MARKET REPORT | 2Q/2020

Greater Tucson Multifamily

NorthMarq

Investment Activity Concentrated in Smaller Deals

Highlights

- The Tucson multifamily market has posted fairly steady performance through the first half of 2020. During the second quarter, vacancy inched higher, but the rate is still lower than one year ago. Rents leveled off in the second quarter after strong gains for the past few years.
- Vacancy inched higher in the second quarter, ticking up 10 basis points to 5.3 percent. The rate has been on a steady improvement cycle in recent years, and the current figure is 60 basis points lower than one year ago.
- Asking rents were flat from the first quarter to the second quarter, holding steady at $839 per month. Average rents are up 4.4 percent during the year.
- Investment activity strengthened in the first half of 2020, spiking by approximately 50 percent from the same time period in 2019. The median price in the first half of the year was $66,100 per unit, while cap rates averaged 5.7 percent.

Q2 Snapshot	Tucson Market
Market Fundamentals	
Vacancy	**5.3%**
- *Year Over Year Change*	**-60 bps**
Asking Rent	**$839**
- *Year Over Year Change*	**+4.4%**
Transaction Activity	
Median Sales Price Per Unit (YTD)	**$66,100**
Cap Rates (Avg YTD)	**5.7%**
Construction Activity	
Units Under Construction	**1,500**
Units Delivered YTD	**160**

Tucson Multifamily Market Overview

While the national economy has been battered by the fallout from the coronavirus, the Tucson multifamily market has proven particularly resilient through the first half of 2020. Vacancy inched higher in the second quarter, but the rate has improved on both a year-to-date and a year-over-year basis. Rents held steady during the second quarter, but will likely dip in the second half of the year. The volume of renter demand remains uncertain in the near term. Tucson's apartment market is usually supported by out-of-area students attending the University of Arizona, but with on-campus classes potentially limited or cancelled for the fall semester, there could be fewer students moving into Tucson for the school year.

Multifamily sales trends in Tucson ran counter to the national trend during the first half of the year. The number of properties that sold in Tucson during the first six months of 2020 outpaced levels from the same period in 2019, while there were steep declines in nearly every major market in the country. The mix of properties changed from the first quarter to the second quarter. While there were several transactions of $15 million or more during the first three months of the year, activity in the second quarter generally involved sales of properties priced closer to $5 million. Cap rates have inched higher thus far in 2020, averaging 5.7 percent, 20 basis points higher than in 2019.

Employment

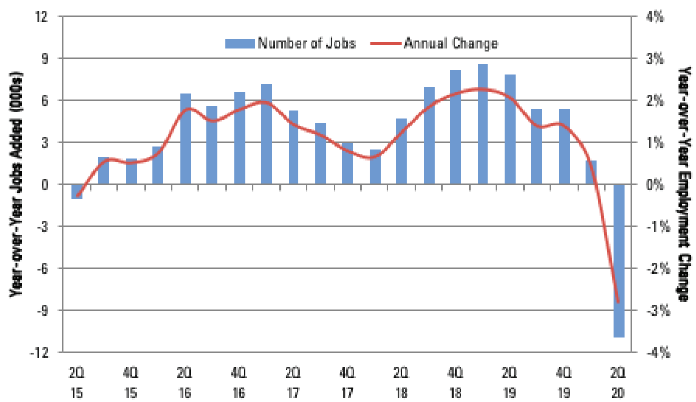
> Short-term job losses in Tucson wiped out gains from the past few years, matching the national trend. During the 12-month period ending in the second quarter, total employment in Tucson was down approximately 2.8 percent, with the removal of nearly 11,000 jobs.

> While most industries in Tucson have contracted since the beginning of the year, construction employment has ticked higher. During the past 12 months, construction employment in Tucson has advanced 4.5 percent with the addition of nearly 1,000 net new jobs. Year to date, 400 construction jobs have been created.

> Earlier this year, Raytheon announced a business consolidation of the company's missiles and defense business will be headquartered in Tucson, combining a local arm of the business with a unit currently located in Massachusetts.

> **Forecast:** Total employment in the Tucson area will likely contract by approximately 2 percent in 2020. While a few industries have recorded steep declines, several of the area's largest employers appear likely to maintain staffing levels.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Year to date, 400 construction jobs have been created

Vacancy

> After reaching the lowest rate in more than a decade during the first quarter, vacancy inched higher in the second quarter, rising 10 basis points to 5.3 percent. Vacancy rates in Tucson almost always rise during the second quarter as students at the University of Arizona leave for summer break.

> Year over year, vacancy has declined by 60 basis points. The local vacancy rate has remained below 6 percent since the beginning of 2019.

> Vacancy has been tightening in the South Tucson/Airport area during recent periods. The vacancy rate in the submarket has declined by 210 basis points annually and is down 120 basis points in the last quarter alone.

> **Forecast:** Apartment vacancy is forecast to creep higher in the second half of the year, as construction activity gains momentum. There could be some decline in renter demand in the second half of the year, especially if the labor market does not rebound quickly.

Vacancy Trends

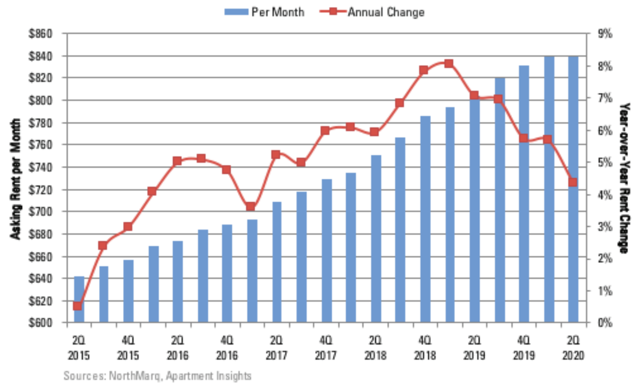
Sources: NorthMarq, Apartment Insights

Year over year, vacancy in Tucson has declined by 60 basis points

Rents

- Following a 1 percent increase during the first quarter, asking rents were flat in the second quarter, holding steady at $839 per month. Leading up to the quarter, local asking rents had posted quarterly gains of at least 1 percent in eight straight quarters.
- Year over year through the second quarter, asking rents have grown 4.4 percent; however, the pace of gains has slowed; annual rent growth one year earlier was 7.1 percent.
- Submarkets in the northern portion of Tucson that have seen robust rent growth in recent years lost momentum in the second quarter. All three northern submarkets with asking rents over $1,000 per month reported declines in the second quarter.
- **Forecast:** Asking rents in Tucson are forecast to decline by approximately 1.5 percent in 2020, ending the year at $818 per month. Annual rent growth has averaged 5.4 percent during the past five years.

Rent Trends



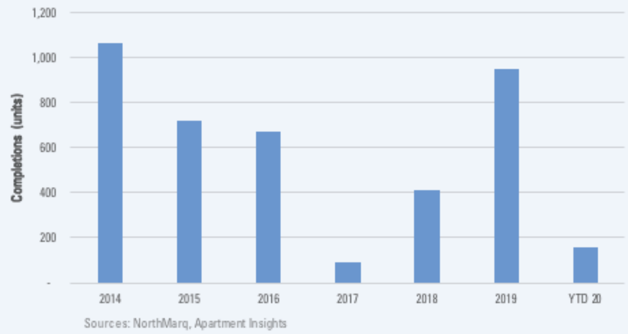
Sources: NorthMarq, Apartment Insights

Asking rents remained flat in the second quarter, holding steady at $839 per month

Development and Permitting

- Apartment completions slowed at the beginning of the year. Developers delivered approximately 160 units in the first half of 2020, down from 280 units during the same period of 2019.
- Approximately 1,500 apartment units are currently under construction, compared to more than 2,000 units one year ago. Nearly half of the units in the development pipeline are located in the University submarket.
- Multifamily permitting remained fairly active in the first half of this year but trailed levels recorded in 2019. Developers pulled permits for approximately 360 multifamily units during the first six months of 2020.
- **Forecast:** Deliveries are forecast to total 850 multifamily units by the end of this year, down from 950 units in 2019.

Development Trends



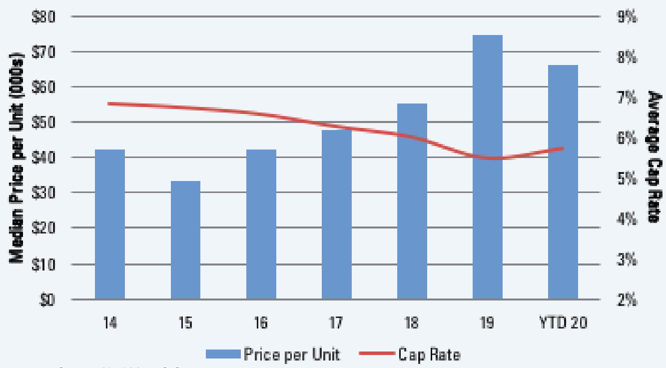
Sources: NorthMarq, Apartment Insights

Approximately 1,500 apartment units are currently under construction

Multifamily Sales

- While sales velocity has slowed dramatically in most major markets in the country, investment activity in Tucson has picked up through the first half of the year. The number of transactions recorded in the first half of the year is up 50 percent from the same period in 2019.
- While more properties are selling, prices have taken a step back. The median price dipped to $55,500 per unit in the second quarter, bringing the year-to-date median price to $66,100 per unit, down 12 percent from the median price in 2019.
- The average cap rate for deals closed during the first six months of this year is 5.7 percent, up 20 basis points from the average cap rate in 2019.

Investment Trends



Sources: NorthMarq, CoStar

The number of transactions recorded in the first half of the year is up 50 percent from the same period in 2019

Recent Transactions in the Market

MULTIFAMILY SALES ACTIVITY

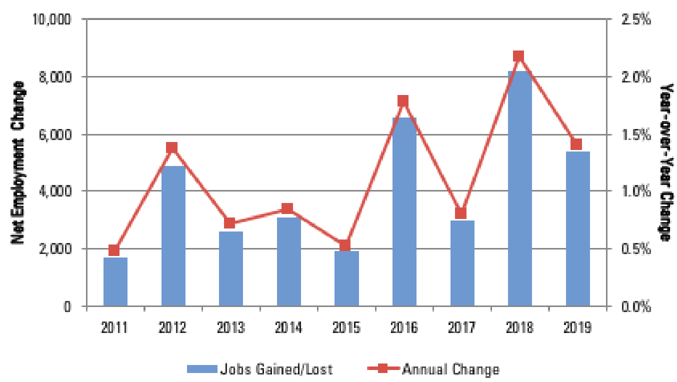
Property Name	Street Address	Units	Sales Price	Price/Unit
El Conquistador Apartments	1881 E Irvington Rd	201	$11,550,000	$57,462
Ridgewood Garden Apartments	3302 S Pantano Rd	171	$11,300,000	$66,081
Sandpiper	2401 E Glenn St	64	$4,700,000	$73,437
Broadway Inn Apartments	8477 E Broadway Blvd	49	$2,755,000	$56,224

Looking Ahead

The Tucson multifamily market should be in a fairly healthy position during the coming quarters. On the supply side, deliveries are forecast to total approximately 1 percent of the total market inventory, a manageable pace of supply growth. Demand will likely soften in response to the COVID-19 fallout, but Tucson does not have a particularly large leisure and hospitality sector, which should limit job losses. Initial announcements for the University of Arizona called for in-person classes, but this plan could change if the state continues to have an accelerating rate of coronavirus cases.

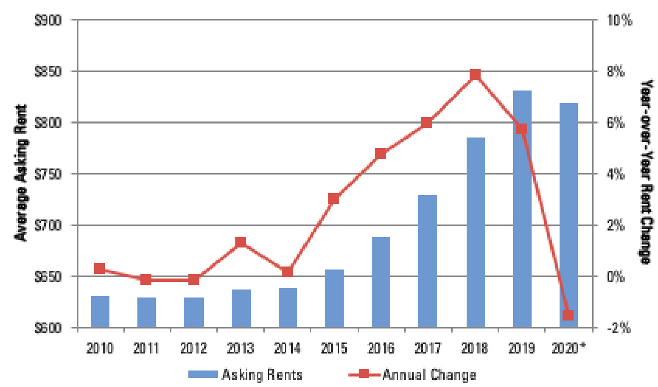
Investment activity in Tucson has been consistent through the first half of 2020, running counter to the national trend. The Tucson market has a large base of local investors who are generally active in transactions near $5 million, and low financing rates should continue to support acquisitions in these sorts of sales. It may take another quarter or two for activity to resume in larger transactions. Cap rates have ticked up slightly but are expected to remain in the mid- to high-5 percent range this year.

Employment Forecast



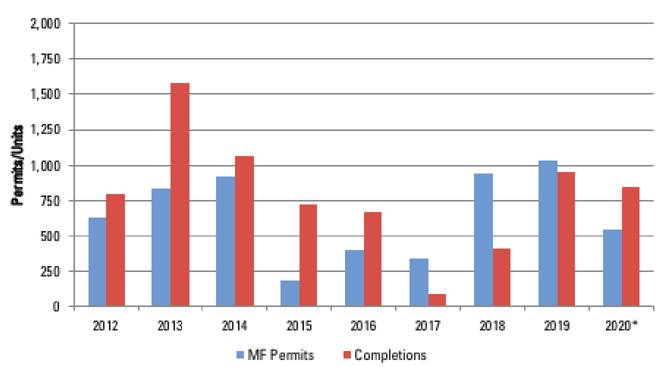
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



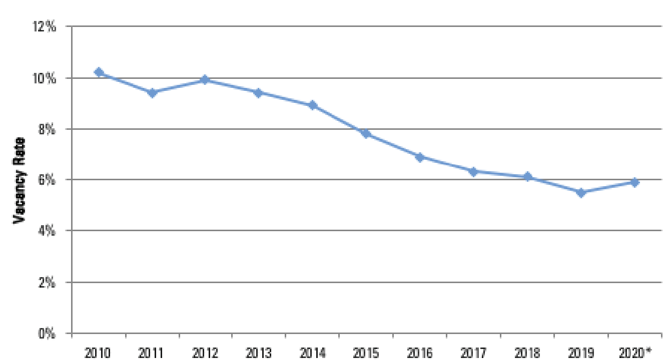
* Year End Forecast
Sources: NorthMarq, Apartment Insights

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

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