



The Barry Apartment Report is a publication covering economic, financial, and valuation trends impacting apartments in the Portland, Oregon metropolitan area.

2017 Forecast: Slower Gains and a Return to a More Normal Market

Current Portland Metro Trends

- Unemployment: 4.2%
- Job Growth: 2.6%
- Population Growth: 1.2%
- Portland-Salem CPI: 2.1%
- Apartment Construction: Permits for around 7,650 units issued in 2016, or up 15% from 2015.
- Apartment Sales: 261 sale transactions in 2016 vs. 285 in 2015
- Apartment Sales Volume: \$2.95 billion in 2016; up 26% from 2015.
- Apartment Values: Up 10% to 15%+ in 2016
- Apartment Income: Up 4% to 6% in 2016
- Apartment Vacancies: 4.1%

This issue of the Barry Apartment Report is based on a recent speech given by Mark D. Barry, MAI and Patrick O. Barry, Certified General Appraiser.

Coming off an unprecedented year in 2015, the 2016 Portland apartment market remained strong. Job growth was robust, though down from previous years. Apartment vacancies were increasing, rents were up, and apartment values showed strong gains.

Portland Economy: Good news in 2016 includes Nike's continued expansion and the continued growth of Portland's tech scene. Some large Oregon companies that were sold include Mentor Graphics (\$4.5 billion), FEI Co. (\$4.2 billion), and Lattice Semiconductor (\$1.3 billion). The 2016 figures shows that 29,600 wage and salary jobs were added in Portland metro, with unemployment dropping from 5.1% to 4.2%. The December 2016 data shows Portland has exceeded the previous peak employment by 111,500 jobs.



8/16 Sale—\$165,625 Unit
48 Unit Gatehouse Apartments
8525 SW Pfaffle St, Tigard



Under Construction
24 Unit Sierra Point Apartments
3359 SE Powell Valley Road, Gresham

Apartment Construction: Coming off a string of active years, apartment construction increased from prior years to its highest point of this cycle, with the most activity since 1996. Permits were issued for 7,650 new apartment units in the four county metro area, versus 6,650 in 2015. Around 60% of the permits for new units were issued in Multnomah County alone. Washington County accounts for 20% of construction while Clark and Clackamas County account for 15% and 5%, respectively. Construction activity remains very slow in Clackamas County, while apartment construction in East Multnomah County is beginning to show some signs of life.

Apartment Vacancies and Rental Rates:

The latest

Multifamily Northwest Apartment Report shows a 4.1% vacancy factor vs. 3.5% in Spring of 2016. 11 of the 20 submarkets showed vacancies below 4%. The lowest vacancies were reported in Washington County and East Vancouver, while the highest vacancies are in Northwest Portland and North Portland. Turnover rents are up around 8.5% over the last year,

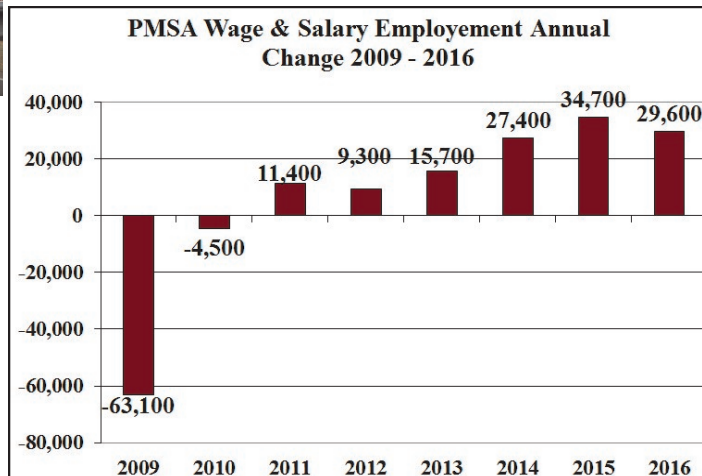
Apartment Expenses: Most properties saw a manageable 2% to 3% property tax increase in 2016. Most other expenses showed little change from the previous year.

Apartment Values: In 2016, apartment values continued their increase to hit new record highs. When considering all sales across the metro area, values were up 8% to 10%. However, large institutional grade suburban properties and new apartments were driving these value increases. When properties over 150 units or properties built after 2014 were excluded, values were up just 3% to 5%.

While values have risen across the entire metro area, not all increases have been equal. Most properties in Clark County and properties east of I-205 have shown 30% year to year value gains. Based on information from CoStar, the following table highlights a few select submarkets and their changes in median values from 2013 to 2016. By no means are the value increases equal across the Portland MSA.



12/16 Sale— \$143,833/Unit
12 Unit Rose City Court Apts
2136 NE Weidler St, Portland



Inside this issue:

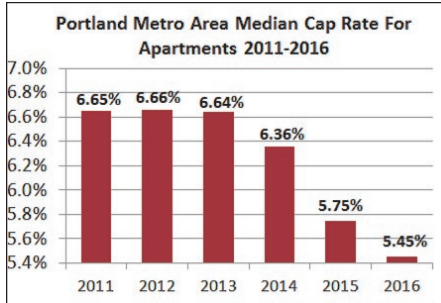
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Washington County - 1960-1990 Built Apts				
	2013	2014	2015	2016
Per Unit	\$60,000	\$75,625	\$99,738	\$110,417
Per Sq. Ft.	\$64	\$84	\$115	\$121
Cap Rate	6.68%	6.63%	5.79%	5.65%

Clark County - 1960-2000 Built Apts				
	2013	2014	2015	2016
Per Unit	\$69,756	\$66,865	\$76,851	\$100,037
Per Sq. Ft.	\$81	\$76	\$78	\$110
Cap Rate	7.20%	7.02%	6.18%	5.76%

City of Portland Pre-1950 Built Apts				
	2013	2014	2015	2016
Per Unit	\$103,000	\$109,885	\$132,456	\$120,500
Per Sq. Ft.	\$143	\$139	\$189	\$219
Cap Rate	5.85%	5.21%	4.77%	4.69%

East of I-205 - 1960-1990 Built Apts				
	2013	2014	2015	2016
Per Unit	\$60,867	\$70,000	\$74,597	\$97,727
Per Sq. Ft.	\$70	\$80	\$91	\$114
Cap Rate	7.20%	7.21%	6.65%	5.72%



Portland remains on the radar of institutional buyers. ULI ranked Portland No. 3 for Overall Real Estate Prospects and Forbes' 2016 list of Best Places for Business and Careers listed Portland at No. 5.

FORECAST FOR 2017

The incredible pace of urban apartment construction appears to be finally having an impact on the rental market. Our thoughts are as follows:

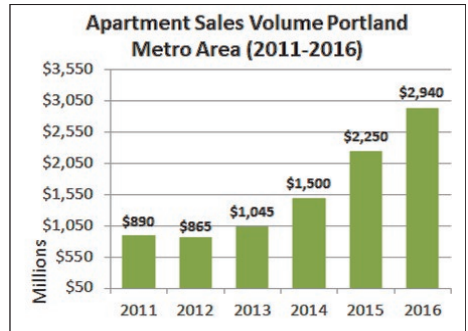
Economy: The metro area job growth in 2016 was robust and near the upper end from expert forecasts. Transportation, business services, hospitality, education/health and government have shown strong job gains over the past 12 months. For the fourth year in a row, Portland had the highest national percentage of inbound moves according to United Van Lines. There are at least three reputable organizations that forecast employment figures for Oregon. If you assumes that employment in the Portland area will grow consistent with the State, the consensus forecasts are for around **24,000 to 29,000 new wage and salary jobs here in the Portland metropolitan area in 2017, and 23,000 to 28,000 new jobs in 2018. Population growth of around 25,000 to 30,000 per year is expected for the Portland metro area.**

Single Family: The single family housing market showed continued strength 2016. Forecasts call for the State of Oregon housing starts to increase around 12% for 2017. If you assume housing starts for the Metro area will grow consistent with the state, **Portland Metro should see permits for around 8,300 new single family homes in 2017.** Condominium development is now part of the

conversation, though there is no sign of condo conversions.

Apartment Construction: New apartment construction increased in 2016, and represents the busiest year since 1996. Based on the latest permit numbers, **we expect there will be permits for 14,000 to 18,000 new units in 2017 and 2018.** The implementation of inclusionary zoning in Portland forced many developers to file for permits prior to the February 1, 2017 implementation date. The City of Portland reported 14,000 units under consideration just prior February 1, 2017, or three times their normal level. These projects will work their way through the system during 2017 and 2018.

Due to questions surrounding inclusionary zoning and hesitation from developers, we expect a slowdown in the application for apartment permits. However, the projects in the pipeline will take a few years to materialize and the slowdown in permit applications may help the large backlog of units be absorbed.



Due to rising land costs, increasing construction costs, low vacancies outside the urban area, and substantial rent increases, **we expect to see more suburban apartment construction. This will include East Multnomah County, Washington County, and Clark County.** Apartment construction in Clackamas county is expected to remain slow.

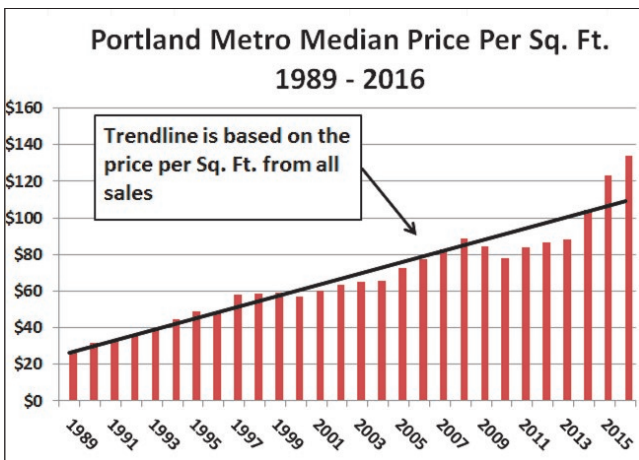


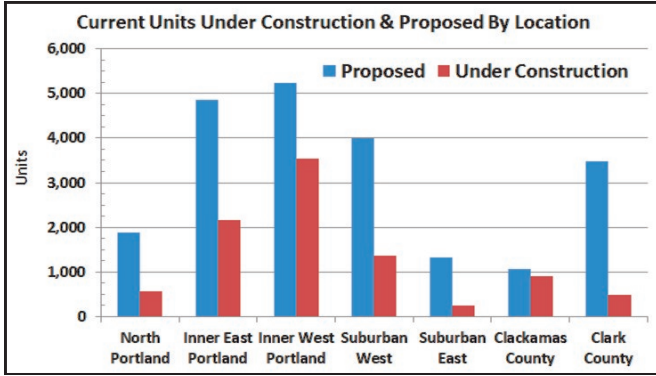
Under Construction
18 Unit N Minnesota Apartments
6195 N Minnesota Ave, Portland

When the long term value trends are considered, as seen in the graph below, the per Sq. Ft., as well as the per unit, values increases seen in 2015 and 2016 push values above the historic trend line. However, rents have also increased

While value increases have slowed in certain areas, there are virtually no submarkets that show flat or decreasing values. The Co-Star figures show a 5.45% median cap rate for 2016. This is down from 5.75% in 2015 and 6.36% in 2014.

Apartment Sales Volume: 2016 was a record year for sale volume. Despite fewer transactions, apartment sales volume from 2016 is 31% above 2015. There were around \$2.95 billion in apartment sales. This represents 264 sale transactions with 16,000 units. This is in comparison with \$2.25 billion in apartment sales and 285 transactions in 2015. The largest 10 sales of 2016 accounted for 34% of the dollar volume.





Most new units will continue to offer concessions until full occupancy is achieved. We expect to see more concessions at seasoned apartments that are competing with the new units.

After years of being an apartment owners market, we anticipate a transition to a market more in balance, especially in the urban core.

7.1% of the sales volume, but only 1.3% of the transactions. Portland continues to have superior yields compared to other west coast cities. **In 2017, we expect to see \$1.75 billion to \$2.25 billion in apartment sales, and 225 to 275 apartment sale transactions.** Recent rules implemented in the City of Portland, along with the real possibility of rent control is making some buyers reluctant to enter the Portland market despite strong investment appeal. However, the overall investment appeal of Portland should continue to attract investors.

Risks: For the past three years, the Portland apartment market has seen few bumps in the road and values have reflected this. As some of these factors that have benefited the apartment market begin to turn, there is risk.

Risks—Currently Occurring

- Interest rates are increasing
- Apartment construction nearing record levels
- Increasing home ownership and home construction
- Increasing apartment regulation (IZ zoning, tenant relocation fees for no-cause & 10%+ rent increase, increased notice times....rent control?)
- A shift in the political climate
- Aging cohort of prime renters

Risks—Potential

- Slowdown in local population growth
- Slowdown in local job growth
- Further increases in regulation
- Macroeconomic events (recession, oil, China, Trump)

CONCLUSION: 2016 was another very strong year for the Portland apartment market. Sales volume and apartment values hit record highs and rent continued to increase. However, **there are some clear warning signs that the breakneck pace we saw in 2015 and 2016 may be behind us.**

During 2017, we expect continued increases in interest rates, increases in apartment vacancies up to 4.5%, some concessions in the urban area, some slow down in apartment sales, and that apartment income will flatten out. **Apartment values are expected to stabilize as we return to a more normal market.**

Apartment Vacancies and Rental Income:

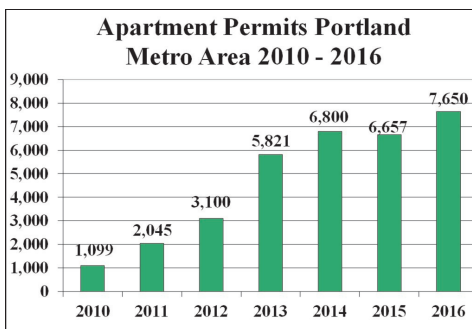
The years of new construction have finally had an impact on vacancies, though the impact has mainly been in areas of heavy construction. Expect a further increase in vacancy rates of urban units, where construction has been most active.

Based on the current vacancy rates, the total number of metro area apartments, and assuming a market in balance will show a 5% vacancy rate, the Metro area has a shortage of around 2,300 units.

Assuming the home ownership rate is around 60% and renter household size is around 2.10 persons, population growth of 25,000 to 30,000 persons translates into demand for around 4,750 to 5,700 units per year across the metro area. The current new supply is greater than demand from population growth. The current levels of supply are chipping away at the shortage of units.

We expect vacancies to approach 4.50% by the end of 2017. Localized vacancies will continue in areas with above average construction and high end rents. While buyers continue to seek “value add” properties, such properties are few and far between.

Some owners are reporting lower turnover rents due to increased competition. In Portland, some rules have been implemented which will temper the increases in income. We expect apartment income will be up by 2% to 5%. **By the end of 2017, we expect the market will be more in balance in the urban area, though a tight market will remain in areas with limited apartment construction.**



Apartment Values: Apartment values showed an increase in 2016, though slower than previous years. There is continued optimism for 2017. We expect slower value increases in the urban core where values showed large jumps from 2013 to 2016. Suburban apartments, which were slower to recover in value, will continue to increase in value. In addition to strong fundamentals (low interest rates, low vacancies, increasing rents, stable expenses) limited inventory is also driving up values, though the inventory is up from 2014. **Apartment values are expected to be stable in 2017 after the break neck pace of 2015 and 2016.**

Interest rates increased in late 2016 by 0.25% and again by 0.25% in March 2017. Two additional increases are expected in 2017 given the strong fundamentals in the US economy. **We expect increasing interest rates will result in a flattening out of apartment values in 2017.**

Apartment Sales Volume: In 2016, Portland saw continued interest from institutional buyers, which accounted for over



1/17 Sale- \$262,500/Unit
8 Unit Santa Lucia Apartments
2934 SE Morrison St, Portland

The Barry Apartment Report

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Turn Back the Clock . . .



NW 13th and NW Overton St – 2009



NW 13th and NW Overton St - 2016



Image Credits: Google Maps

10 Least expensive markets

It's cheaper in the Midwest and the sun belt - outside California

Area	State	Avg rent in 2006
Tucson	AZ	\$615
Columbus	OH	\$642
Indianapolis	IN	\$643
San Antonio	TX	\$660
Salt Lake City	UT	\$667
Kansas City	MO	\$668
Cincinnati	OH	\$675
Cleveland	OH	\$711
Houston	TX	\$724
Portland	OR	\$740

Source: Marcus & Millichap



11/16 Sale—\$125,000 Unit
9 Unit Monroe Manor Apartments
423 Monroe St, Oregon City

We have recently transitioned our market updates to electronic only. We send 2-3 emails a year with updates on the Portland apartment market. You can subscribe or unsubscribe on our website.

www.BarryApartmentReport.com