Portland multifamily market continuing to attract investors

Daily Journal of Commerce I November 6, 2012 I By Lee Fehrenbacher

According to Greg Frick, a partner at HFO Investment Real Estate, "supply is not keeping up with demand" for apartments in the Portland-metro area. (Photo by Sam Tenney/DJC)

Cardinal Group, a private real estate investment firm based in Denver, has watched Portland for years and bided its time.

"If and when job creation starts to pick up, we feel the urban core will really start to benefit," said Eric Frank, one of the company's principals. "As these people come off the sidelines, they're going to be looking for places to live that are probably within 10 minutes of the places they work, with access to mass transit and entertainment – and that's what, really, all of Portland provides."

With Oregon Health and Science University's Collaborative Life Sciences Building set to open in the future, Cardinal Group saw a ripe market. Last week it purchased the 290-unit RiverPlace Square apartment complex in the South Waterfront District. The $77.5 million multifamily transaction was the largest in Portland this year.

Approximately 7,000 faculty members and students are expected to use OHSU's new facility, and Frank added that Portland's compelling lifestyle is attracting young, highly educated professionals to its core. That in turn is attracting investors like Cardinal Group, and experts say it's likely to continue.

Greg Frick, a partner at HFO Investment Real Estate, said a clear indicator is Portland's vacancy rate. At 4.5 percent (according to the U.S. Census Bureau), it's the ninth lowest among the nation's top 75 Metropolitan Statistical Areas.

"I think it just continues to say (Portland has) high barriers of entry," he said. "We have the in-migration coming in and the lack of new supply that's available. Yes, some is being built, but it's not online in full force yet. People are still coming here. It's the place to go, and supply is not keeping up with demand."

Frank said strong demand is one of the main reasons why Cardinal Group pulled the trigger on RiverPlace. Portland, he said, is attractive from an investment standpoint because its downtown core is constrained geographically (by the river and the hills) and politically. So, there is limited opportunity to build new units.

"Politically, there are high barriers to entry, where it's difficult to get projects completed," Frank said. "And that to us is a very important factor, and it's created a strong imbalance between supply and demand where there are substantially more absorptions than completions."

The supply of new rental product has increased in recent years, but it's only about one-third the amount from between 2004 and 2008. According to the third-quarter report issued by Portland State University's Center for Real Estate, 21 apartment complexes – 2,619 total units – are slated to open this year.

In addition, between 10,000 and 15,000 units are either under construction or being planned. Not all of those units will be built, but the data reveals increased competition, according to HFO, and greater demand from investors.

The first three-quarters of 2012 yielded nine apartment purchases for more than $10 million in the Portland-Vancouver, Wash. MSA, according to data from HFF, a national real estate capital intermediary with offices in Portland. HFF also facilitated the financing for the RiverPlace transaction.

One of the largest, the 554-unit LaSalle in Beaverton, sold in March for $77.2 million. In June, the 300-unit Forest Rim in Tualatin sold for $42.15 million; and in August, the 202-unit Axcess 15 in Portland sold for $48.6 million.

Last year, such large purchases accounted for 80 percent of the total dollar volume of apartment trading, according to the Metro Multifamily Housing Association. That's expected to taper off next year, but experts say non-institutional transactions less than $10 million should pick up as more private investors vie for a place in the market.

That has put downward pressure on capitalization rates; they're hovering between 5.25 and 6 percent – the lowest for the market in years. Low vacancy rates and strong rents also may boost Portland's apartment market next year.

But with banks still somewhat hesitant to lend, new projects could encounter challenges.

"You have to be well-healed to make those things happen," Frick said, "and so I think that's going to keep us in this cycle a little longer than you'd typically see coming out."

Frank said Cardinal Group feels like it has entered the market at the right time, with occupancy and rents ($1.68 per square foot in the downtown core) beginning to firm up, and a lot of room left in the housing cycle.

To that end, Cardinal Group plans to invest significantly in upgrades for RiverPlace, which hasn't been touched since it was built in the early '90s. Frank said he preferred not to comment on the budget, but said improvements are important because many condominiums were converted to apartments in Portland during the recession and now renters' expectations are higher.

In addition to new interior finishes, Cardinal Group will add a rooftop deck, three dog parks (one with an agility course), a sizable fitness center with a yoga studio and private, fenced yards for some of the units.

That work will begin in three to four months, and Frank said Cardinal Group is in the process of selecting its design/construction team.

Frank expects more investors to attempt to enter the Portland market in the near future, and so uniqueness will increase the value of RiverPlace.

"We don't want it to be just another standard upgraded apartment community," he said. "We really want it to have a different twist."