2008 MISSOULA HOUSING REPORT

"Current Knowledge, Common Vision: Growing a Missoula to Treasure"

Released April 14, 2008

A Community Service Provided by the Missoula Organization of REALTORS®

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Notes for Reading the Report

1. As in our past reports, we use data that are publicly available and statistically valid. Our interpretation of the data in some cases may lead to judgments that we believe are sound, but you may disagree with. If so, we invite your comments – that way we can continue to improve this yearly report.

2. Unless otherwise noted, data presented in the text and figures are for the Missoula Urban Area, which includes the City of Missoula and its neighborhoods and surrounding urbanized area, defined as: Downtown, Central Missoula, University, South Hills, Fairviews/Pattee Canyon, Rattlesnake, Bonner, East Missoula, Clinton, Turah, South Hills, Linda Vista, Miller Creek, Lolo, Target Range, Orchard Homes, Big Flat, Blue Mountain, Mullan Road, and Grant Creek. Some data represent only the city or all of Missoula County, and are noted as such.

3. "Median" is a term used often in this report and is an important term to understand. A median is the amount at which exactly half of the values or numbers being reported are lower and half are higher. A median can be more or less than an "average," which is the amount derived by adding the total of all values being reported and dividing by the number of individual values. So a median home price, for example, is the price of the one home, among all prices being considered, that has half of the other homes that are less in price and half that are more in price. In many instances, including reports of home prices, a median can be a more accurate representation than an average, because the sale prices of a very few extraordinarily expensive houses will significantly raise the average, but have little effect on the median.

4. Research for this report was conducted principally by the Missoula Organization of REALTORS® (MOR). Also contributing to the report were the University of Montana Bureau of Business and Economic Research and a consulting contributor to "The State of the Nation's Housing," a yearly release from the Joint Center for Housing Studies of Harvard University. All of these contributors also served as sources of this report's data and information; other sources were the US Census Bureau, US Bureau of Economic Analysis (BEA), US Internal Revenue Service (IRS), US Department of Housing and Urban Development (HUD), Montana Department of Labor and Industry, National Association of Residential Property Managers (NARPM), Missoula Housing Authority (MHA).

5. MLS refers to the Multiple Listing Service operated by the Missoula Organization of REALTORS® for the orderly correlation and dissemination of listing information so participants may better serve their clients and customers and the public

Message From the Coordinating Committee

April 14, 2008

This "2008 Missoula Housing Report" is the third such annual report to the community. This year's report, like last year's, benefits from improvements and expansion – thanks to suggestions from interested readers like you.

In 2008 we've again added a number of new measures relevant to an accurate assessment of our housing market. We have also dropped some measures from last year in favor of data that we believe will inform you better and more accurately than in the 2006 and 2007 reports. Finally, this year we have added considerably more interpretation of data and, in particular, have attempted to show inter-relationships among the various types and topics of data presented.

You should know that when we say "we," the reference is to the Coordinating Committee for the Housing Report. Beginning with last year's report, that committee became dramatically more inclusive, reaching throughout the Missoula regional community for members who represent diverse industries, causes, and points of view related to the local housing market.

Our overall purpose in devoting the many hours required to produce this report remains the same as when the Missoula Organization of REALTORS® provided its first "State of Missoula Housing Report" in March of 2006. That purpose is …

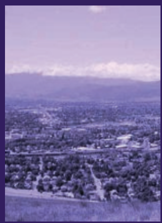
> *… to compile a credible, neutral, comprehensive snapshot of Missoula housing and housing-related information that can be used as a tool by community members and policy makers which, combined with their traditional wisdom, can contribute to the creation of a common vision about how to address housing preferences and choices as Missoula evolves into a vibrant city.*

Perhaps the most important words of this statement are "neutral" and "common vision" –

"Neutral" indicates our intent to provide accurate and unbiased data related to housing. Why? Because issues of housing, land use, and growth may be unsurpassed in their ability to elicit argument and emotion. There's nothing wrong with argument and emotion, but we strongly believe that they require, above all else, a grounding in fact, logic, and reason. That is what this report attempts to provide.

"Common vision" refers to our ability as a community – despite our great diversity of backgrounds and opinions – to join together, explore, discover, and implement effective responses to our most daunting challenges.

With great respect for the land we all call home, and for the entire Missoula community that shares that land, we invite you to read this report and get involved in meeting our housing challenges. We hope that by providing this report, we will trigger discussions and actions that will further contribute to a shared community vision and leave a positive legacy for future generations of Missoulians.



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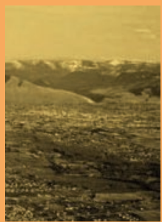


Executive Summary

The Home Ownership Market

In 2007, the number of homes sold in the Missoula Urban Area declined from the prior year. Also, the percentage gain in the median price of homes sold in 2007 was at its lowest level of the past six years. The local decline parallels, but lags, what has taken place in the Mountain States and in the US as a whole. Days on market (DOM) was at its highest level of the past seven years.

The overall financial activity for the year reflects a slight reduction of loan volume that coincides with the cooling of the market. Interest rates remained fairly level. Selected non-traditional mortgage products are no longer offered by certain lenders, who have in some cases had to tighten their underwriting guidelines. Foreclosures in the Missoula real estate market jumped in 2007.

The Residential Rental Market

Higher costs for 2-bedroom rental units (by far the most popular size rental in the Missoula area) are clearly the biggest challenge to rental affordability in our market. Although comprehensive data for Missoula rental markets in 2007 is limited, it remains clear that the Missoula rental market remained tight, with very low vacancy rates and increasing rental costs.

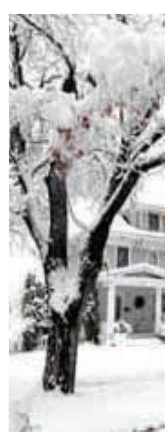
The Missoula Housing Authority has 754 available vouchers that subsidize rent to private landlords for eligible program participants. At the end of 2007, 1,079 families were on the waiting list for these vouchers. In addition, the current waiting list for Public Housing numbers 1,051 families. The waiting lists for the homeless cumulatively totaled more than 100 individuals and also more than 100 families at the end of 2007.

Land Availability, Lot Sales, and New Construction

Developable land in the Missoula Urban Services Area currently consists of just under 7,000 acres and is calculated, without regard for zoning, to accommodate just under 33,000 dwelling units. When current zoning is added to the mix, however, the number of potential new dwelling units is greatly reduced, putting developable land at a premium. To address the increasing cost and unavailability of developable land, the Missoula City-County Office of Planning and Grants recently implemented the Urban Fringe Development Area (UFDA) planning project.

Sales of empty lots in 2007 seem entirely out of keeping with past years. While the number of lots sold soared by 55% over record sales in 2006, the price per lot decreased by 37%. This apparent price drop is explained, however, by the fact that the average size of lots sold in 2007 was considerably smaller than in past years. The number of building permits issued for new construction of residences in the city of Missoula has declined in each of the past two years – by 19% from 2005 to 2006 and by 17% from 2006 to last year.

Missoula is wrestling with dramatically increasing costs of residential construction. From 1996 to 2006, of 14 housing cost components, only four increased by less than double the overall inflation rate, and another four components increased at more than triple the rate of inflation. Missoula's overall housing costs increased during these 10 years by 64%, far outstripping the inflation rate of 28%.



Trends in Population, Income, and Poverty

According to US Census Bureau estimates, Missoula County's population has increased about

1.7% per year since 1990 – slightly less than the historical rate of 1.9% per year since 1950. Since the mid-1990s, Missoula County has grown by about 1,200 persons per year. Recent net migration increases have been substantial, though not at levels of about 15 years ago. For many years Missoula County has been gaining about 500 to 1,200 people annually through net migration. Smaller net increases have been provided by live births exceeding deaths.

Missoula County's per capita income has been increasing by about 2% per year in real (inflation-adjusted) terms. In 2007, non-farm labor income jumped by its largest percentage of the past decade probably owing largely to the addition of new jobs in telecommunications**.**

Missoula County unemployment has been trending downward for most of the past decade, standing at about 2.6% in 2007. About 18½% of Missoula County households have incomes below the poverty threshold. More than 60% of county households have incomes of double the poverty threshold or higher.

Housing Affordability

In 2007, the income needed by a Missoula family for a Housing Affordability Index (HAI) of 100% is $60,672 – which means a family whose income is at that level could comfortably afford a median priced home (or any home priced lower than the median). The HAI for the past seven years shows that increases in median home prices since 2003 have significantly outstripped increases in median family incomes. As a consequence, fewer families are able to afford the median priced Missoula home.

In Missoula, nearly two-thirds of the owner occupied households in the youngest age group spend 30% or more of their gross incomes on housing, while nearly half of households in the next-younger age group exceed the 30% of income recommended maximum.

For renters, an even greater percentage of those in the youngest age group exceeds the 30% recommended monthly maximum. Also, in the oldest age group, the percentage of those whose rent exceeds the 30% level is nearly as high as for the youngest group.

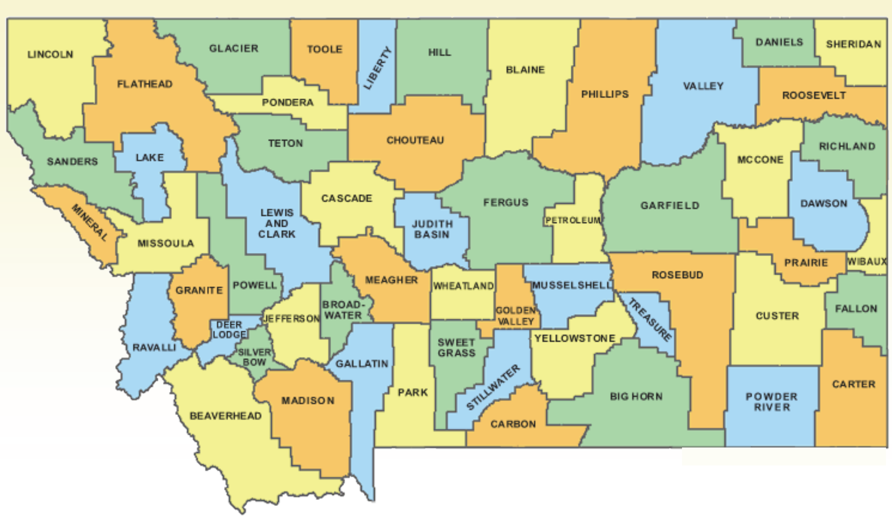
Conclusion and Outlook

For 2007, data related to the Missoula housing market reveal two indications that are of greatest importance:

Some data indicate a softer real estate market – data such as that for number of homes sold, median sales price of homes, and building permits issued.

Missoulians' income growth remains strongly positive and unemployment continues to trend downward. Yet, despite this "good news," the "bad news" about housing in recent years is truer than ever: more and more Missoula families are finding their incomes insufficient to own or rent modest homes and apartments, and many more families are paying an overly large share of their incomes for housing – threatening their financial well-being.

The challenge to keep home prices and rents within reach of working families with average or below average incomes is a challenge that requires a cooperative, community-wide response.



The Home Ownership Market

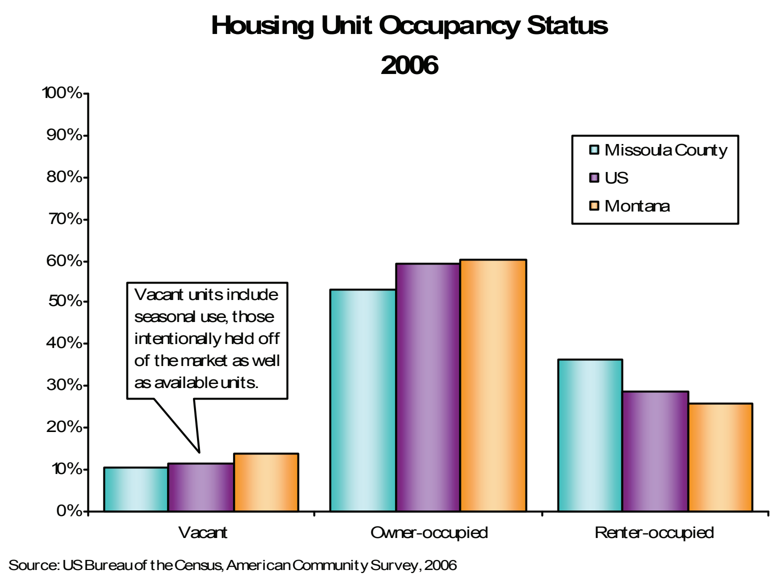
Sales of Homes in 2007

Housing Occupancy

Compared with the entire state of Montana and with the US overall, Missoula County has proportionately fewer residences that are owner occupied and more that are renter occupied, as shown in Figure 1. The divergence of Missoula County from state and national figures is not great, however, and may be explained mostly or entirely by Missoula being the home of the University of Montana – as many students are renters and few are homeowners.

The vacancy levels of a little more than 10% shown in Figure 1 are probably overstated, particularly for Missoula County, because vacancies include residences that are used only seasonally or are temporarily vacant.

Figure 1: Missoula Homes Are Occupied by Fewer Owners and More Renters Than Montana and US Homes



Median Volume and Price Trends

In 2007, signs appeared that the housing downturn afflicting many markets across the US may also be affecting Missoula – though far less seriously thus far.

For the first time in the past five years, the number of homes sold in the Missoula Urban Area declined from the prior year (Figure 2). Also, although year-over-year home prices continued to go up, the percentage gain in 2007 was at its lowest level of the past six years.

Homes sold in Missoula dropped by 13%, from a record 1,586 in 2006 to 1,385 in 2007. The median price of the homes sold in 2007 climbed by almost 6%, from nearly $207,000 in 2006 to just under $220,000 last year. While that gain is significant – and is particularly strong in light of dramatic decreases in numerous US metropolitan markets – it doesn't match the 7% and higher increases registered in most previous years of the 2000s.

Despite the slowing of the median home price appreciation, significantly fewer homes were sold in 2007 at prices that are affordable to most Missoulians. For example, the sale of homes for amounts under $200,000 decreased by 150 in 2007 from 2006.

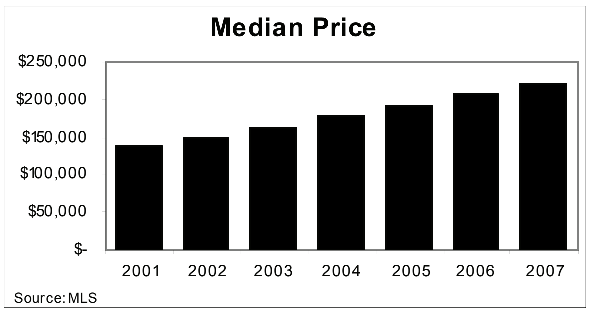
Figure 2: Homes Sold in the Missoula Urban Area Declined for the First Time in 5 Years, With Slower Price Appreciation

Fig. 2A: Number and Median Price of Homes Sold

Year	Missoula Annual Sales	Median Price	% Change
2001	1,211	$ 138,000	-
2002	1,119	$ 149,500	7.69%
2003	1,150	$ 163,000	8.28%
2004	1,290	$ 179,000	8.94%
2005	1,536	$ 192,000	6.77%
2006	1,586	$ 206,850	7.18%
2007	1,385	$ 219,550	5.78%

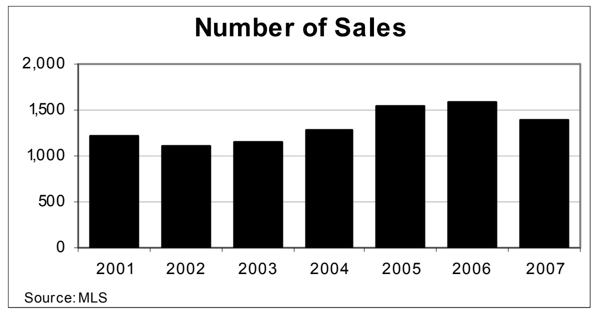
Source: MLS

Fig. 2B: Trend in Number of Homes Sold



Source: MLS

Fig. 2C: Trend in Median Price of Homes Sold



Source: MLS

Comparative Trends in Home Prices

Does the slowing of home price appreciation seen in Missoula in 2007 indicate that our market will follow much of the US into a housing industry recession? Figure 3 suggests this might happen, though the Missoula market is generally free of numerous elements – in particular, a large percentage of homes financed through subprime mortgages – that have plagued other areas.

Nonetheless, home price appreciation in Missoula fell to just over 2% growth in the 4th quarter of 2007. As Figure 3 shows, this decline parallels, but lags, what has taken place in the Mountain States and in the US as a whole.

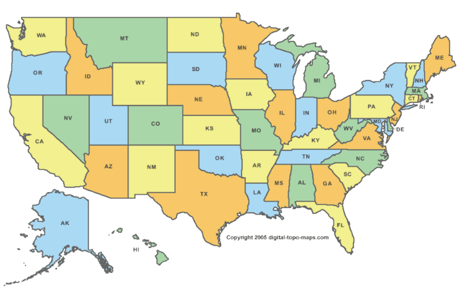
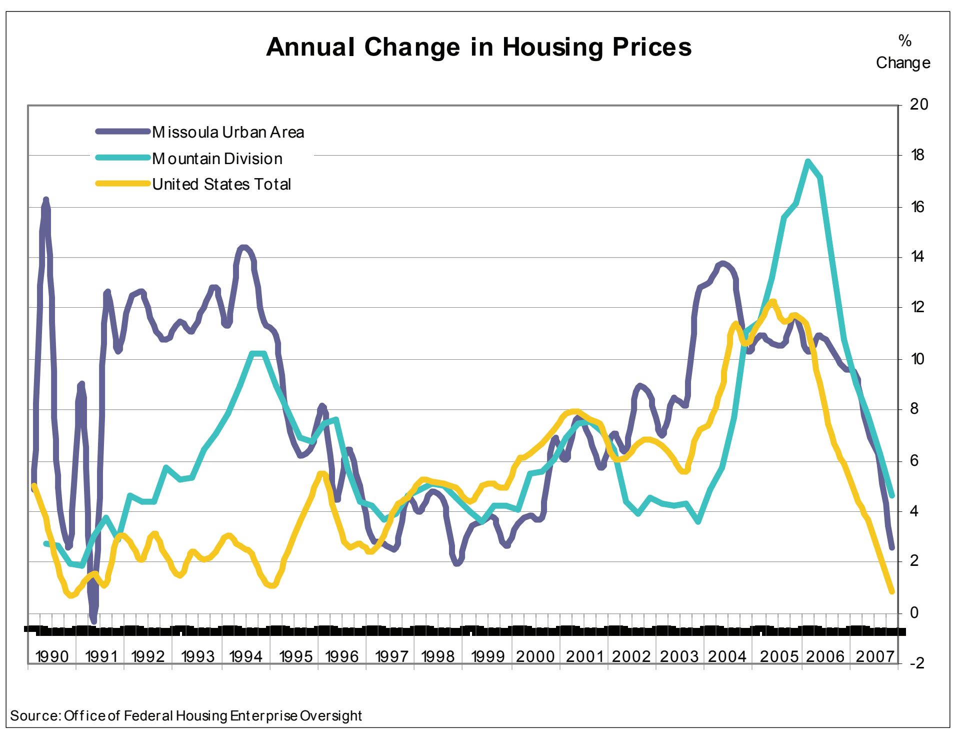


Figure 3: Home Price Increases Slowed in U.S., Then Mountain States, Then Missoula



Source: Office of Federal Housing Enterprise Oversight

There are some important differences, however, in these price trends for the US, Mountain States, and Missoula. Price gains for the Mountain States peaked at a far higher level (in 2005-06) and have dropped more dramatically than for either Missoula or the US. This decline was led by virtual price collapses in Nevada and Arizona, both of which registered negative appreciation (price declines) in 2007. As for the country as a whole, the outsized influence of home price trends on both coasts – where values have fallen into negative growth territory in several populous states (led by California, New Jersey, Massachusetts, and Florida) – has depressed national price gains for nearly three years and held overall price gains below those of both the Mountain States and Missoula in 2006 and 2007.

Uncertainties about where our local real estate market may be headed are not cleared up with a look at the average home's days on market (DOM) in 2007. As Figure 4 shows, DOM in the first half of last year soared to its highest level of the past seven years (126 days). But DOM for the year's second half retreated to a level generally in line with the second half of recent past years. Nonetheless, 2007's average DOM for the full year, like the first half, was the highest recorded in the past seven years.

Figure 4: Mixed Signals From Missoula Area Homes' Days on Market

Days on Market			
Year	January →June	July →December	Annual Average
2001	113	100	107
2002	100	85	93
2003	99	104	104
2004	106	102	102
2005	114	107	109
2006	109	111	110
2007	126	107	116

Source: MLS

DOM is not a mere academic indicator or one that solely affects people who are selling their homes. DOM is one measure that can be factored into home appraisals and also loan availabilities.

What's more, according to both the National Association of REALTORS® and the Joint Center for Housing Studies of Harvard University, an increase in DOM is one indication of a "down" market. But it is not by itself conclusive, and – as discussed above and in later sections of this report – other indicators present a mixed bag of signals on the Missoula market's direction.

REAL ESTATE FINANCE ACTIVITY IN 2007

The overall financial activity for the year reflects a slight reduction of loan volume that coincides with the cooling of the market. Interest rates remained fairly level, as Figures 5A and 5B show.

Figure 5A: 2007 Mortgage Interest Rates Fluctuated in a Narrow Range …

Mortgage Types	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Year End
30 Year Fixed	6.00%	6.125%	6.50%	6.25%	6.00%
15 Year Fixed	5.75%	5.75%	6.125%	5.75%	5.50%
FHA / VA	6.00%	6.00%	6.375%	6.00%	5.815%
5/1 ARM	5.875%	5.75%	6.375%	5.75%	5.75%
MBOH	5.75%	6.00%	6.00%	6.125%	6.125%

Figure 5B: … and Were Consistent With Recent Years' Rates
Year-End Conventional Rates

	2001	2002	2003	2004	2005	2006	2007
30 Year Fixed on 12/31	7.25%	5.75%	5.75%	5.625%	6.125%	6.25%	6.00%

MORTGAGE LOANS

While the Missoula real estate market has thus far largely escaped impacts of the nationwide housing and credit crisis, a pronounced impact has been felt regarding the availability of mortgage products.

Selected non-traditional mortgage products (such as subprime loans, and also – in some cases – loans requiring little or no documentation and/or down payment) are no longer offered by certain lenders, who have in some cases had to tighten their underwriting guidelines. This tightening can raise interest rates for some borrowers or exclude them entirely from qualifying for loans they might easily have gotten before the national crisis developed.

In response to the crisis, the Federal Reserve Board has proposed changes to the Home Ownership and Equity Protection Act that would mandate more stringent requirements and transparency in home mortgage lending. The intent would be to allow consumers to make decisions about home mortgage options more confidently, with reasonable assurance of less exposure to risk. Other pending proposals would protect consumers and limit choices for non-traditional mortgage products.

As market conditions continue to change, a borrower's prospects for pre-approval of a loan changes with them. Those who will most feel the effects of any changes are prospective borrowers who lack good credit, a steady income, or cash reserves.

DOWN PAYMENTS

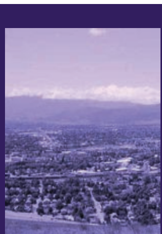
The average down payment, at 3% to 5%, remained generally unchanged through 2007.

FORECLOSURES

Foreclosures in the Missoula real estate market jumped in 2007. Notices of foreclosure sale increased by 15% from 2006 to 2007 and were higher in 2007 by 34% over the average for the prior six years. Meanwhile, cancellation of notices of sale were slightly lower in 2007 than in 2006. As a result, net foreclosures soared in 2007 by 48% over 2006 and by 67% over the 2001-06 average.

Figure 6: Foreclosures Spiked in 2007 to Highest Level in Years

Year	Notice of Foreclosure Sales	Cancellation of Foreclosure Sales	Foreclosures
2001	161	98	63
2002	206	122	84
2003	177	123	54
2004	174	106	68
2005	176	130	46
2006	215	142	73
2007	247	139	108



THE RESIDENTIAL RENTAL MARKET

Rental is an important segment of any housing market, but is especially vital in college towns such as Missoula, where a significant number of students create greater demand for rental housing. In fact, as Figure 1, showed, Missoula's rental market is larger (vs. the owner-occupied housing market) than in Montana or the US.

Approximately 50% of rental units in the Missoula market area are owner managed. While comprehensive statistics on all rental units are not routinely gathered, the Western Montana Chapter of the National Association of Residential Property Managers (NARPM) has begun to gather monthly information from its member property management firms regarding vacancy rate and rental rates for the units they manage.

MARKET RATE RENTAL IN 2006

Figure 7A shows US Census Bureau figures for rental costs in 2006 by size of residences. Higher costs for 2-bedroom units (by far the most popular size rental in the Missoula area) are clearly the biggest challenge to rental affordability in our market.

Data are severely lacking in the past year for a more detailed examination of trends in rental costs. While there were data provided by the NARPM, their data collection system is relatively new and untested, collects data only from NARPM members, and in 2007 collected data only for the period October through December. Therefore, for purposes of this year's Housing Report, we chose to use census data instead to ensure an accurate view of the rental market in Missoula. We hope to include NARPM data in next year's report. Despite the lack of 2007 rental data, it remains clear that the Missoula rental market remained tight, with very low vacancy rates and increasing rental costs.

Figure 7A: 2-Bedroom Rentals Are Comparatively Costly …

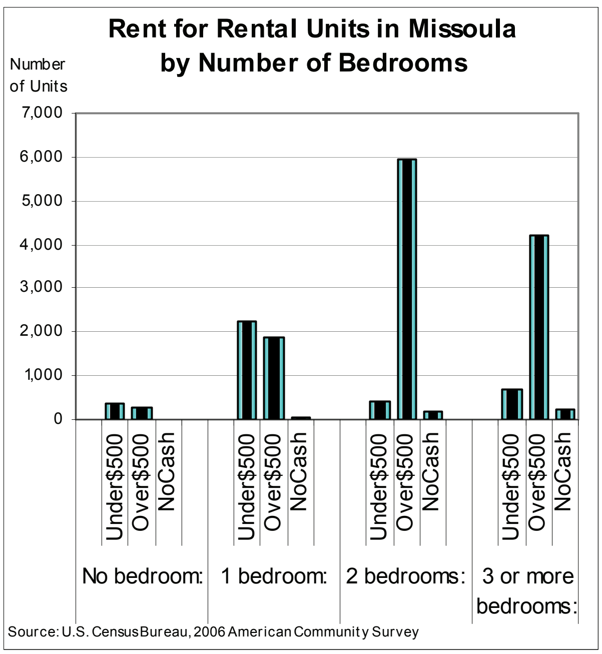
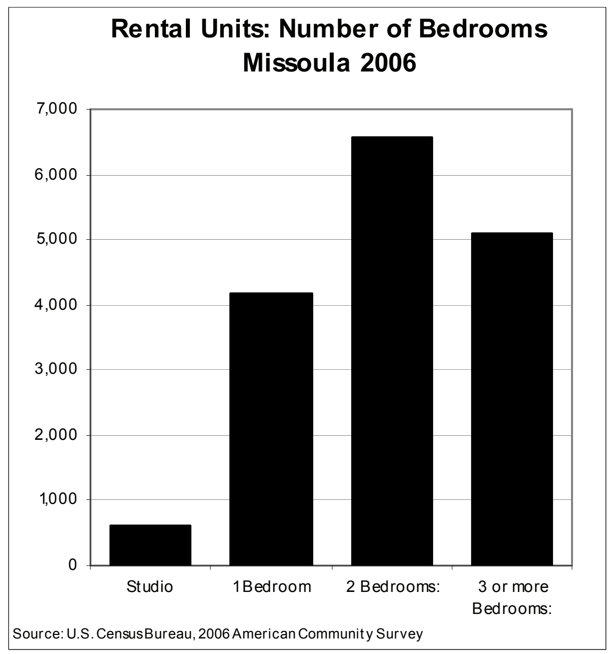


Figure 7B: … and Constitute the Largest Rental Market Segment



STATUS OF RENTAL ASSISTANCE

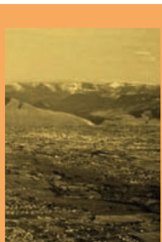
The Missoula Housing Authority (MHA) has 754 available vouchers that subsidize rent to private landlords for eligible program participants. At the end of 2007, 1,079 families were on the waiting list for these vouchers, with an expected wait time of 2½ to 3 years. Those at the bottom of the list will not likely be served until late 2010.

The typical families on the list to receive these vouchers live, work, and pay rent in our community as best they can with their relatively low incomes. Without vouchers some of these families are forced to leave Missoula, even though the labor they might otherwise provide is probably needed in our low to no unemployment economy. Some with voucher assistance improve their situations enough that they become self-sufficient. As shown below in the Affordability section of this report, most experience extreme housing cost burden, meaning a large portion of their income goes to housing. This leaves less income for other essentials, such as food and health care, and further jeopardizes their already shaky family finances.

The year-end 2007 waiting list for Public Housing provided by MHA numbered 1,051 families. Many of these families are also on the voucher list – and perhaps on other lists for assistance as well. Public Housing applicants are listed separately by bedroom size, so wait times vary widely, from a few months to more than two years. The longest wait is for one and two bedroom households.

MHA has four waiting lists for homeless persons, each with different targeting requirements. For example, one of these is for single-room occupancy (SRO), with a waiting list of 59, which accommodates only individuals who are currently homeless. Other lists are limited to homeless families, homeless persons (singles and families) with disabilities, and homeless veterans.

The lists of homeless applicants are broken into two categories with separate wait lists. They totaled more than 100 individuals and more than 100 families at the end of 2007. Evidence indicates that until they can be served, the homeless stay in cars, the Poverello Center, on couches or floors with friends or family, or on the streets.



LAND AVAILABILITY, LOT SALES, AND NEW CONSTRUCTION

UNDEVELOPED LAND

One of the major factors in the cost of housing is the cost of land. In general, land costs will increase as less of it is available. In Missoula County (and also many other communities of the Mountain West), the “squeeze” on costs created by the gradual shrinking of available land is particularly acute, because relatively little developable land can be had at any price.

The problem of too little developable land is most vividly seen in maps – two of which are presented as Attachments 1 and 2 to this report.

More than half of Missoula’s total area consists of public lands – out of reach to all but very limited development, if any. Of the 46% of the county that is in private hands, more than half is held by one landowner, Plum Creek Timber. While this land is not necessarily undevelopable, the amount and pace of development is up to the owner, and is greatly restricted by applicable law, regulations, and citizen opposition.

Of the 21% of Missoula County’s land that is in the hands of private owners other than Plum Creek, significant acreages are subject to severe or prohibitive development constraints, such as wetland dedication, steep slopes, no access, and conservation easements. And of course other large swaths of the remaining land are already developed and occupied, whether for residential, commercial, or industrial uses.

Developable land in the Missoula Urban Services Area currently consists of just under 7,000 acres and is calculated, without regard for zoning, to accommodate just under 33,000 dwelling units. When current zoning is added to the mix, however, the number of potential new dwelling units is greatly reduced, putting developable land at a premium.

To address the increasing cost and unavailability of developable land, The Missoula City-County Office of Planning and Grants recently implemented the Urban Fringe Development Area (UFDA) planning project. The Urban Fringe is the area encompassed by the 201 Sewer Service Planning Area – the area that is slated, by city policy, to ultimately be served by city sewer.

Sales of empty lots in 2007, as shown in Figure 8, seem entirely out of keeping with past years. While the number of lots sold soared by 55% over record sales in 2006, the price per lot plunged by 37%. This apparent price drop is explained, however, by the fact that the average size of lots sold in 2007 was considerably smaller than in past years. The average lot size decline is largely explained by several new subdivisions that offered much smaller lots in 2007, at commensurately lower prices, than was typical in Missoula in 2006 and earlier.

Figure 8: Lot Sales Continue to Climb,
With Price Drop Reflecting Smaller Average Size

Year	Lot Sales	Price
2001	28	$43,450
2002	74	$79,900
2003	58	$75,900
2004	65	$89,500
2005	104	$117,750
2006	111	$115,000
2007	172	$72,000

Source: MLS

PACE AND COSTS OF DEVELOPMENT

The number of building permits issued for new construction of residences in the City of Missoula, shown in Figure 9, has declined in each of the past two years – by 19% from 2005 to 2006 and by 17% from 2006 to last year. The decline in permits issued for construction of single family homes is slightly higher than for all residences.

Figure 9: Fewer Permits Have Been Issued for New Home Construction
for Two Consecutive Years
City of Missoula Building Permits for New Construction

Number of Permits Issued			
	Fiscal Year* 2005	Fiscal Year 2006	Fiscal Year 2007
Single Family	457	374	303
Mutli-Family	19 (166 units)	9 (47 units)	13 (56 units)
Duplex	14	16	14
Subtotal (Residential)	490	399	330
Misc. (fence, garage, etc.)	182	152	200
Total	672	551	530

Source: Missoula Building Inspection Division

(- A fiscal year runs from July 1 of the prior year to June 30 of the year provided.)*

The decline in building permits issued may be explained in part by higher costs of residential construction dampening demand for homes, as an increasing share of potential purchasers find prices beyond their reach. As Figure 10 reports in detail, every component of residential construction increased during the 10 years from 1996 to 2006 by more than the overall US rate of inflation (of 28.5% from 1996 to 2006, as measured by the US Consumer Price Index).

Data for Figure 10 originated in a cooperative effort between the Missoula Building Industry Association (MBIA) and MOR. In 1996, 2001, and 2006, these organizations produced "A Walking Tour of the Costs Associated with Development in the Missoula Urban Area" – an analysis of the various costs incurred in building new homes. The Walking Tour gathered cost data for a 2-bedroom, 2-bath home on a crawl space, with a 2-car garage on a small lot in a new subdivision. (The entire presentation is available on MOR's website missoularealestate.com.)

Figure 10: Most Components of Housing Costs Have Increased Far in Excess of Overall Inflation
Housing Cost Component Increases (Dollars and Percentages*) for Missoula Market

Housing Cost Summary
Cost and Percentage Increase

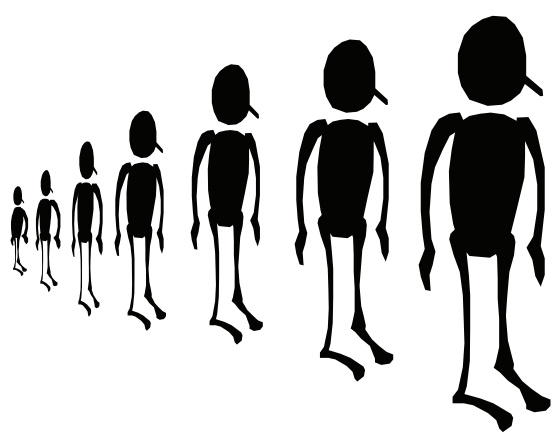
	1996	2006	Change	Percent Increase
Land Costs	$ 8,500	$ 11,156	$ 2,656	31%
Infrastructure Costs	$ 13,265	$ 22,080	$ 8,815	66%
Subdivision & Carrying Costs	$ 5,000	$ 7,000	$ 2,000	40%
Impact Fees & City Permits	$ 850	$ 3,939	$ 3,089	363%
Utilities	$ 50	$ 650	$ 600	1200%
Architect	$ 475	$ 1,500	$ 1,025	215.79%
Excavation, Concrete	$ 9,316	$ 15,935	$ 6,619	71.05%
Framing, Roofing, Siding, Windows, Doors	$ 19,001	$ 33,635	$ 14,634	77.02%
Heating, Plumbing, Electric	$ 10,085	$ 17,145	$ 7,060	70%
Insulation, Drywall, Painting, Trim, Gutters	$ 9,654	$ 12,718	$ 3,064	31.74%
Cabinets, Floor Covering, Fixtures	$ 5,525	$ 7,870	$ 2,345	42.44%
Cleaning, Insurance, Miscellaneous	$ 1,485	$ 3,012	$ 1,527	102.83%
Profit and Overhead	$ 12,480	$ 20,496	$ 8,016	64.23%
Soft Costs	$ 8,327	$ 13,640	$ 5,313	63.8%
Subtotal	$ 104,013	$ 170,776	$ 66,763	64.19%

*Inflation as measured by the US Consumer Price Index over the same period amounted to 28.5%

Of the 14 components listed in Figure 10, only four increased by less than double the overall inflation rate, and another four components increased at more than triple the rate of inflation. The overall increase of 64% in all 14 components is 125% greater than overall inflation. Adding only three of these cost elements – for land, infrastructure, and subdivision & carrying – yields an increase in total lot costs from $26,765 in 1996 to $40,236 in 2006, a gain of $13,470 or 50.3%.

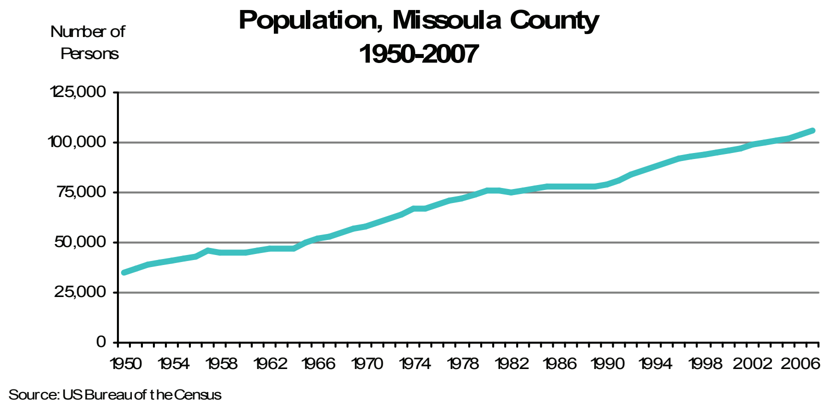
Trends in Population, Income, and Poverty

Population Dynamics



According to US Census Bureau estimates, Missoula County's population has increased about 1.7% per year since 1990 – slightly less than the historical rate of 1.9% per year since 1950. The population growth rate peaked in 1993. However, the absolute growth (in numbers of people rather than percentages) has not declined, because each year's percentage growth is calculated from a higher beginning population. Since the mid-1990s, Missoula County has grown by about 1200 persons per year.

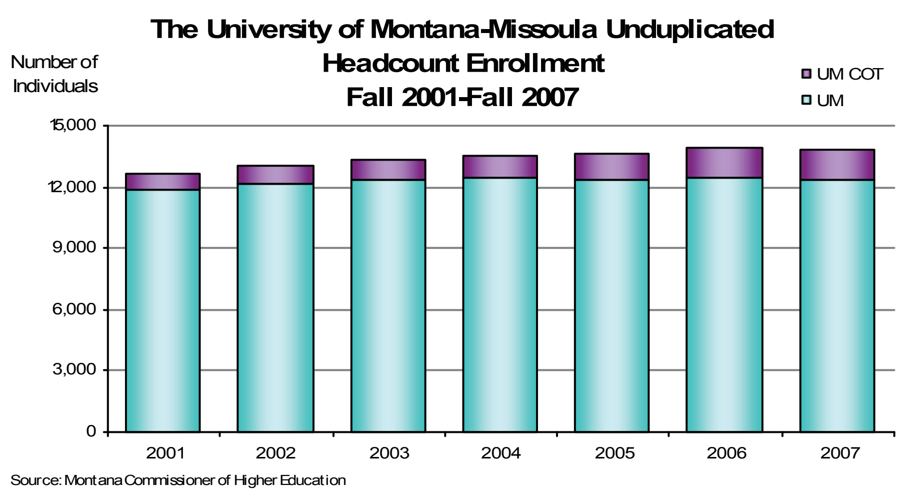
Figure 11: Missoula Population Has Maintained a Steady Climb for Many Years



UNIVERSITY ENROLLMENT

As Figure 12 shows, unduplicated headcount enrollment at the University of Montana-Missoula has remained steady for the past six years, at just over 12,000 students. The College of Technology, affiliated with the university, has increased at a low but steady rate, accounting for almost all of the growth in overall college student numbers.

Figure 12: University of Montana Local Enrollment Has Been Stable



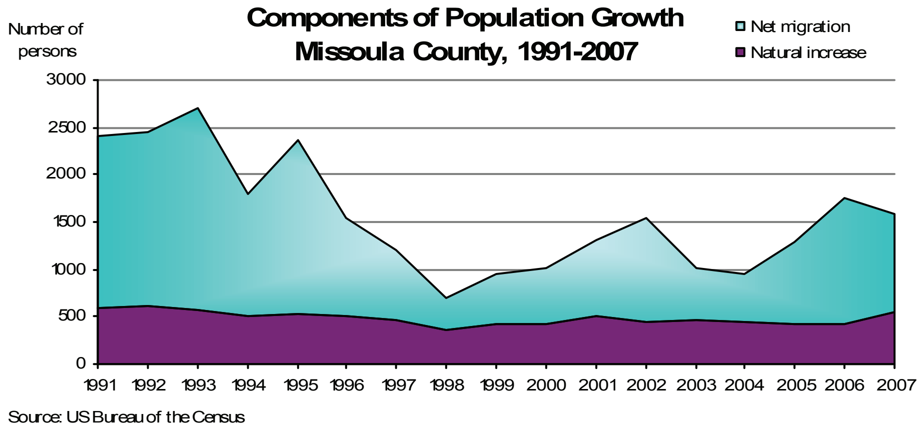
COMPONENTS OF POPULATION CHANGE

Population changes result from two distinct components: natural increase (or decrease), which is the number of live births minus the number of deaths, and net migration, which is the number of people moving into a given area or jurisdiction minus the number of people moving out.

For many years, as Figure 13 shows, Missoula County's annual natural increase in population has hovered at a consistent positive level of plus 500 to 600. Over the same years, however, net migration has swung widely, with net gains of as much as 2,000 in the early 1990s and as little as a few hundred in the late '90s.

Recent net migration increases have been substantial, though not at levels of about 15 years ago. Despite the wide variation in net migration, it has remained positive every year since 1990 (though that contention is challenged by data from the Internal Revenue Service, as explained below).

Figure 13: Missoula's Net Migration Has Been Consistently Positive, but with Significant Swings



MIGRATION

Figures 14A, 14B, and 15 present migration data as reported by the Internal Revenue Service. These data do not capture all migrants, as they include only those filing tax returns (and their dependents) in Missoula County in at least one of two consecutive years. Nonetheless, they provide a reliable picture of the origins and destinations of migrants. From these data, we can see that about 6,000 persons move to Missoula County each year; two-thirds are from another state and one-third from other Montana counties. About 5,500 people annually have moved out in recent years, with less than two-thirds relocating out of state and more than one-third settling in another Montana county.

Subtracting out-migration from in-migration yields net migration – and the conclusion that for many years Missoula County has been gaining population annually through net migration. However those gains have fluctuated considerably.

Figure 14: Most Migrants Come From & Head for Other States

Figure 14A: In-Migrants

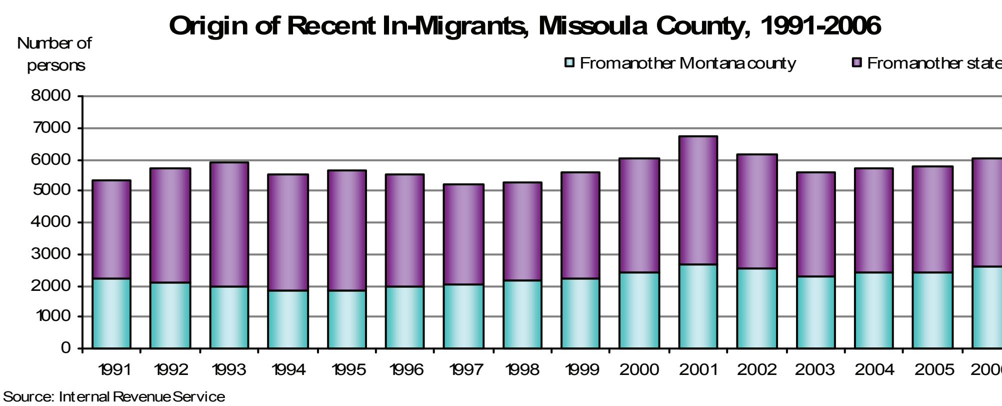


Figure 14B: Out-Migrants

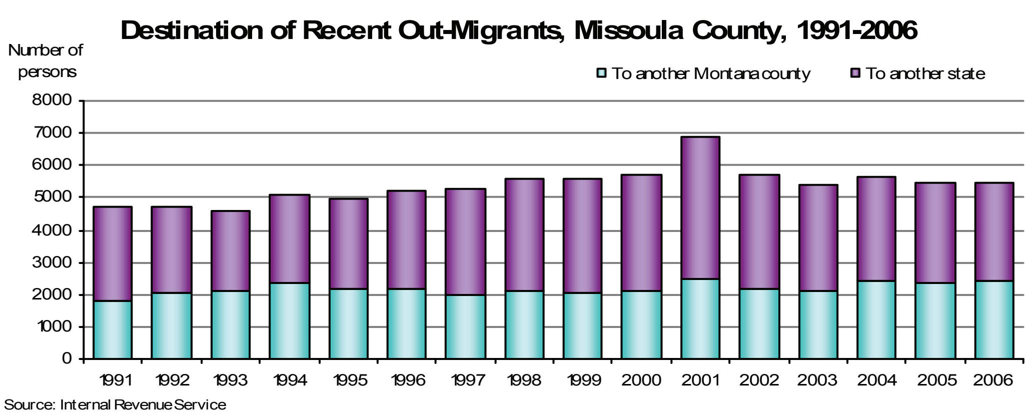
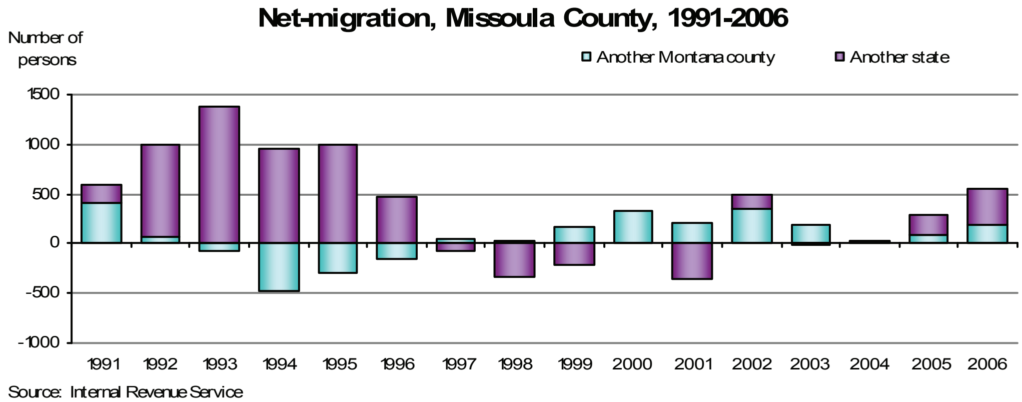


Figure 15: 2006-07 Net Migration Is Strongly Positive for First Time in 10 Years



The IRS data show, in Figure 15, that net migration of out-of-state migrants was strongly positive between 1992 and 1996. Since then, net migration has been less than plus-500 and sometimes at or below zero, with a noticeable upturn in 2005 and 2006.

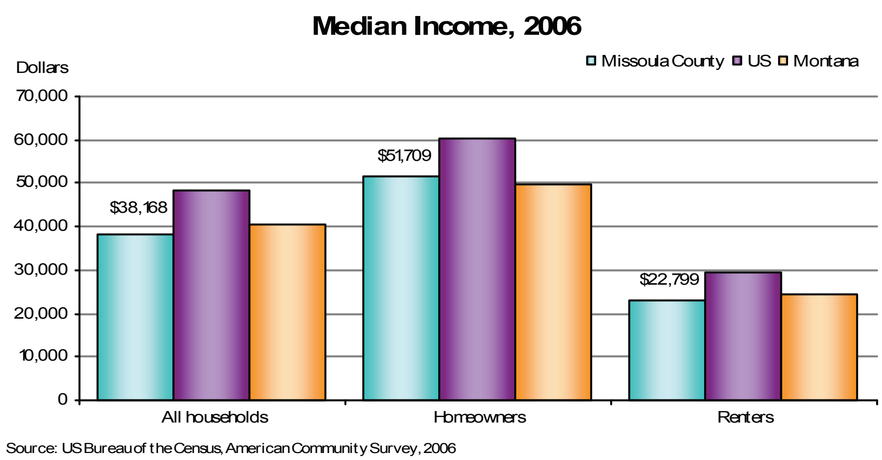
Income and Employment

Income Measures

Figure 16 shows median income in 2006 for homeowners, renters, and overall. (Remember that median is the point at which exactly half of all incomes are greater and the other half are less.)

The median income for Missoula County homeowners in 2006 was more than double the median for Missoula County renters. This relationship holds both nationwide and for all of Montana. However, the income gap between homeowners and renters is wider for Missoula than for the state or the US. As in previous measures, this wider gap may be explained by Missoula's large population of college students, who tend to rent rather than own and have little or no income.

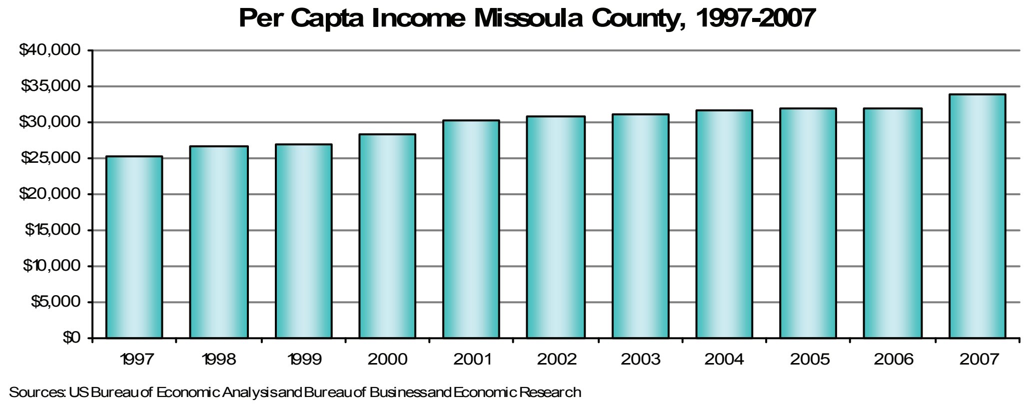
Figure 16: Missoula County Median Household Income Lags That of Montana, U.S.



Another way to measure income is per capita (per person). Per capita income is regarded as a generally reliable a measure of overall economic well-being. It is the average income of all individuals living in an area, derived by adding the total income earned by everyone in a given area or jurisdiction and dividing by the total population (regardless of age or employment status).

Figure 17 shows that Missoula County's per capita income has been increasing by about 2% per year in real (inflation-adjusted) terms. Also evident in the figure is a period of stronger gains in the late 1990s, followed by weaker gains in the 2000s – until 2007, when income accelerated considerably.

Figure 17: Missoulians' Income Gains Accelerated in 2007 …

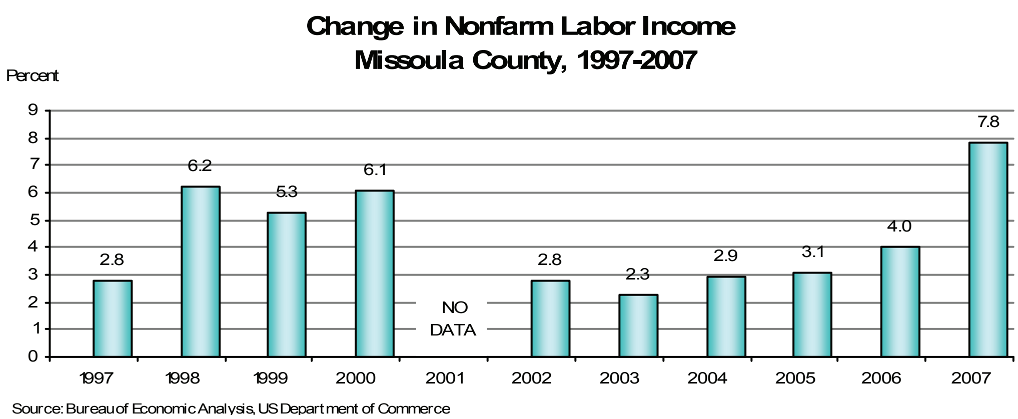


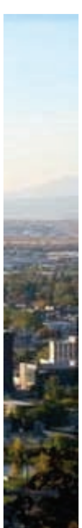
INCOME FROM LABOR

Non-farm labor income is a proxy (similar to; a representative number) for the economic activity at local levels, because it is highly correlated with gross domestic product (GDP – the sum of the value of all goods and services produced in a given area or jurisdiction).

As Figure 18 shows, Missoula County's inflation-adjusted, non-farm labor income increased rapidly in the late 1990s, retreated somewhat – though it stayed positive – in the early 2000s, and in 2007 jumped by its largest percentage of the past decade. Last year's large increase is likely to have been caused principally by the addition of new jobs in the tele-communications industry.

Figure 18: … Exceeding Even the Higher Gains of the Late 1990s



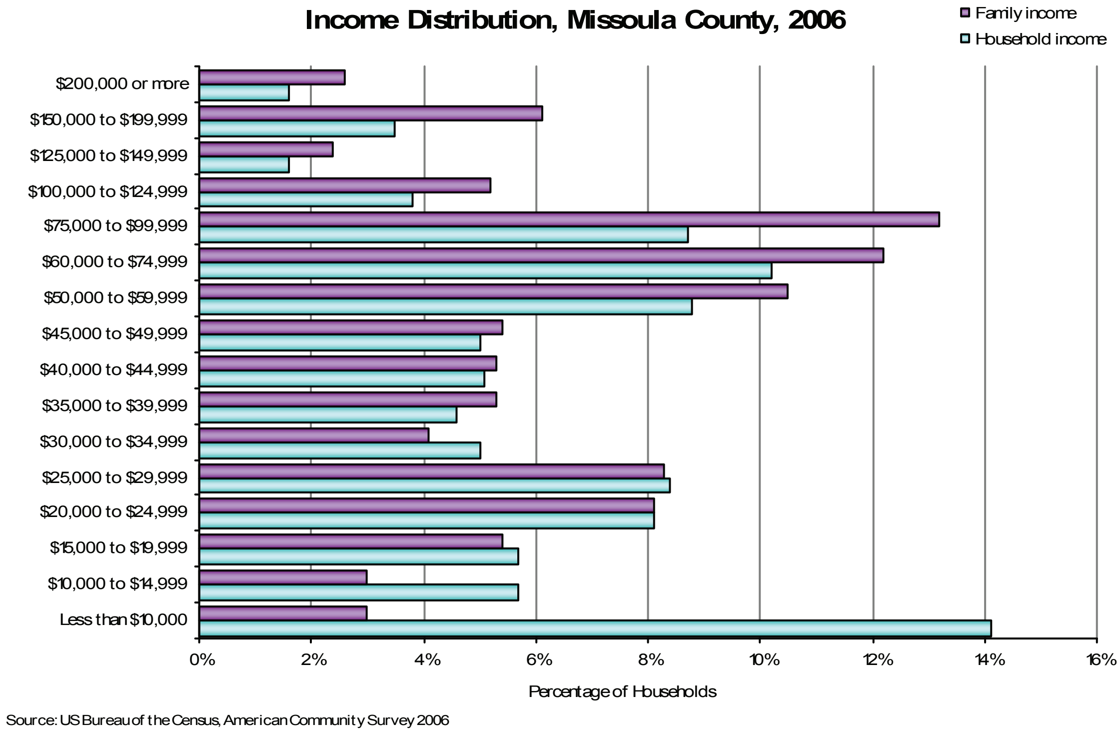


INCOME DISTRIBUTION

The Census Bureau measures family and household income by the various income groupings shown for Missoula County in Figure 19.

The figure clearly indicates that the county's incomes are concentrated at three distinct levels: $60,000 to $74,999, $25,000 to $29,999, and less than $10,000. These concentrations appear to correspond to county employment patterns, with professional workers at the high concentration, service sector workers at the middle, and retirees and students mostly composing the households with under $10,000 incomes.

Figure 19: Local Incomes Are Concentrated in Three Fairly Narrow Ranges



(Family income is that earned by members of a household who are related to each other by birth, marriage, or adoption. Household income is the total earned by everyone residing in a household, whether related or not.)

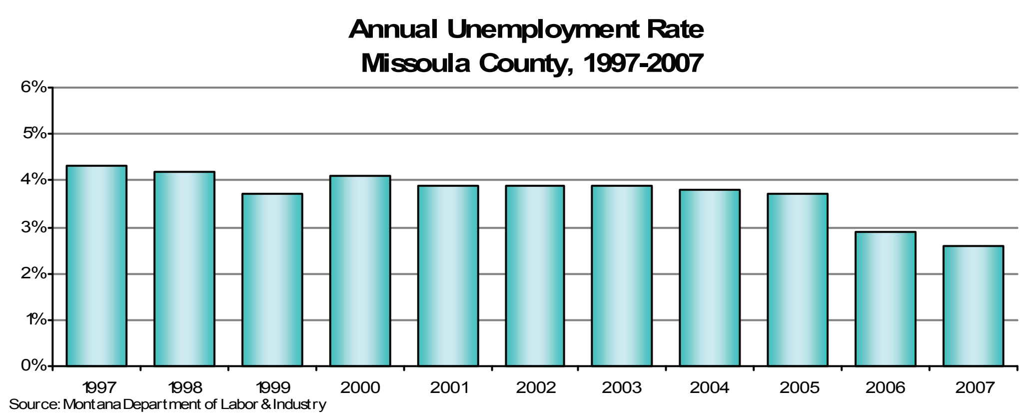
UNEMPLOYMENT

The unemployment rate measures the proportion of persons that are in the labor force (that is, seeking a job) but currently out of work.

Figure 20 shows that Missoula County unemployment has been trending downward for most of the past decade, standing at about 2.6% in 2007. This is a level that many economists consider full employment, because a certain small percentage of workers will be between jobs at any given time, whether the job market is currently favorable or not.

Missoula County's years-long decline in unemployment is similar to that of most counties in Montana, where joblessness has for some time been at levels markedly less than the US as a whole.

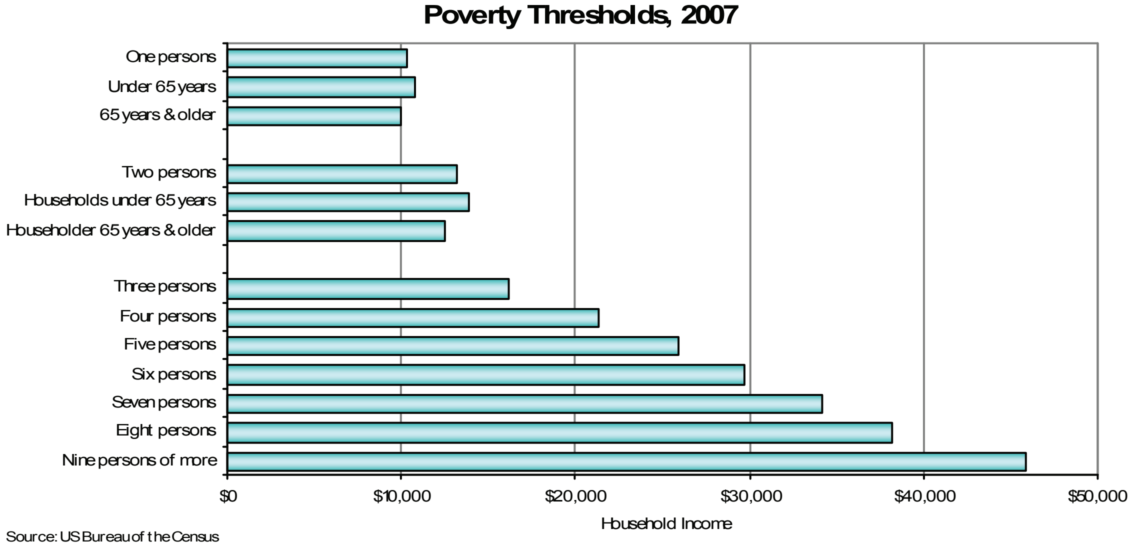
Figure 20: Unemployment Extends Its Steady Long-Term Decline



POVERTY

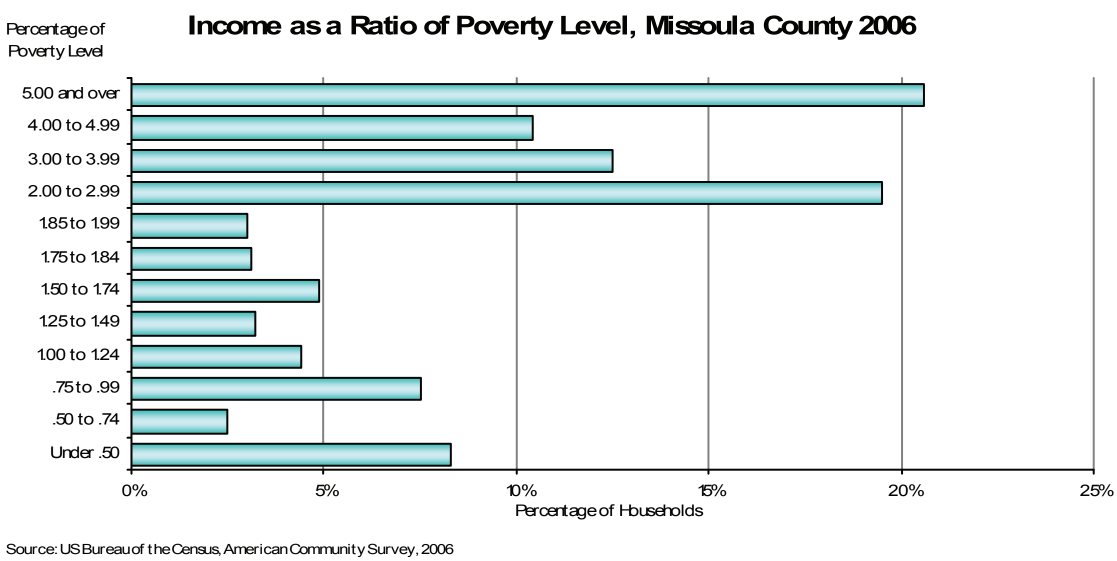
The Census Bureau computes so-called "poverty thresholds" each year – thresholds commonly known as the Federal Poverty Level. As Figure 21 shows, poverty thresholds vary by the number of persons in the household and (for one- and two-person households) by age.

Figure 21: The Federal Government Sets Poverty Thresholds by Household Size and Age



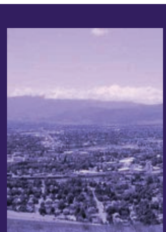
Using the established poverty thresholds shown in Figure 21 and measuring the income of Missoula households yields Figure 22, below, which shows where household income stands relative to the government-set poverty thresholds.

Figure 22: About One in Five County Households Is Under the Poverty Threshold



The figure indicates that about 18½% of Missoula County households have incomes below the poverty threshold that corresponds to their household size and age (as represented by the lowest three bars on the chart, where 1.0 is equal to the poverty threshold).

A slightly higher percentage of county households have incomes that range from the poverty threshold (1.0) to double the threshold (2.0). More than 60% of county households have incomes of double the poverty threshold or higher.



THE HOUSING AFFORDABILITY INDEX

The Housing Affordability Index (HAI) is a comparison of the median price of a home (as discussed in Section 2 of this report) and the median income of households in the community (as discussed in the previous section).

The HAI is a way to indicate what the housing numbers mean to consumers who want to purchase in the local market. It reflects the fact that housing prices, interest rates, terms of loans, and amounts of down payments all affect a home-owner's ability to purchase a home. The HAI also includes estimation of taxes and homeowners insurance.

An affordability index of 100% indicates that, given all the factors that affect ability to purchase, a family with a median income has the income necessary to purchase a median priced home.

The National Association of REALTORS® uses the HAI to quantify housing affordability. To figure the affordability of the payment, it's assumed that 25% of monthly income would go toward the mortgage payment.

Figure 23A shows the HAI for Missoula from 2001 through 2007. In 2007, the income needed for a HAI of 100% is $60,672 – which means a family whose income is at that level could afford a median priced home (or any home priced lower than the median). The HAI shows that a one-person household in 2007 has approximately 54% of the amount of income needed to purchase a home priced at the 2007 median sale price.

Figure 23A: Missoulians' Income Gains Aren't Keeping Up With Home Price Increases …
Housing Affordability Index for the Missoula Area, 2001 - 2007

	2001	2002	2003	2004	2005	2006	2007
Median Home Price (MOR)	$138,000	$149,500	$163,000	$179,000	$192,000	$206,850	$219,550
Down Payment	10.00%	10.00%	10.00%	4.00%	4.00%	4.00%	4.00%
Interest Rate	6.25%	5.75%	5.50%	5.50%	6.75%	6.25%	6.00%
Loan Term	30 years	30 years	30 years	30 years	30 years	30 years	30 years
Median Family Income							
1 person	$30,000	$31,600	$34,200	$37,000	$37,400	$37,800	$38,800
2 person	$34,300	$36,200	$39,000	$42,200	$42,800	$43,200	$44,300
3 person	$38,600	$40,700	$43,900	$47,500	$48,100	$48,600	$49,900
4 person	$42,900	$45,200	$48,800	$52,800	$53,500	$54,000	$55,400
Housing Affordability Index (HAI)							
1 person	68	69	71	66	55	54	54
2 person	78	80	80	75	64	62	61
3 person	88	89	91	85	71	70	69
4 person	98	99	101	94	79	78	77
Median Family Income needed to Purchase Median Priced Home	$36,720	$37,728	$39,984	$46,848	$57,408	$ 58,704	$ 60,672

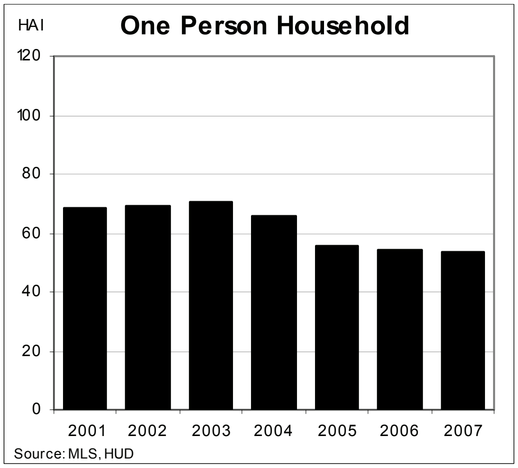
KEY:

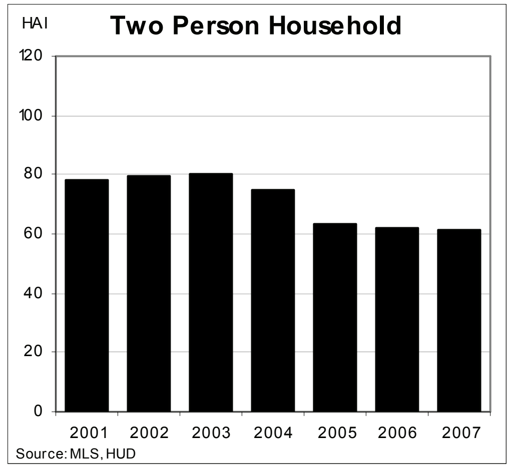
100 - A median income family can marginally qualify for housing

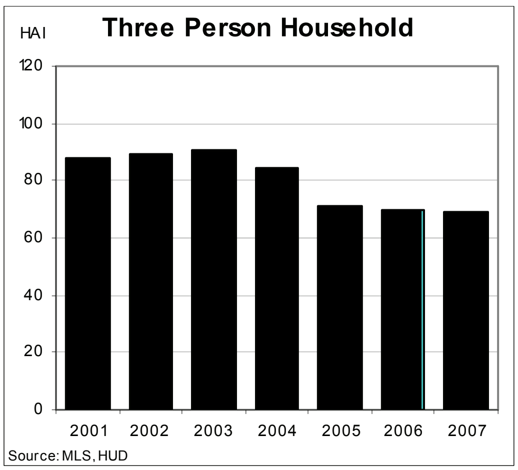
Greater than 100 – A median income family has xx% more income than minimum

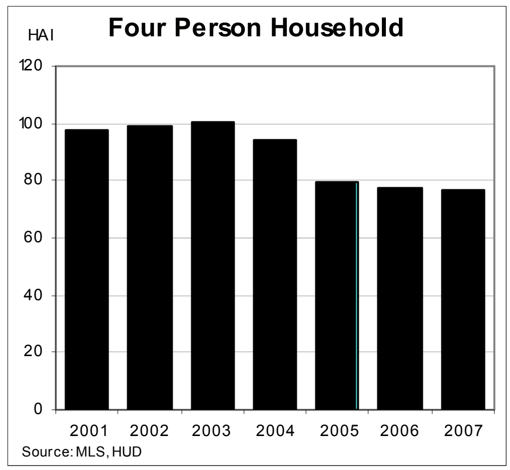
Less than 100 – A median income family has xx% of the income required to qualify

Source: MLS, HUD









The HAI for the past seven years shows that increases in median home prices since 2003 have significantly outstripped increases in median family incomes. As a consequence, fewer families (of any size) are able to afford the median priced Missoula home.

For example, a 4-person family at the median Missoula income ($55,400) had 77% of the income required to qualify to purchase a median priced home (at $219,550). Yet this family would fare better than families of one, two, or three persons – their median incomes provided even lower percentages of the incomes needed to qualify for purchase of a median priced home.

Availability of Affordable Housing

Based on income data reported as median family income, Figure 24 shows the number of homes available in the Missoula area to households by their size and income. Numbers include condominium and single family housing. The figure shows that smaller households have fewer units from which to choose.

Figure 24: Fewer Homes Are Affordable for Smaller Households
As Tabulated From MOR MLS on 3/1/2008

	Annual Income	Price of Affordable Home Based on 25% of Median Income	Price Range Searched	Units Available
1 Person	$38,800	$138,969	$138,969↓	21
2 Person	$44,300	$158,660	$138,970 ↔$158,660	20
3 Person	$49,900	$178,763	$158,661 ↔$178,763	39
4 Person	$55,400	$198,454	$178,764 ↔$198,454	70

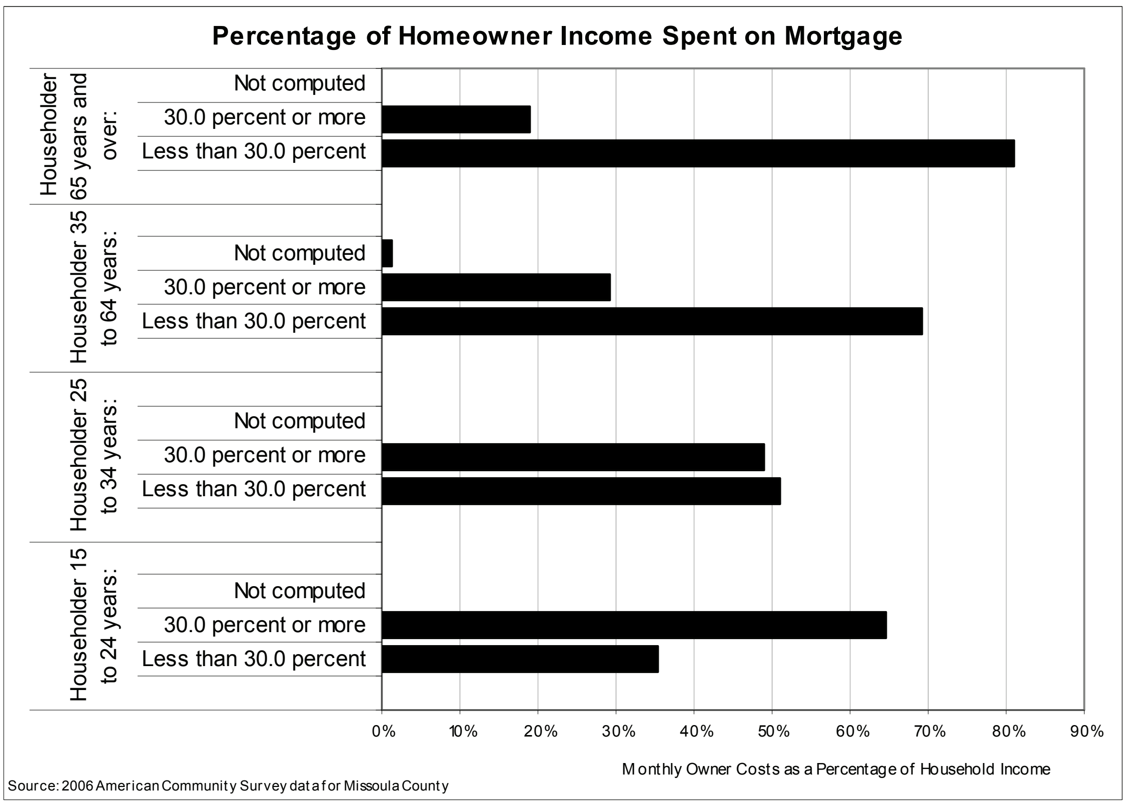
Source: MLS

*Calculations do not include taxes or insurance

SHARE OF INCOME SPENT ON HOUSING

Experts and professionals in real estate and financial planning generally agree that no more than 30% (and, more safely, 25%) of a family's gross monthly income should be spent on housing. Figure 25 shows the percentage splits of owner households, divided into four age groups, between those who spend less than the recommended maximum 30% of income on housing and those whose housing expenditure exceeds the 30% level.

Figure 25: Housing Costs Disproportionately Burden Younger Homeowners …

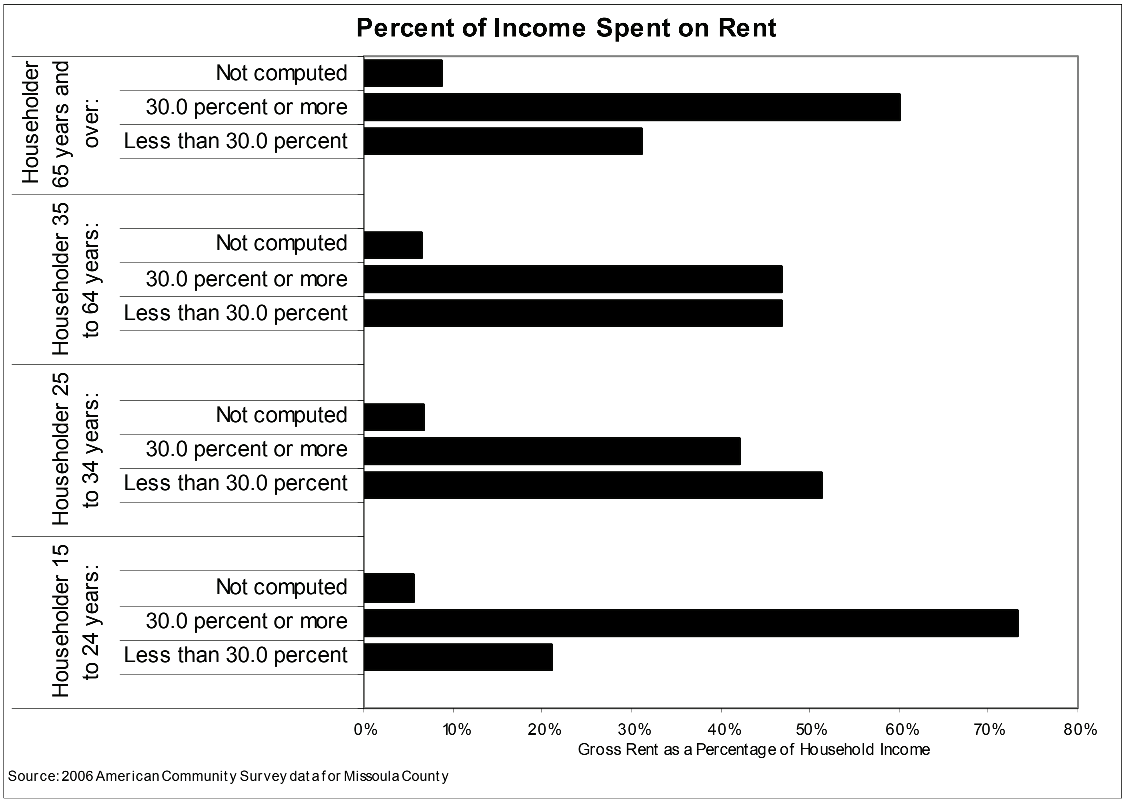


In Missoula, nearly two-thirds of owner households in the youngest age group spend 30% or more of their gross incomes on housing, while nearly half of households in the next-younger age group exceed the 30% recommended maximum.

Far fewer homeowners in the upper two age groups are burdened with excessive payments. This is attributable in part to members of the older generations having purchased their homes before prices began their relentless advance, with many of them having paid down most or all of their mortgages; those mortgages would mostly be far lower in monthly payments than today's typical mortgages.

For renters, divided into the same age groups, an even greater percentage of those in the youngest age group exceeds the 30% recommended monthly maximum, as shown in Figure 26.

Figure 26: … While Heavy Rent Costs Hit Both Youngest and Oldest



Among renters, those in the older age groups do not show the same low level of incomes going to housing as among homeowners. In fact, the profile of those in the oldest age group reveals that the percentage of those exceeding the 30% level is nearly as high as for the youngest group.

CONCLUSION AND OUTLOOK

For 2007, data related to the Missoula housing market reveal two indications that are of greatest importance:

1. Some data indicate a softer real estate market – data such as that for number of homes sold, median sales price of homes, and building permits issued.
2. Missoulians' income growth remains strongly positive and unemployment continues to trend downward. Yet, despite this "good news," the "bad news" about housing in recent years is truer than ever: more Missoula families are finding their incomes insufficient to own or rent modest homes and apartments, and many more families are paying an overly large share of their incomes for housing – threatening their financial well-being.

Regarding a possible softening of the local market, signals – in the form of the data presented in this report – are highly mixed. That makes it very difficult to come up with reliable answers to critical questions regarding the future: Is the Missoula real estate market headed for a "delayed" downturn on the scale that much of the rest of the US is already experiencing? Or is the data of 2007 the weakest that Missoula will see, because our market's continuing strengths will save it from the worst effects seen elsewhere?

We will likely be able to answer those questions with considerably more confidence toward the end of 2008. However, a look at events nationally would strongly suggest that home prices in Missoula would, at a minimum, soften further in the current year. In "The State of the Nation's Housing 2007," the Joint Center for Housing Studies of Harvard University observes that –

> *Home sales and starts usually head down before prices. Declining sales, and the inventory overhang left in their wake, increase the length of time homes are on the market as well as buyers' resistance to higher prices. Eventually motivated sellers – like home builders and investors with unoccupied homes for sale – reduce their prices.*

To the extent that decreasing sales of homes and increasing days on market are reliable indicators of price declines to come, we may see lower sale prices in our market for 2008 and perhaps into 2009.

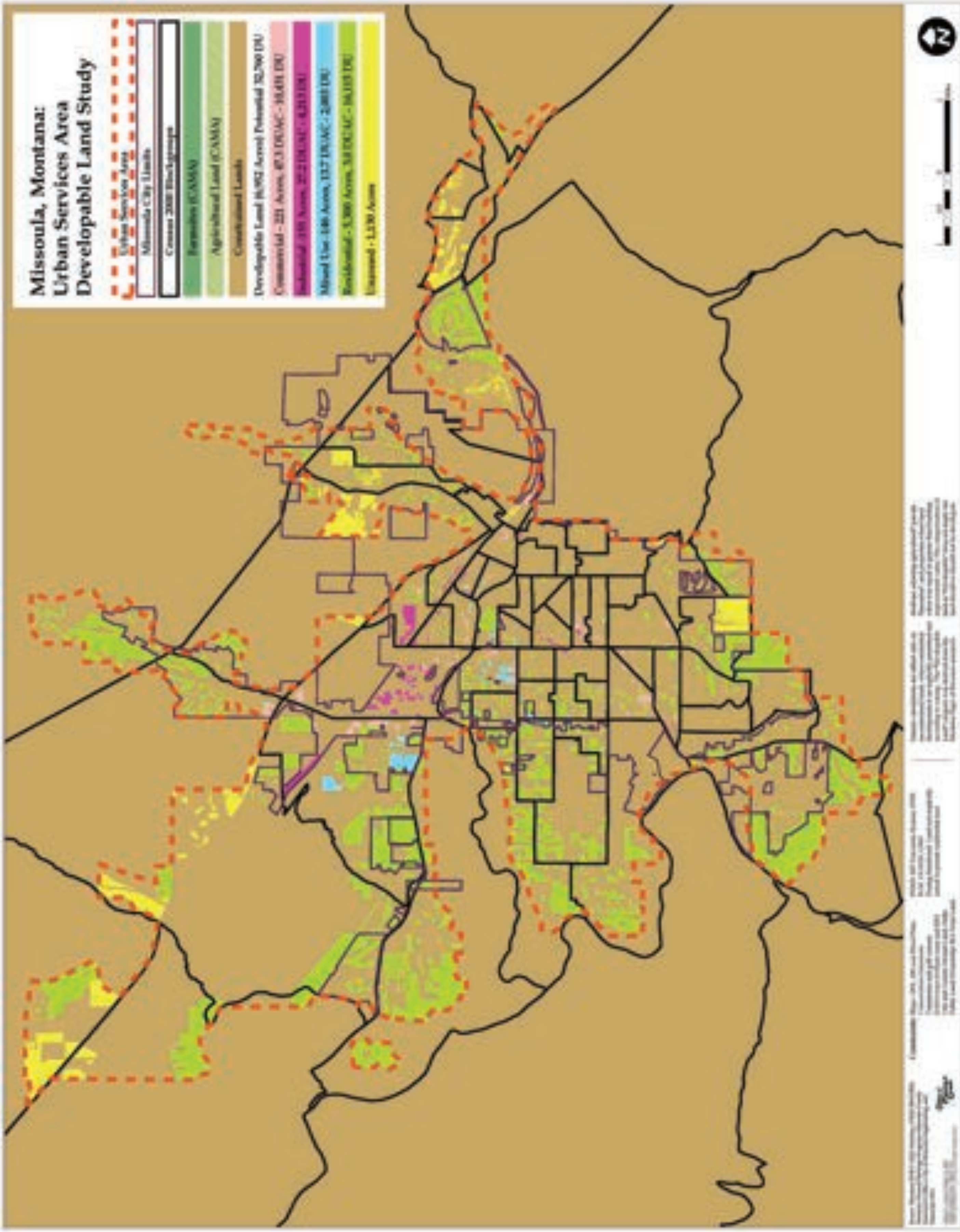
Answers are not likely to come so soon, or so readily, concerning the relentless advance of home and rental prices at paces that exceed the ability of most Missoulians' incomes to keep up. More worrisome still is that this inability to keep up is occurring while economic times have been relatively good. We may collectively shudder to think what might happen if income gains diminish and unemployment increases.

In this case, too, as with home prices, indicators at the national level are ominous. "The State of the Nation's Housing" reports that, "In just one year, the number of households with housing cost burdens in excess of 30% of income climbed by 2.3 million, hitting a record 37.3 million in 2005." Crossing the 30% threshold greatly imperils family finances, as "severely cost-burdened households in the bottom quartile [of household spending] had just $436 a month left to cover all other needs [but housing] in 2005."

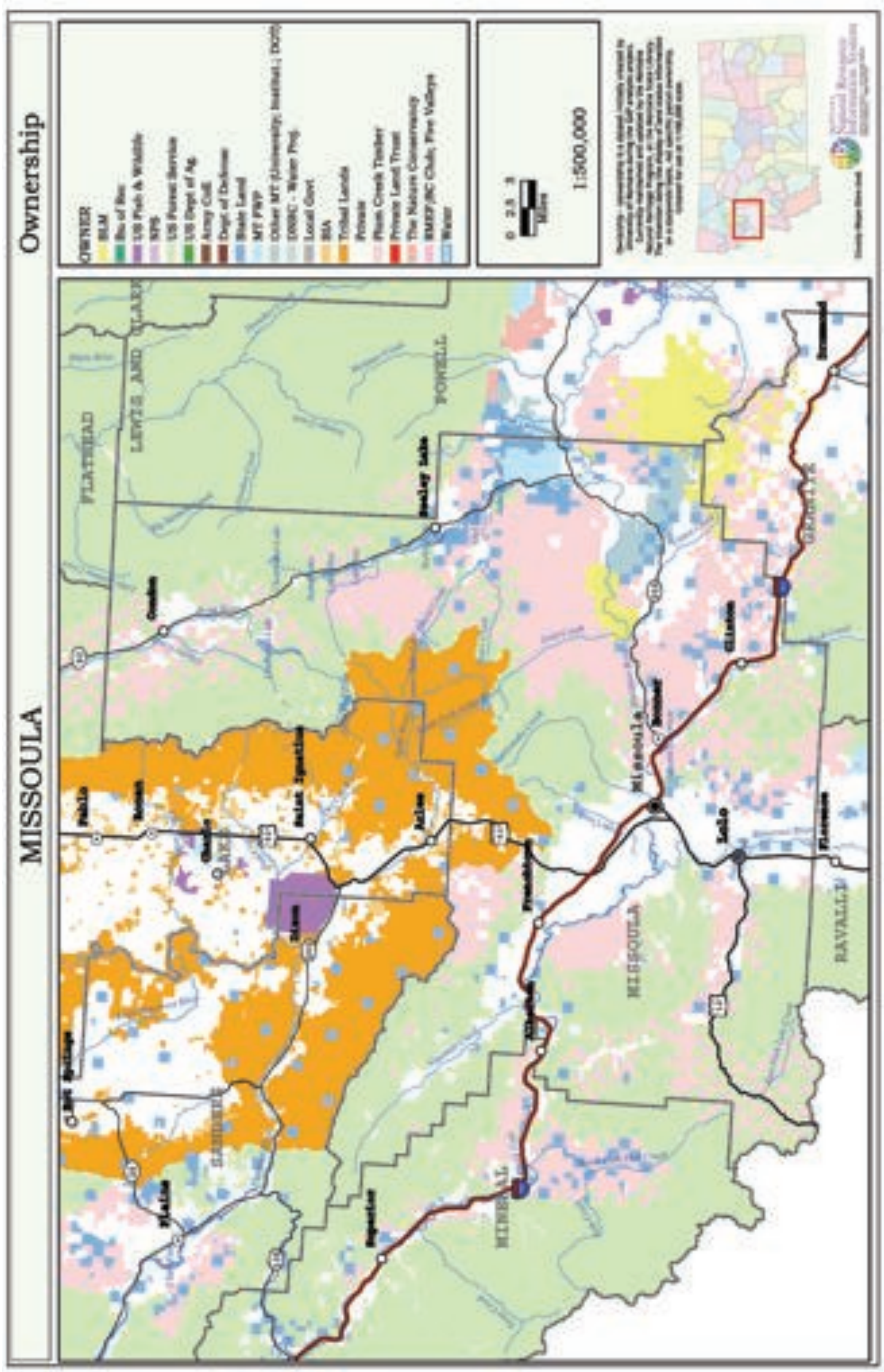
Yet, we would assert that the Missoula market has at least two significant advantages working in our favor. The first is quite practical: If any downturn we may experience lags the national market, we have more time to find solutions. The second is less tangible, but we'd hope no less real: We are resilient people with the blessing of a diverse economy.

To capitalize on these and any other advantages we may enjoy, we must understand that increased housing costs are triggered not only by price hikes in materials and labor, but also in a wide variety of other inputs, such as infrastructure (public and private utilities) and government fees and permits. As such, the challenge to keep home prices and rents within reach of working families with average or below average incomes is a challenge that requires a cooperative, community-wide response.

Builders, developers, real estate brokers, business owners, and leaders in government and nonprofit organizations all recognize the importance of having a workforce that lives in the community and are focusing on making that happen.


Missoula, Montana:
Urban Services Area
Developable Land Study

Attachment 2



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