MARKET REPORT | 4Q/2018

Greater Phoenix Multifamily

NORTHMARQ

Rent Growth, Employment Gains Fueling Phoenix Apartment Market

Highlights

- The Greater Phoenix multifamily market closed 2018 on a high note, with vacancy remaining low and rents posting significant increases. Renter demand remains strong enough to keep vacancy tight even as new units are delivered.
- Vacancy was 5.7 percent at the end of the fourth quarter, matching the rate from the third quarter. The rate declined by 10 basis points in 2018, following a 20-basis-point improvement in 2017.
- Greater Phoenix continues to record some of the strongest rent increases in the country. In 2018, asking rents spiked 8.9 percent, reaching $1,074 per month. Rents rose 1.7 percent during the fourth quarter, a typically slow period for rent growth.
- Apartment construction slowed during the fourth quarter, and deliveries in 2018 lagged levels from 2017. Projects totaling more than 11,000 units are currently under way, and deliveries will likely pick up in 2019.
- Sales of apartment properties slowed a bit in the fourth quarter, but transaction velocity in 2018 was nearly identical to 2017 levels. Sale prices pushed higher, with the median price reaching $120,000 per unit. Cap rates compressed in 2018, averaging 5.2 percent for the year and 5 percent in the fourth quarter.

Phoenix Multifamily Market Overview

The Greater Phoenix multifamily market recorded another year of strong performance in 2018, with renter demand fueled by a robust pace of job growth. Employers added nearly 80,000 new jobs in 2018, and renters moved into a net of more than 9,000 apartment units during the year. Vacancy remained in a tight range for most of the past year, and the rate actually dipped a bit from one year earlier despite an active year of construction from multifamily developers. With the economy doing well, heightened renter demand and tight vacancy rates, operators raised rents nearly 9 percent in 2018.

Market Indicators

	4Q/2018
Vacancy	→
Rents	↑
Transaction Activity	↓
Price Per Unit	↑
Cap Rates	↓

Summary Statistics

Summary Statistics	Phoenix Market
Vacancy Rate	**5.7%**
- Change from 4Q 2017 (bps)	**-10**
Asking Rents (per month)	**$1,074**
- Change from 4Q 2017	**8.9%**
Median Sales Price (per unit YTD)	**$120,000**
Average Cap Rate (YTD)	**5.2%**

Phoenix Multifamily Market Overview (cont.)

While the number of properties changing hands slowed slightly at the end of 2018, the investment climate for local multifamily properties remains strong. Despite some market volatility, the median price during the fourth quarter reached the highest figure for any single quarter on record, and the median price for all of 2018 spiked from 2017 levels. Price increases were reflected in cap rates, which compressed to the low-5-percent range in 2018, with some of the lowest cap rates recorded in transactions that closed during the fourth quarter.

Submarket Statistics

Submarket Name	4Q 2018 Vacancy	4Q 2017 Vacancy	Annual Vacancy Change (BPS)	4Q 2018 Rents	4Q 2017 Rents
N Scottsdale/Fountain Hills	4.6%	5.5%	(90)	$1,359	$1,264
S Phoenix/Laveen	4.6%	6.0%	(140)	$1,016	$901
Gilbert/Superstition Springs	4.7%	4.9%	(20)	$1,123	$1,036
S Scottsdale	4.8%	5.1%	(30)	$1,434	$1,304
E Mesa/Apache Junction	4.9%	3.7%	120	$1,027	$956
Chandler	5.0%	4.8%	20	$1,205	$1,110
NW Black Canyon	5.1%	4.9%	20	$893	$836
N Mesa	5.1%	4.4%	70	$907	$832
Ahwatukee Foothills	5.2%	6.4%	(120)	$1,182	$1,089
Deer Valley/N Peoria	5.2%	5.9%	(70)	$1,115	$1,017
Peoria/Sun City	5.3%	5.1%	20	$1,059	$959
Goodyear/Avondale	5.3%	5.3%	0	$1,070	$997
Union Hills/Cave Creek	5.4%	6.0%	(60)	$1,083	$984
S Mesa	5.5%	5.6%	(10)	$975	$924
E Central Phoenix	5.6%	5.7%	(10)	$974	$897
N Paradise Valley	5.8%	5.4%	40	$1,291	$1,120
W Central Phoenix	5.9%	4.3%	160	$748	$767
Metrocenter	6.0%	7.9%	(190)	$822	$772
Central City/Sky Harbor	6.0%	5.7%	30	$1,426	$1,302
S Gilbert/Queen Creek	6.0%	6.2%	(20)	$1,226	$1,163
Glendale	6.2%	6.0%	20	$823	$753
Maryvale/Estrella	6.3%	6.0%	30	$817	$772
North Mountain	6.4%	5.3%	110	$950	$850
S Tempe	6.4%	5.9%	50	$1,149	$1,061
N Tempe	6.5%	6.0%	50	$1,202	$1,135
Central Black Canyon	6.7%	7.2%	(50)	$756	$695
N Central Phoenix/Alhambra	6.8%	5.8%	100	$969	$892
NE Central Phoenix	7.3%	9.9%	(260)	$1,223	$1,072
Central Phoenix/Encanto	7.8%	6.8%	100	$1,272	$1,085
S Paradise Valley	9.5%	6.1%	340	$1,078	$1,008

Employment

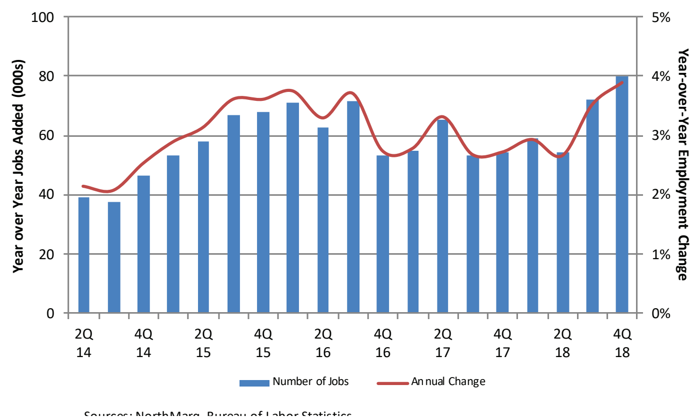
> Employers in Greater Phoenix expanded payrolls at one of the fastest rates in the country in 2018, adding 79,700 net new jobs in the year, for a growth rate of 3.9 percent. This represented the strongest year of local job growth since 2005.

> Growth has been led by the professional and business services sector, which expanded by 16,900 positions in 2018—growth of 4.8 percent. During the past five years, nearly 55,000 professional jobs have been created in Greater Phoenix.

> Industrial development in the West Valley is resulting in new jobs in the manufacturing and warehousing sectors. Andersen Corporation is opening a new window manufacturing facility in Goodyear that will add 400 jobs; after Ball Manufacturing opened a new facility in the city in 2018. Manufacturing employment expanded by more than 5 percent in the past year with the addition of nearly 7,000 new jobs.

> **Forecast:** After strong gains in 2018, the pace of local employment growth is forecast to slow in the year ahead. The Greater Phoenix employment market is forecast to expand by approximately 2.9 percent with the addition of more than 60,000 jobs.

Employment Overview



2018 was the strongest year of local job growth since 2005

Vacancy

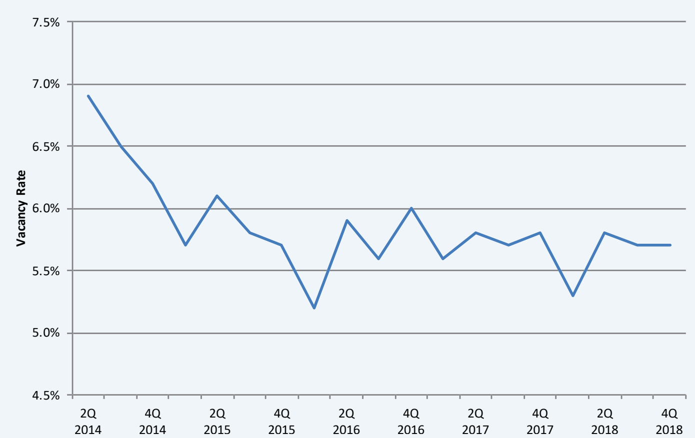
> The vacancy rate in Phoenix was flat from the third quarter to the fourth quarter, ending 2018 at 5.7 percent. Vacancy declined 10 basis points in 2018, following a 20-basis point decline in 2017.

> Vacancy has remained in a very tight range over the past few years. Since the beginning of 2015, vacancy has averaged 5.7 percent, and the rate has ticked up to 6 percent just twice in the past 16 quarters.

> Some of the submarkets in the northern portion of the Greater Phoenix market have been recording some of the strongest vacancy improvements. In 2018, the North Scottsdale/Fountain Hills, Deer Valley/North Peoria, and Union Hills/Cave Creek submarkets each posted annual vacancy declines of more than 50 basis points.

> **Forecast:** The vacancy in the Greater Phoenix market is forecast to tick up 30 basis points in 2019 to 6 percent.

Vacancy Trends



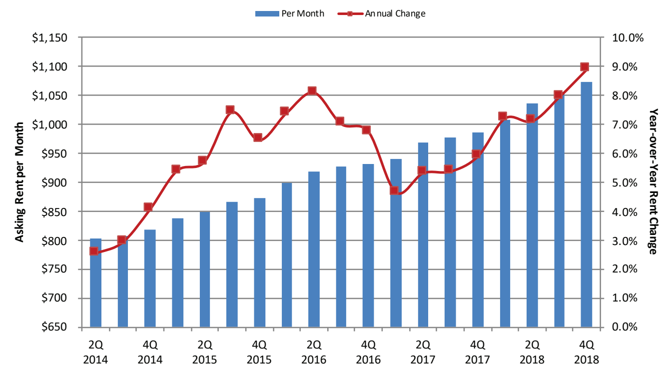
Sources: NorthMarq, Apartment Insights

Vacancy has remained in a very tight range over the past few years

Rents

- The Greater Phoenix area has posted some of the strongest rent increases in the country. Asking rents ended 2018 at $1,074 per month, 8.9 percent higher than at the end of the preceding year.
- Asking rents rose 1.7 percent in the final three months of 2018, the strongest fourth-quarter increase in more than 10 years. Rents are expected to post similar gains in the first few quarters of 2019.
- After posting above-average gains in recent years, rent growth in the Southeast Valley lagged the pace of increases in the rest of the Greater Phoenix area in 2018. Asking rents in Tempe, Chandler, and Gilbert averaged approximately 7 percent last year.
- **Forecast:** Asking rents in Greater Phoenix are expected to increase about 6 percent in 2019. Rents grew at an average rate of 6.4 percent per year from 2015-2017 before spiking last year.

Rent Trends



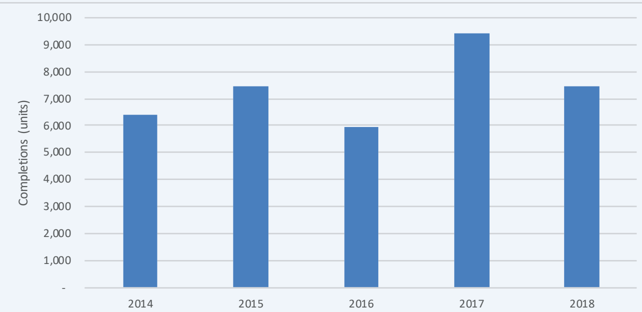
Sources: NorthMarq, Apartment Insights

The Greater Phoenix area has posted some of the strongest rent increases in the country

Development and Permitting

- Following the delivery of more than 2,500 apartments during the third quarter, completions slowed in the final three months of the year, with approximately 1,100 units coming online. In 2018, completions totaled nearly 7,500 units, down approximately 20 percent from the 2017 total.
- Developers continue to move projects into the construction pipeline to meet demand. Approximately 11,300 units were under construction at the end of 2018, up more than 10 percent from the total one year earlier.
- Multifamily permitting slowed by about 15 percent during the fourth quarter, following an uptick during the preceding three months. Total multifamily permitting in 2018 reached approximately 8,200 units, a 4 percent dip from the total in 2017.
- **Forecast:** Developers are forecast to complete approximately 8,500 new units in the Phoenix market in 2019. Completions have averaged approximately 7,300 units per year since 2014.

Development Trends



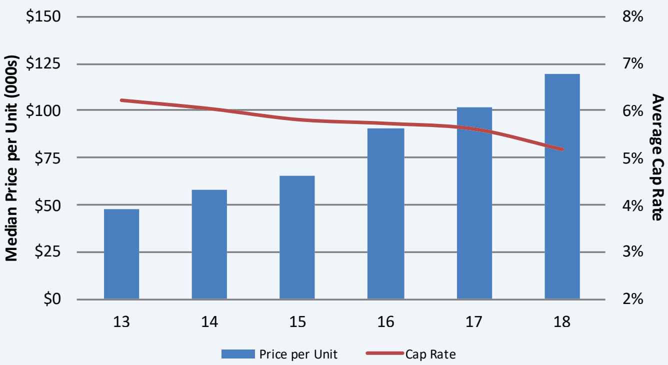
Sources: NorthMarq, Apartment Insights

In 2018, completions were down approximately 20 percent from the 2017 total

Multifamily Sales

- After accelerating in the middle part of the year, sales velocity slowed during the fourth quarter of 2018. Despite the dip in the final few months of the year, sales velocity in 2018 was nearly identical to levels from 2017, highlighting steady investor demand for local multifamily properties.
- Multifamily prices reached an all-time high in the final three months of 2018. The median price during the fourth quarter was more than $138,000 per unit. For the full year, the median price was $120,000 per unit, up more than 17 percent from the median price in 2017.
- Cap rates compressed in 2018, including a dip during the fourth quarter. For the year, cap rates were approximately 5.2 percent, about 40 basis points lower than the average from 2017. During the fourth quarter, the average cap rate in closed deals was approximately 5 percent.

Investment Trends



> *Sales velocity in 2018 was nearly identical to levels from 2017*

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

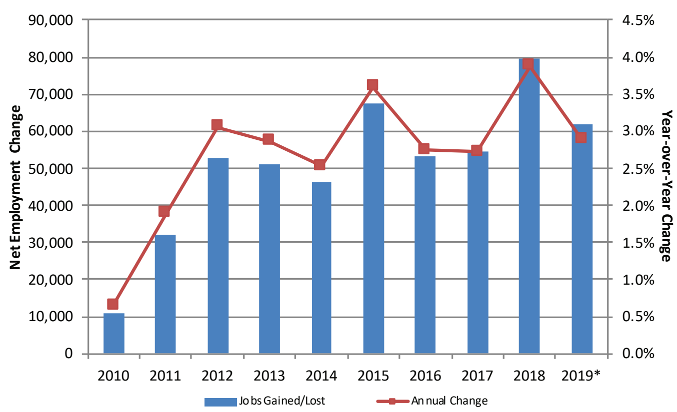
Property Name	Street Address	Units	Sales Price	Price/Unit
San Melia	14435 S 48th St., Phoenix	488	$105,300,000	$215,779
Crescent Highland	4626 N 16th St., Phoenix	349	$90,000,000	$257,880
Tides at South Tempe	4130 S Mill Ave., Tempe	442	$55,500,000	$125,566
Argenta	4104 E Broadway Rd., Mesa	396	$50,275,000	$126,957
BeckenRidge	17625 N 7th St., Phoenix	308	$31,550,000	$102,435
Tides at East Arcadia	5401 E Thomas Rd., Phoenix	181	$26,600,000	$146,961

Looking Ahead

The Greater Phoenix multifamily market is poised for another strong year of property performance in 2019.The market has proven able to absorb the elevated levels of new construction; during the past two years, the vacancy rate has actually trended lower even as more than 16,000 new units have been delivered. With vacancy low and absorption consistently high, rents have been surging. Asking rents have increased at an average rate of 7 percent annually during the past four years, with a slightly lower pace of growth anticipated in the year ahead.

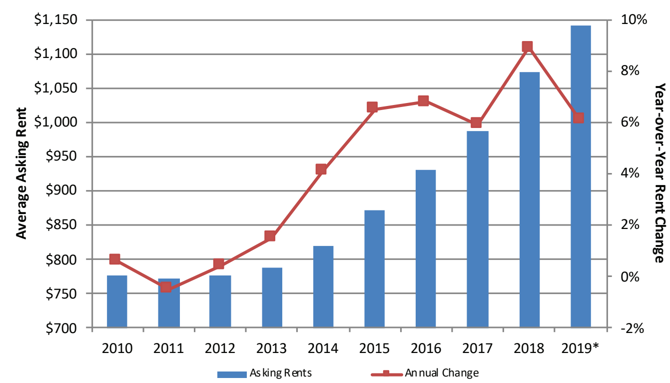
Sales velocity has had some quarterly volatility, but investment activity remains resilient in Greater Phoenix. Prices have pushed higher and cap rates have compressed, but investors are still seeing upside potential in the market, supported by rent increases that have outpaced projections in each of the past few years. Cap rates have ticked lower by about 20 basis per year since 2012, with some of the most rapid compression occurring in recent quarters. It is unlikely cap rates will trend much lower than they are, but there have been few signs of upward pressure to this point in the cycle.

Employee Forecast



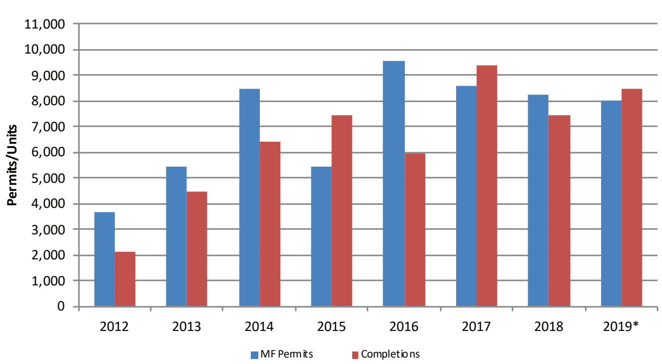
* Year End Forecast

Rent Forecast



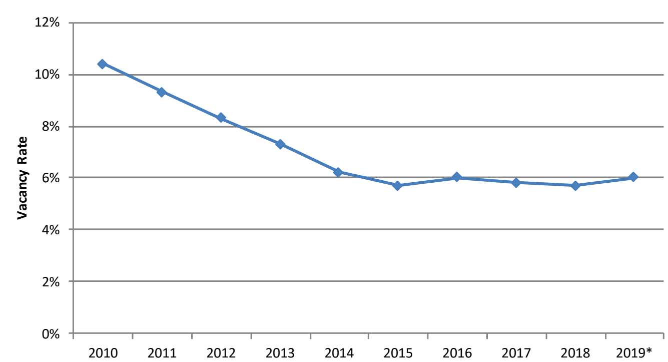
* Year End Forecast
Sources: NorthMarq, Apartment Insights

Construction & Permitting Forecast



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

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Apartment Insights

About NorthMarq

As a capital markets leader, NorthMarq offers commercial real estate investors access to experts in debt, equity, investment sales, and loan servicing to protect and add value to their assets. For capital sources, we offer partnership and financial acumen that support long- and short-term investment goals. Our culture of integrity and innovation is evident in our 60-year history, annual transaction volume of $13 billion, loan servicing portfolio of more than $55 billion and the multi-year tenure of our more than 500 people.

For more information, contact:

Bill Hahn
EXECUTIVE VICE PRESIDENT – INVESTMENT SALES
602.952.4041
bhahn@northmarq.com

James DuMars
SENIOR VICE PRESIDENT, MANAGING DIRECTOR – DEBT & EQUITY
602.508.2206
jdumars@northmarq.com

Trevor Koskovich
PRESIDENT – INVESTMENT SALES
T 602.952.4040
tkoskovich@northmarq.com

Pete O'Neil
DIRECTOR OF RESEARCH
602.508.2212
poneil@northmarq.com

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