Northmarq

MARKET INSIGHTS

Vacancy flat in response to heightened absorption

CONSTRUCTION ACTIVITY

UNDER CONSTRUCTION	37,461
UNITS DELIVERED	2,548

MARKET FUNDAMENTALS

VACANCY RATE	6.4%
YEAR-OVER-YEAR CHANGE	+160bps
ASKING RENTS	$1,614
YEAR-OVER-YEAR CHANGE	-0.6%

TRANSACTION ACTIVITY (YTD)

MEDIAN SALES PRICE	$233,700

Phoenix Multifamily
1Q 2023

HIGHLIGHTS

- Operational performance in the Greater Phoenix multifamily market was fairly steady to start 2023. Vacancy was flat and rents inched lower by a few dollars per month. The pace of new development is forecast to accelerate in the coming quarters, which should lead to increases in the local vacancy rate.
- After rising throughout 2022, vacancy stabilized in the first quarter of this year. The rate held steady at 6.4 percent, matching the figure at the end of last year. During the past 12 months, vacancy has pushed up 160 basis points.
- Rents ticked lower in the first quarter, dipping to $1,614 per month. This followed a sharper decline at the end of 2022. Year over year, average rents have dipped 0.6 percent, although many suburban submarkets have recorded more significant declines.
- Investment activity remained light at the start of this year, although there was an uptick in activity in March, particularly in sales over $90 million. Cap rates trended higher, reaching an average of 5.3 percent. The median price has retreated, totaling $233,700 per unit year to date.

PHOENIX MULTIFAMILY MARKET OVERVIEW

The Greater Phoenix multifamily market stabilized during the first quarter, after weakening in the second half of last year. The local vacancy rate remained unchanged, matching the level from the end of 2022. Vacancy had trended higher in each of the previous five quarters, but the rate stabilized as the pace of absorption accelerated after slowing throughout much of the preceding year. While the pace of net renter move-ins picked up in recent months, rents recorded a minimal decline. Current rents are slightly lower than one year ago, as decreases in recent quarters have offset increases from earlier periods. The competitive impact of new supply was minimal during the first three months of the year but is expected to play a larger role in market fundamentals in the coming quarters.

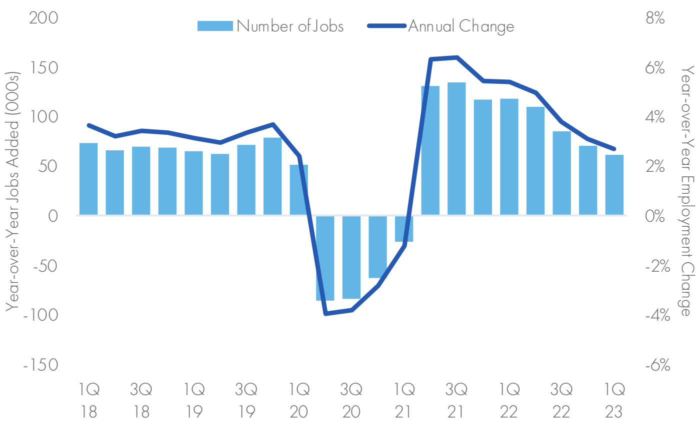
The local investment market has recorded limited transaction volume in recent quarters, following peak levels of activity throughout all of 2021 and the first half of 2022. While sales velocity was light in the first quarter, the greatest transaction activity occurred in March, which could set the stage for a handful of additional property sales in the coming quarters. Factors that should contribute to additional investment volume include rising cap rates and declines in per-unit pricing, resetting the expectations for the current market conditions. During the first quarter, cap rates averaged approximately 5.3 percent, and some properties have traded with cap rates near 5.5 percent. Late in the quarter, there was an upswing in larger transactions; more than half of the deals that closed in March sold for more than $90 million.

EMPLOYMENT

- The local employment market continues to expand, although the pace of growth is more modest than in recent quarters. Year over year, employers have added nearly 62,000 jobs, a 2.7 percent gain.
- The education and health services sector has been expanding to keep up with the demands stemming from rapid population growth. In the past year, employment in the sector has increased by 5.9 percent with the addition of more than 21,000 workers. Since 2015, the sector has posted average growth of more than 4 percent per year.
- The Phoenix area is recording elevated development and growth in industrial sectors. Construction employment has surged by nearly 5 percent in the past year, adding 7,300 net new jobs. Manufacturing employment has expanded by 4.2 percent year over year with 6,000 new positions.
- **FORECAST:** Continued population growth will support the need for additional gains in the local labor market. Employers are forecast to add approximately 30,000 jobs in Phoenix in 2023, a 1.3 percent expansion.

Year over year, employers have added nearly 62,000 jobs.

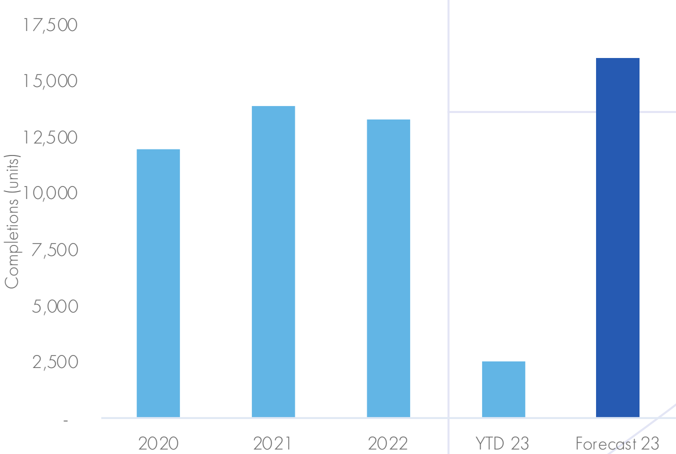
EMPLOYMENT OVERVIEW



Sources: Northmarq, Bureau of Labor Statistics

Completions are expected to track about 20 percent above 2022 levels.

DEVELOPMENT TRENDS



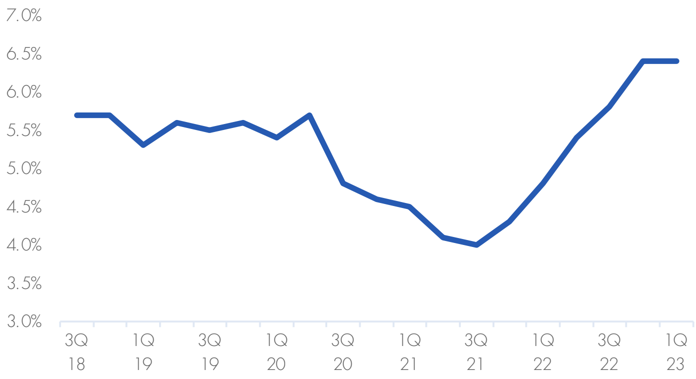
Sources: Northmarq, Apartment Insights

DEVELOPMENT & PERMITTING

- During the first quarter, projects totaling more than 2,500 units were delivered in Greater Phoenix, 19 percent higher than during the same period in 2022. Completions are expected to track about 20 percent above 2022 levels throughout the rest of this year.
- Construction activity has been on an extended upswing in recent years, as developers seek to keep pace with demand associated with population growth. Projects totaling nearly 37,500 units were under construction at the end of the first quarter, up from about 29,000 units one year earlier.
- Permits for approximately 3,500 multifamily units were issued during the first quarter, down nearly 5 percent from levels in the first quarter of last year. Multifamily permitting activity peaked late in 2022, when developers were pulling an average of 5,500 permits per quarter.
- **FORECAST:** Apartment deliveries are on pace to reach a cyclical high in 2023, with projects totaling approximately 16,000 units slated to come online. Last year, more than 13,000 units were delivered.

The vacancy rate was 6.4 percent in the first quarter.

VACANCY TRENDS



Sources: Northmarq, Apartment Insights

VACANCY

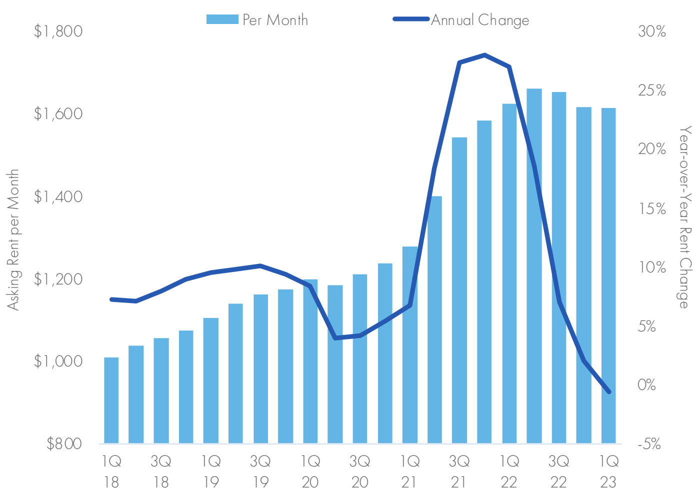
- Vacancy steadied at the start of 2023, after trending higher in each of the preceding five quarters. The rate was 6.4 percent in the first quarter, matching the level at the end of last year.
- Despite stabilizing in the first quarter, vacancy has pushed up 160 basis points year over year. The rate had retreated to an all-time low in mid-2021, but current vacancy levels are at their highest points since 2014.
- Much of the recent rise in vacancy rates has been recorded in mid- and lower-tier properties. Class B vacancy rates ended the first quarter at 6.4 percent, up from 5 percent one year ago, while vacancy in Class C properties has spiked 200 basis points year over year to 6.1 percent.
- **FORECAST:** Vacancy is expected to trend higher in the coming quarters as the pace of deliveries gains momentum. Vacancy is forecast to rise 90 basis points in 2023, ending the year at 7.3 percent.

RENTS

- Rents inched lower in the first quarter, dipping $2 per month from the year-end 2022 figure. Average rents ended the first quarter at $1,614 per month. The modest dip represents a break from a longer-term trend of healthy first-quarter rent gains; from 2018-2022, rent growth averaged 2.6 percent during the first three months of the year.
- After recording some of the strongest rent growth in the nation in 2021 and the first half of 2022, current rents are nearly identical to levels from one year ago. Year over year, average rents have dipped 0.6 percent.
- Rent trends have been mixed across the market. In many of the submarkets in and around Central Phoenix, rents have generally risen about 2 percent year over year. In some of the suburban submarkets in Tempe, Gilbert, and Ahwatukee, rents have declined between 2 percent and 5 percent on average during the past 12 months.
- **FORECAST:** There will be some downward pressure on rents in submarkets where competition from new space is most significant. However, renter demand is on pace to exceed 2022 levels, supporting rents at the market level. Average rents are forecast to inch up 2 percent to approximately $1,650 per month.

Average rents ended the first quarter at $1,614 per month.

RENT TRENDS



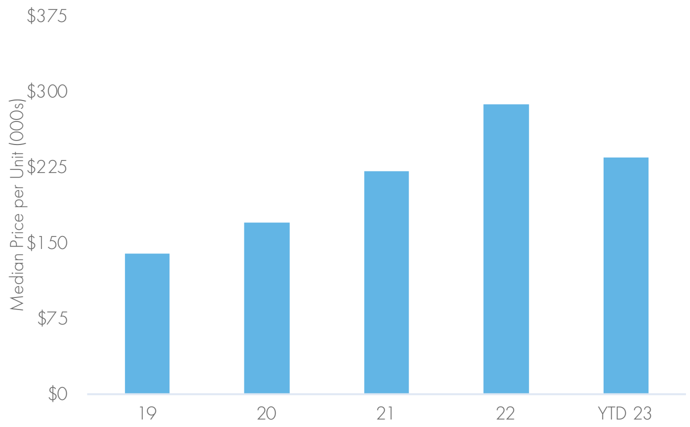
Sources: Northmarq, Apartment Insights

MULTIFAMILY SALES

- Sales velocity in the first quarter dropped approximately 50 percent from transaction levels recorded during the final three months of last year. Compared to one year earlier, transaction activity was down 74 percent in the first three months of 2023.
- Pricing reached approximately $233,700 per unit in the first quarter, down 19 percent from the median price in all of 2022. Prices began to retreat late last year; the median price during the fourth quarter was $242,400 per unit.
- Cap rates rose about 25 basis points during the first quarter, averaging 5.3 percent. In recent quarters, properties have generally changed hands with cap rates between 5 percent and 5.5 percent.

Pricing reached approximately $233,700 per unit in the first quarter.

INVESTMENT TRENDS



Sources: Northmarq, CoStar

RECENT TRANSACTIONS MULTIFAMILY SALES ACTIVITY

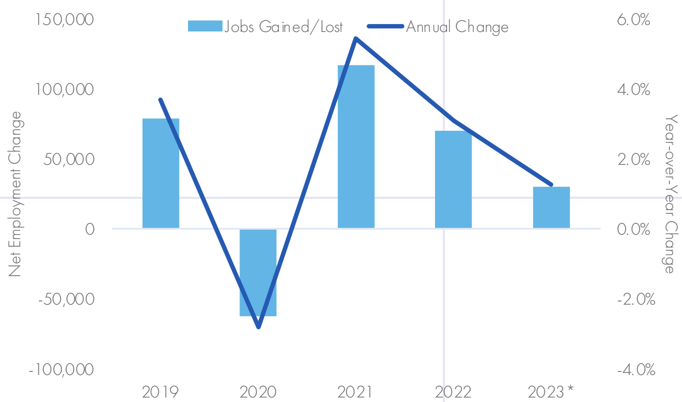
PROPERTY NAME	STREET ADDRESS	UNITS	SALES PRICE	PRICE/UNIT
Sweetwater at Metro North	2902 W Sweetwater Ave., Phoenix	520	$115,000,000	$221,154
Tempe Station	2323 E Apache Blvd., Tempe	400	$110,000,000	$275,000
Aventura	10350 W McDowell Rd., Avondale	408	$102,500,000	$251,225
Ironwood at Happy Valley	24025 23rd Ave., Phoenix	296	$90,280,000	$305,000
Pillar at Fountain Hills	16550 E Avenue of the Fountains, Fountain Hills	147	$68,300,000	$464,626

LOOKING AHEAD

The volume of new supply growth scheduled to be delivered in the Greater Phoenix multifamily market has garnered significant attention leading into 2023. This year will prove to be an active one for new construction with approximately 16,000 units scheduled to come online. While there will be supply-side pressures in place in the market in 2023, renter demand is off to a stronger start than was originally forecast. Demand is being supported by continued gains in the local labor market and in-migration from other generally more expensive regions. While renter demand is not expected to keep pace with new construction, operators of existing properties should record enough net absorption to keep rents near current levels, and potentially inch higher as newer, more expensive units come online. After reaching all-time lows, vacancy rates will likely end this year closer to the region's long-term average.

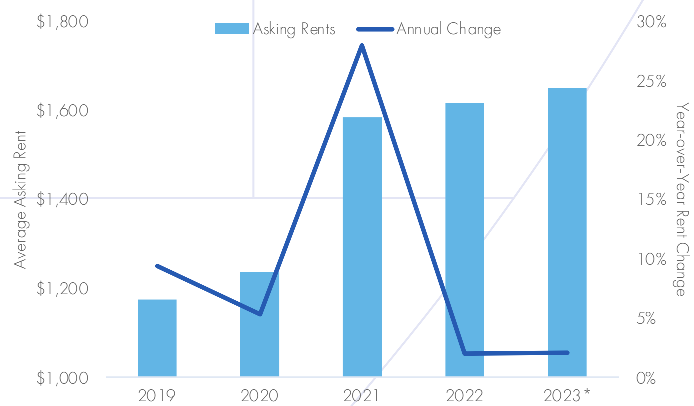
The investment market is expected to continue to record restrained sales velocity for at least another quarter or two, although with buyers and sellers closing the expectations gap, it is likely that the market has already reached its bottom for quarterly transaction activity. Cap rates have been pushing higher in recent quarters, a trend that was repeated in the first few months of this year. Eventually, cap rates will support investment activity. Looking to the near-term outlook, developers will continue to track lease-up rates and concession packages at new projects when determining the health of the leasing market. The greatest unknown impacting the investment market will likely be the operational strength of existing properties. If the local employment market remains strong enough to support additional renter household formation, investment conditions could outperform expectations.

EMPLOYMENT FORECAST



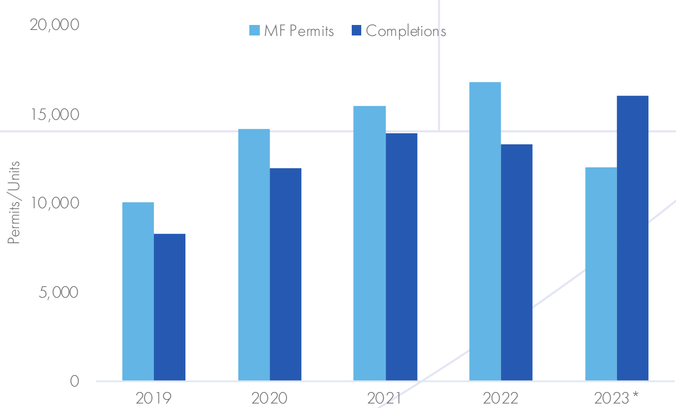
* Year End Forecast
Sources: Northmarq, Bureau of Labor Statistics

RENT FORECAST



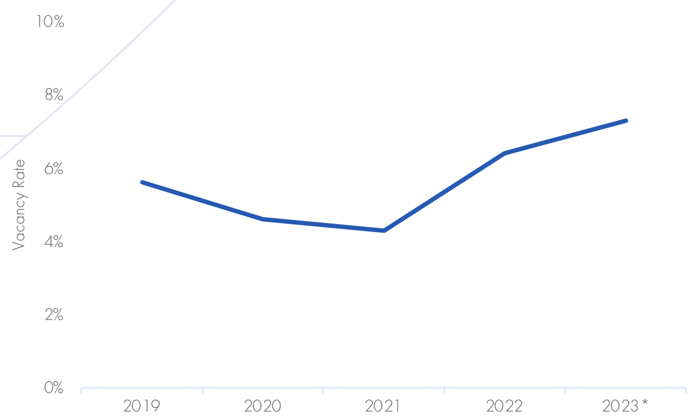
* Year End Forecast
Sources: Northmarq, Apartment Insights

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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