NAI Black’s roots have been in Spokane for over 50 years. We’re committed to being an active partner in the Inland Northwest’s great history and its vibrant future. NAI Black is proud to manage, lease, and market for sale commercial real estate properties throughout Spokane and the region. We look forward to our continued role in building a dynamic and vital Inland Northwest.
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Another Great Year for NAI Black

Last year, I reported that “we sailed through 2014” with a record year of transactions completed on behalf of our clients, which resulted in a profitable year for our company. Well, 2015 was also an outstanding year for NAI Black. We helped our clients achieve their real estate goals in an unprecedented number of ways. It truly was another year we hit on all cylinders.

Our Coeur d’Alene office, which has grown to four brokers, has expanded our ability to serve our clients and added to our success as a company. The 25 brokers in our downtown Spokane office accomplished their goals and enjoyed the success of serving their clients well. Some deal highlights for the year included arranging an 80,000-square-foot build-to-suit transaction for Comcast in Liberty Lake with an aggregate rent of over $13 million. That new office will create 650 new jobs for Spokane County. Another major project was the lease-up of Regal Plaza (Target development) on Spokane’s south side. We also had several major building sales in 2015, including the former Nut Factory building and the Ashley Furniture building along I-90. Overall, our retail, industrial, and office leasing transactions were up for the year.

Thank you to Black Commercial President Jeff Johnson for all your dedication and hard work in directing our successful team of brokers. I would encourage our readers to invest in Jeff’s book on real estate investing titled Cash Flow Forever. It’s a great read!

Our property management company, Black Realty Management, had a wonderful year as well. Kim Sample, Vice President of Multifamily Operations, continued to provide outstanding service to existing clients and also secured a number of new accounts for our company. We now manage almost 3,000 apartment units. The commercial side of the management business, led by President Tom Hix and Associate Vice President David Wright, continued to maintain high occupancy and low expenses for our clients.

NAI Black’s accounting staff, led by CFO Gloria Ries, continues to do an amazing job for all of our clients. Our maintenance company...
continues to flourish, saving our clients thousands of dollars on routine maintenance assignments.

Bryan Walker, President of Black Development, continues the planning of the former Painted Hills Golf Course, a 100-acre property in the Spokane Valley. In addition, we finished up Crosby Estates and completed another phase at our Twin Bridges subdivision, both located in the Valley. We are really excited to be working on another large residential subdivision project in Rathdrum, Idaho. On the commercial side, we are working on several new retail projects and recently completed a new Chipotle build-to-suit in Coeur d’Alene, Idaho.

It was an honor to once again be selected by readers of the Inland Business Catalyst Magazine as the best commercial real estate company in the Inland Northwest, as well as to be listed as the largest commercial real estate firm in the area by the Spokane Journal of Business. Additionally, we are thankful to be selected by our franchisor, NAI Global, as one of the top companies in NAI, which is the single largest network of independently-owned real estate companies operating throughout the world. In an effort to give back to our community, we are sponsoring Bemiss Elementary School in the Hillyard neighborhood through a program called Bite 2 Go, which provides weekend meals to children in need throughout the school year.

Thank you to all of our clients, customers, loyal staff, brokers, and employees. You are simply the best! We could not do it without you. It’s really fun for me to come to work and start my 36th year in the business leading this fine company into the future.

David R. Black
NAI Black, Chief Executive Officer
With Vacancy Rates Down, Spokane Retail Looks Great for 2016

The Spokane retail market is poised for a strong 2016. In 2015, we saw continued absorption of quality vacant spaces in high-traffic areas and increased development by new tenants to the market.

The Central Business District (CBD) saw vacancy rates continue to tighten from 9.6% in 2014 to 9.5% in 2015. Recent average retail rental rates were $13.67, but the limited number of Class A sites now have landlords demanding over $20 per square foot NNN. The opening of the Grand Hotel has expanded the retail core to the east with the opening of Urban Outfitters adjacent to River Park Square and Carhartt announcing plans to open its second store in Washington State and its first store in Eastern Washington in the Bennett Block building. River Park Square continues to have an impressive tenant roster including Nordstrom, Apple, and The North Face, all of which bring shoppers to downtown Spokane. Macy’s closing creates a challenge for the CBD, but also provides the opportunity to bring a new national tenant to Spokane to further anchor the downtown shopping experience.

North Spokane continues to be the first market in which most retailers look to locate based on the strong demographics and traffic counts on Division Street. Vacancy decreased from 13.8% in 2014 to 11.5% in 2015, and average rental rates increased from $13.27 to $16.24. A limited supply of available space has led to more ground leases. In addition, landlords with top sites willing to do a build-to-suit are able to command rents up to $35 per square foot NNN. Costco’s relocation further north near the entrance of the North-South Freeway shows the company’s faith in the Washington legislature to fully fund the North-South Freeway and their confidence in North Spokane’s future growth and expansion. Further demonstrating this trend, Trader Joe’s and Natural Grocers are set to open their first North Spokane locations in 2016.

The South Hill remains one of the most difficult markets for retailers to enter due to high barriers of entry and the lack of available space for lease.
Vacancy is still the lowest of any trade area at 4.2% with average rental rates at $18.50 per square foot and new construction rental rates as high as $33 per square foot NNN. The successful lease-up of Regal Plaza at Palouse, anchored by Target, continues to be a beacon drawing developers and retailers seeking to find new opportunities to build successful retail developments to satisfy tenant demand.

The Spokane Valley saw its vacancy rate tighten from 8.3% in 2014 to 7.2% in 2015, and average rental rates increased from $11.71 to $12.28 per square foot. Panera Bread opened its first Spokane location off Sullivan Road near the Spokane Valley Mall and continues to draw big crowds as a hot new player in the market. The Panera Bread property was sold to an investor at a sub 5% capitalization rate in 2015, showing that investment-grade tenants and the demand for quality real estate returns has brought historically low cap rates across the mountains to Spokane.

West Spokane is seeing strong activity even as everyone is on pins and needles waiting for word from the Governor to see if he will approve the Spokane Tribe’s planned Hard Rock Hotel & Casino. The vacancy rate for the West Plains is down to 7.4% and recent rental rates are up to $15.81 per square foot. The announcement of Grocery Outlet and Dollar Tree in Airway Heights is proof that the West Plains is a growing market for retailers and retail developers to consider.
A Light at the End of the Spokane Office Market Tunnel

Eastern Washington and Spokane job growth showed positive gains in many sectors of the Inland Northwest economy in 2015, and this growth is expected to continue in 2016. The Spokane office market experienced slow improvement during 2015 with vacancy rates remaining flat and rental rates slightly improving. Landlords are only beginning to see some light at the end of what has been a seven-year tunnel. Tenants continue to enjoy a world of rental concessions and tenant improvement packages. New construction is still slow, but we have seen positive signs with the entry of a new 80,000-square-foot call center building for Comcast and a new 44,000-square-foot building for Next IT. We expect an increase in demand for office space in the coming year and the market should shift to be more in the landlord’s favor. The overall office market was flat in 2015 with absorption at 100,256 square feet. Vacancy was up slightly from 15.3% in October 2014 to 15.8% in October 2015 (based on a survey of 542 buildings having 13,784,376 total square feet, with 2,175,145 vacant square feet).

Office

The overall CBD market survey consisted of 71 buildings containing 3,099,567 total square feet. Market vacancy increased from 397,133 square feet in October 2014 to 485,131 square feet in October 2015, with negative absorption of 1,953 square feet. In looking at this segment in terms of building “class,” Class A vacancy was 11% in 2015, which was up 0.94 basis points from October 2014. Class B vacancy was 19.7% in 2015, but the average recent rental rate increased from $14.47 to $17.62 per square foot. Class C vacancy decreased from 15.1% in October 2014 to 9.1% in 2015. The CBD office space vacancy increase was mostly due to the relocation of downtown office tenants to periphery and Spokane Valley office markets.

The suburban office sector showed no strength with vacancy increasing from 16.7% in October 2014 to 17.5% in October 2015.
Medical Office

Change remains the key constant in the Inland Northwest healthcare sector. National health insurance giant, Kaiser Permanente, announced earlier in December 2015 that it has agreed to acquire Group Health Cooperative. Providence Health Care has reached an agreement with the Catholic-based health system, St. Joseph Health, to combine both systems into a single network. Both hospital executives are upbeat and anticipate positive changes and growth in their industry in 2016.

The medical office market was strong in 2015, with vacancy decreasing from 13.2% in October 2014 to 10.2% in October 2015. Absorption for this period was 158,853 square feet. Rental rates increased from $25.56 to $26.02 per square foot (or 2% growth).

Washington State University (WSU) College of Medicine continues to work towards their medical school accreditation. WSU hopes to have their charter class by fall 2017. The School of Medicine’s location in the heart of Spokane will bring a large economic boost to the city and fuel an already dynamic medical community.
Low Vacancy Rates and an Increased Demand Create a Solid Market for Industrial Space

NAI Black and its market report partners surveyed 28,441,583 square feet of industrial space contained in 1,248 buildings in our fall 2015 survey. The average vacancy rate for the entire survey was a low 4.8%, down from 5.9% for the same period in 2014. This is the first time since the Great Recession that industrial vacancy rates have maintained a rate under 6% for a consecutive 12-month period. With the low vacancy, rental rates are on the rise.

The survey also revealed a substantial increase in recent rental rates in both industrial office and warehouse space. In fall 2014, the average rental rate for industrial office and warehouse space per square foot per month was $0.52 and $0.30, respectively. In the same period in 2015, industrial office rates rose to an average of $0.78 per square foot per month, while warehouse rates hit $0.39 per square foot per month. With an improved market and increased demand for industrial space, landlords no longer need to provide concessions like free rent and tenant improvement dollars to fill space. As higher rates become the norm, it should spur developers back into action and increase the sale of industrial land.

In 2015, there were a number of significant industrial land sales to both developers and users. A developer purchased 16 acres in the West Plains for a build-to-suit for an automotive parts distribution company new to the Spokane market. With the lack of available space, a build-to-suit was the tenant’s only option. The land was purchased for $2 per square foot and the developer constructed a 250,000-square-foot building for the new company. Another investor/developer purchased 10.9 acres on Trent Avenue just east of Sullivan Road for $1.58 per square foot. He plans on developing an RV storage facility on a portion of the property and will subdivide the remaining site into a small industrial park called TAPA Business Park. He will have six industrial lots for sale in the park for owners and users.
There was a low supply of industrial buildings for sale in 2015 with sales ranging from $56 to $63 per square foot. A tenant at the Spokane Industrial Park wanted to purchase and own a building, but with the lack of available properties for sale on the market, their only option was to buy land and construct a new building. The user found an 86,000-square-foot industrial site on North Haven Street and purchased it for $280,000. Within a few months, the user had a brand new concrete tilt-up building from which to operate their business.

In 2014, the legalization of marijuana (I-502) had a major impact on the absorption of vacant industrial space. It was predicted that 50% of the marijuana growers would fail in business and bring a substantial amount of warehouse space back on the market. Through 2015, that hasn’t been the case. Successful growing operators have taken over any operations that have failed and have kept that warehouse space off the market. There could be additional fallout as the marijuana market adjusts and matures, potentially adding industrial space to the market in 2016.

With low vacancy rates and an increased demand for space, 2016 will be a solid market for owners of industrial buildings and a market of increasing rents for tenants.
“Rental rates are increasing as more businesses want to take advantage of the positive momentum and locate downtown.”

Events, Conventions, and New Businesses Mean Downtown Spokane Is Poised for Growth

Downtown Spokane continues to grow and be a vibrant place to work, shop, dine, and have fun. This growth and the addition of new businesses to the downtown core has increased retail sales and created a lot of positive activity in the area. Vacancy rates are declining and rental rates are increasing as more businesses want to take advantage of the positive momentum and locate downtown. All of this activity will be the catalyst for future entrepreneurial real estate ventures.

Retail leasing activity has steadily increased over the past two years. Quality national retailers such as Anthropologie, Urban Outfitters, Sephora, Athleta, Lululemon, and Carhartt have leased space or expanded downtown. Each of these companies wants to capitalize on the growing number of visitors and shoppers flocking to downtown Spokane. Emblematic of these emerging market trends (and what will add to a substantial increase in visitors and shoppers) is the opening of the new 716-room Grand Hotel, the expansion of the Convention Center and River Park Square, and the coming $64 million facelift to Riverfront Park. With these improvements, retail space in the downtown core is being leased up as quickly as it becomes available. Retail space is limited and only a few key space opportunities remain. One of those limited space options is a build-to-suit on the parking lot adjoining Bennett Block. Expect to hear an announcement in 2016 of a game-changing national retailer opening on this site. Spokane retail rental rates are on the increase with lease rates ranging from $24 to $30 per square foot net in the core, and $14 to $16 per square foot net outside the core.

In regard to office leasing, downtown lease rates have remained flat for many years. This trend is starting to change as more office businesses...
want to locate downtown where the action is. In addition, many young entrepreneurs and start-up companies are attracted to office space in the renovated older buildings downtown that offer an exposed brick and beam atmosphere. Creative developers and investors answered this call in 2015, investing in Spokane’s rich abundance of historic brick buildings. Notable redevelopment included the former Dutch’s and Huppin’s buildings, as well as the Bennett Block, Globe, Hutton, and Cutter buildings. We expect standard office lease rates to remain steady through 2016. Space in unique and desirable rustic buildings will experience increasing rental rates, which we expect to advance beyond $19 to $20 per square foot by the end of 2016.

In addition to the rehab of downtown’s historic office buildings, a number of historic industrial buildings have been rehabbed and converted to office space. One example of this is the 27,000-square-foot Cold Storage Building at 116 West Pacific Avenue. This building was refurbished for office use and is in the process of being purchased by a downtown company. The next major building that is perfect for renovation is the Macy’s building. Macy’s recently announced the closing of their downtown Spokane store, which is a loss for downtown shoppers, but could result in another major renovation project. Much of the upper floor space in the building has sat vacant for years. With its key location in the downtown core, the Macy’s property is a prime candidate for a very exciting redevelopment project.

Also contributing to the positive outlook for downtown Spokane in 2016, is the ever-increasing visitor traffic and spending. Attendance at Spokane’s signature events such as Hoopfest, Bloomsday, NCAA Championship basketball, Spokane Empire Football (previously Spokane Shock), Spokane Chiefs Hockey, along with record numbers of national convention attendees will keep downtown growing. These events, along with an active business community promoting downtown Spokane, bodes well for a very vibrant and exciting future for this area in 2016.
Spokane & Coeur d’Alene Are Starting to Heat Up

The investment real estate market remained strong locally, regionally, and nationally in 2015. With lending institutions ready and able to make loans, the appetite for investment real estate remains very high. Investors are looking for the higher yields provided by real estate compared to the yields available in the financial markets. With the stock market in flux and bank deposit yields in the 0.5-1.0% range, investors are seeking alternative investments and real estate has filled the need to obtain those higher returns.

As competition for investment properties has intensified in large metropolitan markets, yields have been driven down causing real estate investors to look at secondary markets like Spokane and Coeur d’Alene. For example, a 20-year McDonald’s ground lease was recently offered for sale in New Jersey at a 3.5% cap rate! There is a lot of cash that has been sitting idle on the sidelines looking for higher yields. Much of this money is held by baby boomers seeking retirement income who are looking to increase the return on their retirement cash with minimal risk. As a result, we are seeing many all-cash transactions in the investment real estate market.

The biggest problem facing potential investors in the Spokane and Coeur d’Alene markets has been the low supply of quality income-producing properties. Spokane is a conservative community and many real estate investors have a buy-and-hold mentality. This has created substantial competition for the few quality income properties that become available and has driven down cap rates.

Cap rates have remained historically low through 2015. One example in Spokane was the sale of the CLS Plasma building at 2126 North Monroe Street to an investor from California doing a 1031 exchange. That property sold at a cap rate of 5%. Average Spokane-area deals are trading in the 6.5%-7.5% cap rate range. Cap rates vary depending on the strength of the tenant, lease term, and the quality, age, and location of the asset.

As we look forward in 2016, if there is any significant increase in interest rates, this could result in a slight increase in cap rates. It does appear that if we have additional interest rate increases, they will come slowly and should not have a major effect on the investment real estate market. Investors will continue to search for the higher yields that can be found in real estate, and this should result in an active and strong investment real estate market for the Spokane/Coeur d’Alene area for 2016.
The overall outlook for the Coeur d’Alene and Kootenai County real estate markets in 2016 is bright.”

In 2015, the Kootenai County commercial real estate market had one of the best years since the 2008 recession. We experienced record breaking sales and leasing activity in all sectors, including investment and multifamily properties.

The office market has few vacancies in the Class A inventory with rates steady in the $18 to $24 per square foot range. For the first time in years, Class B and C office markets have seen a favorable absorption rate on buildings that had sat vacant for 12 to 24 months, with rates ranging from $10 to $14 per square foot.

Our retail market is growing steadily, with national retailers continuing to inquire about new development opportunities in our area. Anchored shopping centers are experiencing stable occupancy with few vacancies, with rents ranging from $14 to $18 NNN.

The industrial market is the strongest it has been in 20 years. There is virtually no vacancy in incubator space from 1,000 to 3,000 square feet, and only a few buildings are available in the 3,000 to 6,000 square foot range. Given the tight industrial market, we anticipate that some spec development will occur in 2016. Rental rates range from $6 to $8 per square foot modified gross range.

The investment sales market in 2015 for office, retail, and industrial buildings saw substantial activity with cap rates dipping to the low 6% range. Due to the lack of inventory and moderate to low vacancy rates in these markets, we anticipate continued demand for investment properties in Kootenai County.

The real proof of a strong market is a renewed interest in commercial land by both users and investors. In 2015, we saw more land sales than since the recession. Odem Corp, one of the Northwest’s largest beverage distributors, purchased 15 acres in Hayden for a new 92,000-square-foot distribution center. A new industrial park is planned in Post Falls, and national retailers and QSRs are grappling for the last few remaining parcels in Coeur d’Alene. All of the prime land suitable for Class A office development has been sold.

Development of new multifamily projects has slowed a bit since a peak from 2013 to 2015, which saw close to 500 units come on line. There is still interest from developers for well-located parcels of land in Kootenai County, but we foresee fewer multifamily development projects over the next few years. The overall outlook for the Coeur d’Alene and Kootenai County real estate markets in 2016 is bright.
2016 Should be a Profitable Year for the Multifamily Investment Market

A stable and very healthy multifamily market continued for both Spokane and Kootenai counties in 2015. Exceeding the 2014 overall average occupancy rate of 96.9%, third quarter 2015 ended strong with an average occupancy rate at 97.6%. High occupancy rates were coupled with increased rental rates, providing the best apartment market we have seen in well over a decade.

Pent-up demand, restrictions on single-family home financing, student loan debt, and the continuing trend of a flexible lifestyle are the primary driving forces behind this robust apartment market. Published data from the National Apartment Association and the National Family Housing Council determined that half of all new family households formed this decade will live in rental housing.

Spokane County

New multifamily construction, with the addition of 870 new units in 2015, did very little to impact the overall market; however, by third quarter 2015, the Spokane Valley saw the softening of vacancy rates as they reached upwards to 6.3%. Of the 870 new construction units, 662 were built in the Spokane Valley.

Overall average vacancy rates in March 2015 were 2.1%, and by the end of October, rates rose upwards to 3.3% for all unit types – still far below the 5% vacancy rate considered by many to be the marker for stabilized occupancy. When breaking out vacancies by unit type, the lowest vacancies are in studio units at 0.8% vacancy and 3+ bedroom units at 4.4% vacancy. We saw a modest 1% increase in average rental rates from $744 at year-end 2014 to $751 at third quarter 2015. From 2010 to 2015, average rental rates have climbed a total of 13.3%.

Kootenai County

In December of 2014, Kootenai County had an average apartment vacancy rate of just 1%. By third quarter 2015, vacancy rates had fallen again to a historical low of a meager 0.7%. In 2014, Kootenai County added 404 new rental units, and in 2015 we saw this number decrease with the addition of only 73 new units supplied to the market. Vacancy in the 3+ bedroom units dropped from 3.6% at the first of the year to 0.4% at the end of October 2015, reflecting an almost immediate absorption of all 3+ bedroom units that were put on the market.
Apartment Sales

The Spokane County apartment sales market was very solid in 2015 with just under $50 million in closed multifamily transactions. Sixty-four percent of those sales were from a couple of large property packages. One was a three-property sale totaling $24 million and the second was a two-property sale totaling $8.1 million. The average sales price per unit increased across the region from $45,000 per unit in 2014 to just over $50,000 per unit in 2015. That price per unit was based on 832 units sold in 2015. Cap rates remain historically low, with newer projects selling in the low 6% range and older projects selling around 7%. Apartment investment sales remain a very strong asset class both locally and nationally.

2016 Forecast

The 2016 forecast for Metropolitan Spokane is expected to have a continued strong multifamily market; however, we can expect some softening of occupancy rates throughout 2016 due to the 731 permitted and/or under construction units. We anticipate rental rates to be flat, and more so in the submarkets where the majority of new construction has been and will be built including, but not limited to, the Spokane Valley. Average rental rates throughout the remainder of the area should continue to see slow but steady incremental increases.

With 320 units permitted and/or under construction, Kootenai County can expect to see vacancy rates remain historically low with inventory staying far below the current demand. Kootenai County should also expect a steady, incremental upward movement of rental rates throughout 2016.

As for the multifamily investment market, we anticipate that 2016 will continue to be a very profitable year with a high demand from investors and historically low cap rates.
Opportunities Increase
As Transactions Become More Challenging

In 2015, the business brokerage market saw increased listing activity on behalf of business sellers and a steady number of business sales, but slightly fewer buyers in the market for businesses with a value of less than $5 million. There were also fewer buyers for businesses priced under $1 million, which is usually the most active part of the business opportunity market. With increased banking regulations, it has been more challenging for buyers of small businesses to obtain bank financing. This has led to buyers requesting a larger portion of the purchase price to be financed by the seller. In the past, sellers have financed a portion of the business sale, but that has been a small portion of the overall transaction. In 2015, we saw the seller-financed portion of the sale increasing. In today’s low yield environment, a seller can benefit by carrying back a short-term note (under ten years) for a portion of the sales price and benefit from receiving an attractive interest rate of 5% to 6% on the amount financed.

The expectations of many business sellers have changed in the last few years. The baby boomer generation now interested in selling their businesses seem to have overly optimistic pricing goals and are asking for higher multiples than many buyers are willing to pay. On the other hand, today’s buyers have a desire to purchase a fairly priced business that will provide them with both a job and a return on their invested capital.

According to the International Business Broker’s Association (IBB) Q2 Market Report for 2015: “More Baby Boomers are making the tough emotional decision to sell their business and part with their ‘baby.’ However, the majority of Boomers still haven’t made the move—many because they can’t separate their personal identity from that of their business,” says Scott Bushkie of Cornerstone Business Services, M&AMI. “In the near future, we may see a glut of Boomers coming to the market all at once. And if that happens, valuations are likely to decline due to an oversupply of businesses on the market.”

Overall, small business sales in the Spokane/Coeur d’Alene area were strong in 2015, especially in the food and beverage categories, including restaurants, bars, coffee shops, gas stations, and convenience stores. As retail consumption continues to strengthen, so will the demand for these types of business opportunities. With a steady demand from buyers and a low supply of good businesses, it will be a good market for those sellers who price their businesses appropriately.
2016

Greater Spokane Market Report

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