

Greater Tucson Multifamily

Accelerating Job Growth Fueling Vacancy Declines, Rent Gains

Highlights

- > The Tucson multifamily market continued to gain momentum in the third quarter, with vacancies tightening and rents rising. The investment market strengthened in response to improving market conditions.
- > Vacancy dipped 30 basis points to 5.6 percent in the third quarter, and the rate is down 40 basis points year over year.
- > Asking rents rose 2 percent in the third quarter and are up 6.9 percent in the past 12 months. Current asking rents in Tucson are averaging \$820 per month.
- > Investment activity accelerated in the third quarter, while pricing was consistent. The median price has been approximately \$75,000 per unit this far in 2019, while cap rates have averaged 5.8 percent in transactions that have closed year to date.

Tucson Multifamily Market Overview

The Tucson multifamily market continued to improve in recent months. Operating conditions in the market generally strengthen in the third quarter, as students return to Tucson for the start of the new school year. That trend continued in 2019, following an unusually strong second quarter where vacancy held steady even through the summer months. A driver of the consistent renter demand in Tucson has been an active local labor market. With demand for apartments strong, the local vacancy rate, which fell 30 basis points in the third quarter, is currently at its lowest point in more than 20 years.

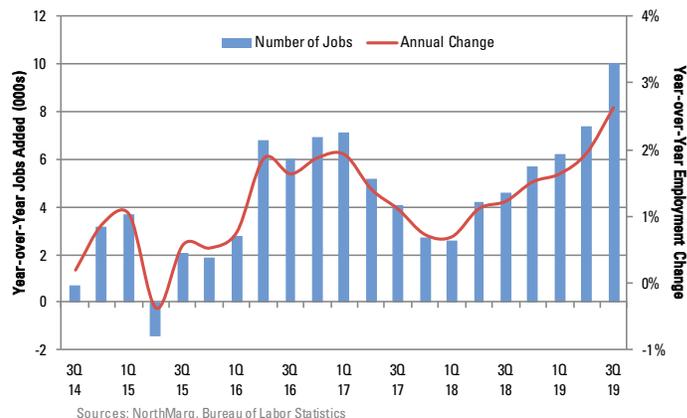
Q3 Snapshot	Tucson Market
	Market Fundamentals
	Vacancy 5.6%
	- Year Over Year Change -40 bps
	Asking Rent \$820
	- Year Over Year Change +6.9%
	Transaction Activity
	Median Sales Price Per Unit (YTD) \$74,800
	Cap Rates (Avg YTD) 5.8%
	Construction Activity
	Units Under Construction 2,195
	Units Delivered YTD 646

Investment activity in Tucson has accelerated in each of the past two quarters. While activity levels in sales of properties for more than \$10 million have been quite consistent throughout the first three quarters of the year, the rise in transaction counts has occurred at the lower end of the pricing spectrum. Property sales of assets priced below \$10 million have picked up in recent quarters, resulting in a wider range of multifamily complexes changing hands. While the mix of properties that have sold has changed, cap rates have remained on a consistent trajectory, compressing modestly for the sixth consecutive year.

Employment

- > The pace of employment growth in Tucson accelerated in the third quarter. Year over year, employers have added 10,000 new jobs, a 2.6 percent increase. Last year at this time, fewer than 5,000 jobs had been added.
- > The manufacturing and construction sectors have both posted strong gains, contributing to the overall expansion of the local labor market. The sectors have combined to add 2,300 workers in the past year, a growth rate of 5.4 percent.
- > The leisure and hospitality sector has accounted for 1,700 new jobs in the past 12 months, an expansion of nearly 4 percent. The sector is expanding at its fastest pace in nearly five years.
- > **Forecast:** Employment growth has continued to gain momentum throughout the year. In 2019, employers in Tucson are forecast to create 10,000 net new jobs, a 2.6 percent expansion of local payrolls.

Employment Overview

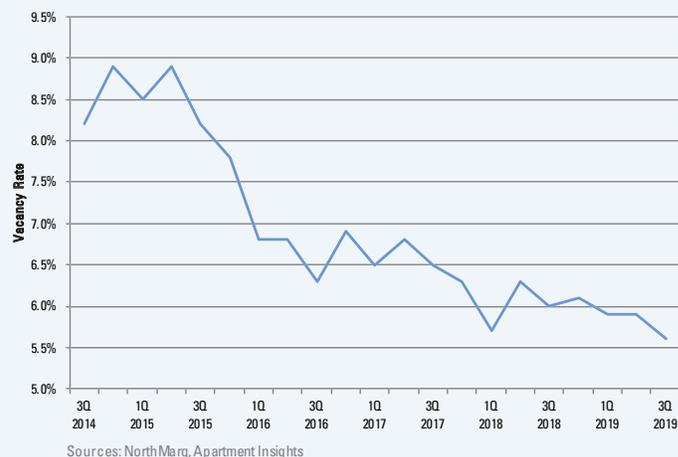


Year over year, employers have added 10,000 new jobs, a 2.6 percent increase

Vacancy

- > After holding steady in the second quarter, vacancy in Tucson fell 30 basis points in the third quarter, dipping to 5.6 percent. This is the lowest quarterly vacancy rate in Tucson in more than 20 years.
- > The current vacancy rate is 40 basis points lower than one year ago. This marked the eighth consecutive quarter where the Tucson multifamily market had recorded a year-over-year vacancy decline.
- > Vacancy in the University submarket has remained low even as new units have been delivered. Nearly 1,500 apartment units have come online since 2012, including more than 300 units thus far in 2019. Vacancy in the University submarket ended the third quarter at 4.8 percent.
- > **Forecast:** Vacancy is forecast to end the year at 5.9 percent, down 20 basis points from the year-end 2018 figure. This would mark the seventh consecutive year with a recorded vacancy decline.

Vacancy Trends

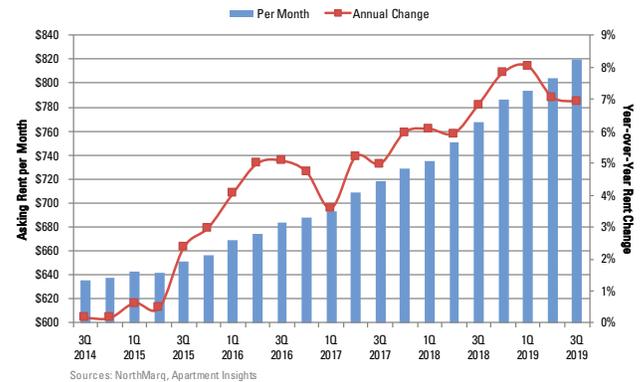


Vacancy in Tucson dipped to 5.6 percent, the lowest quarterly vacancy rate in more than 20 years

Rents

- > Asking rents posted their strongest quarterly increase of 2019 during the third quarter, rising 2 percent from the previous period. Asking rents reached \$820 per month during the third quarter.
- > Year over year, asking rents have advanced 6.9 percent. Annual rent growth was averaging 3 percent as recently as 2015, but the pace has accelerated significantly during the past few years.
- > Three submarkets in the Tucson market now feature asking rents above \$1,000 per month. Generally, these submarkets are in the northern portion of Tucson, with Oro Valley/Catalina and Northwest Tucson leading the way. One year ago, only one submarket in the market had rents over \$1,000 per month.
- > **Forecast:** Asking rents in Tucson are expected to rise approximately 6 percent in 2019, building on a gain of nearly 8 percent last year. Rents are forecast to end the year at \$833 per month.

Rent Trends

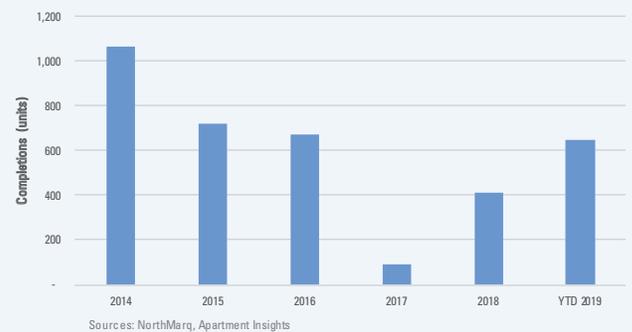


Three submarkets in the Tucson market now feature asking rents above \$1,000 per month

Development and Permitting

- > After developers delivered fewer than 300 units in the first half of 2019, the pace of new construction gained momentum during the third quarter. Projects totaling approximately 365 units came online in the third quarter.
- > Apartment construction is ramping up in the Tucson metro area. There are nearly 2,200 units currently under construction, up 10 percent from the total in the second quarter.
- > Multifamily permitting slowed slightly during the third quarter, with permits for approximately 215 units issued. Year to date, permits for nearly 800 multifamily units have been pulled, up 37 percent when compared to levels from one year earlier.
- > **Forecast:** Deliveries are forecast to pick up during the fourth quarter. For the full year, approximately 1,400 units are scheduled to come online.

Development Trends

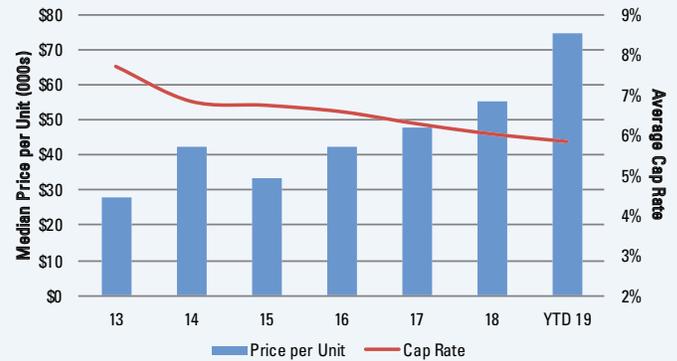


Year to date, permits for nearly 800 multifamily units have been pulled

Multifamily Sales

- > Sales of apartment buildings accelerated in the third quarter, with activity levels spiking more than 30 percent from the second quarter. While activity has picked up in recent months, property sales through the first three quarters of 2019 are down 30 percent from the same period in 2018.
- > Per-unit pricing has been very consistent in 2019. The median price year to date through the third quarter was \$74,800 per unit, nearly identical to the figure from the first half of this year. The median price is up approximately 35 percent from the median price in 2018.
- > Cap rates compressed a bit during the third quarter, averaging in the mid-5-percent range. Thus far in 2019, the average cap rate is approximately 5.8 percent, down 20 basis points from the average in 2018.

Investment Trends



Property sales through the first three quarters of 2019 are down 30 percent from 2018

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

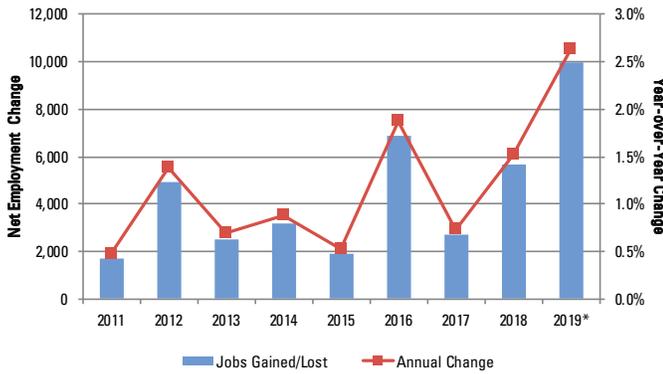
Property Name	Street Address	Units	Sales Price	Price/Unit
Pima Canyon	750 W Orange Grove Rd., Tucson	240	\$44,850,000	\$186,875
Palm Canyon	2255 W Orange Grove Rd., Tucson	368	\$40,300,000	\$109,511
Domain 3201	3201-3225 W Ina Rd., Tucson	289	\$37,750,000	\$130,623
Saddle Ridge	450 W Cool Dr., Tucson	248	\$26,000,000	\$104,839

Looking Ahead

The Tucson multifamily market is expected to continue to post healthy performance through the remainder of 2019 and into next year. One of the primary drivers of the strengthening property metrics has been an accelerating pace of job growth. That trend is expected to continue in the coming quarters. Amazon announced plans to double its local workforce at the company's Tucson distribution center, a move that is expected to result in approximately 1,500 new jobs. With employment on an upswing, renter demand for apartments is likely to remain healthy, even as the pace of new development accelerates.

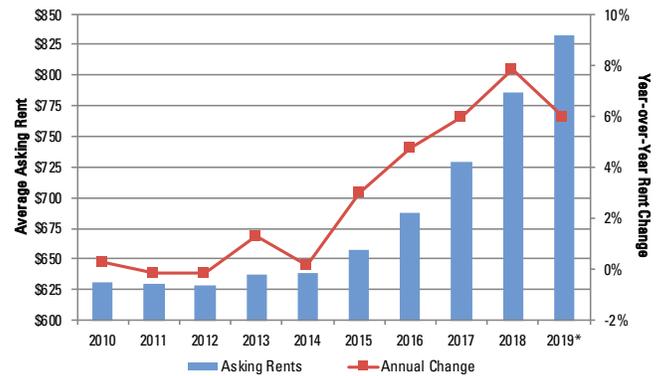
Investor demand is likely to remain elevated in the coming quarters as the Tucson market continues to post strong property performance. With vacancy rates at lows that haven't been reached in more than two decades, rents are growing at nearly two-times the market's long-term annual average. The strengthening cash flows are supporting cap rate compression; cap rates have dipped below 6 percent and are not showing any signs of trending higher in the coming quarters. Sales velocity has accelerated in recent quarters and activity typically peaks at the end of the year, so several properties will likely change hands in the fourth quarter.

Employment Forecast



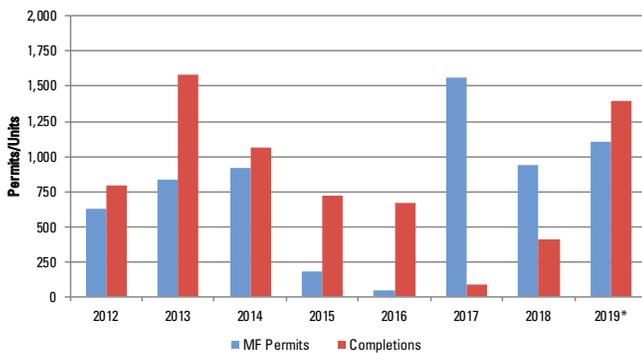
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



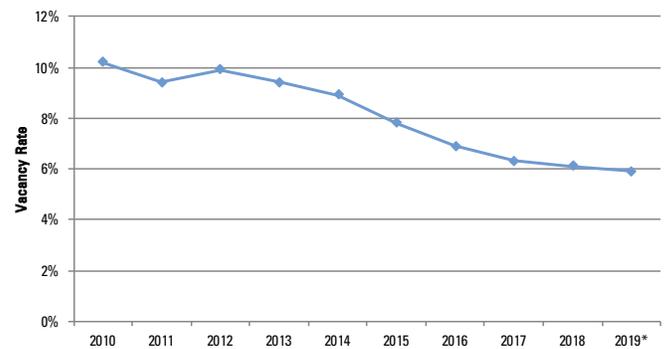
* Year End Forecast
Sources: NorthMarq, Apartment Insights

Construction & Permitting Forecast



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

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Apartment Insights

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 to more than \$57 billion and the multi-year tenure of our more than 550 people.

For more information, contact:

Bill Hahn

EXECUTIVE VICE PRESIDENT – INVESTMENT SALES

602.952.4041

bhahn@northmarq.com

James DuMarsSENIOR 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

Copyright © 2019 NorthMarq Multifamily, LLC.

The information contained herein has been obtained from sources deemed reliable. While every reasonable effort has been made to ensure its accuracy, we cannot guarantee it. No responsibility is assumed for any inaccuracies. Readers are encouraged to consult their professional advisors prior to acting on any of the material contained in this report.

