MARKET REPORT

Multifamily

Tucson Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

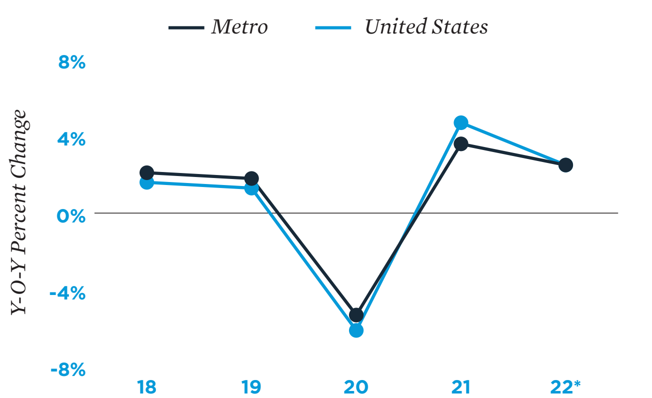
2Q/22

Labor Market Shifts Spark Multifamily Performance Gains and Investor Fervor

New tech-related roles support strong household formation. Tucson's unemployment rate fell to 3.7 percent in February 2022, the lowest level since before the financial crisis. The growth of the local semiconductor and autonomous driving segments has helped put Tucson in a position to surpass pre-pandemic employment highs during 2022. In addition, expansions from Raytheon and biotech firms, such as Roche, are helping the area retain more University of Arizona alumni than in the past. This economic growth is aiding renter demand, especially in the Class A segment, as younger professionals with above-average incomes represent a prime demographic for luxury properties. Skilled labor opportunities will facilitate a rate of household formation during 2022 that ranks among the top 10 nationally.

Performance improvement all-encompassing. Tucson recorded a widespread demand surge in 2021, with nearly all submarkets reporting year-over-year vacancy compression of at least 70 basis points. All seven Tucson submarkets posted sub-3 percent vacancy rates at the end of last year. These tight conditions suggest heightened competition for available units will persist during the remainder of 2022, sparking additional rent increases and leasing at newly delivered properties. During the first quarter of this year, metrowide vacancy trimmed another 10 basis points, highlighted by a 100-basis-point drop in Catalina Foothills during the first quarter of this year.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.; RealPage, Inc.

Multifamily 2022 Outlook

9,500 JOBS *will be created*

EMPLOYMENT:

Job creation will expand payrolls by 2.5 percent, resulting in the metro surpassing the 2019 job count by year-end. The metro's high proportion of government jobs helped insulate the market from more severe pandemic-related job losses.

700 UNITS *will be completed*

CONSTRUCTION:

Coming off a record-setting year for development in Tucson, inventory is projected to rise 0.8 percent during 2022. This is still a sizable slate of rentals, compared to the five-year trailing average of 550 units per year.

40 BASIS POINT *decrease in vacancy*

VACANCY:

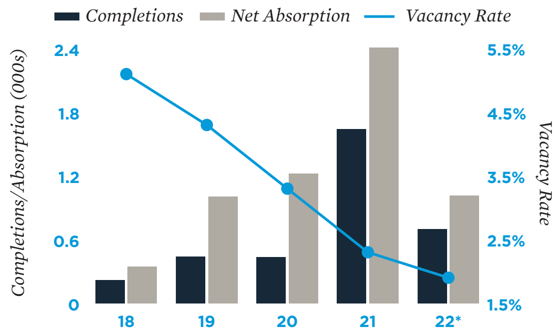
The resumption of more on-campus activities at the University of Arizona and the return of office workers to in-person operations will further bolster renter demand. By year-end, vacancy will reach 1.9 percent, a record low for the metro.

14.2% INCREASE *in effective rent*

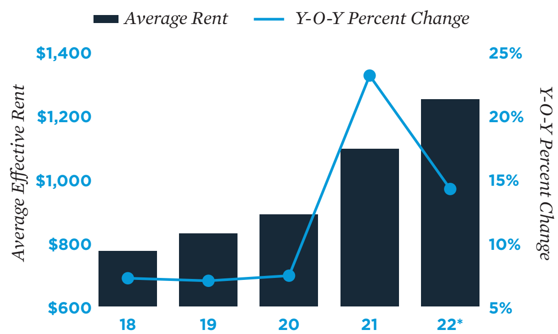
RENT:

Following a 22.9 percent surge in 2021, upward forces remain in effect this year, elevating the average effective payment to $1,249 per month. This gain puts the two-year rate of growth above 40 percent.

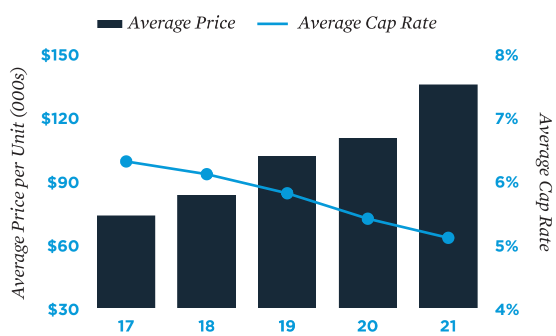
Supply and Demand



Rent Trends



Sales Trends



** Forecast*

Sources: CoStar Group, Inc.; Real Capital Analytics; RealPage, Inc.

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Price: $250

1Q 2022 - 12-Month Period

CONSTRUCTION

1,977 units completed

- Central Tucson-University added the most supply last year at approximately 850 apartments, followed by East Central and Southeast Tucson, where roughly 300 units were added in each locale.
- Builders have roughly 1,400 units currently under construction in the metro; however, half are slated to arrive during 2023.

VACANCY

140 basis point decrease in vacancy Y-O-Y

- The Catalina Foothills and Casas Adobes-Oro Valley submarkets both reported vacancy slipping below 2 percent during the first quarter of 2022, joining Airport-Drexel Heights-Sahuarita.
- Despite elevated completions, Class A vacancy in the Central Tucson-University submarket fell 210 basis points to 1.6 percent in 2021.

RENT

23.0% increase in the average effective rent Y-O-Y

- Historically low availability helped lift the average rental payment to $1,125 per month at the end of March.
- The metro's two highest cost submarkets, Catalina Foothills and Casas Adobes-Oro Valley, recorded some of the strongest rent gains, at 25 percent and 24 percent, respectively.

Investment Highlights

- Transaction velocity rose greatly in Tucson during 2021, with more trades occurring than any period on record dating back to 2000. Record deal flow was most apparent in the over $20 million tranche. Within this segment, assets with more than 100 units are garnering heightened attention, with first-year cap rates for larger Class A assets usually around 3 percent and lower-tier yields closer to 4 percent. Estimates for the first quarter of 2022 have maintained this trend, but rising interest rates may give buyers pause moving forward into this year.
- Rising prices in Phoenix and major West Coast markets led to more outside investors targeting multifamily assets in Tucson. As a result, more 80-unit-plus properties were purchased by first-time buyers in Tucson last year than in previous periods.
- An increase of institutions and out-of-area buyers in the metro is lifting per-unit entry costs. Buy-side pressure manifested in Tucson recording one of the sharpest rises in average sales pricing among major U.S. metros last year at more than 20 percent. This gain lifted the average price point to approximately $135,200 per unit.