MULTIFAMILY MARKET ANALYSIS

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The strong market fundamentals persist in multifamily, but the new construction is coming. For now Portland remains one of the tightest markets in the nation with a vacancy rate of 3.55%. Both local and national investors are seeking to position equity, and have been drawn to the market conditions that make apartments an attractive, low-risk investment. However, with thousands of units in the planning, permitting, or construction phases, there is concern that the market could become overbuilt. According to appraiser Mark Barry: "Many developers are chomping at the bit to get back in the game. In 2013, we're in a sweet spot. When we get into 2014 and 2015, the apartment market will be more in balance. It will no longer be a landlord's market."

The Barry's forecast that rent increases will subside after mid-2013 and will flatten out over the next two years as landlords compete for tenants. They predict that apartment vacancies will increase to 4% to 4.5% by the end of this year and possibly as high as 5.5% by the end of 2014. This will result in a shift from a landlord's market to a more balanced market over the next 18 to 24 months.

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Multifamily construction has been ramping up, but still below 2004-2008. In 2012 there were multifamily building permits issued for 2,687 units in the tri-county area. In 2011 permits were issued for 1,696 units in the three county metro area, compared to 1,100 in 2010, according to the Barry Report. From 2004-2008 an average of 4,700 units came online annually.

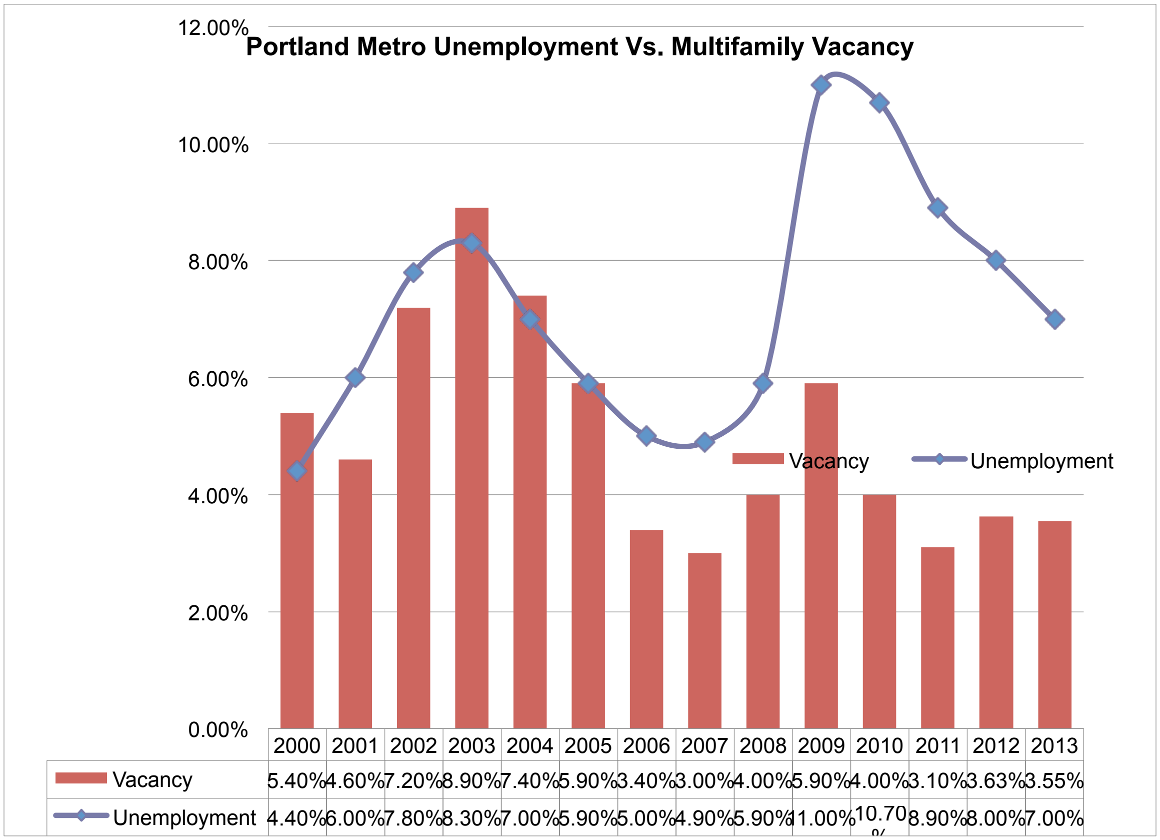
The high demand for rentals is expected to persist over the next several years and absorb the new construction projects. Strong fundamentals including low interest rates, low vacancy rates, and increasing rents have spurred new projects, as developers work to capitalize.

Axiometrics, a leading provider of apartment data and market research, reports that effective rent growth remained steady during February, at a rate of 3.53%, but that the pace of rent growth has been slowing in recent months. February's effective rent growth rate was the lowest since August 2010. Occupancy remained strong nationally with an average rate of 94.13% in February. This rate is up 35 basis points (bps) from February 2012 and 71 bps from February 2011.

“A pattern has emerged this year, as effective rent growth for Class A properties has really slowed down, Class B rates have remained relatively steady, but Class C rates have continued to increase,” said Ron Johnsey, president for Axiometrics. “Rents had been pushed so much at the upper end of the market it was inevitable we would begin to see a slowdown in growth for Class A properties, but we may also be seeing some impact from new properties coming online in certain markets. As new deliveries increase later this year and next, the trend could become even more pronounced.”

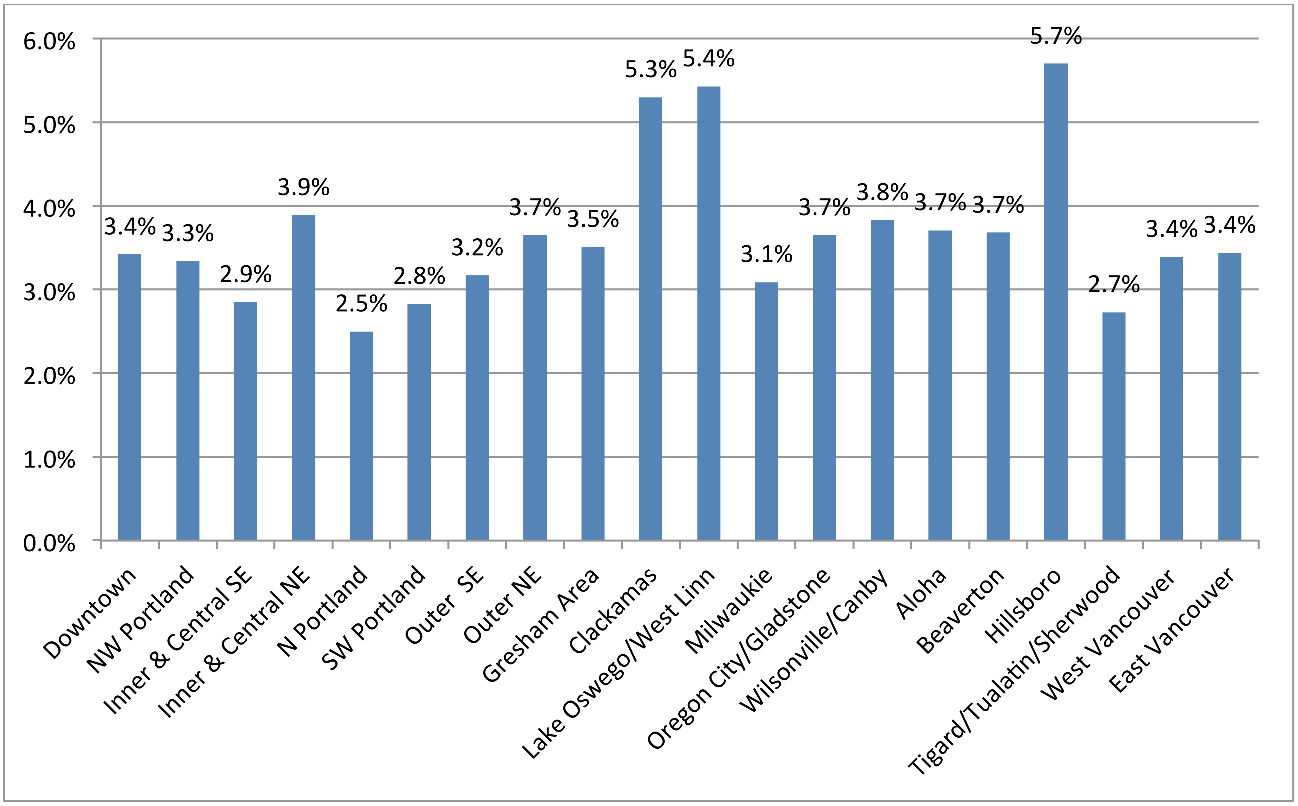
Unemployment rates are positively correlated with vacancies as shown in the chart below. Portland currently has an unemployment rate of 7.0 percent, which is lower than the state average of 7.9 percent and the national average of 7.3 percent.

Figure 1: Unemployment and Multifamily Vacancy, Portland Metropolitan Area



These market factors have driven vacancy rates in historically undersupplied Portland to among the lowest in the nation. The highest overall vacancy submarket was 5.7 percent in Hillsboro and the lowest was Inner & Central SE at 2.85 percent. The highest vacancy rate among studios was Hillsboro at 14.3 percent. The highest vacancy rate for 1 BD, 1 BA was Hillsboro at 6.9 percent, while the lowest was Outer SE with 1.95 percent. For 2 BD, 1 BA the highest vacancy was Downtown at 5.56 percent and the lowest was West Vancouver at 1.8 percent. Eight submarkets reported a 0 percent vacancy rate among 3 BD, 1 BA, but many of these were based on less than 100 units surveyed. Inner SE and Inner NE reported 0 percent for 3 BD / 2 BA, while Oregon City / Gladstone had a 12.6 percent vacancy rate for 3 BD / 2 BA.

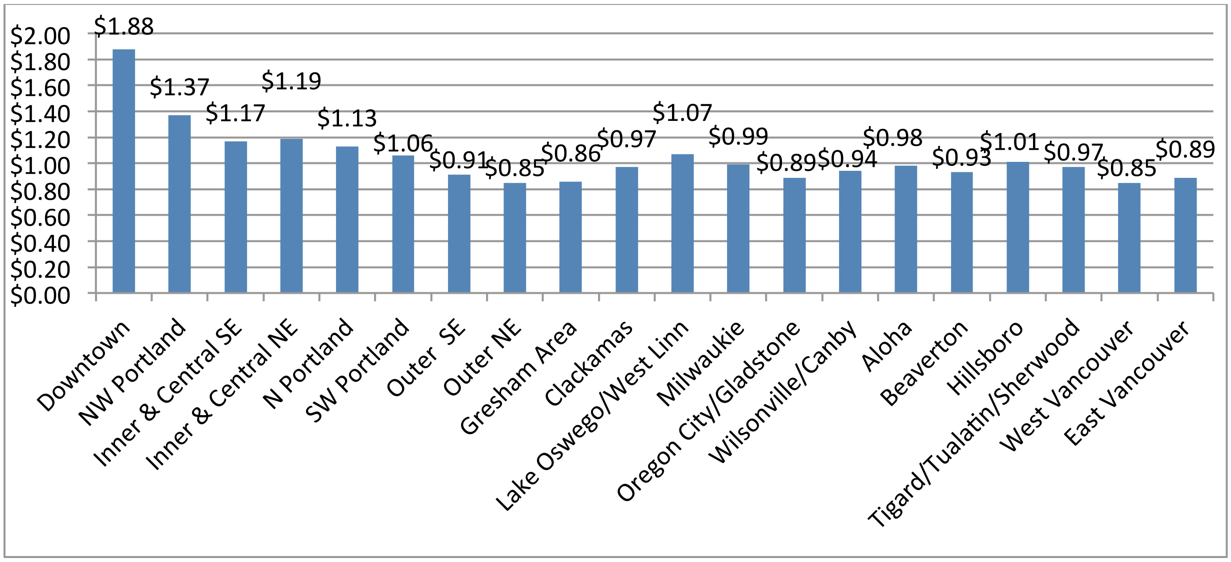
Figure 2: Vacancy Rates by Submarket Spring 2013 Portland Metropolitan Area



Source: MMHA

The submarket with the highest overall rent/SF is downtown Portland with a $1.88 average, followed by NW Portland at $1.37. The lowest overall rent/SF is shared between Outer NE at $0.85 per square foot. The highest rent/SF for studios was Downtown at $1.96 and the lowest was Wilsonville / Canby at $0.82. The highest rent/SF for 1 BD, 1 BA was Downtown at $1.96 and the lowest was Outer Northeast at $0.92. The highest rent/SF for 2 BD, 1 BA was Downtown at $1.55 and the lowest was $0.82 in West Vancouver.

Figure 3: Rent / SF by Submarket Spring 2013 Portland Metropolitan Area



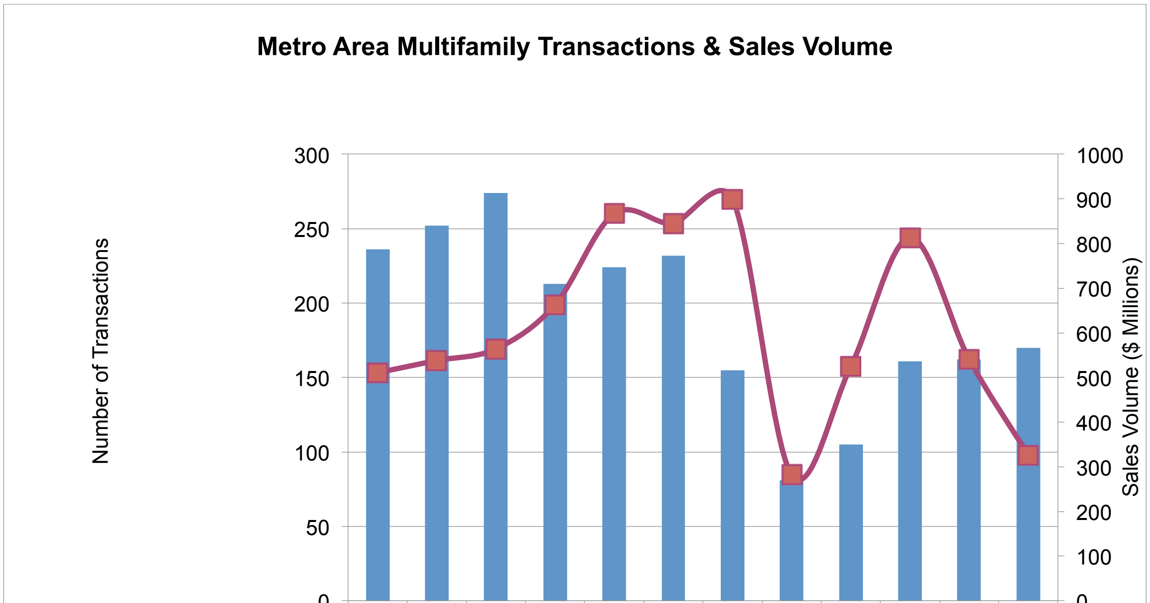
Source: MMHA

In Portland, approximately 70 percent of the apartments were built in the 1970s. These properties are often in the 8-60 unit range, have varying levels of deferred maintenance, and many sell in the $50,000-$80,000 per unit range depending on rents, location, condition, and other factors. In the second quarter of 2013 the sold price per unit was $68,300. The average number of units sold per property was 40 in second quarter 2013 and 37 in the first quarter of 2013.

There have been two deals with a sales price over $10 million in the second quarter of 2013. The Cyan (338 units) in Downtown Portland sold for $95.5 million and Green Leaf Springs (266 units) in Northeast Portland sold for $16.1 million.

In 2012 there were 162 transactions and $541 million in sales volume compared with 161 transactions and $813 million in 2011. As of July 2013, there have been 170 transactions and $326 million in volume year to date. Due to the solid market fundamentals, apartments remain the favored asset class of investors in Portland and throughout the nation. Experts are projecting that the increases in sales volume and transactions will continue to be strong in 2013 and over the next several years.

Figure 4: Multifamily Transactions and Sales Volume, Portland Metropolitan Area, July 2013 Year to Date



	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Number of Transactions	236	252	274	213	224	232	155	81	105	161	162	170
Sales Volume	511	538	564	663	867	845	899	282	525	813	541	326

Source: Costar

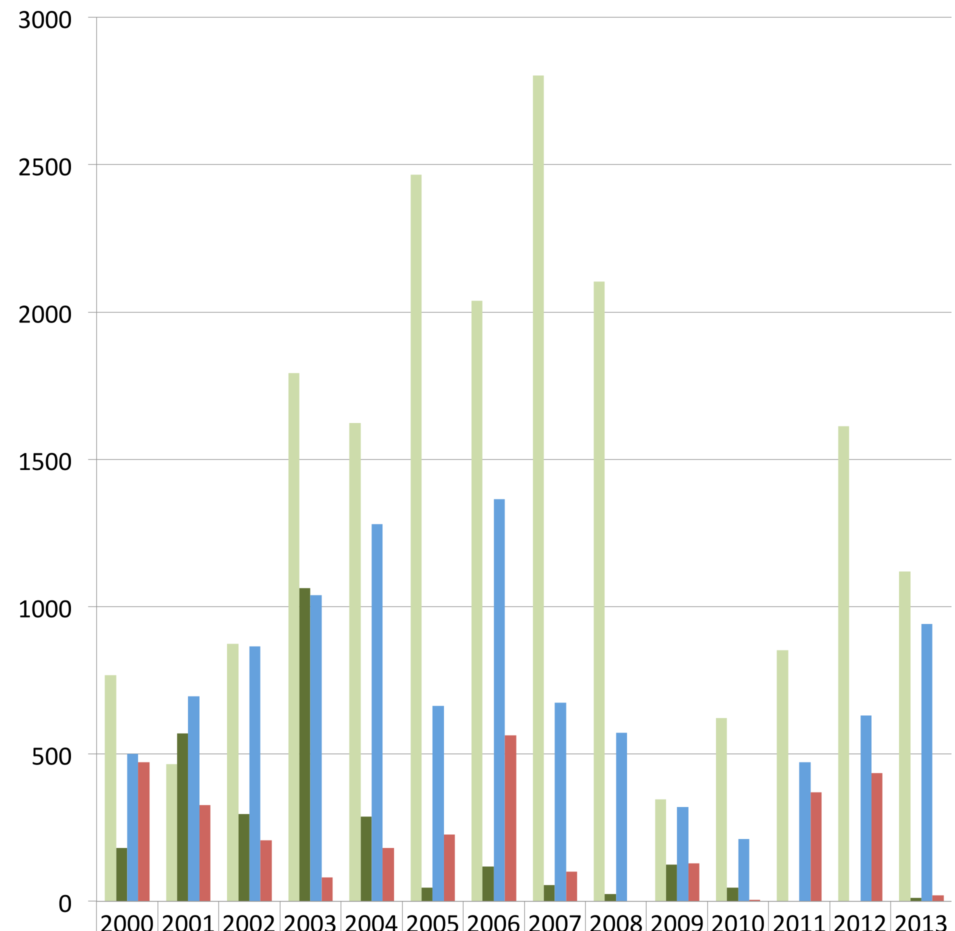
Through May 2013, multifamily building permits have increased within the metro area compared to 2012. Permits have been issued for 1,119 multifamily units built in the City, which is on pace to surpass last year's total of 1,612. According to the Barry Report there are 8,000 new units projected in 2013 and 2014 with half of these slated for Multnomah County. Washington County has already surpassed 2012 for the number of new units this year at 942 units through May.

In the April 2013 MMHA Report Mark and Patrick Barry astutely observed a number of trends that have emerged in new apartment construction:

- Currently there are twice as many units under construction as units that have been recently completed.
- Almost three times as many units have been proposed as recently completed.
- Close-in east Portland accounts for almost 1/3 of the proposed units.
- Very little activity in market rate apartment construction in East Multnomah County area.
- Average size is approximately 50 units in urban east side and 100 units in urban west side.

- In the suburbs, most projects under construction or recently completed are over 150 units.

Figure 5: Multifamily Building Permits Issued, May 2013 Year to Date



	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
City of Portland	767	465	874	1793	1623	2466	2038	2802	2103	345	622	852	1,612	1,119
Multnomah Co. (excluding Portland)	181	570	297	1062	288	46	119	56	24	125	47	0	0	12
Washington Co.	501	695	866	1040	1279	664	1364	674	572	319	212	473	630	942
Clackamas County	473	327	208	81	181	226	564	100	0	128	5	371	435	20

Source: US Census

Mark and Patrick Barry predict that despite the uptick in new apartment construction, the market will not become overbuilt. They emphasize the projected population growth of 25,000-30,000 per year and that the new units will be delivered in intervals. They expect that some neighborhoods will experience slow absorption, higher vacancies, and possible concessions until there is sufficient time for the new units to be absorbed. ■