building type tend to be very stable and long-term. Throughout the 1990s, this category reflected vacancy rates below 4% and in most years was below 2%.

The vacancy rate of the *Multi-Tenant* category shows a continuing downward trend to 4.30% for 2006, down from 5.02% in 2005 and 6.69% in 2004. This category has always shown the highest vacancy rate throughout the history of this survey. This category is really the pulse of the industrial rental market. Multi-tenant spaces are mostly smaller and, as the economy cycles up or down, this category is most affected. Over the last several years, there were usually 35 or more spaces

for rent at any one time. This year that number is down to 15 to 25, again showing the strengthening of this market segment. With general national, regional, as well as local economic indicators showing a continued solid economy, this category is expected to show continued stability in the 2007 survey.

The greatest decrease occurred in the *Multi-Tenant: Less Than 20,000 Square Feet* category, which had shown the largest increase in 2003. The 2003 rate was an all-time high of 16.78%; in 2004, the rate was 10.26% and in 2005 had a rate of 4.97%. The 2006 survey shows a further reduction to 4.45%. In a review of prior survey data, many small spaces were available with a large percentage of spaces in older, modest-quality buildings. As movement begins to occur, the better buildings are occupied first — as tenants begin to shuffle in the market, they look for better buildings to occupy. When asking rents were reasonably low, a tenant could move into a better building for pennies per square foot in additional rent. A review of the raw 2005 data certainly reflects this type of movement was occurring, but it has now slowed. *Multi-Tenant: Over 20,000 Square Feet* spaces tend to be in better quality buildings, and this category showed a modest decrease in vacancy rate from 2005 to 2006 of 6.21% to 4.63%, respectively. This category is still considered balanced in terms of general supply and demand.

The 2002 survey data suggested that possible stabilization was beginning to occur. The results of the following three surveys supported this forecast. The improvements made in market vacancy rates over the past years were seen as the beginning; now the 2006 survey confirms that

the market has returned to equilibrium and appears to be functioning as a more typical Eugene industrial market. Brokers interviewed during this process have shared a continued optimism, and the reduction in vacancy across all industrial property categories indicates a significant change suggesting the West Eugene industrial rental market is substantially improved.

Throughout the troubled vacancy rate times, the market for buying quality industrial property stayed very tight. In fact, as correctly priced industrial properties became available, both users and investors quickly acquired those properties. Users prefer to acquire existing properties for two reasons: 1) in this market, purchasing existing facilities

STRUCTURE TYPE	STRUCTURE SIZE	VACANCY RATE
All Structures	< 20,000 sf	6.37%
All Structures	> 20,000 sf	0.42%
Single-Tenant	< 20,000 sf	9.61%
Single-Tenant	> 20,000 sf	0%
Multi-Tenant	< 20,000 sf	2.22%
Multi-Tenant	> 20,000 sf	1.29%

Market Analysis (Continued from page 2)

is substantially cheaper than the cost to build new; 2) users of industrial properties are not real estate developers and are not interested in the time-frame necessary to acquire permits and construct a new building. As this market continues to strengthen, the prices of existing facilities will continue to increase at a rapid pace. The decline in the rental market did not greatly affect the price of properties being purchased. The quick acquisition of properties and the lack of inventory, driven more by the requirements of tax-deferred 1031 exchanges, help maintain good price levels. In all likelihood, if there is not a change in the tax code, exchanges are still going to drive a large portion of property acquisitions.

Vacancy rates of other geographic areas were sampled. The Prairie Road/Highway 99/River Road area, which had seen an increase in vacancies, has improved recently. The vacancy levels reflected those in the broader west Eugene area. The small market areas of Eugene and Springfield do tend to reflect the same dynamics overall and, as one area shifts, all areas tend to shift.

The Springfield area, which reflected a vacancy rate increase from 2001 and an additional increase in 2002, did begin to stabilize in 2003. The Springfield market now reflects rates similar to west Eugene market. Brokers working in that market have indicated a substantial increase in activity.

Rental Rates

A bright spot in the 2005 survey was the realization that rent levels throughout the market are beginning to increase. This trend is continuing as based on the 2006 interviews. All those interviewed expect the rent increases to continue. Most leases are written for terms between three and five years; many of these leases are now being rewritten and are reflecting this tightening market, with higher rents being negotiated. As mentioned in the 2005 report, brokers had indicated a general reluctance for tenants to cross the threshold of 40 cents per square foot. As would be expected, the newer and/or better-quality buildings are best able to achieve the higher rents initially. As these rent levels have continued to increase throughout the market, second tier rent levels are increasing.

As mentioned earlier, new construction costs have increased dramatically over the last two years as the prices of concrete and steel have risen. In the Eugene/Springfield market, rent levels have not increased at a rate commensurate with the increased cost of construction. When viewing other markets such as Medford, Bend and Salem, general rent levels in those markets have increased as the cost of construction has risen. Most likely in the next few years, rent levels in this market will begin to increase as with other markets around Oregon, becoming more in line with the cost of construction.

As this survey was conducted, brokers indicated that it is becoming more difficult to find good quality space for tenants and, therefore, most assume there will be new construction within this market area. The one difficulty everyone mentioned is the lack of available land for the construction of new properties, as Eugene is beginning to experience a very limited supply of buildable industrial sites.

The sale activity of industrial properties has been reasonably good over the last 24 to 36 months. The sale price per foot for most of these buildings has been increasing at a quicker pace than the rise in rental rates, which would suggest one of two possibilities: either buyers are expecting increases in rent levels in the near future or, more likely, with a lack of available inventory to purchase, people are being forced to buy properties at higher prices and accepting lower returns. These lower returns are being accepted because of the maintained low interest rates.

This survey strongly indicates the softness in the industrial market is over. The recovery appears to have occurred and industrial lease rates, as well as vacancies, have return to the pre-2000 levels. Over the next 12 to 24 months, rent levels will likely continue to increase and vacancy will continue to tighten. There is a need for the development of additional industrial properties in all categories of size and quality. The main limiting factor to the expansion of industrial space is the limited land supply. Rent levels will continue to increase; as new construction occurs, rents will have to increase to levels above 50 cents per square foot, which has generally not occurred in this market.

SINGLE-TENANT STRUCTURES

	TOTAL AREA (sf)	VACANT (sf)	VACANCY RATE
1991	2,536,620	12,240	0.48%
1992	2,546,795	5,000	0.20%↓
1993	2,535,795	15,000	0.59%↑
1994	2,535,795	68,208	2.69%↑
1995	2,535,795	10,720	0.42%↓
1996	2,568,178	87,436	3.40%↑
1997	2,560,858	80,193	3.13%↓
1998	2,627,862	6,600	0.25%↓
1999	2,614,442	30,032	1.15%↑
2000	2,539,530	24,547	0.97%↓
2001	2,688,330	163,040	6.06%↑
2002	2,688,330	195,897	7.29%↑
2003	2,688,330	201,615	7.50%↑
2004	2,681,547	101,254	5.25%↓
2005	2,663,723	40,833	1.53%↓
2006	2,663,723	77,440	2.91%↑

MULTI-TENANT STRUCTURES

	TOTAL AREA (sf)	VACANT (sf)	VACANCY RATE
1991	891,596	66,009	7.40%
1992	1,090,340	39,326	3.61%↓
1993	1,109,540	34,450	3.10%↓
1994	1,109,540	39,326	3.54%↑
1995	1,159,940	29,250	2.52%↓
1996	1,287,176	43,404	3.37%↑
1997	1,320,496	40,100	3.04%↓
1998	1,505,830	77,968	5.18%↑
1999	1,519,811	38,408	2.53%↓
2000	1,517,123	44,480	2.93%↑
2001	1,548,458	183,300	11.84%↑
2002	1,548,458	165,702	10.70%↓
2003	1,548,458	156,052	10.08%↓
2004	1,513,511	80,419	5.31%↓
2005	1,531,335	87,285	5.70%↑
2006	1,531,335	25,623	1.67%↓