Market Insights

Greater Tucson Multifamily 4Q 2021

Northmarq

Construction Activity

1,313

Units under construction

1,422

Units delivered (YTD)

Market Fundamentals

4.4%

Vacancy

+10bps | Year over year change

$1,100

Asking Rent

+23.7% | Year over year change

Transaction Activity

$113,200

Median sales price per unit (YTD)

Additional Rent Growth Likely as Labor Market Rebounds

Highlights

- The Tucson multifamily market closed a very strong 2021 with rents continuing to advance at a rapid clip. Developers were active throughout the year, and 2022 is expected to be another year of healthy construction levels.
- Vacancy in Tucson recorded a minimal increase in 2021. The rate rose 10 basis points for the year to 4.4 percent. This marked the first annual vacancy increase in Tucson since 2012.
- Apartment rents in Tucson continued to increase during the fourth quarter, rising 4.5 percent. For all of 2021, rents spiked 23.7 percent, reaching $1,100 per month.
- The sales of apartment properties accelerated in the final months of the year, nearly doubling total transactions from the previous quarter. The median sales price rose to $113,200 per unit while recent cap rates averaged 3.4 percent.

Tucson Multifamily Market Overview

The Tucson multifamily market thrived in 2021 as rents gained momentum throughout the year, and the vacancy rate remained far lower than the historical average, despite a steady pace of new development. The pace of rent growth during the fourth quarter was among the fastest of the major markets in the country, setting the stage for continued increases in the coming year. The local labor market has been adding back workers but has not made the full recovery posted in nearby Phoenix or in other markets throughout the Southwest. The 2022 outlook calls for additional recovery in area employment, which should support demand for apartment properties.

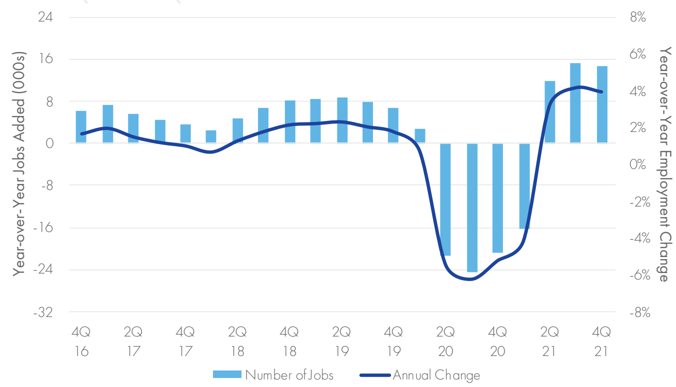
After sales velocity tracked 2020 levels for much of the year, the local investment market gained momentum in the final few months of 2021. The number of properties changing hands rose 70 percent from the third quarter to the fourth quarter, with sales topping $50 million recording the greatest increases. Pricing trends reflected the accelerating investor demand and the sharp rise in property revenues. The median price advanced more than 50 percent in 2021, fueled by the steepest annual rent growth on record and tight vacancy conditions. Prices continued to push higher in the fourth quarter, when nearly 40 percent of the properties sold traded for more than $200,000 per unit.

Employment

- Employment in Tucson expanded by approximately 3.9 percent in 2021 with net job additions totaling 14,700 positions. While the local economy remains in recovery mode, total employment is still down approximately 10,000 positions from the pre-COVID peak.
- Employers in the manufacturing sector added 1,900 jobs to payrolls in 2021, a growth rate of 7 percent. Annual growth in manufacturing employment has averaged 3.2 percent since 2015.
- During the fourth quarter, Leonardo Electronics announced plans to expand its presence in the Tucson area by constructing a new 120,000-square-foot semiconductor laser manufacturing facility. Construction will begin in the first quarter of 2022 and will create 170 additional jobs over the next five years. The company currently has approximately 200 employees in the area.
- **Forecast:** The Tucson labor market is expected to record another year of gains in 2022. Employers are forecast to add 11,500 new jobs in 2022, a gain of about 3 percent.

> Local employment has expanded by nearly 3.9 percent in 2021, an addition of 14,700 jobs.

Employment Overview



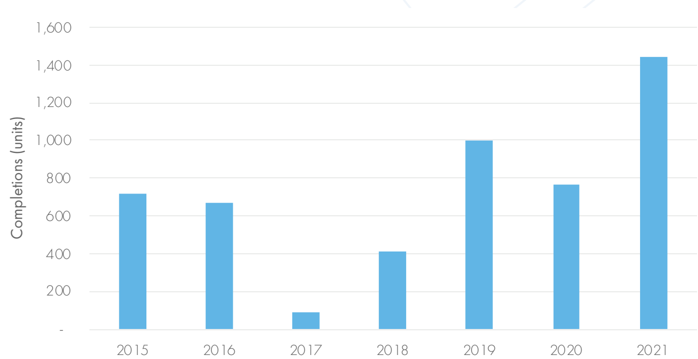
Sources: NorthMarq, Bureau of Labor Statistics

Development and Permitting

> Developers pulled permits for 950 multifamily units in 2021.

- The pace of apartment deliveries accelerated in Tucson in 2021. Developers brought over 1,400 units online, nearly doubling the number of units that were delivered to the market in 2020.
- Construction activity increased over the past several quarters in response to the ongoing renter demand for apartments in Tucson. There were over 1,300 units under construction in the region at the end of the fourth quarter, an increase of 4 percent compared to activity at the end of 2020.
- Developers are responding to consistently low vacancy rates and persistent renter demand by stepping up permitting activity. Developers pulled permits for approximately 950 multifamily units in 2021, an increase of 50 percent compared to permitting activity in 2020.
- **Forecast:** After deliveries peaked in 2021, projects totaling approximately 1,100 units are forecast to be delivered in the year ahead. Deliveries have averaged approximately 725 units per year since 2015.

Development Trends



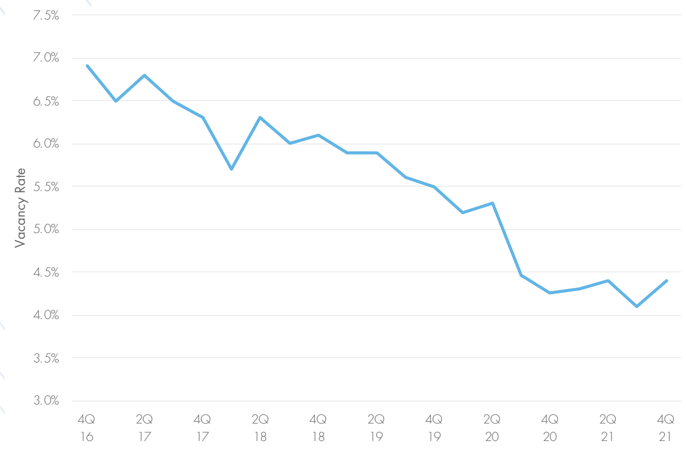
Sources: NorthMarq, Apartment Insights

Vacancy

- The vacancy rate ticked up during the final months of 2021, rising 30 basis points to 4.4 percent. The rate has been mostly stable for the past six quarters, remaining between 4.1 percent and 4.5 percent since the second half of 2020. The average rate in the Tucson region since early 2015 has been 6 percent.
- Vacancy inched up 10 basis points in 2021. The modest uptick recorded in 2021 was the first annual vacancy increase in the market since 2012.
- Absorption totaled nearly 1,200 units in 2021, down from nearly 1,300 units one year ago. Recent absorption totals have outpaced the market's long-term average by about 25 percent.
- **Forecast:** The vacancy rate in Tucson has been trimmed in half in recent years. The rate is forecast to creep lower in 2022, likely falling 20 basis points to end the year at 4.2 percent.

> "Vacancy inched up 10 basis points in 2021.

Vacancy Trends



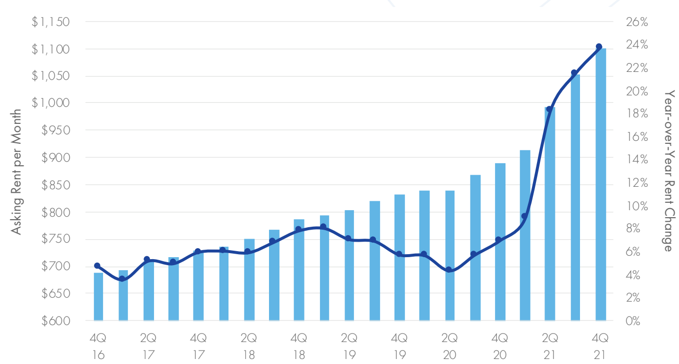
Sources: NorthMarq, Apartment Insights

Rents

- Asking rents in Tucson continued to post strong gains through the end of the year, marking the sixth consecutive quarter of growth. Rents rose 4.5 percent in the fourth quarter, ending 2021 at $1,100 per month.
- Local asking rents surged 23.7 percent in 2021, building on gains that have averaged 6.6 percent per year since 2017. This marks the largest annual rent growth on record.
- Some of the strongest rent growth is occurring in the more expensive submarkets at the northwest boundaries of the Tucson market. In 2021, rent growth in Oro Valley/Catalina topped 30 percent, while the increase in the Northwest Tucson submarket totaled approximately 27 percent.
- **Forecast:** After several consecutive quarters of rapid rent increases, the pace is forecast to cool somewhat in 2022. Rents in Tucson are forecast to rise 7.5 in 2022, ending the year at approximately $1,180 per month.

> "Local asking rents surged 23.7 percent in 2021.

Rent Trends



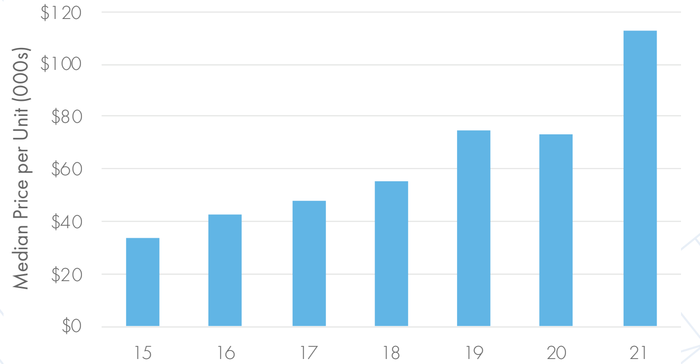
Sources: NorthMarq, Apartment Insights

Multifamily Sales

- Sales of multifamily properties accelerated in the final months of the year, increasing by 70 percent from the previous quarter. The rise at the end of the year pushed activity levels for the full year ahead of the pace recorded in 2020. Sales velocity in 2021 was up 11 percent from the preceding year, while transaction dollar volume spiked by more than 50 percent.
- With rents on a rapid upward trajectory and investor demand accelerating, prices pushed higher. The median price soared more than 50 percent in 2021, rising to $113,200 per unit.
- Cap rates compressed throughout 2021, with investors accepting lower initial rates of return in anticipation of implementing rent increases going forward. During the fourth quarter, properties generally traded with cap rates ranging from 3 percent to 3.5 percent.

The median price soared more than 50 percent in 2021.

Investment Trends



Sources: NorthMarq, CoStar

Recent Transactions

Multifamily Sales Activity

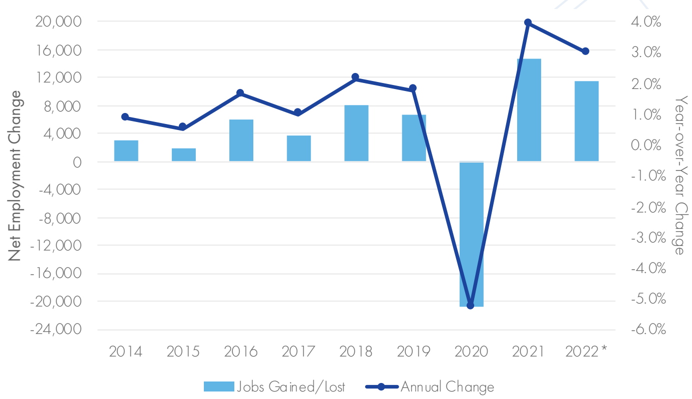
Property Name	Street Address	Units	Sales Price	Price/Unit
Desert Shadows Apartments	7425 N Mona Lisa Rd., Tucson	338	$69,300,000	$205,030
Villas las Naranjas	1345 S Kolb Rd., Tucson	410	$65,500,000	$159,756
Casa del Coronado	201 W Blacklidge Dr., Tucson	208	$27,500,000	$132,212
Villas las Toronjas	6639 E Broadway Blvd., Tucson	135	$20,300,000	$150,370
Silverado Apartments	5000 S Country Club Rd., Tucson	132	$15,775,000	$119,508

Looking Ahead

Another year of significant activity is forecast for the Tucson multifamily market in 2022. Renter demand for units has been elevated in each of the past two years, and developers are increasing activity to meet demand. There are a handful of new construction projects that are forecast to deliver in the year ahead, with developers expected to complete more than 1,000 new units for the third time in a four-year period. To this point, vacancy has trended lower, and the combined forces of tightening vacancy and newer, more expensive units entering the market has fueled rapid rent growth in recent years. Assuming employment growth continues on its current trajectory and housing demand remains elevated, rents should continue to trend higher in 2022.

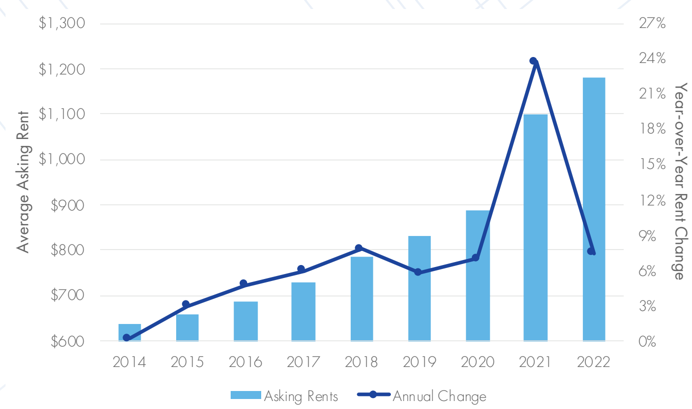
Investment demand is forecast to remain elevated in the Tucson area for the next several quarters, as the momentum established in the fourth quarter will likely carry over into 2022. The rapid cap rate compression that occurred in 2021 shows no sign of reversing course, and with rents expected to continue to expand at an accelerated pace, cap rates may remain in current ranges for at least a few more quarters. In recent periods, there has been an increase in the number of multi-property portfolio sales in the Tucson area, as some newer buyers look to acquire multiple properties as they establish or increase operations in the market. This trend could continue in the year ahead.

Employment Forecast



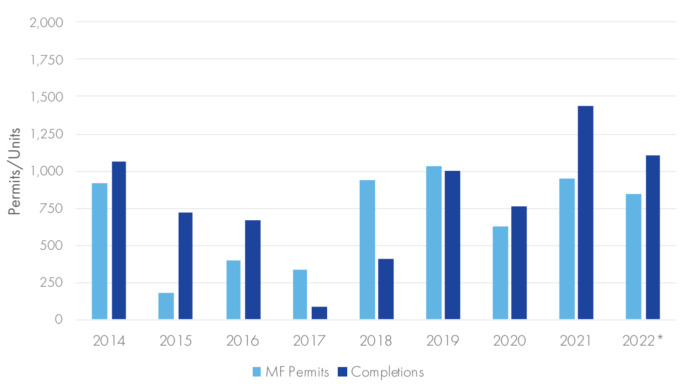
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



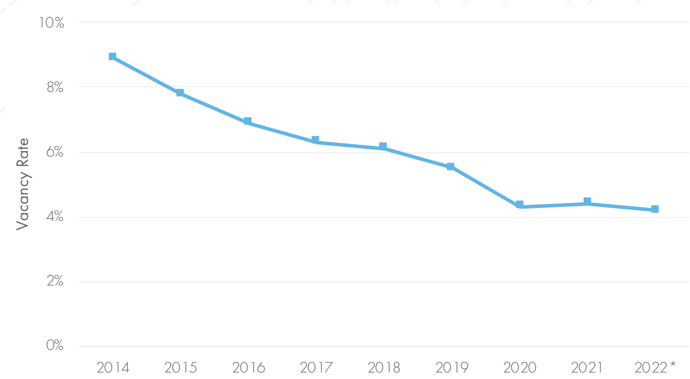
* Year End Forecast
Sources: NorthMarq, Apartment Insights

Construction & Permitting Forecast



* Year End Forecast
Sources: NorthMarq, Apartment Insights, Census Bureau

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Apartment Insights

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