



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

## 2016 Forecast: Values Reach New Highs—Is It Different This Time?

### Current Portland Metro Trends

- Unemployment: 4.3%
- Job Growth: 3.2%
- Population Growth: 1.6%
- Portland-Salem CPI: 1.2%
- Apartment Construction: Permits for around 6,500 units issued in 2015, or down 4.5% from 2014.
- Apartment Sales: 285 sale transactions in 2015 vs. 220 in 2014
- Apartment Sales Volume: \$2.25 billion in 2015 ; up 50% from 2014.
- Apartment Values: Up 10% to 20%+ in 2015
- Apartment Income: Up 4% to 7% in 2015
- Apartment Vacancies: 3.5%

*This issue of the Barry Apartment Report is based on two recent speeches given by Mark D. Barry, MAI, Apartment Appraiser and Patrick O. Barry, Appraiser Assistant.*

In 2015, the Portland apartment market surpassed all expectations and set many records along the way. Job growth exceeded all forecasts, apartment vacancies were decreasing, rents were up, and apartment values showed unprecedented gains.

**Portland Economy:** Good news in 2015 includes Intel's continued construction in Hillsboro; Nike's major expansion which began in early 2015; Adidas's recently announced expansion; Under Armour's entrance in to Portland, and the continued growth of Portland's tech scene. The February 2016 figures shows that 34,600 wage and salary jobs were added in Portland metro over the last year, with unemployment dropping from 5.2% to 4.3%. The February 2016 data shows Portland has exceeded

the previous peak employment by 81,000 jobs.



3/16 Sale—\$119,167 Unit  
12 Unit Lombard Apartments  
5195 SW Lombard Ave, Beaverton

**Apartment Construction:** As a surprise to some, apartment construction was down slightly in 2015. Permits were issued for 6,500 new apartment units in the four county metro area, versus 6,800 from 2014. Over 62% of the permits for new units were issued in Multnomah County alone. Washington County accounts for 25% of construction while Clark and Clackamas County account for 10% and 3%, respectively. Construction activity remains virtually non-existent in Clackamas County, while apartment construction in East Multnomah County is beginning to show some signs of life.



22 Unit Pettygrove Apartments  
2240 NW Pettygrove Street, Portland

**Single Family Market:** The median sales price in Portland metro is \$315,000 as of early 2016, which is up 10.5% in the last year. There are just two months of inventory. Single family home values continue to increase, and new construction has followed. We saw permits for 6,600 new homes in 2015, which is up significantly from 2014, but remains relatively low historically. In comparison, an average of 9,500 single family homes were built per year from 1996 to 2007.

**Apartment Vacancies and Rental Rates:** The latest *Multifamily Northwest Apartment Report* shows a 3.5% vacancy factor vs. 2.9% in Fall of 2015. 14 of the 20 submarkets showed vacancies below 4%. The lowest vacancies were reported in Clackamas and East Vancouver, while the highest vacancies are in Northwest Portland and Wilsonville. Turnover rents are up around 13% over the last year,

**Apartment Expenses:** Most properties saw a manageable 2% to 3% property tax increase in 2015. Water and sewer rates have increased again with \$80 to \$100 per unit per month being the new normal. Most other expenses little change from the previous year.

**Apartment Values:** In 2015, apartment values saw a sharp increase from the previous year, and are at new record highs with values up

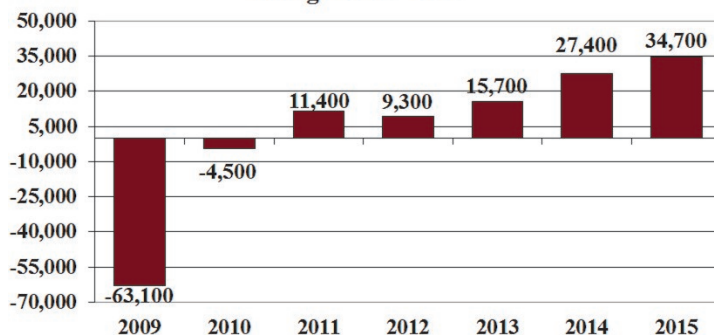


11/15 Sale— \$160,875/Unit  
20 Unit Classic Apartments  
2056 NW Glisan Street

### Inside this issue:

- 2016 Forecast 2 & 3  
Turn Back the Clock 4

PMSA Wage & Salary Employment Annual  
Change 2009 - 2015





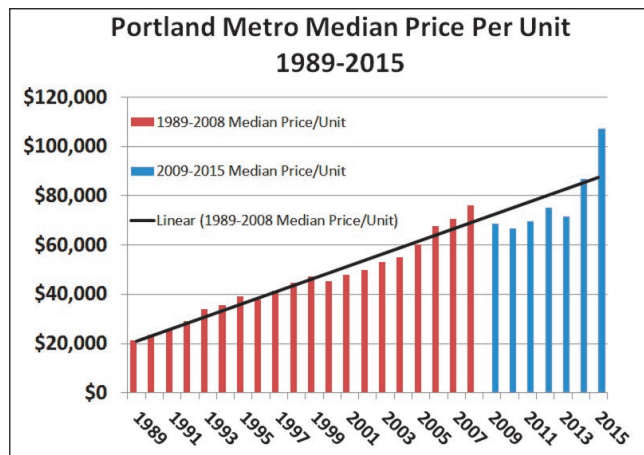
10/15 Sale – \$85,833/Unit  
24 Unit Fircrest Apartments  
803 SE 187th Avenue, Gresham

anywhere from 10% to 20%+ from 2014 based on the submarket. When the long term value trends are considered, as seen in the graph below, the per unit values increases seen in 2015 push values above the historic trend line. However, average rents have followed a similar trend.

Price increases were seen across all markets, including older suburban units that had been slow to recover. The Co-Star figures show a 5.75% median cap rate. This is down from 6.36% in 2014 and 6.64% in 2013. However, the sales from the fourth quarter of 2015 and first quarter of 2016 show a slight decline in the median \$/Sq. Ft. and \$/unit, and slightly higher overall capitalization rates.

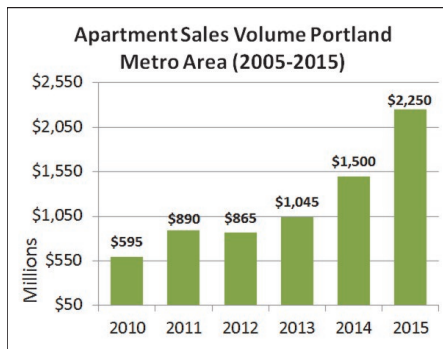
**Apartment Sales Volume:** 2015 was a record year for sale volume. There were around \$2.25 billion in apartment sales. This represents 285 sale transactions with 15,000 units. This is in comparison with \$1.50 billion in apartment sales and 220 transactions in 2014, or a 30% increase in transactions.

Portland remains on the radar of institutional buyers. Forbes' 2015 list of Best Places for Business and Careers listed Portland at No. 3.



### FORECAST FOR 2016

As many of the various apartment market indicators remain at or close to record levels, the question remains, "How long will this party last?" Our thoughts are as follows:



**Economy:** The metro area job growth in 2015 exceeded all forecasts. Transportation, business services, hospitality, education/health and government have shown strong job gains over the past 12 months. ULI 2015 Emerging Trends ranks Portland 9th among 75 metro areas for real estate prospects. For the third 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 assume that employment in the Portland area will grow consistent with the State, the consensus forecasts are for around 25,000 to 30,000 new wage and salary jobs here in the Portland metropolitan area in 2016, and 20,000 to 30,000 new jobs in 2017. 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 strengthened in 2015. Forecasts call for the State of Oregon housing starts to increase around 20% for 2016. If you assume housing starts for the Metro area will grow consistent with the state, Portland Metro should see permits for around 8,000 new single family homes in 2015. At least one condominium is under construction in the Pearl and more are anticipated.

**Apartment Construction:** New apartment construction slowed slightly in 2015, but this is not felt to represent a new trend. Based on the

latest permit numbers, we expect there will be permits for 13,000 to 16,000 new units in 2016 and 2017. Since 2013, most of the construction activity is in Multnomah County, and most of it near the urban core. 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.

**Apartment Vacancies and Rental Income:** Despite all of the new apartment construction in recent years, vacancy rates remain low, with just a slight increase in YTD 2016. This reinforces the strength of the Portland market. 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 4,000 units.

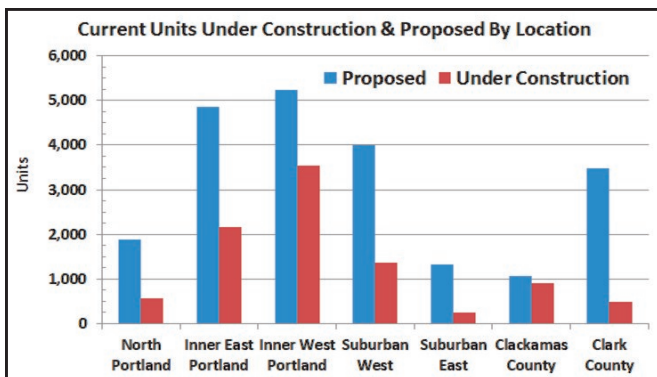
Assuming the home ownership rate is around 60% and renter household size is around 2.10 persons, this population growth of 25,000 to 30,000 persons translates into demand for around 4,750 to 5,700 units per year. The current new supply is only slightly greater than demand from population growth. The current levels of supply is struggling to make up ground on the shortage of 4,000 units.

We expect vacancies to remain below 4.00% for most of 2016, but to increase by year end. Some localized vacancies may occur in areas with above average construction and high end rents. Buyers are continuing to seek "value add" properties. However, as the values of these properties in their "as-is" condition increases, the major renovations are more difficult to justify. Most new construction is offering concessions until full occupancy is achieved. Expect this trend to continue.

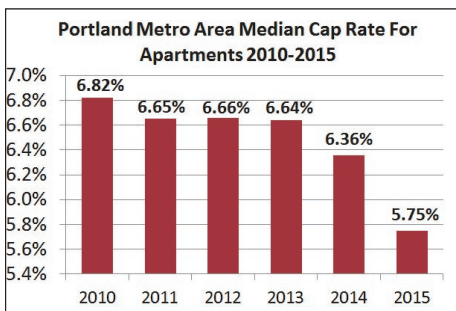


Footprint Hollywood (Micro-units)  
1521 NE 41st Avenue, Portland





With most economic indicators favoring apartment owners, expect landlords to remain aggressive and apartment income will be up by 3% to 6%. **We expect that a "landlords market" will continue in 2016 but we expect the market will be more in balance in 2017.**



**Apartment Values:** Apartment values showed a staggering year over year increase in 2015. There is continued optimism for 2016. In addition to solid 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 2016 after the break neck pace of 2015.**

Interest rates increased by 0.25% in late 2015, and additional increases are

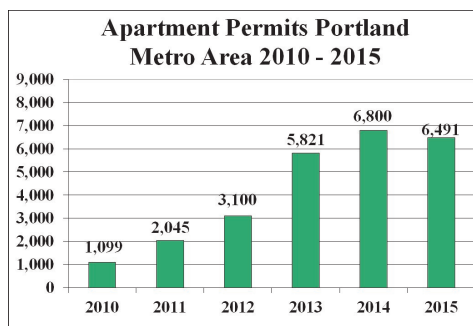


11/15 Sale- \$107,143/Unit  
14 Unit Maple Grove Apartments  
3025 SE Maple Street, Milwaukie

expected in 2016 given the strong fundamentals in the US economy. However, most major economists forecast a low interest rate environment for the near term future.

#### **Apartment Sales Volume:**

In 2015, Portland saw growing interest from institutional buyers, which accounted for over 71% of the sales volume, but only 13% of the transactions. Portland continues to have superior yields compared to other west coast cities. **In 2016, we expect to see \$1.75 billion to \$2.25 billion in apartment sales, and 225 to 275 apartment sale transactions.** In recent years, we have seen some reluctance of apartment owners wanting to sell due to a lack of alternative investments. In 2015 some owners chose to sell their outlier properties. These outliers may include properties with historically high expenses, poor locations, negative external influences, properties purchased during a previous peak, or properties with a difficult tenant profile.



**Risks:** For the past two years, all major market forces have been benefiting the Portland apartment market and values have reflected this. There is some risk and uncertainty as to when these indicators no longer favor apartments. These risks include the following:

- **Increasing interest rates**
- **Increased apartment construction**
- **Increasing home ownership**
- **Slowdown in local population growth**
- **Slowdown in local job growth**
- **Aging cohort of prime renters**
- **Increasing renter protections**
- **Macroeconomic event (recession, oil, China)**

**CONCLUSION:** 2015 was the strongest years on record for the Portland apartment market. Sales volume and apartment values hit record highs. Vacancies showed a decline, apartment construction slowed slightly, rents increased, and financing was readily available. The only downside to speak remains not enough properties for sale.

Barring any major unforeseen events, all indications point to another strong year for apartments. Expect low vacancies, increased apartment construction, more modest increases in income, and continuing strength in apartment sales, but apartment values are expected to stabilize.

#### **HEARD ON THE STREET**

*"With millennials looking toward homeownership as they continue to age and start their families, demand will begin to diminish. The greatest development opportunities will come from the suburbs, which not only will be in higher demand but also have seen less development than central business districts. Job growth in suburb markets is also a plus."* Bendix Anderson—NREI Magazine

*"It's like musical chairs. If you don't add more chairs to the game, people get squeezed out of the game."* - Joe Cortright, Portland Economist discussing apartment supply and demand

*"Rent control is an Econ 101-level policy disaster. If you happen to get one of the rent controlled units, good for you. But it's basically a lottery of who wins and who loses."* - Jerry Johnson, Johnson Economics

*"The policy decision that would most rapidly lower housing costs is changing Portland zoning code to allow more apartments to be constructed in neighborhoods where only single-family homes are allowed."* - Aaron Mesh—Willamette Week

*"To use a car analogy, there's a lot more people who are looking for Chevrolets than are looking for BMWs. And a lot of what's been built in Portland lately has been high-end rental housing. If there's less supply at the lower end of the housing market, those prices are going to go up."* - Nick Sauvie, Rose Community Development

*"The data suggests the bull market for apartments, which began in 2010, is on its last legs."* Laura Kusisto, Wall Street Journal article of April 8, 2016.

# The Barry Apartment Report

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Mark D. Barry & Patrick O. Barry

## Turn Back the Clock . . .



SE 31<sup>st</sup> & Division - 2009



SE 31<sup>st</sup> & Division - 2015



N Cook St & Williams - 2009



N Cook St & Williams - 2015



2/16 Sale—\$188,333 Unit  
9 Unit Collins Circle Apartments  
1505 NE 64th Avenue, Portland

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