PHOENIX EYES INDUSTRIAL PROSPECTS, INDUSTRIAL PROSPECTS EYE PHOENIX

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Phoenix is known for its strength as a logistics and distribution market. This is particularly true in the Southwest Valley, which has become the poster child for all that makes Phoenix industrial space great: strong population growth, a deep and qualified workforce, an abundance of land and building opportunities, and a lower-cost, business-friendly regulatory environment.

As of the second quarter, these benefits helped the Southwest Valley emerge as No. 1 in the nation for industrial prospects looking for space (based on interest from at least 83 tenants with a maximum requirement of more than 30 million square feet). These prospects include national and regional distribution centers, third-party distribution providers, major ecommerce users, and a robust food and beverage sector led by companies like Fairlife Dairy, UFI, Ferrara Candy and Red Bull. It also comes from the reshoring of manufacturing from organizations like Hutamaki, Ball Enclosure and Anderson Windows.

Data centers continue to flock to Phoenix as well, purchasing about 2,000 acres over the past 24 months and positioning the Valley among the nation's top five U.S. data center markets. Data center interests like Microsoft, Vantage Data and Google have selected Phoenix for its low natural disaster risk, ample affordable land and reliable energy, which, in Maricopa County, is competitively priced at an average $0.064 per kilowatt hour (a $0.03 decrease in price since 2014).

These fundamentals have pushed the overall Phoenix industrial vacancy rate to a 10-year low of 6.7 percent and spurred 6.3 million square feet of new industrial construction, as of the second quarter of 2019. Much of this construction is speculative and designed to serve middle-market occupants requiring 50,000 to 200,000 square feet.

Industrial absorption continues to exceed new construction deliveries — as it has in Metro Phoenix for 5.5 consecutive years. The West Valley is also absorbing about 2.5 million square feet of middle-market space annually. This leads us to believe that any new space delivered will be absorbed quickly. Among this will be a significant percentage of middle-market users. These include major job creators like United Foods International, Integrated CBD, and Central Garden & Pet, which help make up the backbone of Phoenix's industrial and supply chain marketplace.

Sustained in-migration (much of it from California) of both businesses and residents, as well as construction of a new Northern Parkway and Loop 202 extension, continue to drive Phoenix's industrial growth. This has created new employment corridors and enhanced business efficacies via speed-to-market — all factors that continue to make Phoenix a smart industrial bet in 2019 and well beyond.

PHOENIX APARTMENT MARKET REMAINS RED-HOT; FUELING INFLUX OF NEW CAPITAL, SPIKE IN TRANSACTIONS

It isn't just temperatures that are scorching in the Phoenix metro this summer. The multifamily rental market is hot as well; and vigorous demand is coming from both renters and investors.

Investors are snapping up apartment properties and paying hefty prices. Buyers spent $3.72 billion on 94 Phoenix-area apartment complexes in the first half of 2019, a 41.8 percent jump from the first half of 2018. Sales in the $50 million range experienced the greatest rate of acceleration.

The Driving Factors Behind Strong Demand

Phoenix is the fastest-growing city in the U.S., according to recently released data from the U.S. Census Bureau. The region saw an increase of 25,288 new residents between 2017 and 2018, topping all other U.S. cities. One reason for that growth is that Phoenix remains more affordable than many other large U.S. metros. People are flocking to the Valley from high-cost, high-tech cities like Los Angeles and San Diego. Phoenix also boasts a thriving job market that includes a fast-growing, high-paying tech sector. Other booming industries include bioscience/healthcare and financial services.

In fact, the Phoenix metro led the U.S. for new jobs created from May 2018 to May 2019 with 66,500 nonfarm jobs, representing 3.2 percent job growth, according to a new U.S. Bureau of Labor Statistics report. Another 60,000 new jobs are forecast in 2019.

Robust net migration and job production are fueling the increased demand for new housing in Phoenix. This has led to a multifamily development boom. Developers delivered nearly 2,000 new units in the first quarter of 2019, well ahead of the 2018 pace, with another 10,500 units in the pipeline.

Despite new construction, Phoenix's rents remain among the fastest-growing in the U.S. The metro has ranked in the top two for apartment rent growth for the past several years. The average rent was $1,105 in the first quarter of 2019, up 9.5 percent year over year. Phoenix is forecasted to be a top contender for U.S. rent growth again in 2019. The market also boasts a healthy 94.7 percent occupancy rate.

Meanwhile, Phoenix single-family home prices are expected to hit record highs in 2019 as home appreciation continues to climb.

New Capital Floods the Apartment Market

Investors from California have historically pursued Phoenix apartment assets. Now, however, there is a surge in new large investors from Colorado, Texas, Seattle and Portland, Ore. There is significantly more capital in the Phoenix-area market than multifamily properties to acquire, and most deals have upward of 10 to 12 offers.

Another factor fueling strong transaction activity is the capital markets. The 10-year Treasury yield over the past 90 days has fallen dramatically, meaning financing for apartments is about 100 basis points lower than a year ago. Some of the largest players in the market are both buying and selling assets, even though pricing has increased significantly. This is because the debt they can obtain on new acquisitions is markedly cheaper.

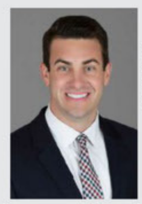
The median price of Phoenix apartments pushed higher to start the year. It was $136,700 per unit in the first quarter of 2019, a 15 percent jump from 2018. The average cap rate compressed by 5 percent and, for some newer properties, it is as low as 4.5 percent.

New Product Emerging on the Outskirts

Most new multifamily development over the past five years has been infill projects in East Valley, Scottsdale, Chandler, Tempe, and downtown and midtown Phoenix. However, a new emerging product type is low-density, single-family rental communities with 4,400 units stabilized, in lease-up or under construction, with another 2,900 units in the pipeline.

These "lock-and-leave" units are being developed on the city's peripheral in communities like Goodyear, Gilbert, Buckeye and Peoria, which, historically, have seen little new construction. Land is less expensive on the outskirts than in urban infill markets, and single-level development costs are cheaper.

While urban infill continues, costs continue to rise. Single-family rental



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communities represent an attractive property type that feels more like a community, with a backyard and no one living above or below the tenant. Accordingly, they are drawing strong rents. The two largest renter profiles for this new product are downsizing Baby Boomers and the more experience-driven Millennials.

Baby Boomers can live in a home similar to what they are accustomed to without the maintenance headaches and having to tap into their retirement savings for a big down payment. Meanwhile, Millennials like the flexibility of a lease, yet want the comfort of a home rather than a high-rise.

What Does the Future Look Like?

The Phoenix multifamily market expects to continue to boast strong performance in 2019 and 2020. Experts anticipate continued rapid rent growth, healthy absorption, strong development activity and an extended run of low vacancy rates. The apartment investment market got off to a quick start to 2019, which has paved the way for what will likely be another dynamic year.