



**City of
Portland, Oregon**
Bureau of Development Services
FROM CONCEPT TO CONSTRUCTION

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BDS Financial Advisory Committee

Meeting Notes
Tuesday, April 27, 2021

FAC Members Present:

Jeff Renfro, Multnomah County
Jerry Johnson, Johnson Economics
Mike Paruszkiewicz, Northwest Natural
Mike Wilkerson, ECONorthwest
Paul Delsman, DRAC
Peter Hulseman, Northwest Economic Research Center
Sean Green, DRAC
Tom Potiowsky, Portland State University

City Staff Present:

Andy Peterson, Special Projects, BDS
Beth Benton, Property Compliance Manager, BDS
Brenda Fahey, Technology & Continuous Improvement (TCI)/Recruitment & Training Manager, BDS
Brian Landoe, Analyst, Parks & Recreation
Claudio Campuzano, Finance, Property & Technology Manager, Parks & Recreation
David Kuhnhausen, Permitting Services Manager, BDS
Dave Tebeau, Residential Inspections Services Manager, BDS
Doug Morgan, Plan Review Services Manager, BDS
Elliot Lisac, Financial Analyst, Water
Elisabeth Reese Cadigan, Manager, Bureau of Environmental Services
Elshad Hajiyev, Deputy Director, BDS
Kathy Lyndon, Financial Analyst, BDS
Kim Tallant, Land Use Services Manager, BDS
Kyle O'Brien, Budget & Finance Manager, BDS
Ray Galinat, Financial Analyst, BDS
Rebecca Esau, Bureau Director, BDS
Sarah Huggins, Analyst, Parks & Recreation
Tammy Croll, BDS Training & Workforce Development (Meeting Host)
Tyler Berry, Financial Analyst, PBOT

Handouts

- Business Continuity Plan Summary
- Non-Cumulative Cost Recovery Report
- Workload Measures Report
- Large Projects – 6-Month Comparison
- Programmatic Growth Rates

1. Welcome

BDS Director Rebecca Esau welcomed Financial Advisory Committee (FAC) members and City staff and convened the meeting. Director Esau expressed appreciation for the committee members in attendance and their input. The focus of the meeting will be looking ahead of what is on the horizon for the Portland construction industry.

2. BDS Finances & Financial Planning Update

Bureau's Current Financial State

Deputy Director Elshad Hajiyev provided an overview of the meeting and explained that the purpose of this meeting is to get insights from FAC members on the economic outlook and development in the City of Portland.

Kyle O'Brien explained that the overall financial picture has not changed much since the last FAC meeting in January 2021. The monthly revenue for BDS is very volatile and depends on large project applications coming through each month. This fiscal year the lowest monthly cost recovery rate was 47 percent and the highest was 98 percent. BDS is operating at an average 70 percent cumulative cost recovery rate for FY 2020-2021 through March 31, 2021.

At the end of March 2020 when the pandemic began, BDS had a reserve balance of \$85.5 million. A year later, in March 2021, the reserve balance declined to \$61.5 million. BDS is drawing on average two million dollars per month from reserves. To reduce the draw on reserves to a level which can be sustained through the downturn, BDS implemented cost saving measures (Citywide mandatory furloughs, voluntary furloughs, voluntary schedule reductions, voluntary severances, and layoffs). Effective March 1, 2021 there were 11 layoffs in the workforce. The reserve draw was \$861 thousand in the month of March.

Overall, the demand for services are declining which impacts BDS' financial situation. Current economic conditions and the pandemic have resulted in less large project activity. Historically, large project activity makes up between 20 to 50 percent of BDS revenue depending on the year. Workload levels are down across the board, and the **Large Projects – 6 Month Comparison** handout shows large project valuation down 57 percent year over year. BDS is not anticipating a quick revenue rebound.

3. Current Economic Trends Discussion

Economic Outlook Discussion

Kyle began the economic outlook discussion by asking for the committee's economic expectations now compared to the last the time we met in January 2021 and potential effects on development in Portland. There has been a 15 percent rise in the cost of construction and availability of materials has been a concern. The construction industry is seeing as much as three times slower delivery of materials. In addition to low availability of materials due to COVID-19 related supply chain disruptions, the new Amazon fulfillment center and data center development are further exacerbating construction material cost and access issues. While there is overall pent-up demand, concern was conveyed that high costs may lead to a stall in construction activity. Although we are coming out of the pandemic due to vaccines, the timing of a potential construction stall is still unknown. Additionally, due to media exposure of sustained riots and continued property destruction, Portland has a long way to recover its perception as a desirable place to invest.

Elshad asked committee members what they see happening in the next year or so with interest rates/inflation and potential effects on new construction activity. The committee does not believe inflation will be a long-term concern. Inflation typically occurs when there are rapid increases in labor

costs. The materials side of construction costs has increased and are this is expected to continue. Labor costs are not expected to increase significantly as federal programs wind down.

Multi-family

The current multi-family sector is overbuilt and is experiencing increasing construction costs. Additionally, rental rates have been stagnant for about five years in the urban areas. Furthermore, approximately 2,500 units are in progress to be complete in the Northwest and downtown core. The prospect of rising cap rates may also apply downward pressure to development. Rents in the suburbs are escalating at six to seven percent in the last several months. These current trends favor multi-family development shifting to suburban areas as people are looking for more space and lower price per square foot.

Office/Retail/Restaurant

The office space market has not changed since we last met in January 2021—banks are hesitant to fund downtown office space projects due to the high level of uncertainty. Currently office space is overbuilt with less demand for space due to increased telework. There may not be further development for the next few years. While overall sentiment has moved away from full time telework, many workers still desire to work at least part from home, which should lead to a gradual recovery of existing office space. Even as workers come back into the downtown core, employees teleworking will create headwinds for the recovery of the retail and restaurant industries.

As we overcome the public health crisis, the amenity value and demand still exist in downtown Portland with solid evening cultural activities. The data confirms that as soon as restaurants, concerts, and other amenities open back up people show-up. This pent-up demand coupled with potential American Rescue Plan Act (ARPA) & restaurant recovery programs could help with general recovery of existing space but will most likely not translate into further development in the near future. According to restaurant industry groups, high end estimates show that forty to fifty percent of restaurants have been lost during the pandemic. The end of the eviction moratorium has the restaurant industry concerned of additional losses.

For further analysis of business closures, Mike Wilkerson with ECONorthwest recommended a few data sources such as Prosper Portland for data on business level activity and the Quarterly Census of Employment and Wages (QCEW).

Economic Recovery

As we all look forward to an economic recovery, an important question is how the City of Portland will perform compared to the surrounding Metro. Another question is if pent-up demand can offset increased costs and lack of raw materials. There is also the issue of Portland rehabilitating its national image to attract federal and regional investors.

While there are government programs such as ARPA, President Biden's Infrastructure and Families Plan, and landlord compensation funds that may help with the general economic recovery, the effects will largely be determined in how local jurisdictions utilize available funds. There are some small county projects (behavioral health centers, clinics, libraries, etc.) stemming from federal funds; however, many large projects are outside of the City of Portland. Regarding future infrastructure projects in the pipeline, there is the possibility of a new Burnside Bridge project in the next decade.

In the last financial cycle, all sectors had record high activity all at the same time. As a comparison to the current environment, this kind of rebound is highly unlikely to happen again especially with commercial

corporate campus expansions, office, and hotel sectors. This time around, the recovery is expected to be industry specific— the IT data centers, and warehousing sectors will catch-up with the contained demand while other sectors may never recover to levels prior to the pandemic. The committee's expectations for the construction industry recovery timeline remains the same as when the FAC last met in January 2021. There was already a decrease in land use reviews prior to the pandemic. In the next one to two years, Land Use applications are expected to recover.

Over the next two to three years, multi-family is expected to lead the recovery. Minimal recovery is expected in the commercial/office space and no recovery is expected in the hospitality sector. Additionally, there may be a shift from larger centralized development to smaller projects located in neighborhood hubs.

Recommendations

The current BDS funding model is counter-cyclical being focused on pre-paid fees for service. The committee recommended seeking out General Fund or other alternative funding sources in addition to these fees for service to make revenue collections less volatile. BDS cannot change market demand; therefore, it is important to maintain quality level of service to the public.

The committee also recommended that recovery models be industry specific, rather than based on a date expectation for all industries.

Meeting notes prepared by Kathy Lyndon, and Ray Galinat, BDS