MARKETBEAT

TUCSON

Multifamily Q2 2023

	YOY Chg	12-Mo. Forecast
8.09% Vacancy Rate	▲	▼
141 New Deliveries, units	▲	▲
$1,182 Effective Rent, Per Unit	▲	▬

(Overall, All Property Classes)

ECONOMIC INDICATORS Q2 2023

	YOY Chg	12-Mo. Forecast
399K Tucson Employment	▲	▲
3.4% Tucson Unemployment Rate	▲	▲
$72.9K Tucson Median Household Income	▲	▲

Source: BLS, Census Bureau

Source: apartmentinsights.com

Tucson Economy:

In the second quarter of 2023, the US economy continued to exhibit resilience, with favorable implications for commercial real estate. Year-over-year (YOY) median household income grew from $69,700 to $72,900, supporting consumer spending and retail sales. Real GDP was up 2.1%, indicating strength amid economic headwinds. Of significance, the consumer price index reflected 11 consecutive months of decreasing inflation, dropping from 8.6% to 4.0% YOY. In Tucson positive trends persisted, with median household income rising from 3.2% YOY. Nonfarm employment increased 1.5%, reflecting a stable, if not robust, job market. The unemployment rate declined from 3.7% to 3.4%, suggesting improved labor conditions.

Market Overview:

Tucson's average multifamily vacancy rate increased 0.60% to 8.09% in Q2 2023, representing a 26.81% increase YOY. The Tucson market's leasing activity slowed as the new year turned, but toward the end of the first quarter regained velocity. The average gross apartment rent without utilities increased $7 (0.61%) from Q4 2022 to $1,164 per unit/$1.53 per square foot (sf). Of completed transaction in the quarter, only two exceeded 40 units, which extended the Q1 2023 drastic slowdown in sales volume in the 40+ unit apartment market. The two properties sold for an average of $82,000 per unit and $154.93 per sf.

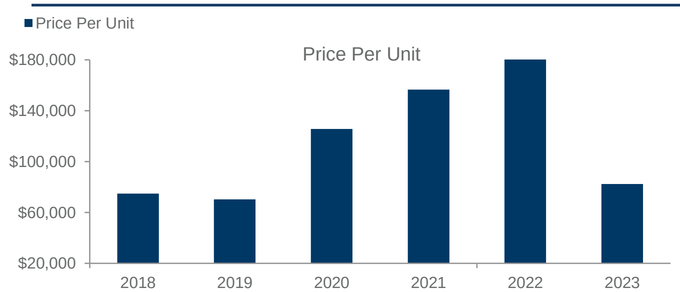
Rents and Lease-up Duration:

The first half of 2023 saw slower leasing than expected, but as mid-year approached, the pace picked up. Managers reported that less favorably located buildings and those with inferior curb appeal were hit harder than their counterparts. This can be attributed to tenants doubling up with roommates or moving in with family and friends to save money. Apartment Insights reports on 15 submarkets, of which four recorded gross rents above $1,400/unit. From Q2 2022, Tucson's average gross rent rose $23/month, a 1.98% increase. During the second quarter, gross rents increased in twelve submarkets, with a high of $41 in Tucson Mountain Foothills. The lowest average gross rent for Tucson was reported in the South-Central Tucson submarket at $972. Average gross rents fell in two submarkets, with the highest drop of $13 (-1.21%) occurring in the South Tucson/Airport submarket.

Supply vs Demand:

In the first half of 2023, zero transactions occurred for properties over 100 units. This trend is expected to continue as many owners and investors remain on the sidelines monitoring interest rates. Demand has softened as many investors have returned to their local market with pricing softening nationally. Demand still significantly outweighs supply as new inventory slowly reaches the market. Pricing adjustments have been tempered in Tucson relative to national averages due to low supply and a steady rental market. There were only 21 transactions from properties 10-100 units in Tucson for the first half of 2023.

SALE PRICE PER UNIT



OVERALL VACANCY & EFFECTIVE RENT

TUCSON

Multifamily Q2 2023

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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	2,615	6.85%	+11.53%	$1,579	$1.64	-1.86%
Northwest	8,695	6.97%	+11.76%	$1,454	$1.56	+1.16%
Catalina Foothills	5,726	7.97%	+35.27%	$1,244	$1.62	+1.60%
Northeast	1,987	6.09%	+31.36%	$1,495	$1.54	+0.93%
East	8,221	7.51%	+30.62%	$1,104	$1.48	+0.09%
North Central	8,197	8.76%	+36.64%	$995	$1.44	+3.51%
Flowing Wells	8,644	9.19%	+13.71%	$1,016	$1.65	+6.88%
Foothills	3,921	7.33%	+36.01%	$1,362	$1.68	+3.96%
University	4,509	7.80%	+13.97%	$1,219	$1.93	+5.57%
South Central	6,595	7.74%	+23.77%	$972	$1.48	-0.97%
Pantano/Lakeside	5,412	9.97%	+35.90%	$1,076	$1.52	-4.35%
South/Airport	6,165	8.68%	+60.02%	$1,063	$1.66	+12.04%
Southwest	2,415	8.82%	+48.97%	$1,073	$1.47	+2.42%
Southeast	956	8.79%	-14.24%	$1,594	$1.53	+12.48%
Market (Total/Average)	**74,058**	**8.03%**	**26.81%**	**$1,232**	**$1.59**	**3.10%**

*Submarket Marana excluded from report due to low inventory

Source: apartmentinsights.com

Financing:

"From a lender's viewpoint, anticipated loan volume shrunk from the previous year's production. Out of 21 closed transactions, 13 were purchase money requests, demonstrating the strong demand for multifamily in the Tucson market. However, over the course of this year, underwriting has become more challenging. As market level expenses increased, a rise in vacancy rates/collection loss, and continuing interest rates hikes stress our DSCR standards. Typical loan to value ratio for new purchase requests fell between 60-65% with an occasionally 70%. The increased activity in the bond market and an approximate 75 bps increase in the effective federal funds rate from Jan 3rd to July 11th, 2023, have had a direct impact on lending rates. We anticipate the remainder of 2023 to have steady loan production, both purchase request, and refinance. Currently we are quoting 30-45 days to close for purchase request, and 60 plus days for refinance requests. While underwriting stresses have been more challenging, the fundamentals for Tucson multifamily are strong."

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

Outlook:

The first half of 2023 saw the institutional market come to a halt, leading to not one sale over 100 units in Tucson. The under 100-unit market saw a steady stream of sales occur as many long-time owners did not want to ride the uneasy wave of the market. Demand dropped perceptibly but still heavily outweighed supply. As other markets saw significant declines in value, the Tucson market for small and mid-sized complexes remained relatively strong. Rent growth also started to experience some flat-lining with a nominal (normal in most years pre-2018) 3.10% YOY rent growth over Q2 2022. Along with continued interest rates hikes throughout the year, upward pressure on cap rates will continue to meet investor return requirements. Transactions are getting tougher as the gap between seller expectation and buyer's feasibility spread.

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