Northmarq

MARKET INSIGHTS

Investors shift into Class B properties

HIGHLIGHTS

- Operating conditions in the Tucson multifamily market were steady in the first quarter, with vacancies flat and rents dipping slightly.
- Area vacancy was unchanged in the first quarter, remaining at 8.2 percent. Year over year, the vacancy rate in Tucson has risen by 70 basis points.
- Local rents inched lower by 0.4 percent during the first quarter to $1,182 per month. Current rents are up 1.5 percent from one year ago.
- The local investment market got off to a stronger start to 2024 than during the prior year, with a handful of Class B properties changing hands. The median sale price was $159,700 per unit. Cap rates have ranged between 5.5 percent and 6.5 percent.

TUCSON MULTIFAMILY MARKET OVERVIEW

Multifamily property performance in Tucson stabilized in the opening months of the year after softening at the end of 2023. The vacancy rate went unchanged in the first quarter, although rents recorded a modest dip. Despite the quarterly decrease, current area rents are still slightly higher than levels recorded during the first quarter of last year. Gains have been led by newer assets. Properties built after 2010 averaged a 1.6 percent rise in rent since early 2023 to $1,738 per month. The relative stability in vacancies in the first quarter coincides with slowed deliveries as only 300 new units came online in the opening months of the year, after 2,000 units were delivered in 2023, the highest annual total in the region in nearly 30 years.

There was a consistent flow of multifamily investment transactions in Tucson at the start of the year, following the trend of slowing activity in the past 12 months. A greater share of properties that traded were in parts of the Tucson market that command higher rents, such as Oro Valley and Catalina Foothills. This has resulted in higher per-unit prices, even during a period where vacancies are above lows from a few years ago, and cap rates have pushed higher. With properties in top submarkets trading, the median sale price has risen by 6 percent since last year, reaching $159,700 per unit. Cap rates are up roughly 100 basis points from one year ago, averaging between 5.5 percent and 6.5 percent.

CONSTRUCTION ACTIVITY

UNDER CONSTRUCTION	3,863
UNITS DELIVERED	336

MARKET FUNDAMENTALS

VACANCY RATE	8.2%
YEAR-OVER-YEAR CHANGE	+70bps
ASKING RENTS	$1,182
YEAR-OVER-YEAR CHANGE	1.5%

TRANSACTION ACTIVITY (YTD)

MEDIAN SALES PRICE	$159,700

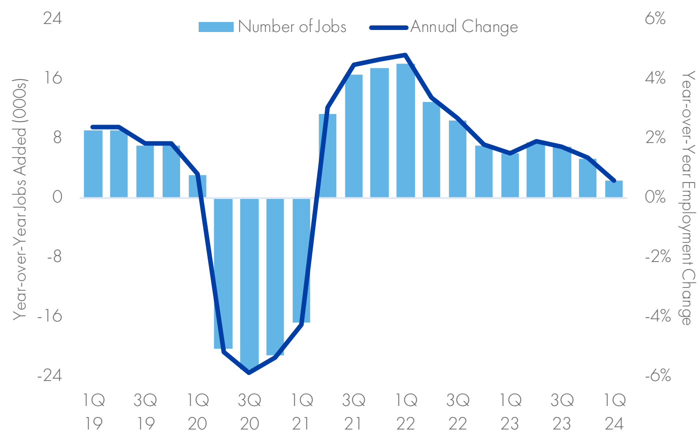
Tucson Multifamily
1Q 2024

EMPLOYMENT

- The local labor market has been expanding at a modest pace. Area employers added 2,300 workers to payrolls in the past 12 months, a 0.6 percent increase in total employment.
- While employment trends were mixed across sectors during the past year, a handful of industries posted strong gains and accounted for the bulk of the growth. The manufacturing sector added 1,300 workers in the past 12 months, an increase of 4.7 percent.
- MicroStar Logistics, a keg and pallet recycling company, is opening a 270,000-square foot facility in Tucson. Located in the Rita Ranch Commerce Center, the MicroStar operation will employ roughly 200 workers in Southeast Tucson.
- **FORECAST:** Total employment in Tucson should continue to grow through the rest of 2024, though at a slower pace than in recent years. Area employers are projected to add around 1,500 jobs in 2024, a 0.4 percent increase.

Area employers added 2,300 workers to payrolls in the past 12 months.

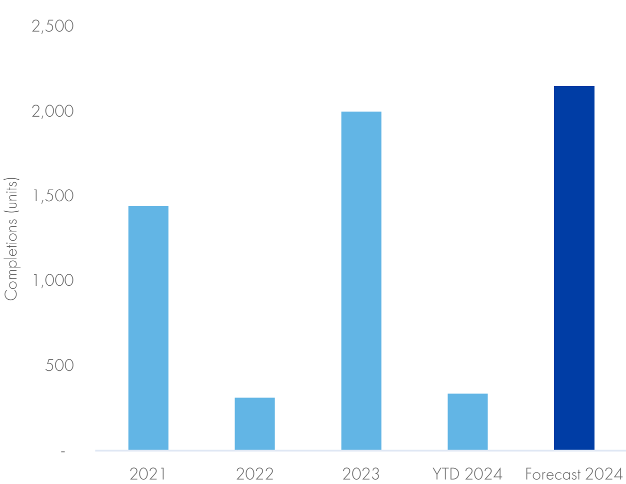
EMPLOYMENT OVERVIEW



Sources: Northmarq, Bureau of Labor Statistics

More 3,800 units are currently under construction.

DEVELOPMENT TRENDS



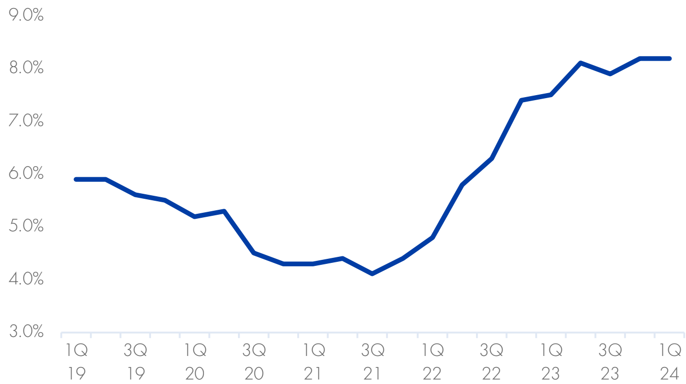
Sources: Northmarq, Apartment Insights

DEVELOPMENT & PERMITTING

- Multifamily deliveries slowed after completions spiked in the previous quarter. Projects totaling more than 300 units came online during the first quarter after more than 1,000 units were delivered in the fourth quarter of 2023.
- More than 3,800 units are currently under construction in Tucson, up by 11 percent from the same time last year. Projects totaling nearly 400 units began construction in the last three months alone. The majority of new construction continues to take place in Northwest Tucson, where nearly 1,800 units are currently being built.
- Multifamily permitting has started 2024 at a slower pace than in recent years. Developers pulled permits for just 180 units in the last three months, a 71 percent decrease from the peak levels posted at the beginning of 2022.
- **FORECAST:** Deliveries will continue to come online at an elevated pace through the rest of this year. Projects totaling 2,150 units are scheduled for completion by the end of 2024.

The vacancy rate is up 70 basis points from one year ago.

VACANCY TRENDS



Sources: Northmarq, Apartment Insights

VACANCY

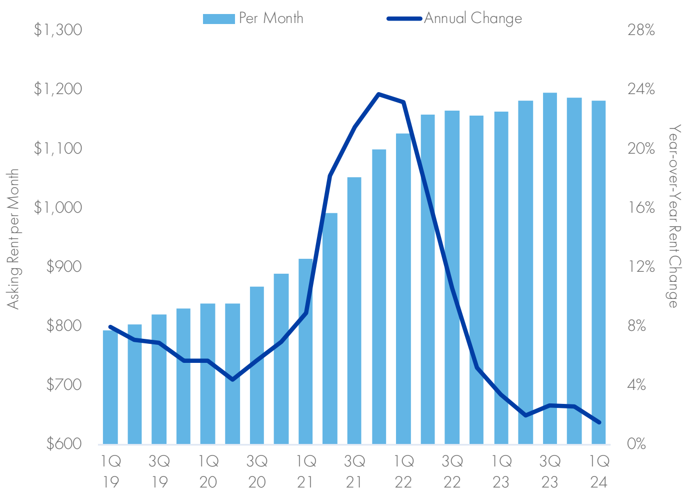
- Area vacancy leveled off in the first quarter, maintaining the same 8.2 percent figure as during the end of 2023. While the rate stabilized in early 2024, it is up 70 basis points from one year ago.
- The northern parts of town tended to fare better than central and southern submarkets. The greatest improvement in vacancies was recorded in the Northeast Tucson submarket. The vacancy rate in this submarket fell 110 basis points in the first quarter to 7.1 percent. In the neighboring Catalina Foothills submarket, local vacancy is also 7.1 percent, matching the year-end 2023 figure.
- Vacancy in Class B properties are currently recording the lowest rates across all asset classes at 7.6 percent, nearly the same as one year prior. In the same time period, the weakness in the market has been concentrated in the Class C segment, where vacancies rose by 180 basis points.
- **FORECAST:** With deliveries elevated for the second consecutive year, local vacancy is expected to continue to trend higher. The rate is forecast to reach 8.5 percent in 2024, a rise of 30 basis points.

RENTS

- While vacancy steadied, rents in Tucson continued to dip lower at the start of the year, posting a second consecutive quarterly drop. Area rents declined by 0.4 percent during the first quarter to $1,182 per month. Despite declining during the past six months, local rents are up 1.5 percent in the past year.
- Most submarkets in Tucson had small shifts in rent during the past 12 months. One of the exceptions occurred in the South Central Tucson submarket, which has recorded steep increases. Year over year, rents in the submarket rose 7.9 percent to $1,041 per month.
- Class C rents have pushed higher in the past year, reaching $937 per month in the first quarter. As recently as late 2020, average Class C rents were below $700 per month.
- **FORECAST:** Rent growth in Tucson is expected to continue at a slower pace than last year as renter demand in the area is met with large numbers of new units on the market. Average rents are projected to rise by about 1 percent in 2024 to approximately $1,200 per month.

Local rents are up 1.5 percent in the past year.

RENT TRENDS



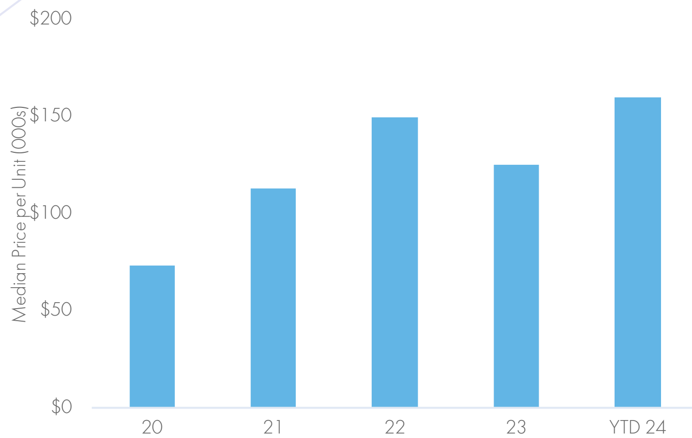
Sources: Northmarq, Apartment Insights

MULTIFAMILY SALES

- Transaction volume in Tucson got off to a healthy start in the first few months of the year, well ahead of the pace that was established in the first quarter of 2023. Total sales in the first quarter equaled roughly one-third of the number of transactions recorded in all of 2023.
- The median price in the first quarter was $159,700 per unit, a 27 percent increase from the 2023 figure. This increase in pricing is partially due to the share of higher-tier assets being sold. Year to date, most transactions have involved Class B properties, while activity in 2023 was concentrated almost entirely in older Class C assets.
- Cap rates have risen steadily in the past 12 months from the lows of 2022 and early 2023. Cap rates have averaged between 5.5 percent and 6.5 percent, about 100 basis points higher than one year ago.

The median price in the first quarter was $159,700 per unit.

INVESTMENT TRENDS



Sources: Northmarq, CoStar

RECENT TRANSACTIONS MULTIFAMILY SALES ACTIVITY

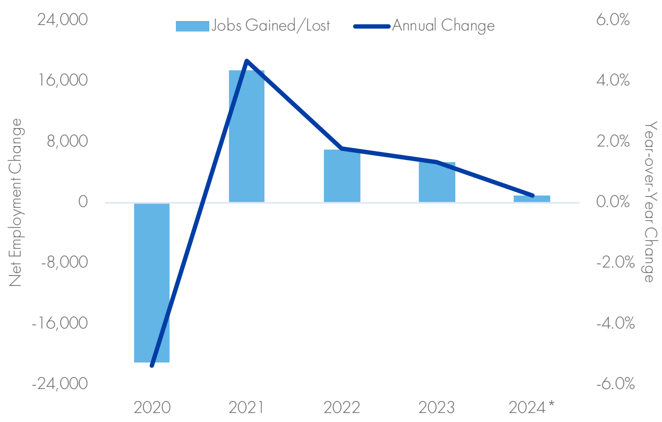
PROPERTY NAME	STREET ADDRESS	UNITS	SALES PRICE	PRICE/UNIT
The Peak at Oro Valley	8215 N Oracle Rd., Tucson	330	$59,800,000	$181,212
Wasko Modern Apartments	2302 E Fort Lowell Rd., Tucson	38	$6,070,000	$159,737
Riverside Suites	1725 E Limberlost Dr., Tucson	33	$5,150,000	$156,061

LOOKING AHEAD

The coming year will be an active one for new multifamily construction in Tucson, with developers on pace to deliver more than 2,100 units in 2024, following the completion of projects totaling 2,000 units in 2023. This two-year period represents a new high for local inventory growth and was fueled by dynamic property performance a few years ago when projects started to move through the construction pipeline. The local inventory of apartment units will have increased by about 2.5 percent by the time this year's forecast projects are completed, and local population growth and employment expansion are not expected to match this rate. As such, area vacancies will likely rise and operators will encounter challenges implementing rent increases.

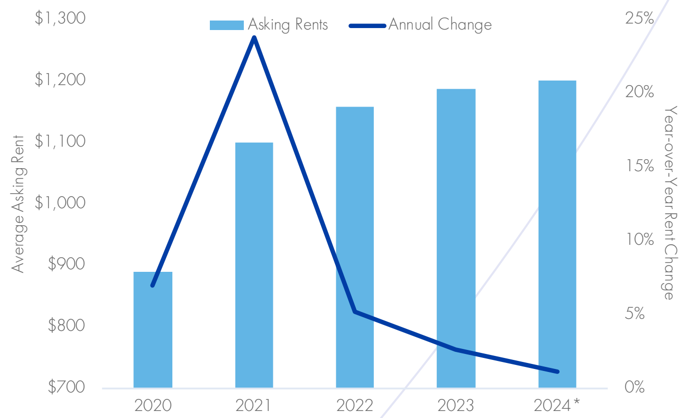
Investment trends in Tucson have been mixed in recent years. Activity spiked in 2022, before slowing dramatically in 2023. Additionally, activity last year was limited exclusively to older, Class C assets, a product type that makes up the bulk of the local inventory. This year, the market will likely shift again, with investors likely to pursue a wider range of rental assets. This trend has begun to emerge; the properties that have traded to this point in 2024 have been higher quality assets in submarkets that command higher rents. Transactions involving Class A assets are typically limited, as developers have historically held newly built properties rather than selling.

EMPLOYMENT FORECAST



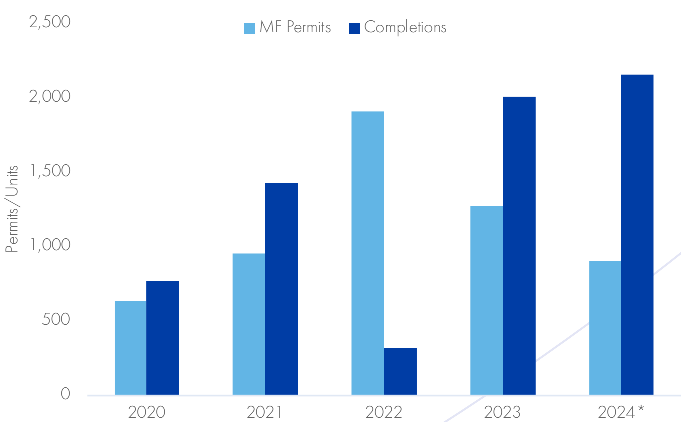
** Year End Forecast*
Sources: Northmarq, Bureau of Labor Statistics

RENT FORECAST



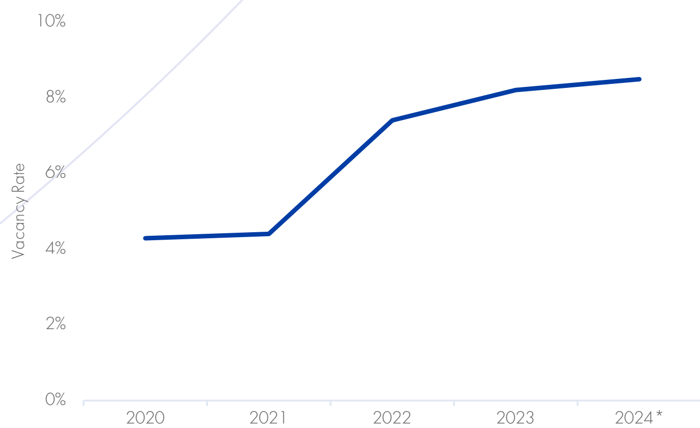
** Year End Forecast*
Sources: Northmarq, Apartment Insights

CONSTRUCTION & PERMITTING FORECAST



** Year End Forecast*
Sources: Northmarq, Apartment Insights, Census Bureau

VACANCY FORECAST



** Year End Forecast*
Sources: Northmarq, Apartment Insights

FOR MORE INFORMATION, PLEASE CONTACT:

TREVOR KOSKOVICH
President–Investment Sales
602.952.4040
tkoskovich@northmarq.com

JESSE HUDSON
Regional Managing Director–Investment Sales
602.952.4042
jhudson@northmarq.com

BRANDON HARRINGTON
Managing Director–Debt & Equity
602.508.2204
bharrington@northmarq.com

RYAN BOYLE
Vice President–Investment Sales
602.952.4050
rboyle@northmarq.com

CHRIS MICHL
Associate Vice President–Investment Sales
602.952.4051
cmichl@northmarq.com

LOGAN BACA
Senior Associate–Investment Sales
602.952.4052
lbaca@northmarq.com

PETE O'NEIL
Director of Research
602.508.2212
poneil@northmarq.com

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