

PARTNERS IN DEVELOPMENT

Future economic development requires flexibility, creativity

Oregon's economy has suffered severe impacts from the recession.

This is reflected, in part, in the near total absence of new development projects in our cities and towns. Even before the lending crash, there were indications of softening markets and tightening financing.

The foundation is here for recovery: Oregon has long been one of the more innovative states in accomplishing development because of the strength of our climate for public-private partnerships. Our land-use policy and urban planning strategies are still thought of as exemplary not only in the U.S., but are studied in other countries as well.

Tax increment and other financing tools are as strong in Oregon as they are in any jurisdiction, and the state has benefited more than many others from other federal resources such as New Markets Tax Credits.

All of these are attributes of public-private partnerships. In the past, there have been three reasons for government to subsidize or otherwise participate in a development project.

- First, the government may request that the owner change something about a project to accomplish public goals, and the government pays for the incremental increase in cost. Examples include brownfields re-use, historic building rehabilitation, and achievement of high renewable design standards.

- Second, the government may request that a project suppress its revenues to achieve some policy outcome, such as



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the restricted rents in an affordable housing project. In these situations, the government subsidy fills a financing gap that exists because the reduced project revenues are not enough to support large enough loan for the cost of the project. If the project were able to charge market-rate rents, it could borrow the money for its construction costs.

- The third reason is that the project is desirable, but outside the parameters of what the private sector will do on its own because it is ahead of the market, utilizes new financial, legal or design technology, or actually makes a market for a particular neighborhood. Examples of market-making are the publicly-assisted transportation improvements in the Pearl District and the public support of residential development on brownfields in that area.

These public contributions allowed the Pearl to prove itself a viable development market.

The recession has increased our awareness of the fourth paradigm for public-private partnerships. The fourth paradigm can be summarized as guest desirable projects that cannot be financed by the private sector alone because project revenues do not support the debt service necessary for their development costs.

In the past, a skilled development team would have been able to borrow 75 or 80 percent of a project's cost from a bank at a

relatively low interest rate. Now, banks are more likely to require more pre-leasing, and provide only 50 or 60 percent loan-to-value on a recourse basis. This requires developers to "fill the gap" with a greater percentage of high-cost mezzanine financing that must be paid off quickly — which means projects are not financially feasible because their costs are higher and, in this market, their revenues are lower.

Economic indicators are improving. If this recession follows the common pattern, the jobs recovery will lag by eight to 12 months, creating a demand for new facilities for employers in our area in the next 14–18 months and beyond. To meet this demand, the development cycle will have to start soon.

This means it is time for Oregon's economic development resource agencies to be creative and willing to take well-considered risks in order to position Oregon to meet the recovery in stride. The recession is an opportunity to learn how to address the fourth paradigm. The tools now being developed to address it should not be short-term tools.

The fourth paradigm will influence the nature of public-private partnerships well into Oregon's future.

By addressing it creatively and effectively, we can strengthen Oregon's economic platform and improve our regional economy.

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