



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

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Economic Outlook

December 2016

The United States economy has continued its moderately paced expansion over the past year. In November 2016 unemployment rate measured in at 4.6%, down from 5.0% during the same month of the previous year. Though the difference is slight, broader measures of unemployment including workers employed part time for economic reasons have also declined, indicating a healthy labor market. After over 7 years of economic expansion it appears the economy is finally at or very near full employment. Recent gains in wage growth also affirm the overall strength of the labor market.

United States real GDP is growing, though at a slower pace than during previous economic expansions. Reasons for the tepid growth rates are numerous. Demographic changes to the economy over the past decade produced lower than expected growth rates as baby boomers move into retirement. The next large demographic cohort, the millennial generation, has yet to enter its prime wage-earning years. Most recently, the struggling oil market and relative strength of the dollar have produced a significant drag on the economy. However, at the recent December 2016 Federal Open Market Committee (FOMC) meeting, the Federal Reserve decided the economy was strong enough to warrant an increase in the Fed Funds rate for just the second time since the recession. Further rate hikes are expected in 2017, though this will be dependent on incoming data presenting a favorable economic outlook.

Much like the national economy, Oregon has also experienced economic growth. The November 2016 unemployment rested at 5.0%, down from 5.6% of a year earlier but up slightly from 4.5% in May 2016. Unemployment in the Portland Metropolitan Statistical Area (MSA) has followed trends similar to the state economy. In October 2016, the unemployment rate was at 5.0%, down from 5.3% of a year earlier but up from a post-recession low of 4.2% in March 2016. The recent increase in unemployment was at least in part due to discouraged workers re-entering the labor force. The overall labor market remains very strong. The Oregon and Portland economies are typically more volatile in comparison to the nation in its entirety, and can see increases in unemployment rates despite decreases nationwide. Looking forward, Oregon faces headwinds similar to the national economy. A strong US dollar and weak global demand has the potential to adversely affect the manufacturing sector, dragging on growth.

The struggles of the housing industry in relation to the financial crisis are well documented. Fortunately, the Portland MSA has largely recovered from these woes. More recently the focus has been on affordability. Existing home sales have been robust and home prices are rising. Multifamily construction has continued to grow, and single family construction is trending upward, though supply constraints still exert upward price pressure. The dearth of new home construction following the financial crisis contributed to an overall undersupply in homes. If



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developers are able to build new homes to meet demand, there should be some relief in upward price pressure to more sustainable levels. If significant increases in new home construction do not materialize, affordability problems will persist. Long-term, one challenge facing the City of Portland will be to meet the housing demands of the millennial generation as they transition from renting to home ownership.

Recent years have seen exceptionally strong growth in the multifamily sector. Following the financial crisis, individuals and families unable to afford ownership transitioned into the rental market. This contributed to low vacancy rates and rising prices, spurring development. Multifamily development growth rates are still positive despite the wealth of units developed, though there are signs development is leveling off somewhat at the current high level. A key financial concern for the bureau in the coming years will be monitoring revenue from the multifamily sector. Fortunately, population growth estimates for the Portland MSA suggest the city will continue to gain from inward migration, increasing housing demand and decreasing the risk of overbuilding.

Historically, the bureau has obtained significant revenues from large projects, and this will continue in the future. The bureau technically classifies large projects as those with at least \$3 million in valuation, while also tracking projects valued over \$10 million and \$20 million. Large multifamily developments have constituted the vast majority of large project activity at the bureau during the economic recovery. The multifamily market remains strong; however, BDS will monitor the health of the industry going forward and determine if large project activity in this area is sustainable. The bureau is also concerned with the impact of the new City of Portland Inclusionary Zoning (IZ) policy on multifamily construction, slated to begin in February 2017. Economists are in general agreement that IZ policies, if not structured with the proper incentives, have the potential to restrict housing supply.

Most economists agree the US economy will experience further growth in the 2017 calendar year. However, there are significant risks to the economy that provide uncertainty to economic projections. A strong dollar and weak global demand for exports both present significant challenges going forward. Furthermore, the bureau can potentially experience revenue volatility amid an aggregate economic expansion. Large project activity contributes to this volatility, as their timing and size are difficult to predict. In addition, the construction industry does not necessarily expand and contract in conjunction with the aggregate economy. The economy is larger, more diversified, and therefore more stable than any specific industry. These risks aside, current economic conditions and recent data suggest the bureau will be on solid financial footing in 2017.