RED CAPITAL GROUP®

Market Overview

Portland, Oregon

Multifamily Housing Update June 2011

EXECUTIVE SUMMARY

In March, the *Wall Street Journal* wrote off Portland as one of the two most economically miserable metropolitan areas in America: but what a difference a few months can make. Since the infamous misery index was published, Portland has posted some conspicuously good employment numbers, perhaps leading the *WSJ* to designate it the "Comeback Kid" instead of the "place where young people go to retire."

Payroll employment increased at an 11,500-job, 1.2% rate in the first quarter, easily topping the nation's 0.9% average advance, and a sharp acceleration from 4Q10's sub-par 4,700-job, 0.5% performance. Goods producing industries were the principal catalysts as meaningful growth was recorded in the electronics and semiconductor manufacturing sectors and in the closely related wholesale trade and transportation industries. Construction payrolls firmed as well, as the "home construction" and "specialty trade contractor" subsectors were essentially flat during 1Q11 after three years of continuous losses; and even slightly positive in the 12-month comparison in April.

Seasonally-adjusted data also were encouraging. This series indicates that metro employers created a net of 8,900 new jobs in 1Q11, the largest number in a single quarter since 2006. The preliminary April report was consistent with the trend, suggesting that 3,300 new workers were added to payrolls in that month.

At the same time, the metro unemployment rate — which the *WSJ* featured prominently among its rationale for Portland's low standing — fell 110 basis points March to April to 8.8%, near the 8.7% US average. The metric was as high as 11.7% last year.

The ***RED Research*** payroll forecasting model expects steady improvement through 2012. The model projects a gain of 18,800 jobs this year and a 32,000-job add in 2013.

Increased demand for independence and better housing accompanied enhanced career opportunities. As home price weakness remains a barrier to ownership, the apartment sector realized the lion's share of it. Tenants absorbed a net of 652 units in 1Q, the largest number of first quarter net move-ins registered in eleven years. Against no additions to supply, occupancy increased 60 basis points sequentially and 250 bps year-over-year to 96.1%, **RED 50** 4th highest**.**

Rent trends also were constructive. Metro average asking rents increased for the fourth consecutive quarter, in this case by $4 (0.5%) to $843. Concession levels receded slightly, allowing effective rents to rise $5 (0.6%) to $783. Measured on a year-over-year basis, effective rents were $31 (4.1%) higher, representing the strongest Portland up-move in more than two years and the fourth largest y-o-y gain recorded among the **RED 50** markets.

The Northwest submarket enjoyed the strongest demand and pricing power as tenants were drawn Downtown and were prepared to pay for the privilege. Submarket properties notched 190bps and 1.0% sequential quarter occupancy and effective rent increases to 92.3% and $1,136. At the other end of the spectrum the suburban East Gresham submarket posted Portland's only sequential rent decline (-0.6%) to $672, the lowest submarket average in the metro area.

Since our last report, investment activity was largely confined to repositioning plays in Gresham. Each of three spring metro trades of note involved a Gresham property. We estimate that the cap rates applicable to the two institutional quality assets ranged from the mid-4% to 5% area.

SNAP SHOT

	Y-o-y change	Projected 2011
Vacancy (3.9% - 1Q11)	▼ 2.5%	▼ 0.5%
Effective Rents ($783 –1Q11)	▲ 4.1%	▲ 5.6%
Cap Rate (5.0% - 1Q11)	▼ 1.3%	▼ 0.2%
Employment (964.8m - 1Q11)	▲ 11.5m	▲ 18.8m

KEY POINTS

- Tenants rushed to secure apartment space as the economic recovery gained momentum and the multifamily market tightened. Metro properties absorbed an 11-year first quarter high net of 652 units, sending occupancy 60 basis points higher sequentially to 96.1%, the fourth highest comparable **RED 50** level.
- Effective rents increased for the fourth consecutive quarter, in this case by $5 (0.6%) to $783. Although it was the smallest sequential quarter gain in a year, it raised the metro's year-over-year comparison from 2.8% in 4Q10 to a **R50** 4th highest 4.1%.
- Reis expect average metro occupancy to reach 96.6% by year-end and effective rents to increase 5.6% during the calendar year.
- The supply and demand proposition for institutional quality properties favored sellers. Investors were compelled to bid aggressively for the few properties for sale, plunging acquisition cap rates below 5%.
- Employing a 5.0% generic cap rate, **RCR** estimate that a typical metro investment will yield an 11.4% 5-year holding period total return, ranking 3rd highest among the **R50**.