MARKETBEAT

TUCSON

Multifamily Q4 2022

CUSHMAN & WAKEFIELD | PICOR

	YoY Chg	12-Mo. Forecast
7.46% Vacancy Rate	▲	▲
97 New Deliveries, units	▼	▲
$1,157 Effective Rent, Per Unit	▼	▬

(Overall, All Property Classes)

ECONOMIC INDICATORS Q4 2022

	YoY Chg	12-Mo. Forecast
393K Tucson Employment	▲	▲
3.8% Tucson Unemployment Rate	▲	▲
$63.6K Tucson Median Household Income	▲	▲

Source: BLS, Census Bureau

Source: apartmentinsights.com

Tucson Economy:

Tucson's fourth quarter of 2022 employment increased to 393,000 jobs, up 2.2% over Q4 2021. At 3.8%, the local unemployment rate matched that of the same quarter a year prior and is forecast to increase in the year ahead. Household formation grew 1.9% year-over-year (YOY) with median household income increasing 5.8% YOY from $60,100 to $63,600. Nationally, consumer spending grew at a healthy 8.5% rate and retail sales were similarly up 8.4% YOY. Inflation persisted over 7.0%, high relative to recent years, while consumer and corporate balance sheets remain cash strong.

Market Overview:

In the fourth quarter, Tucson saw the average vacancy rate increase 1.20% to 7.46% from the previous quarter, which is also a 3.08% increase year over year (YOY). The Tucson market's occupancy declined correspondingly by 520 units, while the average gross apartment rent without utilities decreased $8 (.69%) from Q3 2022 to $1,157 per unit/$1.53 per square foot (sf). In reviewing transactions for properties with 40 or more units in consecutive quarters, the average price per unit increased by a dramatic $57,893 per unit and $11.83 per sf to a total of $250,944 per unit and $293.23 per sf.

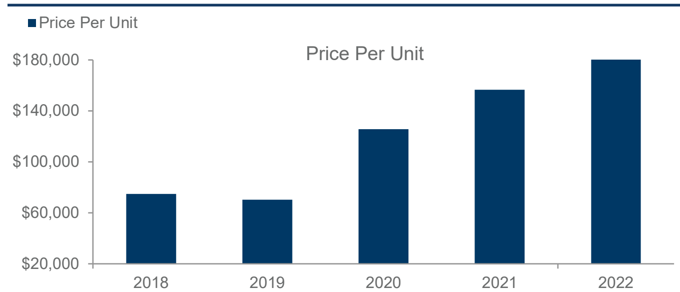
Rents and Lease-up Duration:

The end of 2022 saw a decline and slowdown in the rental market. Units being marketed at pre-adjustment rental numbers are slow to lease. This softening in rents results from the market changes and renters exercising caution financially to not stretch outside of their means. In surveying local managers, many cite Q4 as the slowest leasing quarter in Tucson since 2019. Units which would previously have leased within days are now taking weeks or months to lease. The City of Tucson is still working to fill the need to place affordable housing tenants. Subsidized rents are only slightly below market rents with the goal of enticing owners and managers to fill vacancies with lower income tenants. Going forward in 2023 and beyond, Tucson will likely experience softer YOY rent increases than in recent years.

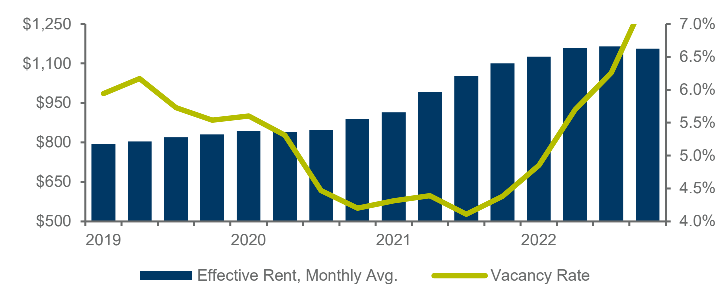
Supply vs Demand:

Supply and Demand in the Tucson MSA has completely flipped from the beginning of 2022. Owners who had pricing expectations based on property values in the first half of the year have had to adjust to the new reality if they wish to move their product in this market. For multiple reasons, Q4 2022 saw considerably fewer transactions than in previous quarters. First, interest rates for commercial apartment building investment have increased nearly 300 basis points in a 12-month window. Second, softening in the rental market has caused more cautious underwriting and projections by buyers when evaluating deals. Third, each year, regardless of the market's strength, a seasonal slowdown is experienced during the holidays. In 2023, the market will likely cool and require closing the gap between seller's expectations and purchasers' willingness to pay.

SALE PRICE PER UNIT



OVERALL VACANCY & EFFECTIVE RENT



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MARKET STATISTICS

SUBMARKET*	INVENTORY (UNITS)	VACANCY RATE	YOY VACANCY RATE CHANGE	AVG EFFECTIVE RENT/UNIT	AVG EFFECTIVE RENT PSF	YOY % EFFECTIVE RENT GROWTH
Oro Valley/Catalina	2,279	6.14%	29.31%	$1,449	$1.55	2.51%
Northwest	8,695	7.15%	46.29%	$1,586	$1.65	0.69%
Catalina Foothills	5,726	5.97%	43.55%	$1,419	$1.52	0.90%
Northeast	1,987	8.40%	64.04%	$1,211	$1.58	5.73%
East	8,221	7.74%	38.37%	$1,430	$1.48	4.70%
North Central	8,197	8.12%	45.93%	$1,083	$1.45	5.10%
Flowing Wells	8,524	8.37%	27.12%	$959	$1.39	10%
Foothills	3,780	6.85%	41.31%	$1,000	$1.62	8.03%
University	4,509	3.86%	3.5%	$1,331	$1.64	13.22%
South Central	6,595	7.30%	32.73%	$1,210	$1.92	4.16%
Pantano/Lakeside	5,412	8.73%	54.75%	$985	$1.50	6.46%
South/Airport	6,058	7.27%	58.73%	$1,067	$1.50	16.16%
Southwest	2,415	5.77%	5.89%	$1,027	$1.65	6.04%
Southeast	956	15.53%	59.75%	$1,059	$1.45	37.26%
Market	**5,240**	**7.66%**	**39.38%**	**$1,201**	**$1.56**	**8.64%**

*Submarket Marana excluded from report due to low inventory

Source: apartmentinsights.com

Financing:

"Commercial and Multifamily lending activity is expected to contract in 2023 compared to 2022's robust transaction volume. From a lender's perspective, investor demand has tapered as a result of rising interest rates and changing economic conditions. Treasury yields across the board have increased since early 2022, and are anticipated to rise well into 2023. Furthermore, lenders need to account for the anticipated Federal Funds Rate increases throughout the year to continue tamper inflation, which will continue to impact the short end of the yield curve resulting in higher short-term borrowing costs for financial institutions. The good news is that from a market perspective Tucson has relatively low vacancy, modest rent growth, and a lower price per unit compared to other markets. We don't anticipate a massive market downturn or a substantial decrease in property values, but we do expect values to remain stagnant or experience a slight decrease/normalization of values as cap rates have shown some upward trajectory."

Adam Coggshall & Robert Motz – Pima Federal Credit Union – rmotz@pimafederal.org – 520-202-0672

Outlook:

Tucson's multifamily investment market slowed drastically in Q4 2022, experiencing lower transaction volume, more pricing adjustments, and a softening in rents. While many markets have been impacted by economic headwinds, Tucson's MSA will likely remain strong due to limited inventory and difficulty building new product in central Tucson locations. Many investors are still eager to enter or grow their Tucson portfolio, but the pricing has to pencil given the current lending environment. Pricing is expected to lower slightly to get to a cap rate that makes sense for investors. As cap rates continue to increase, cash buyers are likely to become competitive again, as they have been priced out of the market in recent years due to low cost of debt.

ALLAN MENDELSBERG
Multi-Family Team, Principal
+1 520 546 2721 / amendelsberg@picor.com

JOEY MARTINEZ
Multi-Family Team, Principal
+1 520 546 2730 / cmartinez@picor.com

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