

Greater Phoenix Multifamily




New Supply Coming Online, Even as Demand Growth Cools

Highlights

- > All markets are being impacted by the COVID-19 outbreak, but to this point, the Phoenix multifamily market has performed quite well. Vacancy is only slightly higher than one year ago, and that is due largely to seasonal factors and an increase in new supply.
- > Vacancy rose 30 basis points during the second quarter, reaching 5.7 percent. Increases in the summer months are common; the rate has risen during the second quarter in each of the past 10 years.
- > Rents dipped slightly in the second quarter as the market softened and uncertainty surrounding the economy rose. Asking rents ended the second quarter at \$1,184 per month, up 4 percent year over year.
- > Multifamily development is active in 2020. Developers completed more than 7,200 apartment units during the first half of the year, with another 15,100 units currently under construction.
- > Investment activity slowed but has not stopped completely, and prices and cap rates are demonstrating continued strength. The median price is up 20 percent year to date, reaching \$166,000 per unit, while cap rates are averaging 5 percent.

Phoenix Multifamily Market Overview

The Phoenix multifamily market has performed fairly well through the first half of 2020, even as the local economy has been impacted by the volatility brought on by the COVID-19 outbreak. Job losses in Phoenix have been significant, but the pace of local layoffs has been less severe than cuts being recorded at the national level. In recent years, Phoenix had led the country in apartment rent growth, but with local demand drivers less robust than in years past and projects totaling thousands of new units coming online, rents inched lower during the second quarter.

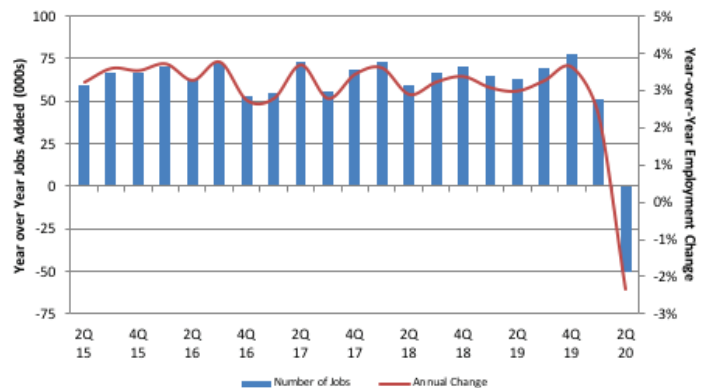
Q2 Snapshot	Phoenix Market
	Market Fundamentals
	Vacancy 5.7%
	- Year Over Year Change +10 bps
	Asking Rent \$1,184
	- Year Over Year Change +4.0%
	Transaction Activity
	Median Sales Price Per Unit (YTD) \$166,000
	Cap Rates (Avg YTD) 5.0%
	Construction Activity
	Units Under Construction 15,113
	Units Delivered YTD 7,264

Entering 2020, the Phoenix multifamily market was coming off of its strongest year of investment activity in more than a decade, and activity through the first two months of the year closely tracked 2019 levels, before the pandemic stalled transactions. During the second quarter, a handful of properties traded, with prices generally trending higher and cap rates holding steady near 5 percent. Uncertainty has hindered velocity in recent months, but the new market reality will become increasingly transparent going forward. In the second half of the year, the ability for operators to collect rents and maintain occupancy levels is expected to impact transaction counts.

Employment

- > The pace of job losses in Greater Phoenix was less severe than cuts at the national level during March and April, and jobs have begun to come back fairly quickly. Year over year through the second quarter, area employment was down 2.3 percent with a net loss of approximately 51,000 jobs.
- > The leisure and hospitality sector has been hit hardest during the economic shutdown. Prior to the onset of job losses, the sector accounted for 10.9 percent of total employment in Greater Phoenix, a figure that was slightly lower than the national share.
- > One of the companies that has grown in the current climate is moving into the Phoenix metro area. During the second quarter, Zoom Video Communications announced plans to open a location in the Phoenix area, likely near Arizona State University in Tempe. The company is expected to hire up to 250 software engineers in the new location during the next few years.
- > **Forecast:** Every major employment market in the country is forecast to record net job losses in 2020. COVID-19 cases escalated in the Phoenix area late in the second quarter, which could result in a sluggish local labor market in the third quarter.

Employment Overview



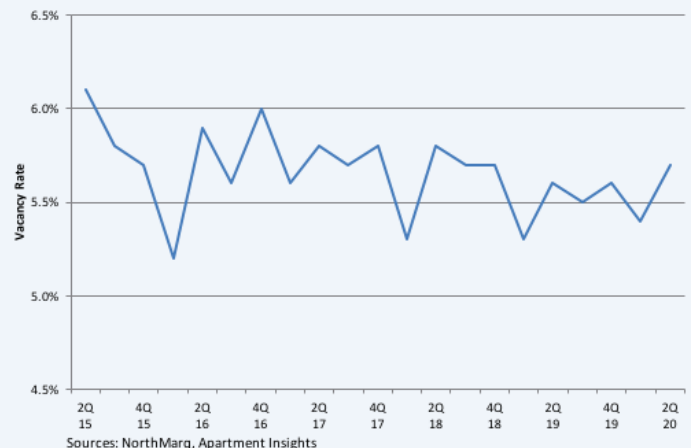
Sources: NorthMarq, Bureau of Labor Statistics

During the second quarter, Zoom Video announced plans to open in the Phoenix area

Vacancy

- > Vacancy rose 30 basis points during the second quarter, with the rate reaching 5.7 percent. Vacancy increases during the second quarter in Greater Phoenix are common; the local vacancy rate has ticked higher in the second quarter in each of the past 10 years.
- > The current vacancy rate is 10 basis points higher than one year ago. The rate has remained below 6 percent in every quarter since the beginning of 2017.
- > Net absorption of units during the first half of 2020 totaled approximately 2,300 units, with tenants moving into a net of more than 400 units. Absorption thus far in 2020 is lagging levels from the same period in 2019 by approximately 45 percent.
- > **Forecast:** The vacancy rate in Greater Phoenix is forecast to rise 60 basis points to 6.2 percent in 2020. The rate will be pushed higher by a rise in new construction and a slower pace of net absorption.

Vacancy Trends



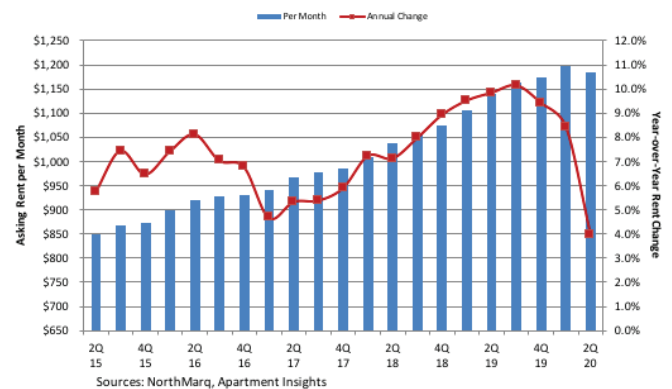
Sources: NorthMarq, Apartment Insights

Vacancy rose 30 basis points during the second quarter, reaching 5.7 percent

Rents

- > After a 2 percent increase during the first quarter, asking rents contracted in recent months. Rents inched down 1.2 percent during the second quarter, reaching \$1,184 per month.
- > Despite the modest dip during the second quarter, current rents are up 4 percent when compared to one year earlier. Prior to this most recent quarter, annual rent growth had averaged more than 8 percent since the beginning of 2018.
- > The strongest annual rent gains are being recorded in some of the submarkets in the West Valley. Areas such as Goodyear, Glendale and Peoria have posted year-over-year rent increases that are among the highest in the Phoenix market.
- > **Forecast:** After steep increases in recent years, rents in Greater Phoenix will likely contract slightly in the second half of the year. For the full year, asking rents are likely to dip approximately 1.5 percent.

Rent Trends

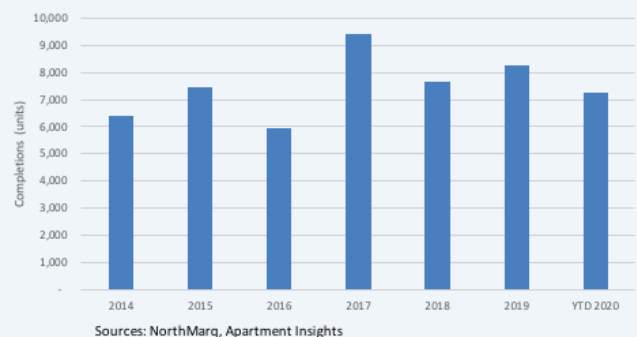


Despite the modest dip, current rents are up 4 percent compared to one year earlier

Development and Permitting

- > Multifamily developers delivered projects totaling nearly 2,700 units in the second quarter, bringing the total for the first half of the year to more than 7,200 units. Apartment completions in the first half were up 76 percent when compared to the same period in 2019.
- > Apartment construction is forecast to remain active during the next several quarters. Projects totaling more than 15,100 units are currently under construction, 27 percent higher than one year ago.
- > After developers pulled permits for 4,400 multifamily units in the first quarter, activity slowed in the second quarter. Multifamily permitting totaled approximately 1,400 units in the second quarter. Year to date, permitting levels for multifamily units are ahead of last year's activity.
- > **Forecast:** The pace of multifamily development will likely slow a bit in the second half of the year, as disruptions in the supply chain delay some projects. Deliveries for the year are forecast to total approximately 11,500 units.

Development Trends

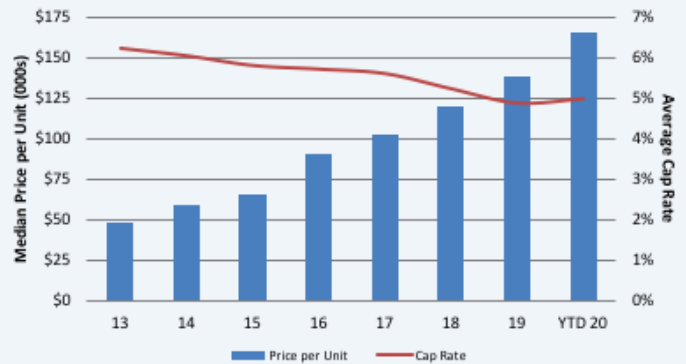


Projects totaling more than 15,100 units are currently under construction

Multifamily Sales

- > Sales activity cooled significantly during the second quarter as investors stepped back to evaluate the impact of the coronavirus outbreak on property operating fundamentals. Nearly one dozen properties sold during the second quarter, down approximately 75 percent from the total during the first quarter.
- > Prices rose even as activity levels slowed. The median price in the first half of 2020 was \$166,000 per unit, up 20 percent from the median price in 2019. In transactions that closed in the second quarter, the median price topped \$200,000 per unit, the highest figure on record for an individual quarter in the Greater Phoenix market.
- > After compressing slightly in the first quarter, cap rates inched higher in the second quarter. For the first half of the year, cap rates averaged approximately 5 percent, nearly identical to the average for 2019.

Investment Trends



The median price in the first half of 2020 was \$166,000 per unit

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

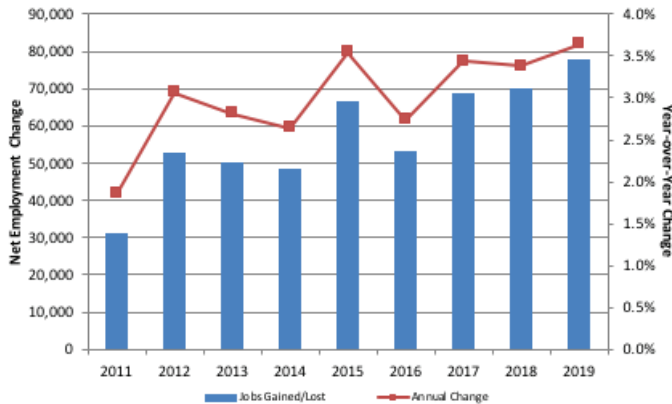
Property Name	Street Address	Units	Sales Price	Price/Unit
Tides at South Tempe	4130 S Mill Ave., Tempe	442	\$71,500,000	\$161,765
Park Place at Fountain Hills	16725 E Avenue of the Fountains, Fountain Hills	230	\$63,250,000	\$275,000
Metro at Zanjero	9450 W Cabela Ave., Glendale	253	\$55,407,000	\$219,000
Superstition Canyon	1247 S 96th St., Mesa	200	\$42,000,000	\$210,000

Looking Ahead

The Greater Phoenix multifamily market will likely record some softening in 2020, after a decade of improving market fundamentals. The market had been fueled by a robust pace of demand growth, but renter demand is expected to slow this year as the labor market softens and in-migration declines. The market will be impacted by a supply-demand imbalance in the near term. Apartment development should reach a cyclical peak in 2020, which will put upward pressure on vacancy and flatten rents. Despite the disruption likely to occur in the market in the coming quarters, the long-term demand drivers in Greater Phoenix are healthy.

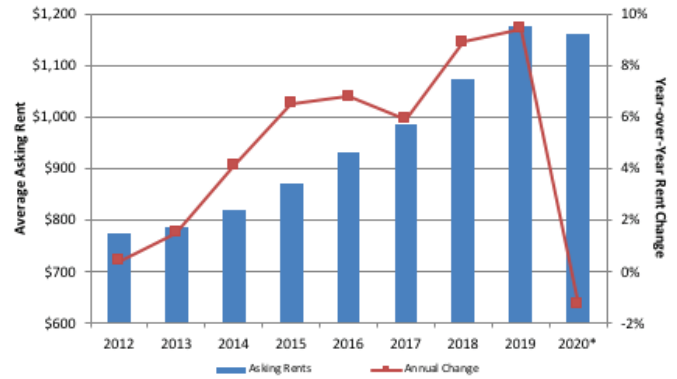
After the Greater Phoenix multifamily market recorded its strongest year for investment activity in more than a decade in 2019, transaction volume was expected to cool in 2020. This trend was amplified by the outbreak of the COVID-19 pandemic, which created several layers of uncertainty. While transaction velocity has slowed considerably—but not stalled completely—prices have risen in the properties that have sold. In the second half of this year, activity should regain momentum, as some of the uncertainty lifts and property cash flows in the new environment can be accurately evaluated. The consistently low interest rates available in the market will continue to support low cap rates.

Employment Forecast



* Year End Forecast

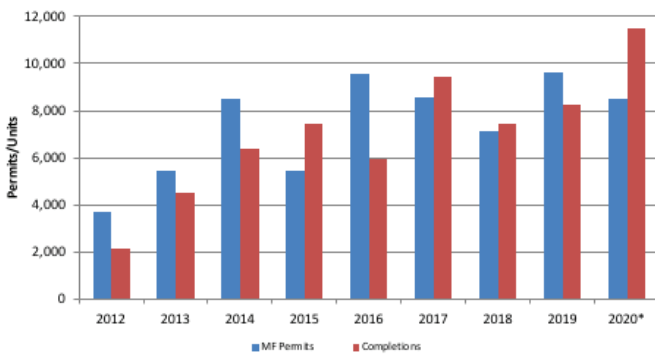
Rent Forecast



* Year End Forecast

Sources: NorthMarq, Apartment Insights

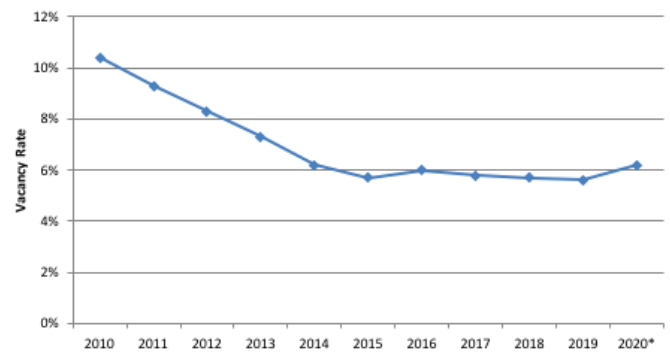
Construction & Permitting Forecast



* 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 more than \$14 billion, loan servicing portfolio of more than \$61 billion and the multi-year tenure of our nearly 600 people.

For more information, contact:

Bill Hahn

EXECUTIVE VICE PRESIDENT – INVESTMENT SALES

602.952.4041

bhahn@northmarq.com

Brandon Harrington

MANAGING DIRECTOR – MULTIFAMILY DEBT & EQUITY

602.508.2204

bwharrington@northmarq.com

Trevor Koskovich

PRESIDENT – INVESTMENT SALES

602.952.4040

tkoskovich@northmarq.com

Pete O'Neil

DIRECTOR OF RESEARCH

602.508.2212

poneil@northmarq.com

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