The Real State®
The Real State of the Phoenix Commercial Real Estate Market

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ENHANCING REAL ESTATE ASSETS

JANUARY 2022

Who's Investing in Phoenix Commercial Real Estate?

In recent years, Phoenix has transcended its past reputation as a boom-and-bust market. Domestic commercial real estate investors can leverage affordability and logistical advantages versus pricier U.S. markets, while companies with international portfolios can access diversification in a fast-growth region.

Not surprisingly, the industrial market has been the hotbed of activity for out-of-state and in-state investors. According to the *Phoenix Business Journal*, for example, Los Angeles-based Silver Creek Development and Phoenix-based Mutual Development Partners are currently building or planning a total of 3.3 million SF between dozens of buildings worth $560 million across the Phoenix metro. Contour, a privately held real estate development company in Costa Mesa, Calif., is working on a trio of projects in Buckeye and Mesa totaling about 3.6 million SF.

How active has foreign money been? For perspective, the *Phoenix Business Journal* noted that the $1.16 billion in foreign investment during the past three years is nearly equal to what was spent during the previous decade. Taiwan Semiconductor, of course, represents the largest foreign investment deal in the state's history. Notable deals have included Singapore-based Manulife's purchases of Allred Park Place in Chandler and Diablo Technology Park in Tempe for a total of $167.75 million, and the acquisition of Block 23 in downtown Phoenix by Canada-based City Office REIT, for $150 million.

Multifamily sales set volume records in 2021, in no small part due to out-of-state investment interest. Tides Equities and Decron Properties, both out of L.A., have been among the most active players in the market. Foreign investment predominately involves Canadian buyers, such as the Oxford Properties Group's $146 million acquisition of Ten01 on the Lake in Tempe last year.

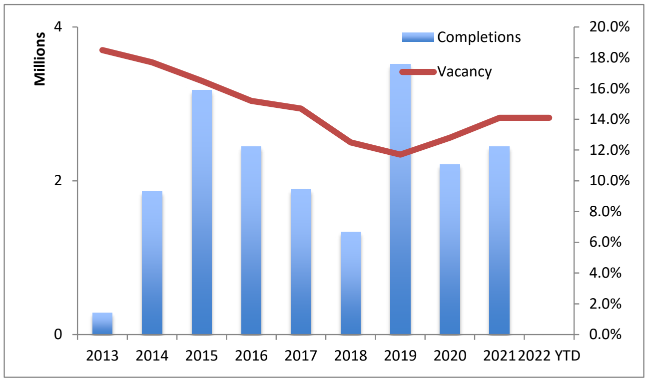
On a related note, the burgeoning build-to-rent market is also attracting out-of-state, as well as in-state, money. In Q4 2021, San Diego-based Logan Capital Advisors acquired NexMetro's Avilla Paseo single-family rental community in Deer Valley for $417,980/unit, while GTIS Partners LP, a New York real estate private equity fund manager and developer, recently purchased a Glendale site with plans to build 144 units. Local build-to-rent builders such as NexMetro, Walton Global, Empire and Christopher Todd are going strong, with over 5,000 units currently and more than 7,000 units underway.

In multifamily, part of the challenge for investors is strategizing where to deploy capital, with prices up and cap rates down. For multifamily property owners considering an exit point, this might be a good time to consider a 1031 exchange into a higher-yielding sector.

Looking forward, it appears the trend of local, national and international interest in the Valley will persist. In recent weeks, Montreal-based Xnrgy Climate Systems announced plans to build a 1 million SF U.S. headquarters and manufacturing facility in either Mesa or Chandler. Meyer Burger, a Swiss solar company, announced the selection of Arizona as the location for a new manufacturing facility, beating out Tennessee and Georgia.

Whether you are located in Arizona, out of state, or in another country, we welcome the opportunity to discuss the best available options for buying and selling commercial real estate investment properties. The team at R.O.I. Properties is ready to help you formulate a strategy for success that aligns perfectly with your business goals. Please contact us at: info@roiproperties.com or 602-319-1326.

Office



The removal of COVID-19 restrictions on Arizona businesses and a rise in vaccinations have encouraged employers to welcome employees back to the office, contributing to a perception the market is turning a corner. The feeling is welcome given that the pandemic disrupted Phoenix's consistently positive performance—but there is still a road to recovery.

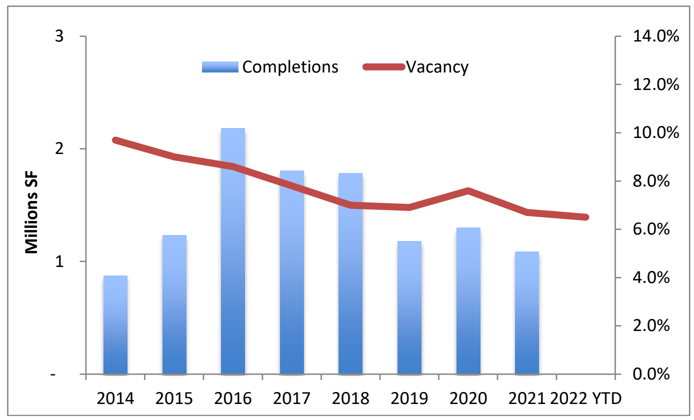
Real estate decision-makers have become more comfortable making long-term leasing decisions again, and quarterly leasing volume returned to near pre-pandemic activity in Q2 2021. Tenants who found their remote workers performed well during the pandemic will stay fully remote or shift to a hybrid work schedule. These tenants are relinquishing unused office space, and as a result, sublease availabilities have surged to a record high. The concurrent rise in leasing activity and sublease availabilities indicates there is no one-size-fits-all solution for operating post-pandemic. There is still a great degree of uncertainty about the long-term effect on office space use.

Retail

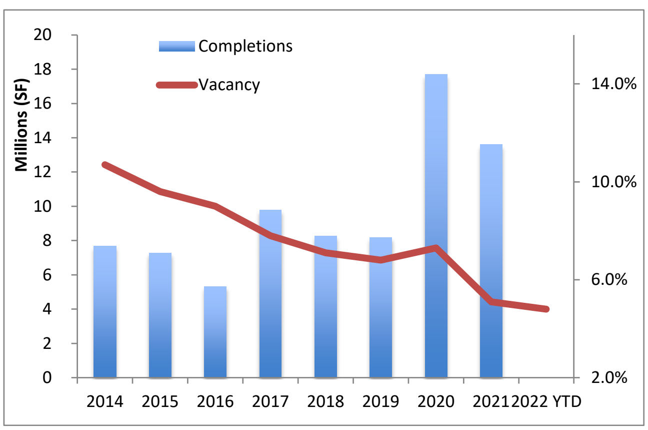
The improving economic and health situation has increased optimism in the local retail market. Leasing activity has accelerated, and new investors are searching for quality assets in Phoenix, wanting to capitalize on one of the top growth markets in the nation.

Despite the improvement, the market still has a road to recovery following the disruption of the pandemic. Phoenix has among the highest vacancy rates among large retail markets. Many retailers closed in the years before the pandemic, due to the evolving retail landscape. Post-COVID, retailers scattered across the market have left behind vacant space from 2,000-SF coffee shops to 20,000-SF gyms and 150,000-SF big box stores.

Still, retailers are penning new leases, especially as consumers feel more comfortable revisiting crowded shopping centers. Consumer demand has been uncharacteristically high for grocery, pharmacy, home improvement, drive-thru, and hobby stores.



Industrial



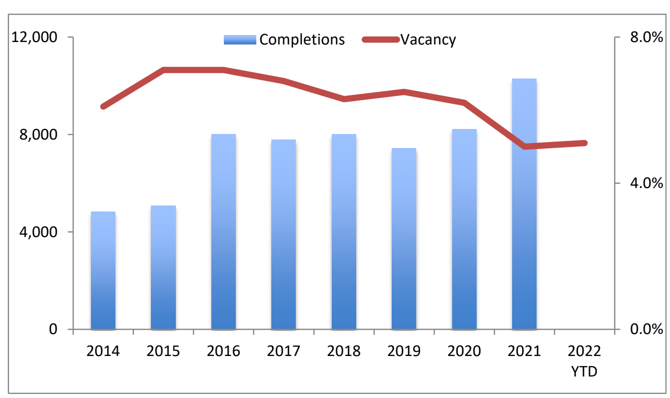
The last two years marked the best years on record in the Phoenix industrial market and there are no immediate signs of slowing. The Valley's rapidly growing consumer base and trends accelerated by the pandemic have bolstered the need for industrial space. The shift away from brick-and-mortar retail to online has generated increased demand for warehouse and distribution facilities.

Phoenix's strong demand drivers and competitive advantage remain in place. Approximately 35 million consumers can be reached within a single day's truck ride from metro Phoenix, fueling industrial space demand among companies in the e-commerce, logistics, and construction industries. Phoenix has also become one of the most active data center markets in the country due to Arizona's tax incentive for data center development, a robust and growing power grid, and the limited occurrence of natural disasters.

Multifamily

Apartment demand, rents, and supply have climbed to unprecedented levels in the Phoenix multifamily market. Before the coronavirus, fundamentals were solid and supported by some of the country's strongest employment and household growth that fueled demand and low levels of single-family inventory. The market's positive performance since the pandemic is bolstered by federal and state aid that has helped people pay the rent and eviction moratoriums that have kept renters in their apartments.

Net absorption climbed in the first three quarters of 2021 and outpaced new supply by a wide margin. But landlords will need to brace for a wave of deliveries over the next few quarters. The construction pipeline is robust and it's limited to top-tier rentals, whereas demand for affordable units has surged. The mismatch in supply and demand will likely push up Class A vacancies in the near term while also feeding affordability concerns in the market.



Residential Snapshot

From December to January, the supply-demand index rose from 392.5 to 464.1, remaining strongly in seller's market range. The market could change quickly if inventory were to increase suddenly or if enough people get spooked by the market dynamics. In an environment of rising interest rates, R.O.I. Properties believes we will see even higher initial demand, which would cause affordability issues for buyers who are most sensitive to interest rate increases. Subsequently, we would expect the market to slow down, with pricing softening a bit, if more inventory hits. Over the past year, the rise in sales prices plus interest rate increases has created a 40% annual increase in the estimated payment for a buyer purchasing a median-size home.

- Affordability is at the forefront of concerns going into 2022, with the main pressure point being supply.
- Total new listings, plus those coming soon, in the month of January equal 6,075 as of the 25th. This is down 8% from this week last year (which was a record low) and down from the pre-pandemic years of 2018 (-24%) and 2019 (-27%).
- Accepted contracts, while down 4% from last year, are still higher than the pre-pandemic years of 2018 (+4%) and 2019 (+22%).
- One indicator of affordability is the market share of affidavits of value recorded as owner-occupant (as opposed to landlord or second home) in public record. From 2015 through the first part of 2021, the market share of owner-occupants ranged between 70-76%. However, from Q1 to Q4 of 2021, that percentage dropped from 71% to 63%. Market share of sales to landlords increased from 14% to 18% and second homes went from 13% to 14%. Acquisitions from iBuyers such as OpenDoor and Zillow declined from 6% to 4%.
- Even as interest rates and payments rise, prices in Greater Phoenix have been rising faster. January's median sale price is up 2.4% over December's median, after rising an average of 1.1% per month in the last half of 2021.

CONSUMER CONFIDENCE

*Shaded areas represent periods of recession.
Sources: The Conference Board; NBER

PRESENT SITUATION

- Consumers' appraisal of current business conditions was more favorable in December.
- 19.9% of consumers said business conditions were "good," up from 17.9%.
- 26.8% of consumers said business conditions were "bad," down from 27.3%.
- Consumers' assessment of the labor market was moderately less favorable.
- 55.1% of consumers said jobs were "plentiful," down from 55.5%; still a historically strong reading.
- 12.5% of consumers said jobs are "hard to get," up from 10.8%.

INDUSTRY EMPLOYMENT AND WAGES

NONFARM EMPLOYMENT
November 2021 - Seasonally Adjusted

2,998,000
Total Nonfarm Employment

Year-over-Year Change
135,800 Numeric | +4.7% Percentage

Employment Details ›

EMPLOYMENT BY SECTOR
November 2021 - Seasonally Adjusted

Total Nonfarm Payroll Em

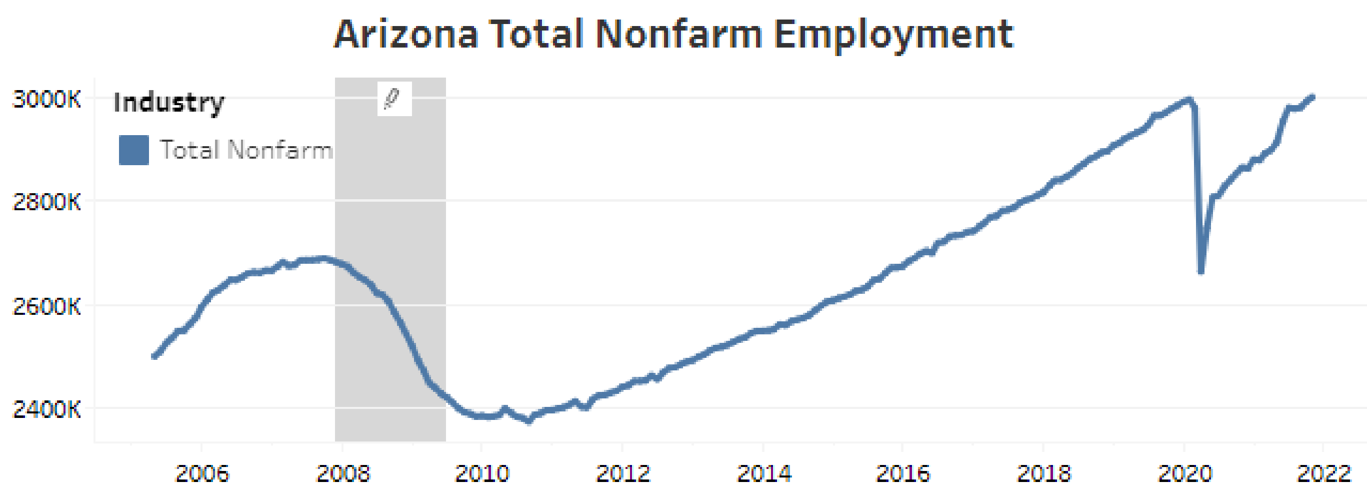
2,998,000
Employment Level

Year-over-Year Change
135,800 Numeric | +4.7% Percentage

ANNUAL AVERAGE WEEKLY WAGES IN ARIZONA (2020)

$1,124 Total, All Industries

Industry Category	Weekly Wage
Goods-producing	$1,367
Natural resources and mining	$1,063
Construction	$1,211
Manufacturing	$1,584
Service-providing	$1,084
Trade, transportation, and utilities	$1,008



Source: https://www.azcommerce.com/oeo/labor-market/industry-employment/

Articles of Interest

Phoenix Business Journal – Jan. 14
Commercial Real Estate: Projects to Watch in 2022

Phoenix Business Journal – Jan. 20
Foreign investors bought $1.2B in Valley office properties in last 3 years

AZ Big Media – Jan. 27
Phoenix industrial market sets all-time records in 2021

Phoenix Business Journal – Jan. 28
Dozens of new hotel projects are in the pipeline for Phoenix metro

Globe St. – Jan. 28
This Will Be an 'Exceptionally' Active Investment Year for Multifamily