JANUARY 2021

TREND report

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The Finance Issue

Making Moves to Elevate the Innovation Ecosystem:

Startup Tucson Launches New Initiative to Attract Remote Workers

Dedicated to transforming the region's economy through innovation and entrepreneurship, the non-profit Startup Tucson has been busy supporting our Tucson area entrepreneurs and small businesses and creating new opportunities for future residents over the last few months. Their four-person team has been working during the pandemic to equip founders with the tools they need to more successfully start, scale or pivot their businesses using a multi-pronged strategy to address today's seismic shifts. Through various partnerships and funding support from the City of Tucson and the Thomas R. Brown Family Foundation, Startup Tucson can provide low and free cost programming to all types of entrepreneurs in our community and support the ever-increasing needs of small businesses and microventures. This is more important than ever as our city looks to recover post- COVID.

In addition to the day-to-day hands-on support of entrepreneurs through trainings and mentorship, Startup Tucson also looks to national trends for new ways to inspire regional economic development. One such initiative, inspired by various other cities around the country, is their recently launched Remote Tucson initiative. Remote Tucson is a coordinated community initiative to entice talented individuals who are currently employed in high-paying remote work positions to permanently relocate to Tucson while continuing to work remotely for those same employers, therefore stimulating our local economy. Through a comprehensive platform, remote workers are encouraged to discover the attractiveness of Tucson as a new home.

The program's long-term goals relate specifically to talent attraction and the greater economic development of Tucson. "Unlike traditional talent attraction, for this program, workers will stay employed in their current positions, allowing them to continue to have pull in outside markets and maximizing their lifetime economic impact in Tucson. They won't only be funneling outside dollars into our economy, but by not replacing current opportunities for local residents, these new residents result in net positive growth for Tucson," said Liz Pocock. Built into the framework of the program is to thoughtfully accept professionals with strong reasons for staying long term in Tucson and with a desire to connect with Tucsonans through mentorship and community involvement. During the program pilot, each remote worker selected will receive over $7,500 in incentives made of a combination of direct funds to help with relocation expenses and other perks and benefits. In the first round, funding and collaboration support will allow for 10 total offers to be made. Financial sponsors of the program include the City of Tucson, Marshall Foundation, MainGate Square, TEP, Pima County, and Bourn Companies.

continued on page 2

CONTENTS

JANUARY 2021

The Finance Issue

1–2 .... Cover Story
3 .... Development Financing in 2020
4–6 .... Top Commercial Sales
7 .... Top Residential Sales
8–9 .... Property Tax Considerations
10 .... Paycheck Protection Program
11–15 .... Market Place
16–17 .... Trillions Now
17 ..... New Pima County Assessor
18 .... An Active Year for Real Estate Finance
19 .... Property Management
20–21 .... Arizona's Recovery Continues
22–23 .... Commercial Property Financing Update
23 .... Construction Pricing
24 .... Looking Forward
25 .... Multifamily Sector Market Outlook
26 .... Editor's Insights

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MAKING MOVES TO ELEVATE THE INNOVATION ECOSYSTEM

» by Sophia Gonzalez

Program benefits are designed specifically to ease in the applicant's relocation experience and make sure they are connected into the Tucson community as quickly as possible. These include:

- $1500 in moving expenses
- A year of free GIG home internet provided by COX
- Housing support provided by SouthwestUrban and partner career support provided by the Talent Store
- Over three-months of complementary coworking at La Suprema, Common Workplace, Brings Coworking and the Post
- Hotel nights at the soon to be completed Hampton Inn/Home 2 Suites
- Welcome benefits including a local gift basket, curated night out, and Visit Tucson attractions passport
- Community memberships within TYP and an art or cultural organization of the applicant's choice

In addition to these perks and benefits, all selected applicants will be paired with a member of the program's Welcome Committee, led by Tucson Young Professionals, to help them plan for their relocation and arrival in Tucson. "We look forward to helping to welcome the talented and energetic people who choose to relocate permanently to Tucson and that want to contribute to our community and our culture," said Zach Yentzer, Executive Director of TYP. Promotional partners include Visit Tucson, Tucson Metro Chamber, Sun Corridor, Rio Nuevo, Local First Arizona, University Arizona Alumni Association, SAHBA and Tucson Association of Realtors.

Applications for the initial round of the program opened in early-November and were closed in December due to overwhelming initial interest. In the month, the pilot application was live, the Remote Tucson website saw 4,000 visitors and received over 500 applications from 39 states across the country. The average salaries of applicants were $128k and they originated from a wide variety of industries including tech, nonprofits, health care, and higher education and from some very familiar employers including Facebook, Teach for America, Pfizer, Amazon and many others. Applicants cited cost of living, quality of life and an existing connection to Tucson as some of the reasons they were considering a move supported by the program. Also of note was that about 60% of all applicants identified as "boomerangs"—individuals that lived in Tucson previously either growing up or attended college here. This indicates that as times have changed with COVID, prior members of our community are looking to return and contribute to Tucson's growth.

"Also of note was that about 60% of all applicants identified as "boomerangs"—individuals that lived in Tucson previously either growing up or attended college here. This indicates that as times have changed with COVID, prior members of our community are looking to return and contribute to Tucson's growth."

The Startup Tucson team, along with a committee of community partners, will select 10 individuals from this application pool to extend offers to in early 2021. Once they accept, the individuals must relocate to Tucson within six months for a minimum of a year. Once the pilot program is completed, Startup Tucson will look to start a second round in 2021 to continue to attract these talented individuals to our community. If interested in supporting the Remote Tucson program or joining Startup Tucson as a mentor or entrepreneurs, visit the Startup Tucson website at www.startuptucson.com.

Sophia Gonzalez is the Engagement Coordinator for Startup Tucson and oversees the hospitality and functionality of online programming and the Roy Place Business Innovation Hub. With an urban development and experiential education lens and with a background in food festivals, cultivation, and ecosystem, she is energized to enter the entrepreneurial ecosystem to make, facilitate, and encourage connections across Tucson, the region, and beyond. Innovation and creativity are already taking place here and she is eager to affirm and draw out the good work and actors committed to making Tucson an exciting place to grow. She can be reached at sophia@startuptucson.com.

» by Caroline Janjić

In March of 2020, when news of the pandemic began to break, commercial real estate lenders were quick to put the brakes on making new loans, particularly in the development financing space. Across nearly all asset classes, real estate development financing dried up overnight.

Development financing requires lenders take a leap of faith. They must look into the future alongside the developer, making assumptions about what can be expected years ahead when a project is built and begins to generate revenue. Though lenders are getting more and more sophisticated at allowing data to drive their decisions, no one had the data required to predict exactly what would follow 2020's coronavirus outbreak.

While some lenders proudly honored loans that had already passed committee, loans that were still in review when the pandemic began to unfold were, at best, significantly delayed. Lenders took a wait and see approach and their return to lending over the course of 2020 has followed the seismic shifts we're seeing in how people live, work, work-out, entertain, shop and learn.

Before considering making new loans, many lenders had to turn their attention to preserving their existing portfolio of loans. Tenants across a variety of asset classes began to request rent forbearance and deferrals from landlords. Congress put in place and recently extended a moratorium on evictions of rental housing tenants struggling to make payments due to COVID-19 related hardship. In some jurisdictions, such moratoriums on tenant evictions were temporarily extended beyond multi-family. In many cases government officials recommended, but did not required, that lenders also extend flexibility to landlords.

In what initially seemed like a lose/lose situation, over the course of the year it became clear that there were some asset classes that were less impacted by the pandemic and some were even positioned to benefit from extraordinary shifts in consumer behavior that would follow. More than just varying from asset class to asset class, the impact of the pandemic has also varied from city to city. As more and more people work remotely, the location in which they live matters less. Workers' willingness to tolerate exorbitant rent goes down. Primary markets begin to lose residents to secondary and tertiary markets.

High density urban assets across multifamily, office, hospitality and retail were hit the hardest as the buzz and synergy of urban life became a thing to fear and residents, office workers, tourists and shoppers began to seek refuge in lower density areas. Student housing suffered as universities turned to remote learning. Senior housing suffered as families opted to care for loved ones at home.

As people moved away from living and working in high density areas, they moved to lower density suburban environments. An incredible acceleration in the adoption of online shopping has led to opportunity in the industrial space, grocery stores, and grocery anchored retail centers, that serve as last-mile distribution centers.

At Iridius Capital, our primary focus in the development space is in the single-family build to rent asset class. We partner with NexMetro Communities to bring Avilla Homes communities to market in Arizona, Texas, Colorado and Florida. The concept offers residents the privacy, security and high-quality interiors of a single-family lifestyle but without the commitment of a mortgage. The low-density nature of the product positions tenants to socially distance from their neighbors and with a mix of 1, 2 and 3 bedroom homes, residents have the space inside their homes that they require as they move to do more from home.

After seeing a complete shutdown of new development financing in the spring, lenders slowly came back to the table in early fall to provide development financing for those asset classes least impacted. Single family build to rent communities have been widely recognized as one of the commercial real estate asset classes best positioned to thrive through and after the pandemic. Rent collection, occupancy and leasing activity remain at or above pre-pandemic levels across our Avilla Homes portfolio.

As capital markets began to reopen, even those borrowers seeking development financing for projects in the least impacted asset classes faced longer closing timelines, stricter underwriting requirements and more stringent loan covenants. No matter how well projects are penciling, lenders are looking to only extend development financing to the most experienced development groups. We expect these conditions to continue well into 2021.

The reduced availability of development financing will constrain new supply. Those development companies already in the lead in their asset classes will be positioned to get further in front of the competition. We're excited to be in the position of having a full pipeline of projects moving forward.

We anticipate that all asset classes will have to wait for the vaccine to be rolled out and life to begin to return to normal before development financing truly becomes available at pre-pandemic levels. Lenders will be watching closely to see which shifts in consumer behavior are temporary and which will outlast the virus. How many people will go back to the office full time? When will business travel resume? How important is it to be in the classroom? The answers to these questions will pave the way to the future of real estate development financing.

Caroline Janjić is Chief Operating Officer at Iridius Capital. Iridius Capital is a real estate company that partners with industry leaders to acquire and develop best in class real estate assets. Together with their partners, Iridius has acquired or developed over $1.5B of commercial real estate, including multifamily, retail, hotel and office assets. Caroline can be reached via email at caroline@iridiuscapital.com.

big deals

Tower 16 Joint Venture Buys Sierra Vista Apartments for $18 Million

Encinitas, CA based Tower 16 Capital Partners and NY based Drake Real Estate Partners paid $18,100,000 for the Sierra Vista Apartments, located at 3535 N 1st Ave. The seller was Sierra Vista Apartments LLC. Built in 1976, the 258 unit property included one, two and three bedroom units. The buyers will make about $4 million in renovations at the property. This was an off-market transaction. The firm intends to build a portfolio of more than 1,000 units in the Tucson market. The property previously sold in 2007 for $10,350,000. 11/25/2020

Buyer: Tower 16 Capital Partners; NorthMarq Capital; Jesse Hudson, Bill Hahn, Trevor Koskovich

Seller: Sierra Vista Apartments LLC; NorthMarq Capital; Jesse Hudson, Bill Hahn, Trevor Koskovich

Sale: $18,100,000; $70,155/unit

Size: 258 units

California Investors Buy Central Walgreen's for $7.4 Million

Santa Clarita, CA based LOGIT LLC and SILMIT LLC (Luciano Forcella, Manager) paid $7,396,226 for the 15,608 SF Walgreens - Cornerstone Plaza, located at 4685 E Grant Rd. The seller was Walgreen Louisiana Co. Inc, through its affiliate DS Tucson AZ Landlord LLC. This Walgreen's was built in 1997. 11/18/20

Buyer: LOGIT LLC and SILMIT LLC; Marcus & Millichap Inc, John Glass

Seller: DS Tucson AZ Landlord LLC; Marcus & Millichap Inc, John Glass

Sale: $7,396,226

Size: 15,608 SF

KB Home Buys Gladden Farms Lots for $4.6 Million

KB Home, Tucson Division (Andrew Gasparro, Director) paid $4,600,000 ($50,000 per finished lot) for 92 lots (40'X120') in the eastern half of Block 27 of Gladden Farms. The lots were purchased from Gladden Phase II, LLC (Crown West Land Group, Dean Wingert, Vice President). This closing represents the final portion of a phase of 405 lots that have been sold and commenced construction in the past four months at Gladden Farms. 11/9/20

Buyer: KB Home, Andrew Gasparro

Seller: Gladden Phase II, LLC; Land Advisors Organization; Will White and John Carroll

Sale: $4,600,000; $50,000/lot

Size: 92 lots

Tucson Investors Buy Portion of Entrada del Oro Shopping Center for $4.2 Million

Oracle and Magee LLC, an affiliate of Town West Realty (Toby Horvath, Manager) paid $4,200,000 for a portion of the Entrada del Oro shopping center at Oracle and Magee including approximately 14,336 square feet of building improvements located at 7861 and 7871 North Oracle Road The seller was The Wright-Pantano LLC (Bruce Wright, Manager). The property was fully leased and occupied by O'Reilly Auto Parts and a Sleep Solutions Outlet. 11/18/20

Buyer: Oracle and Magee LLC

Seller: The Wright-Pantano LLC; VOLK Company agents Rick Borane and Terry Dahlstrom

Sale: $4,200,000; $293/SF

Size: 14,336 SF

Oregon Investor Buys Oracle Canyon Apartments for $4 Million

Beaverton, OR based Oracle Canyon LLC (Kenneth Schnerch, Manager) paid $4,050,000 for the Oracle Canyon Apartments, located at 331 W Pastime Rd. The seller was Tsearch LLC (Serge Shukhat, Member). Built in 1983, the property consisted of 36 units, all two-bedroom/two-bathroom floor plans. 11/17/20

Buyer: Oracle Canyon LLC

Seller: Tsearch LLC; Marcus & Millichap, Hamid Panahi and James Crawley

Sale: $4,050,000; $112,500/unit

Size: 36 units

Larsen Baker Buys Foothills Office Buildings for $3.55 Million

Tucson based Larsen Baker, through its affiliate Skyline Encantada Investors, LLC, (Melissa Lal, Manager) has acquired the 11,840 SF office buildings at the northwest corner of Skyline Drive and Campbell Avenue formerly occupied by Bank of America. The sellers were Arizona Bank and Bank of America. Larsen Baker will redevelop the 1980's era buildings into new high-end office space. The project will be renamed skyCAM. The property redesign, renaming and rebranding will be completed in conjunction with the architectural design firm Repp + McLain. 11/25/20

Buyer: Larsen Baker, Melissa Lal

Seller: Arizona Bank C/O Bank of America

Sale: $3,550,000; $299.83/SF

Size: 11,840 SF

Tucson Investor Buys Vail Self Storage Facility for $3.2 Million

Tucson based Vault at Old Vail Road LLC (Dennis Winans, Manager) paid $3,200,000 for the 330 unit America's Best Storage self storage facility located at 7475 E Old Vail Rd. The seller was America's Best Self Storage LLC, (Scott Sturm, Member). The property features a mix of standard, drive-up units and covered and uncovered RV parking. It features small, medium and large self-storage units ranging from 25 SF to 720 SF. 11/13/20

Buyer: Vault at Old Vail Road LLC; NAI Horizon, Denise Nunez

Seller: America's Best Self Storage Llc

Sale: $3,200,000

Size: 330 units

Beverly Hills Investor Buys Southside Palomino Mobile Home Park for $1.3 Million

Beverly Hills based investor Beverly Crest Estates LLC (Allen Yadgari, Manager) paid $1,300,000 for the Palomino MHP located at 3535 East Alvord Road. The seller was Jesse Amezquita. Built in 1962, Palomino MHP has 61 spaces and was 51% occupied at the time of sale. 11/2/20

Buyer: Beverly Crest Estates LLC; Marcus & Millichap, Michael Escobedo

Seller: Jesse Amezquita

Sale: $1,300,000; $21,311/space

Size: 61 spaces

San Francisco Investor Group Buys Eastside Circle K Convenience Store for $1.17 Million

San Francisco based Skyline Pacific Properties, through its affiliate Skyline Principle Investors II, LLC (Richard C. Ronald, Manager) paid $1,167,000 for the Circle K Gas Station/Convenience Store located at 8702 E Speedway Blvd. The seller was Steven & Ellen Aaronson Family Trust. Built in 1986, the retail building was 2,816 SF. The property previously sold in September 2004 for $840,000. 11/2/20

Buyer: Skyline Pacific Properties (415) 616-5140

Seller: Steven & Ellen Aaronson Family Trust

Sale: $1,167,000; $414.42/SF

Size: 2,816 SF

Beverly Hills Investor Buys Southside Open Sky Mobile Home Park for $1.1 Million

Beverly Hills based investor Beverly Crest Estates LLC (Allen Yadgari, Manager) paid $1,100,000 for the Open Sky MHP located at 3626 East Drexel Road. The seller was Jesse Amezquita. Built in 1972, Open Sky MHP has 43 spaces and was 75% occupied at the time of sale. 11/2/20

Buyer: Beverly Crest Estates LLC; Marcus & Millichap, Michael Escobedo

Seller: Jesse Amezquita

Sale: $1,100,000; $25,581/space

Size: 43 spaces

big deals

Tucson Investor Buys Industrial Building for $975,000

Tucson investor Shamrock 4875, LLC (Chad Berg, Manager) paid $975,000 for the 10,140 SF R & D Building located at 4875 N Shamrock Pl. The seller was Shamrock 3 LLC (John G & Gretchen S Ochoa). Built in 2001, the building sits on an acre lot. 11/24/2020

Buyer: Shamrock 4875 LLC, Chad Berg

Seller: Shamrock 3 LLC

Sale:
$975,000

Size:
10,140 SF

Local Investor Buys Downtown Industrial Property for $950,000

Tucson investor Dennis Arnold paid $950,000 for the 14,968 SF industrial building located at 860 E 19th St. The seller was Fourteenth Street, LLC (Linda Douglas, Manager). Built in 1970, the building sits on 1.3 acres. The property was vacant at the time of the sale. The property previously sold in April 2006 for $507,500. 11/18/2020

Buyer: Dennis Arnold

Seller: Fourteenth Street, LLC; Alpha Commercial Real Estate Service LLC, Pat Welchert

Sale:
$950,000

Size:
14,968 SF

Colorado Investor Buys Industrial Park Lots for $950,000

Monument, Colorado based Sepp and Affiliates, LLC (Eric Sepp, Managing Member) paid $950,000 for the 27.4 acre industrial parcel at Littletown and Wilmot Industrial Park. The Seller was Russo, Russo & Slania (Steve Russo, Partner). The parcel was platted into 24 one-acre industrial lots plus common areas. Sepp intends to offer developed industrial lots, build and lease to suit user properties to industrial and manufacturing users. The property was previously purchased in 2006 for $500,000. 11/10/20

Buyer: Sepp and Affiliates, LLC; Blake Allen Realty, Blake Allen (719) 684-4123

Seller: Russo, Russo & Slania; Arizona First Properties, LLC, Tom DeSollar (520) 400-2732

Sale:
$950,000;
$34,671/AC

Size:
27.4 AC

Nogales, AZ Investor Buys Rio Rico Industrial Land for $940,000

Nogales, AZ based Mesquital Holding Co., LLC (Xavier Fisher, Manager) paid $940,000 for 53.18 acres of ranch land located at the northwest corner of the Interstate 19 W. Frontage Rd. and Camino del Rey David in Rio Rico, AZ. The proposed industrial site was purchased from M&M Pena Blanca, LLC.

Buyer: Mesquital Holding Co., LLC; Xavier Fisher

Seller: M&M Pena Blanca, LLC; Cushman & Wakefield | PICOR, Jose Dabdoub

Sale:
$940,000;
$17,675/AC

Size:
53.18 AC

Year	Month	Active Listings	Units Sold	New Listings	Months Supply	Median Sales Price	Avg. DOM
2019	November	2,288	1,144	1,390	2.0	$232,000	34
	December	2,359	1,221	964	1.9	$241,500	37
2020	January	1,713	1,008	1,851	1.7	$235,250	38
	February	1,868	1,168	1,595	1.6	$245,000	42
	March	2,518	1,399	1,849	1.8	$248,250	36
	April	2,282	1,168	1,329	2.0	$249,000	30
	May	1,737	1,158	1,487	1.5	$240,700	30
	June	1,742	1,452	1,446	1.2	$250,538	36
	July	1,739	1,581	1,578	1.1	$257,500	34
	August	1,329	1,329	1,621	1.0	$261,590	29
	September	1,362	1,362	1,728	1.0	$267,485	24
	October	1,734	1,571	1,853	1.1	$270,000	20
	November	1,383	1,277	1,284	1.1	$277,500	20
	1 mo. change	-20%	-19%	-31%	-2%	3%	0%
	1 yr. change	-40%	12%	-8%	-46%	20%	-41%

Tucson Resale Activity Summary

Source: TARMLS

Year	Month	Active Listings	Units Sold	Months' Supply	Median Sales Price	Avg. DOM	Avg. CDOM
2019	November	152	4	38	$1,057,750	58	58
	December	159	13	12	$1,460,875	126	188
2020	January	179	11	16	$1,300,000	78	94
	February	138	8	17	$1,167,500	90	90
	March	135	13	10	$1,130,000	172	287
	April	121	6	20	$1,530,000	83	116
	May	122	7	17	$1,200,000	71	112
	June	113	15	8	$1,235,000	70	206
	July	109	16	7	$1,285,000	129	233
	August	119	25	5	$1,375,000	87	136
	September	132	19	7	$1,276,000	49	78
	October	138	17	8	$1,499,000	66	151
	November	117	18	7	$1,186,082	70	147
	1 mo. change	-15%	6%	-20%	-21%	6%	-3%
	1 yr. change	-23%	350%	-83%	12%	21%	153%

Tucson Luxury Market Activity Summary

Source: TARMLS $1+ million Sales

big deals

Colonia Del Sol Home Sells for $1,595,000

Built in 1998, this 5,265 SF Contemporary style home is located on 1.62 acres in Colonia Del Sol. Originally listed in October 2020 for $1,595,000, this home was on the MLS for a total of 3 days under one listing. Under this listing, this home sold for 100% of its listing price after 3 days on the market. 11/20/20

Listing Agent: Peter Deluca, Long Realty Company

Selling Agent: Marta Harvey, Russ Lyon Sotheby's Int Realty

Sale:
$1,595,000

Address:
5285 N Corte
Puesta Del Sol
Tucson, AZ 85718

Canyon Pass at Dove Mountain Home Sells for $1,550,000

Built in 2007, this 6,026 SF Mediterranean style home is located on 1.7 acres in Canyon Pass III at Dove Mountain. Originally listed in November 2018 for $1,995,000, this home was on the MLS for a total of 685 days under two listings. Under this listing, this home sold for 86% of its listing price after 311 days on the market. 11/13/20

Listing Agent: Lisa M Bayless, Long Realty Company

Selling Agent: Peter Deluca, Long Realty Company

Sale:
$1,550,000

Address:
3818 W Cayton
Mountain Drive
Marana, AZ 85658

Catalina Foothills Estates No. 10 Home Sells for $1,500,000

Built in 2002, this 4,556 SF Spanish Mission style home is located on 1.5 acres in Catalina Foothills Estates No. 10. Originally listed in Octobe 2020 for $1,450,000, this home was on the MLS for a total of 3 days under one listing. Under this listing, this home sold for 103% of its listing price after 3 days on the market. 11/30/20

Listing Agent: Denice Osbourne, Long Realty Company

Selling Agent: Timothy Looney, Realty Executives Arizona Territory

Sale:
$1,500,000

Address:
4681 N Camino Sumo
Tucson, AZ 85718

Alta Vista Village Home Sells for $1,300,000

Built in 2020, this 4,408 SF Contemporary style home is located on .6 acres in Alta Vista Village. Originally listed in May 2020 for $1,395,000, this home was on the MLS for a total of 75 days under two listings. Under this listing, this home sold for 95% of its listing price after 0 days on the market. 11/19/20

Listing Agent: Robin Sue Kaiserman, Long Realty Company

Selling Agent: Robin Sue Kaiserman, Long Realty Company

Sale:
$1,300,000

Address:
16260 N Paseo Valdear
Tucson, AZ 85750

Pima Canyon Estates Home Sells for $1,295,000

Built in 2001, this 3,224 SF Contemporary style home is located on 1.23 acres in Pima Canyon Estates. Originally listed in October 2020 for $1,295,000, this home was on the MLS for a total of 6 days under one listing. Under this listing, this home sold for 100% of its listing price after 6 days on the market. 11/9/20

Listing Agent: Robin Sue Kaiserman, Long Realty Company

Selling Agent: Paula Williams, Long Realty Company

Sale:
$1,295,000

Address:
1308 E Desert
Garden Drive
Tucson, AZ 85718

After over 15 years of practicing law in the U.S., in the years since Proposition 117 implementation in 2014 changing the Arizona property tax regime, explaining property tax is akin to describing some kind of hybridized Dr. Who and Star Trek mini-series plotline.

Nothing is quite as it appears. More than ever, a strategic, multi-year plan coupled with an understanding of available legal and policy avenues is necessary. It is not a simple matter of arguing "comps" and costs and submitting competing appraisal positions.

This year, navigating the valuation landscape was further complicated by the economic disruption of the COVID-19 pandemic. National and Arizona economic indicators are in flux. Almost daily I am asked how property values and property taxes should be estimated in this 'new norm'. How should one adjust for tenant deferred rents or closures in commercial marketplaces, higher unemployment rates, inflationary concerns and increased U.S. debt. Answer—each case should be evaluated on its own merits.

Bottom line—Be Proactive and Strategic

Attorneys, business owners, clients, developers, investors, insurance executives and lenders ask me how The Bain Law Firm PLLC obtains a desired outcome—reduction of valuations, limitation on tax exposure or impact results that increase NOI—when other representatives have not. For property tax clients, our focus is on the strategic reduction of tax exposure and the resulting increase of a project or property's NOI. This occurs during the project planning stage, through construction phases and continues for years after an asset is in service.

In the COVID-19 "new norm," plan for short term interruptions, strategize for the long game, know your exit strategy options (yes, plural), and factor in your (and your pro forma's) resilience and tolerance for risk.

Property tax and related matters, while fluctuating, are costs that can often be managed. Sometimes it may take 2–3 years to achieve significant desired valuation outcomes without litigation. However, be prepared to consider litigation options. Understanding property valuation, tax and related legal considerations and pitfalls is key.

Meanwhile, with the staff turnover in virtually every county assessing office over the last five years, sophisticated firsthand knowledge of the actual statutory options is more important than ever. Below are two commercial scenarios I handled in the last year. The underlying situations have since reoccurred and I share them with you as a cautionary tale.

Hypothetical #1: One Property=Two Contemporaneous Considerations

A. **National Client—Notice of Value:** Client receives an Arizona 2021 tax year valuation notice of $112,000,000 full cash value (FCV) at 75% construction completion for a mixed-use property. National client contacts our office asking if there are paths to successfully obtain valuation reduction based on available legal statutory and local practices.
B. **Same National Client—Parcel Split and Recombination:** Client representatives simultaneously ask how to "sell off" separate project uses. This means the creation of a horizontal parcel regime via parcel split and recombination that almost always triggers a Rule B. [1]

Discussion & Considerations

Estimated real property taxes for a $112,000,000 noticed FCV with a "Rule B" application is approximately $1.414M for the 2021 tax year. Client reports this new property is expected to have phased use "openings" under temporary Certificates of Occupancy beginning August 2020, with projected stabilization in 2022 or 2023.

A. Options to reduce property tax valuation

- *Be Proactive—Key considerations:* client project critical date path, cost of construction, phasing of putting the asset into service, income and expense (actual, proforma, stabilized), equity amongst similar properties similarly situated, statutory options and market sales approaches.
- *Be Strategic—Know the client project and state law:* Constitutional constraints and opportunities, statutory requirements and local policy options are factored in. Hands on, proven legal knowledge and experience of how to prepare, submit and argue an appeal on the record with reservation of rights is crucial. Substantive property tax appeal representation is grounded on the understanding and planning for a potential Tax Court filing.
- *Firm Results—Successful valuation reduction:* One year estimated tax savings of $870,980. Taxable value reduced to $30.3M. Hearing was completed in about an hour and included a focused 100 + page work up that incorporated significant, admissible, primary source materials. This included properly presented Contract Documents, (AIA) contract budget materials, client declarations and certified conformance correspondence.

B. Parcel Split and Recombination

- *Know the client purpose and desired outcome:* What is the client trying to accomplish? Is there a bank covenant breach, a lock rate expiring on a new loan product, litigation requirement or divestiture of a partner, etc.? Check in with the project director, property manager or in-house attorney to understand unintended consequences to the critical date path and project estimates.
- *Firm Advice—Advised client to "hold" and consider other tax implications.* When the client provided information was reviewed, I discovered that a parcel recombination to a horizontal regime would trigger other significant project tax implication over $1M. I brought this to the attention of the project C suite who contacted the TPT and Speculative Builder Tax construction folks. Had a property tax representative not understood the bigger picture, a parcel recombination would have been pushed through without consideration of other consequences that could not be unwound. Know when to "stand down" and wait.
- *Bottom line:* a general understanding of value approaches and traditional appraisal techniques is often not enough. Current, sophisticated life-cycle experience that fosters real understanding of the intended (and avoidance of unintended) consequences of a property tax appeal filing or advisory representation is key. This means think outside the box; again be proactive and strategic.

Hypothetical #2: Church/Religious Worship Properties—Owned vs. Leased

A 50,000-square foot commercial strip center. 2021 tax year FCV $6,600,000 with Limited Property Value (LPV) $2,780,000.

Hypothetical real estate taxes approx. $72,875 or $1.46/sf.

What is the property tax impact difference if the church is the property owner user or is a tenant user and files religious use paperwork to an Arizona assessing office? Is filing religious use application good, bad, or neutral? For the Church? For the owner and the other tenants?

A. Church Owns the Property

- If a property is bought by a church (or is owned by a church), is 100% used for church purposes and qualifies for an Arizona statutory religious use exemption, the real property taxes are often 100% exempt. Meaning $0. This is an example of 100% real property tax exemption.
- If partially exempt, understand the impact to the non-exempt non-church tenants. A Rule B may be triggered that increases real property tax exposure to the non-exempt users. This may in turn NOT be a pass-though expense in a lease to a non-church tenant user.
- *Firm Advice:* before filing exemption paperwork, obtain a property tax estimate of potential impacts, including to the non-religious church tenant property portion.

B. Church as a Tenant in the Property

- A church asks to rent 4,500 sf. Of 50,000 sf property. Church informs landlord it is filing paperwork to obtain statutory real property religious use status for the space. Church asks landlord to sign the landlord assessor religious use filing form.
- *CAREFUL: Neutral or Good, No Rule B Trigger* In some Arizona counties filing religious use paperwork for church leased space does not trigger a Rule B. If a Rule B is not triggered, the LPV would increase to no more than 5%. Impact is potentially neutral or positive for the church and other tenants.
- *BE AWARE: Rule B Trigger* Same scenario as before, however, the County Assessor *does apply* a Rule B. If the church leased portion of the property is granted 'religious use' status for the tax year and receives Class 9 status with 1% assessment ratio, in this hypothetical the LPV would increase from approx. $2,780,000 to $5,768,400 based on FCV $6,600,000. LPV increases over 200% and estimated taxes to the non-exempt portion of the property more than double. Estimated real estate taxes for 2021 tax year increase to approx. $135,000 or $2.70/sf.
- The church tenant would receive Class 9 status for its 4,500 sf, while the overall property is exposed to a significant real property tax increase from $1.46/sf to $2.70/sf. Owners and property managers beware! Unintended consequences do exist and can often be avoided.
- *Firm Advice:* Seek a property tax estimate of potential impacts.

COVID-19—Be Proactive

The COVID-19 public health emergency is expected to continue to have a significant impact on business through 2024. Historically, Arizona property valuations do not quickly adjust in an economic downturn. The current COVID-19 "new norm" impacts private and public sectors alike. It must be a consideration of property valuation and tax appeals.

While COVID-19 as a complicating factor is considered, business decision makers will be well served to understand that Arizona has one of the most convoluted real property tax and valuation statutory regimes in the county. It also provides Arizona property owners robust and multi-tiered appeal options. Arizona's critical date path for appeals and tax court filings is sensitive; there is little room for error.

Be Savvy and Be Aware

Arizona 2022 tax year notices of value are mailed out to taxpayers by **March 1, 2021**. Taxpayers will have a short 60-day window to review and elect to appeal these valuations. Collaborative planning assists management in budgeting for reserves, managing investor expectations and reducing surprises.

Opportunities to work through the maze of exemptions, exceptions to exceptions, pitfalls between traps and significant statutory constraints to obtain valuation adjustments, tax savings and relief do exist.

Take-Aways

"Don't be afraid to give up the 'good' to go for the great."

—John D. Rockefeller

Today, developing and maintaining a robust Arizona property tax valuation appeal plan is critical. In many instances, successfully appealing a valuation for tax year 2022 tax year, may provide savings over a two year or longer period. Planning for capital expenditures, demolition, new construction and changes in use with experienced legal counsel is a sound business move.

Keep in mind, the Arizona property tax regime does not limit actual property taxes to a 5% increase. What may look like an immaterial, simple change in the property and its use, can have large economic implications. Contact a well-informed real estate property tax attorney to preserve your bottom-line before making a costly decision.

1 A "Rule B" application results in release of the statutory 5% increase cap on the taxable value generally set out in Arizona Revised Statute §42-13302(A): "A. In the following circumstances the limited property value shall be established at a level or percentage of full cash value that is comparable to that of other properties of the same or a similar use or classification:
1. Property that was erroneously totally or partially omitted from the property tax rolls in the preceding tax year, except as a result of this section.
2. Property for which a change in use has occurred since the preceding tax year.
3. Property that has been modified by construction, destruction or demolition since the preceding valuation year such that the total value of the modification is equal to or greater than fifteen percent of the full cash value.
4. Property that has been split, subdivided or consolidated from January 1 through September 30 of the valuation year, *except for cases that result from an action initiated by a governmental entity.*" (Emphasis Added)

Jodi Bain is managing partner at The Bain Law Firm PLLC and has practiced in the U.S. for over 15 years. Bain is a real estate attorney that has successfully pursued and completed over 70 Arizona Tax Court cases since the imposition of Prop 117. She is an AV® Preeminent Rated attorney licensed in Arizona & New York, an Arizona licensed real estate broker and is Spanish speaking. Jodi can be reached at jbain@blfaz.com.

CLOSING 2020 WITH SOME GOOD NEWS: PAYCHECK PROTECTION PROGRAM CORRECTIONS AND ADDITIONAL FUNDING

» by Eric Freeman

2020 was a heck of a year, wasn't it? Like many businesses nationwide, our firm went remote overnight. Offices sent their employees home, restaurants converted to mostly take-out and delivery, checkout counters suddenly had Plexiglas, tenants agreed to only essential repairs, and families and friends gathered virtually. Many industries saw an immediate shock to their operations, and real estate was no exception. Leases and loans were renegotiated, rents were deferred or reduced and some tenants went out of business.

In March 2020, Congress passed the Paycheck Protection Program (PPP) as part of the CARES Act, and while good intentioned, the haphazard guidance and lack of clarity on the PPP loan created a host of problems.To close the gap on prior guidance and to extend further aid, Congress passed the Consolidated Appropriations Act on December 21st, 2020 which was signed into law by the president on December 27th, 2020. This legislation includes the much awaited correction for the deductibility of expenses associated with the PPP proceeds, another round of PPP funding and many other useful tools for businesses as we head into the New Year. Apparently, lawmakers only had a few hours to review the 5,593-page bill before taking a vote, so what could possibly go wrong this time?

Problems with the Original Paycheck Protection Program

The pandemic caused an incredible disruption to an otherwise booming economy. As Coronavirus cases continued to rise over the summer, so did the number of shut downs. To incentivize employers to keep employees on the payroll, the PPP created government loan funds administered by the Small Business Association and divvied up by the banks. If businesses spent the majority of those funds on payroll, they could be approved to receive full forgiveness for the loan. Additionally, businesses could use the proceeds to pay for ancillary expenses such as mortgage interest, rent and utilities. The deal was sweet, but the details were bitter. Think of it as the privatization and expansion of unemployment compensation. Guidance changed constantly, even on the basics like how much of the proceeds had to be spent on payroll costs. Initially, the legislation had no requirements on how much of the funds needed to go to payroll as opposed to other costs eligible for forgiveness. Later, we were told 75% had to be spent on payroll and subsequently it changed to 60%.

PPP Loan Forgiveness and Expense Deductibility

The CARES ACT did not specifically address how the associated expenses funded with PPP proceeds would be handled. Though, it seemed they would not be subject to tax upon forgiveness. A few months into dealing with the PPP, the IRS issued guidance that indicated because the PPP loan forgiveness was nontaxable income, the corresponding expenses should be nondeductible to prevent a "double dipping". Let's think about that for a minute…doesn't that ultimately make the PPP forgiveness taxable? As you may imagine with many businesses already struggling to meet expenses and wading through the complexities of the program, this was an unwelcome surprise. Fortunately for taxpayers, this was corrected in the eleventh hour as part of the Consolidated Appropriations Act which made expenses paid for with forgiven PPP loans deductible.

A Fresh Round of PPP Funds

The Consolidated Appropriations Act provides for $284 billion in funding to the Small Business Association for first and second PPP loans to businesses. For any eligible business that received a first PPP loan, they may be able to apply for a second one if they can demonstrate a reduction in revenue of 25% in any 2020 quarter as compared to the same quarter in 2019. In addition, second time borrowers must have less than 300 employees and have used or will used the full amount of their first PPP loan. As with the first round, the maximum loan for any borrower is $2 million. First time borrowers with fewer than 500 employees and eligible for other SBA 7(a) loans will be eligible. This includes sole proprietors, independent contractors, self-employed individuals and non-profits. The same costs eligible for loan forgiveness under the original PPP remain eligible under this new round, namely payroll, rent, mortgage interest and utilities. The eligible costs were also expanded to include the following:

- Costs incurred for the protection of workers or to modify or adapt facilities in order to comply with federal health and safety guidelines resulting from COVID-19
- Costs to suppliers that are essential to the borrower's current operations
- Certain business software or cloud computing services related to product/service delivery, payroll, human resources, sales, inventory, supplies or accounting.

With the expanded funding and modification of the previous program, it appears the interpretation of laws and guidance has only just begun for borrowers and their advisors.

Simplified Application for Certain Borrowers

After numerous modifications to the application process, there is a now a streamlined process for those with PPP loans of $150,000 or less. Under this new process, borrowers must sign and submit a certification that is one page or less and includes:

- The number of employees retained because of the loan
- Total loan proceeds spent on payroll costs
- Total loan amount

While the application process does not require supporting documents to be supplied, borrowers must retain the relevant records for four years in the event of an audit or review.

What Does the Future Hold?

If the past is any indication, there will be many more questions that arise as we get through the first quarter of 2021. In the meantime, the PPP loan will continue to be a lifeline for many struggling businesses. While real estate has not yet been hit as hard as originally anticipated, property owners and ancillary businesses should weigh the benefits of applying for this next round given the remaining uncertainty.

Eric Freeman is a Tax Senior Manager for BeachFleischman PC. He has a Master of Accounting with a focus in tax and he is a licensed CPA in Arizona. He has spent most of his career specialized in the real estate industry and partnership taxation by providing consulting, planning and tax preparation services. Eric offers a unique perspective to the real estate industry from his own experiences of owning and managing real estate investments. He can be reached at efreeman@beachfleischman.com.

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-James P. Robertson, Jr., CCIM, MBA, Associate Broker

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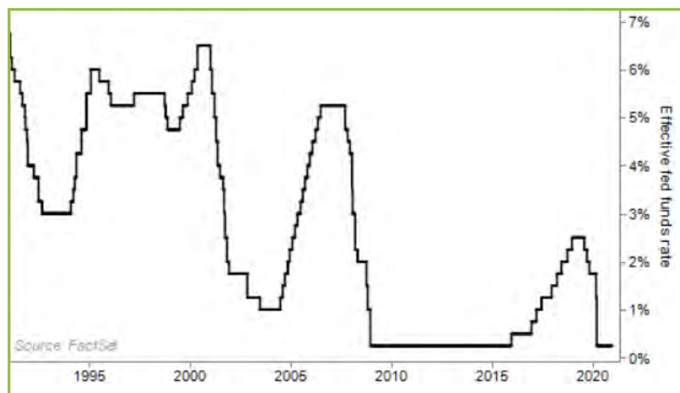
» by Scott Stovall

In previous TREND articles over the past three years, I have shared about the real and persuasive power of the US Federal Reserve (FED) and the influence its monetary policy holds over just about everything. As I have previously written, up until 2019 FED had been attempting to "normalize" interest rates through the Fed Funds Rate (FFR) to provide the FED with interest rate ammunition to address future economic crises. I shared back in 2018 that if FED was not able to normalize FFR in the next 24 months it would illustrate just how dependent our continuing economic health remains on the perseverance of historically low interest rates. The bulk of attention on FED rate action has focused on March 2020 where FED threw everything it could at thwarting the global economic meltdown occurring—including again submarining FFR. However, the real capitulation in FFR started in July 2019, before COVID-19 was even a "thing."

As seen in the long-term FFR chart below, FED turned course in mid-2019 and began reducing the FFR in irrefutable response to the equity and treasury market declines 8 months earlier when the reality of higher interest rates/borrowing costs for companies and consumers were going to negatively impact everything from corporate earnings to junk bond defaults as well as home and auto sales. By 2019, FED learned its lesson that its interest rate increases of the previous 24 months would not be stood for by "Mr. Market" and the greater economy remained reliant on a continued ultra-low interest rate regime.

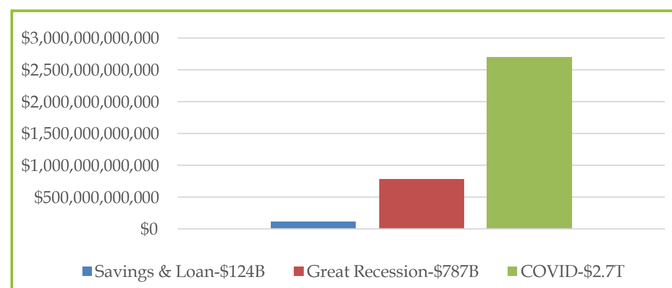


Federal Funds Rate

As the chart above illustrates, we are back down to historic FFR levels here in 2020. This chart also illustrates that in times of crises over the past 30+ years, FED has taken us to ever-lower FFR levels during each sustained financial crisis all the while never being able to "normalize" FFR to the level achieved before each subsequent crisis ensued. It should not go without mention that this chart encompasses the majority of the timeframe that the US has been fully de-coupled from the gold standard and thus able to print currency freely and deficit-spend forcefully as an economic stimulant.

The FFR table above encompasses the impacts of the Savings & Loan Crisis of the late 1980's, the Great Recession and now COVID —the three most prolific crisis-responded events during this period. (The 2001 recession was dramatic in terms of FFR but not crisis spending.) It may not come as a surprise to see that as the power of FFR's influence over the economy wanes during this period (both lower FFR highs and lower FFR lows as each crisis presents itself) another more powerful and potentially destructive stimulant arises in this era of free money printing.

The graph below shows just how prodigious the creation of dollars has been to "tackle" each crisis experienced over just the last thirty years as FEDs monetary policy alone (through FFR) has proven less effective without also increasing fiscal (deficit spending) responses. Each deficit spending response has been increased by multiples and hardly fathomed possible when digesting the debt incurred from the previous crises.



Crises Spending Perspective

A $2.7T COVID crisis spending assumption is based on the amount of CARES funds utilized as of mid-December coupled with an additional $900B approved by year-end. This is a truly astounding level of deficit spending within any 12-month period—let alone in its absolutism. Our country's current gross federal debt sits at $27T today and has increased by 20% within the last 12 months alone (our entire economy is only valued at $20T). Please also remain aware that FED is acquiring $120B in bonds per month (as much as we spent on the *entire* S&L crisis thirty years ago!) in order to maintain lower long-term interest rates (as I have discussed in previous articles). This $1.2T annual FED bond buying comes from continued new money creation/deficit spending as well. Although I am presenting only public debt figures here the levels of corporate debt are at all-time highs and very prone to default dynamics going forward.

All of this federal and corporate debt WILL have to be serviced and then repaid at some point. Will governments and corporates continue to be able to roll over/refinance their debts? Will there continue to always be willing refinancers and at lower and lower interest rates as we have seen the past thirty years? Will OUR government be able to continue to print dollars to buy debt in perpetuity to the tune of trillions per year? In just taking in this historical data presented it should be no surprise as to why FED is in a position to need to maintain historically low interest rates to limit the amount of potentially crushing federal and corporate annual debt service obligations going forward and for as long as possible.

For us in the real estate and capital markets, we should feel on razor's edge these next few years. Through this COVID crisis, projections are for a potential $125B in distressed commercial real estate to trade in the next 24 months and over $300B in distressed deals on the low end (and approaching $650B under worse case) over the next five years. The level of upcoming distressed sales

continued on page 17

NEW PIMA COUNTY ASSESSOR: OFFICE WILL BE MORE TRANSPARENT, BUSINESS FRIENDLY

» by Suzanne Droubie

In the coming weeks, the Pima County Assessor's Office will be rolling out a series of new programs designed around working closer with the business community through the pandemic. In the last year, I've listened to community groups, business owners and individuals while on the campaign trail who voiced their concerns about much-needed reforms inside the office.

While individual issues varied from person to person, a common thread was improving customer service during this health crisis.

With over 24 years of combined experience as a property tax agent, appraiser, real estate agent, and customer service specialist, I am the county's first female assessor since its creation. My motto for the next four years is "Putting the Service back in Public Service."

I still believe the gold standard in public service is personal service; talking face-to-face with the community I serve.

However, during this public health crisis, it has become imperative that we offer the same level of service in new ways, including offering some services virtually for members of the business community who cannot come into our office.

Likewise, we will also ensure the highest health and safety standards for those who must make an in-person visit to the Pima County Service Center.

While these improvements will be rolled out in the first quarter, my senior staff and I will be meeting with the community public this summer at a series of public events to gather more input on service improvements inside the office.

Improving customer service is a top priority for me and I am proud to announce that Mark Baudendistel will be joining our team as Director of Business Services.

He is currently a Senior Commercial Appraiser at the Assessor's office, a position he's held for the last eight years. His experience as a Title Officer, a contractor, and a small business owner in addition to over 20 years of management experience will contribute to the incoming administration's goals.

With a focus on working closely with the business community, Mark will take an active role collaborating with the County's development services department, ensuring that new developments are assessed correctly and that all available tax exemptions are applied wherever they are eligible so that no one is ever forced to pay more than their fair share.

Additionally, Joe Ferguson will be joining my team as the Director of Public Outreach. Well versed in communications as a journalist for over fourteen years, he will be a dynamic conduit between the business community, the public, and my office.

I strongly believe the community deserves to have faith that they can go to the Assessor's office for honest and transparent answers to all of their questions concerning their valuations and property taxes.

He will bring transparency by establishing a rapport with the community through new lines of communication and will work to ensure equitable values for all.

Suzanne Droubie is the new Pima County Assessor as of January 1, 2021. She has over 24 years of combined experience as a property tax agent, appraiser, real estate agent, and customer service specialist, and has the expertise and leadership skills necessary to turn the Assessor's Office into a valuable resource for the constituents of Pima County. She is the first female assessor in Pima County's history. She can be reached at Suzanne.droubie@pima.gov.

TRILLIONS NOW

» continued from page 16

remains highly sensitive to interest rates and FED. *FED has all but promised that FFR will remain at current levels through 2023.*

However, just as COVID was deemed an unforeseen impact, a stressed-out economy and interest rates being actively "managed" ever-lower creates an environment of economic and financial tension. Markets in this state can react/overreact going forward to any real or perceived economic/financial/geopolitical threats in a way that could tangibly upend our hopes and goals for a 2021 stabilization in the CRE industry and a sustained recovery thereafter.

Early 2021 presents itself a time to lock in historically low interest rates at reasonable leverage ratios where the primary source of repayment is sustainable and defensible. Distressed CRE acquisition opportunities will manifest in 2021 and beyond. By patiently waiting for the right acquisition, whose price reflects the actual cash flow generations being achieved in the marketplace at that time (versus layering "pro forma" projections of a better future economy that is not the current reality), may be the prudent approach for defensible CRE cost bases and long-term value creation going forward.

Scott Stovall is a Vice President with National Bank of Arizona. Scott has held VP positions in commercial real estate finance with JPM Chase, Alliance Bank and BNP Paribas in the Tucson, Phoenix and Albuquerque markets as well as a previous principal and CFO of Metro Title Agency prior to joining National Bank in 2016. Scott can be reached via email at scott.stovall@nbarizona.com

2020 WAS AN ACTIVE YEAR FOR REAL ESTATE FINANCE

» by Tim Prouty, Kevin Prouty, Brian Prouty, and Theresa Witz

Goodbye, 2020! Although the CBRE Capital Markets' Debt & Structured Finance team in Tucson enjoyed a record year of production, we are glad to put 2020 in the rearview mirror due to the negative impact the COVID-19 pandemic has had on our community, commercial real estate and clients. We look forward to 2021 with optimism!

When the Federal Reserve responded to the pandemic by massively expanding its balance sheet (again!), other Central Banks followed suit, and global interest rates plunged to a territory none of us expected. The ten-year treasury dipped below .50% for the first time in decades.

Of course, borrowers and mortgage bankers took full advantage and refinanced their eligible properties, while some absorbed the cost of significant prepayment penalties. Once the initial refinancing wave was absorbed, the financing market began to feel the slowdown in acquisitions.

The CBRE Lending Momentum Index declined by 17.6% in Q3, as a sluggish acquisitions market continued to put the brakes on overall lending activity. However, CBRE Capital Markets notes a rise in loan applications in recent weeks—a promising sign for higher year-end closings. Underwriting has become more conservative in the current risk-averse lending environment. Average loan-to-value ratios (LTVs) for permanent commercial and multifamily loans fell in Q3 to levels not seen since the Global Financial Crisis (GFC).

Stabilized multifamily continues to receive strong support from the agencies, while banks and life companies continue to underwrite lower leverage multifamily, industrial and selective office transactions. However, retail and hotel properties, and those properties with transitional issues, remain challenging to underwrite. One promising sign has been the re-emergence of quotes from alternative lenders in recent weeks, a source of capital for transitional properties and distressed situations.

Freddie Mac is focused on purchasing as many loans as possible to come as close to its 2020 cap limit of $82.5 billion. Fannie is doing the same thing. Inflows of new loans into the agencies' pipelines are down materially due to seasonal patterns, and their wider spreads have slowed volume lately.

Next year, agencies will place a strong focus on loans that satisfy their mission-critical categories. Investors with multifamily properties in excess of 20-25% of units that qualify as affordable per the Area Median Income (AMI) Test will get strong bids from both Freddie Mac and Fannie Mae. Please contact us if you would like to determine how your property would be measured against the affordability test.

The pandemic drove the agencies to offer forbearance in debt service payments to borrowers if they, in turn, passed along a similar forbearance in rent payments and evictions to their tenants. The loan payments were not forgiven and typically were added to the back end of the loan. Many landlords made similar arrangements with their tenants.

Fannie Mae announced on December 21 that it would be extending its delegated forbearance program until March 31, 2021. The program's delegation had been scheduled to expire on December 31, 2020. The program details remain largely unchanged from the program as it exists now, including the cash sweep provision, the eviction and late fee moratoriums, as well as the requirement to provide notice to tenants of their rights under the forbearance agreement. For more information about Fannie Mae's program, please visit the Fannie Mae FAQ.

There has been much discussion about "privatizing" the agencies and moving them out of conservatorship. After demonstrating their ability to provide a backstop to the residential markets, the politics surrounding that issue have become more complex. The Federal Housing Finance Agency on Thursday released for public comment a new rule on how much liquidity mortgage giants Fannie Mae and Freddie Mac must maintain.

Additionally, due to fallout from the pandemic and the resulting eco¬nomic slump, the tally of non-agency, Commercial Mortgage-Backed Securities (CMBS) issuance is projected to be only $59.3bn for 2020. That would mark the lowest annual volume since 2012 when CMBS issuers were just start¬ing to gain traction following the Great Recession of 2008-2010. The relative shortage of supply and need for yield continues to be key factors in the tightening.

The private-label CMBS market made a strong finish for end-of-year offerings. Demand continues to be robust, with one of the conduit deals ending up four times oversubscribed.

The two vaccine announcements affirm CBRE's economic forecast and outlook for commercial real estate. We anticipate wide distribution of the vaccine in the first half of 2021 and a return to more typical economic conditions by the second half. During the latter half of 2021, office occupancy should materially increase, and brick-and-mortar retail should more fully benefit from a resumption of activity. Nevertheless, we expect some residual effects of the pandemic—such as increased flexibility for office workers and consumer appetite for e-commerce—to remain prevalent beyond H1 2021. Full recovery in office, retail and hotels will take more than two years. The typically conservative commercial real estate finance sector will reflect, not lead, the various real estate groups as they recover.

We'll close with a positive quote from Mark Zandi, Chief Economist, Moody's Analytics: "[If] we reconvene a year from now, I think we'll feel much better about things. The pandemic will feel like it's almost in the rearview mirror. . . As soon as people feel like the coast is clear, I think growth will pick up and kick into a higher gear."

Kevin Prouty, Tim Prouty, Brian Prouty, and Theresa Witz are members of the Tucson CBRE Debt and Structured Finance Group. They have represented insurance companies, banks and other lenders in Tucson and other Arizona and out-of-state markets for over 30 years. They can be reached at Kevin.prouty@cbre.com, Tim.prouty@cbre.com, Brian.prouty@cbre.com and Theresa.witz@cbre.com.

PROPERTY MANAGEMENT: STAYING FOCUSED DURING THESE UNPRECEDENTED TIMES

» by Ryan Johnson

I think we can all agree when we say that we are looking forward to 2020 being behind us! 2021 will still be difficult, but there is light at the end of the tunnel now that the vaccines are approved and starting to be given. One thing for sure during this pandemic is the high value that is placed on property management companies to help forge through the ups and downs that come along with this crisis.

From the residential property management side of the business, there are still residents that are struggling to pay rent and will probably continue for some time into the future until we can get all of this behind us.

Overall, Tucson has continued to see a strong occupancy rate throughout multifamily assets in the 95% plus range, however, the lingering question is, will this continue to stay constant when the eviction moratoriums are lifted for non-payment of rent filings? This number may be artificially inflated today due to residents continuing to occupy units even though they may be behind on their rent payments. The concern will be that when property owners and management companies start to proceed with evictions, how many units will open from non-paying residents? Most likely there would be a linear movement from one property to another, however, if residents decide to up and leave Tucson altogether for employment reasons or to move back in with their families, this is where we will experience a dip in overall occupancy rates.

There is more assistance that is expected to be forthcoming and from a resident standpoint and is proposed to include at least $600 direct payments to most Americans, $300 a week in extra unemployment, $25 billion in rental assistance and $284 billion for the Paycheck Protection Program that will help small businesses continue to keep residents employed. This assistance is very much needed and will hopefully help to stabilize the rental markets. Coupled with the previous assistance and the proposed future assistance that will be provided will continue to help with rents being paid or payment plans being agreed to.

Interestingly, we have seen a continued uptick in rental rates throughout Tucson, even during the most recent months. Tucson, arguably, still has room for rent growth given it is one of the lesser expensive cities in the country. We have seen more "high profile" businesses coming to the market as well as continued population growth. We have been experiencing the trickle-down effect from Phoenix with investors coming to the Tucson market chasing higher returns, which has been a benefit to the overall property improvement standpoint. In addition, we are seeing tired buildings being rejuvenated into more modern assets with more appealing exterior and interior improvements being completed.

From the commercial side of property management, buildings and units are being vacated or going dark. This is expected to continue for the coming months as businesses are struggling to make rental payments, etc. We have seen long time Tucson restaurants close their doors over the past few months, however, we are seeing some restaurants opening amid this pandemic, which is a positive for the market. It will take time, but we are hopeful that restaurateurs will begin to feel more comfortable opening up new restaurants or expand once there is stabilization within the industry. Industrial buildings have done well and continued to maintain higher occupancy rates, while office space will continue to struggle as companies assess their future needs for space. The transition to remote working has proved that job duties can still be completed outside of an office setting. Companies are finding that they no longer need the large floor plans and high-end/prolific locations that they once carried on their books. As with office space, brick and mortar retail will continue to struggle as more and more of the population are buying everyday necessities from online retailers to avoid direct interactions with other people.

As property owners are looking to cut costs where they can, maintaining a property's curb appeal is one of the most important factors that needs to be addressed. Cutting back on items such as landscaping, exterior improvements, property cleanliness, etc. will make it hard to attract new and retain current residential residents and commercial tenants within properties. When all of this is behind us, those properties that continue to maintain their curb appeal and will come out ahead with higher occupancy and rental rates.

Our firm, Son Property Management, and managers alike play an important role in day-to-day operations of property assets. Staying focused and adapting quickly to meet the needs of residents, tenants, and property owners during these unprecedented times is where the value comes into play of having a property manager at your side. Whether it is working to collect rents or pay bills, managing residents/tenants, or maintaining properties, our focus is to operate each asset to the highest caliber possible.

We will come out stronger after everything that we have had to endure over the course of the past year. Let us all continue to stay strong and healthy and do our parts to help get past this pandemic.

Ryan Johnson is the co-founding partner of Son Property Management, along with Graham Swanson. Together, Ryan and Graham manage the day-to-day operations of the firm and properties under its ownership and management umbrella. Son Property Management oversees multifamily assets, as well as commercial and industrial assets. Ryan can be reached via email at rj@sonpm.com.

The Arizona recovery continued in the third quarter, although at a much slower pace than during the April-June period. The state has received a significant boost from the CARES Act, with just over $40 billion in federal funds flowing to the state in the second quarter. That supported taxable sales and boosted the recovery in retail trade, warehousing, and transportation jobs. While construction employment rose modestly from June to October, housing permits surged, rising almost one-third over the year in the third quarter.

The outlook for Arizona remains unusually uncertain and continues to be dominated by the pandemic. The baseline forecast assumes that the outbreak recedes from summer highs, but remains elevated. It also assumes significant federal stimulus in the fourth quarter of 2020. Under these assumptions, the state is forecast to return to pre-pandemic employment levels by mid-2021. The pessimistic scenario projects a slower recovery, with the state returning to its prior peak at the end of 2021.

Arizona Recent Developments

Arizona added 55,600 jobs (seasonally adjusted) from June to October. Trade, transportation, and utilities added the most jobs during the period, followed by professional and business services; government; education and health services; leisure and hospitality; construction; other services; financial activities; and information. Manufacturing jobs were stable, while natural resources and mining jobs fell slightly.

Overall, the state has now replaced 193,900 of the 294,600 jobs lost from February to April, for a 65.8% replacement rate. The nation has replaced 54.5% of the jobs lost from February to April.

Note that the state needs to add 100,700 jobs to return to pre-pandemic employment. If the state can continue to add nearly 13,900 jobs per month on average, as it has since June, then employment will be back to pre-pandemic levels next June. However, that may be a difficult pace to maintain, since over-the-month job gains averaged 6,200 during 2015–2019.

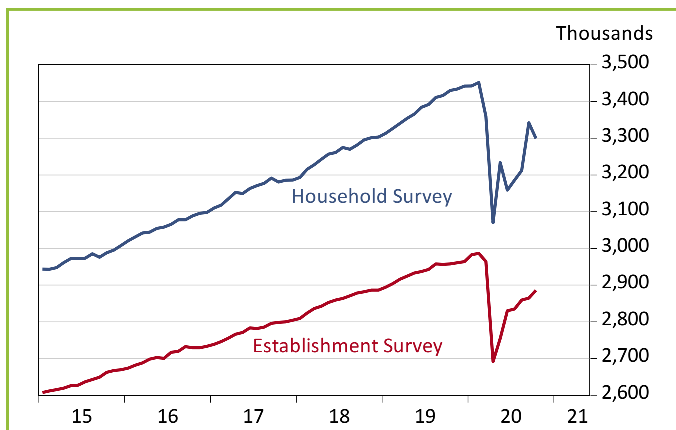


Exhibit 1. The Jobs Recovery in Arizona Has A Long Road Ahead: Employment Measured by the Establishment and Household Surveys, Seasonally Adjusted

Exhibit 1 shows seasonally-adjusted employment from both the establishment and household surveys. As the exhibit suggests, we have a long way to go to replace the jobs lost during the spring.

Seasonally-adjusted employment measured by the household survey experienced a huge jump in September that was not reflected in the establishment survey. These data are always volatile during the current year and seem to be even more volatile than usual this year. This may be related to reduced survey response rates during the pandemic.

The household survey also generates estimates of the state unemployment rate. These estimates have also been very volatile, with the seasonally adjusted state rate falling from 10.7% in July to 5.9% in August then back up to 6.5% in September and 8.0% in October.

The travel and tourism sector continues to struggle with the impact of the pandemic. As Exhibit 2 shows, leisure and hospitality jobs in October were 54,500 below February. Through October, jobs at eating and drinking places have recovered much faster than jobs in accommodation or arts, entertainment, and recreation. Employment at eating and drinking places was down 9.7% in October, compared to -29.4% and -34.3% for accommodations and arts, entertainment, and recreation.

Exhibit 2. Arizona's Leisure and Hospitality Sector Remained Hardest Hit from February 2020 to October 2020, Thousands, Seasonally Adjusted

From February to October, jobs in professional and business services were down 18,100, reflecting losses in employment services (temporary help). These jobs are very sensitive to the business cycle.

Employment in education and health services declined by 14,700 from February to October, reflecting large declines in health care and social assistance (although education jobs were down as well). Job losses in health care and social assistance were fairly evenly distributed across social assistance, ambulatory health care, nursing and residential care facilities, and hospitals.

Two sectors posted more jobs in October than February: other services and trade, transportation, and utilities. Job gains in trade, transportation, and utilities were driven by transportation, warehousing, and utilities. Retail and wholesale trade jobs were up slightly.

Arizona's personal income skyrocketed in the second quarter of 2020, thanks to the CARES Act. State personal income rose 11.6% over the year, driven by a 62.2% increase in transfer receipts. Net earnings by place of residence fell by 0.8% and income from dividends, interest, and rent fell by 1.3%.

According to estimates from the U.S. Bureau of Economic Analysis, the CARES Act pumped $40.2 billion into Arizona in the second quarter. The largest contribution came from the Economic Impact Payments (Recovery Rebates), which added $23.4 billion to state income. Absent CARES Act funds, Arizona's personal income would have declined by 3.8% (or -14.4% annualized) from the first to the second quarter.

While construction jobs have weakened during the pandemic, housing permit activity has surged. Preliminary seasonally adjusted housing

permit data suggest that statewide total permits were up 25.2% year to date through October compared to last year. Even so, house prices continue to rise at a rapid pace.

Arizona Outlook

The forecast for Arizona depends on global and national economic performance. The current state and local forecasts rely on the October 2020 U.S. forecast generated by IHS Markit, which was based on the following assumptions:

COVID-19 infections and deaths recede from July levels, but remain elevated. This creates stop-and-go openings by states. A vaccine is assumed to become widely available in mid-2021.

The forecast includes current federal fiscal policy actions and assumes legislation enacting a $300/week unemployment insurance supplement from October through December. Further, the forecast assumes $270 billion in stimulus checks are disbursed in the fourth quarter of 2020. As of this writing, it does not appear that this assumption will be met, which suggests that the baseline projections may be too optimistic.

The Federal Reserve maintains its policy rate near 0% until late 2026.

Real foreign GDP contracts by 6.7% in 2020. Growth rebounds to 4.4% in 2021.

The current baseline forecast calls for a sharp rebound in real GDP growth in the third quarter, but the level remains well below the pre-pandemic peak. Thereafter, growth decelerates significantly as the current durable goods spending overshoot unwinds, fiscal stimulus fades out in 2021, and the pandemic accelerates this winter.

The national forecast sets the stage for Arizona's recovery, summarized in Exhibit 3. In the baseline, state jobs are expected to decline by 2.0% in 2020, on an annual average basis. Jobs rebound in 2021, rising 4.3%, followed by 3.2% growth in 2022.

	Actual	Forecast		
	2019	2020	2021	2022
Growth Rate				
Nonfarm Jobs	2.8	-2.0	4.3	3.2
Personal Income	5.0	6.4	0.9	5.8
Retail Plus Remote Sales	7.7	9.5	4.4	3.1
Population	1.6	1.4	1.5	1.5
Level				
Unempl. Rate	4.7	7.6	6.3	5.2
Housing Permits	46,580	53,526	49,885	46,880

Exhibit 3. Arizona Outlook Summary

On a quarterly basis, the baseline forecast calls for Arizona jobs to return to their pre-pandemic peak in the second quarter of 2021. Keep in mind that this assumes a major federal fiscal stimulus package in the fourth quarter of 2020. The pessimistic scenario envisions a slower recovery, with state jobs reaching pre-pandemic levels at the end of 2021.

Overall, Arizona population growth is forecast to hit 1.5% in 2021 (fiscal year basis) and then gradually decelerate as the aging of the baby boom generation raises deaths while births stabilize and recover weakly.

The combination of remote sales with traditional retail beginning at the end of 2019 artificially boosts growth in the combined category in 2020. The forecast calls for growth in the retail plus remote sales sector to rise by 9.5% in 2020, then decelerate to 4.4% in 2021 and 3.1% in 2022.

The baseline forecast calls for nonfarm payroll jobs in Phoenix to decline by 2.0% in 2020, then rebound with growth of 4.0% in 2021 and 3.3% in 2022. Maricopa County generates the bulk of the job gains for the metropolitan area during the next decade. However, job gains in Pinal County are expected to be robust, in part driven by expanding auto/truck manufacturing in the county.

The Tucson metropolitan area also generates a solid recovery from the pandemic. Tucson nonfarm payroll jobs are forecast to decline by 3.2% in 2020. Growth returns in 2021 with a 3.4% increase, followed by 2.1% growth in 2022.

Risks to the Outlook

The risks to the outlook primarily revolve around the progress of the outbreak. Exhibit 4 shows three scenarios for Arizona nonfarm jobs.

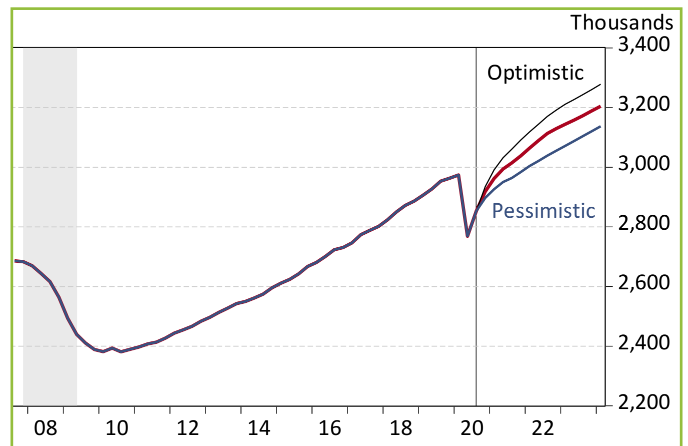
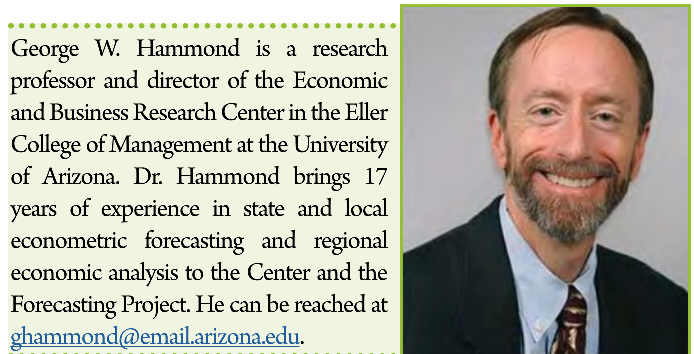


Exhibit 4. Three Scenarios for Arizona Nonfarm Jobs. Arizona Jobs Take Longer to Recover Under the Pessimistic Scenario.

The pessimistic scenario assumes that the progress of the outbreak is less controlled than under the baseline, with large negative impacts on consumer spending, particularly services. The result is a slower recovery. Under this assumption, Arizona jobs return to their pre-pandemic peak in the fourth quarter of 2021.

The optimistic scenario assumes a less threatening progression of the outbreak, with correspondingly faster gains in consumer spending. The result in this case is faster growth in the near term. Under this assumption, Arizona jobs return to their pre-pandemic peak in the first quarter of 2021.

George W. Hammond is a research professor and director of the Economic and Business Research Center in the Eller College of Management at the University of Arizona. Dr. Hammond brings 17 years of experience in state and local econometric forecasting and regional economic analysis to the Center and the Forecasting Project. He can be reached at ghammond@email.arizona.edu.



» by Cynthia Hammond

Welcome 2021, and goodbye 2020! So, what's up in commercial property financing? It is available for most property types, but terms have changed. We will explain the landscape for lending on commercial projects today, and how it has changed this year.

We began 2020 with ample capital allocated to commercial real estate debt and equity investments and the economy generally humming. Then COVID-19 hit, and beginning mid-March the capital markets took a deep dive. The second quarter saw the economy contract by a seasonally adjusted annual rate of 31.7% and consumer spending drop by 43%. Commercial real estate debt and equity investors hit the brakes, being unable to clearly gauge the risk in their CRE investments. National loan originations declined 48% in the second quarter 2020 compared to a year earlier, and commercial property sales declined 68% over the same time period. Hardest hit were hospitality, retail and office properties, where national lending volume year over year in Q2 declined 81% for hospitality, 74% for retail, and 71% for industrial loans. Multifamily and industrial properties fared better, with lending volume dropping 44% for industrial and 24% for multifamily.

Thankfully, the economic stimulus package brought a sharp rebound in CRE financing in Q3 & Q4. Lenders who were on the sidelines from March through July are now back lending, albeit at a lower level. 3rd quarter origination volume s is 47% less than last year. Securitized financing came back beginning in July, with 2020 US non-agency CMBS loan volume estimated at $59.3 billion, down 39% from 2019.

Interest rates have plummeted with the COVID induced recession, and are anticipated to remain low through 2021 and beyond, until the pandemic abates to a level allowing the resumption of full business activity.

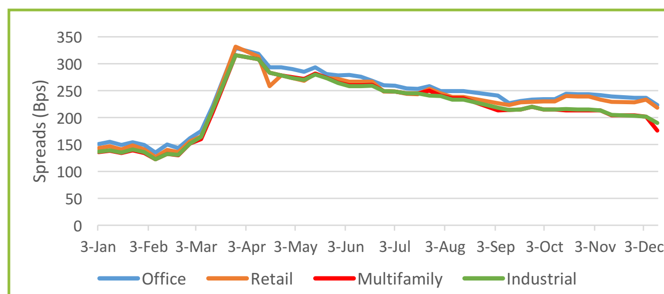
The 10-year Treasury bond yield stands at .93% as of 12/23, down 50% from 1.88% on January 2, 2020. LIBOR short term rates stand at .14% (30 day), down 92% from the 1.73% rate seen in January.

10-Year and 30-Year US Treasury Yields

While interest rates are way down, lenders are requiring a higher interest rate spread over the index to maintain an interest rate that is competitive with alternative investments such as corporate bonds. Spreads rapidly rose in the 2nd quarter, and have been steadily declining since, as seen in the chart at right.

Current national average interest rate spreads over the 10-year Treasury bond for 50-59% loan to value are reported at 2.23% for office, 2.18% for retail, 1.76% for multifamily and 1.90% for industrial properties.

Arizona has benefited from its lower cost of living, pro-business environment, and preponderance of COVID friendly lower density housing



Asking Spreads Over Treasuries: 10-Year Loans with 50–59% LTV

and office options, which is bringing population and employers to our state. This is causing lenders to prefer making loans in, over some larger markets. Industrial and multifamily are in strong demand, followed by medical office, self-storage, grocery anchored or essential service tenanted retail, suburban office, urban high rise office and lastly, lodging properties.

Lenders are generally preferring multi-tenant properties. Industrial property loans are readily available for projects ranging from small tenant "incubator" assets to larger distribution projects, preferably with multiple tenants. We recently closed an $8 million non-recourse life company loan on a multi-tenant industrial project with a 10- year term at a 3.19% rate, at 60% loan to value.

Multifamily loans are available for all asset types, with lenders looking carefully at the rent collections. Workforce and Class A housing where collections have been strong through COVID furloughs are readily financeable. We are presently financing a Class B/C master metered property for a client who will renovate it, but not change the workforce housing tenant profile. Leverage for this non-recourse transitional bridge loan is coming in at 75% of total cost with a minimum 1.25 debt coverage ratio, with a 3 year fixed or floating interest rate in the very low 4's, interest only, with a 1% lender origination fee, and no repayment guaranty.

Construction financing for multifamily or preleased industrial or grocery anchored retail is available, however most banks are now requiring full repayment guaranties. Loans with the borrower's principals guaranteeing completion and carve-out "bad boy" acts are available at 55-65% of cost, with rates ranging from 4.25% to 5.5%, from select community banks and debt funds. Leverage up to 75% of cost requiring a completion and interest carry guaranty is available with rates in the low 6's to mid 7's. Lenders generally charge origination fees ranging from .5% to 1%. Life companies are offering combined construction & permanent loans of 5 to 30 years for these assets, generally at 50-65% of cost, with completion and sometimes repayment guaranties until C of O with leasing at a specified minimum level, after which it becomes non-recourse.

Office financing has become tricky, as lenders do not know how office occupancy will change post pandemic, so they cannot easily gauge demand. High sublease office supply is causing lenders to be much more cautious in office building financing. The suburban walk-up property designed for social distancing is more readily financeable today, at leverage around 55–60%.

Retail financing, despite the precipitous drop in loan volume, is available. We recently closed a refinance loan on a Sprouts anchored center, at 44% of value for a 17 year fully amortizing loan at 3.25% with a life company. We are also arranging financing for another Southern Arizona Sprouts anchored

continued on page 23

2020 IS GONE, BUT HOW HAS IT AFFECTED CONSTRUCTION PRICING

» by David Ollanik

To say this year has been a long, strange trip would be an understatement. I fully expected ALL industries to be shut down, and we would all be trying to figure out what to do with ourselves as we waited for the pandemic to be over. Interestingly enough, construction was deemed an essential industry and we have seen record activity in a year that I would have bet the farm would have been the most challenging financially. Whether it was spurred on by record low interest rates or just sheer will to complete projects already in the pipeline, I cannot say for certain why we are seeing such robust activity. However, there have been consequences to this increased activity and the effects of COVID-19 on the supply chain that resulted in impacts to construction industry pricing.

Volume: An article recently identified that Arizona has experienced an 18% increase in construction activity this year over last. As firms fill their backlogs and labor pools are stretched to meet this demand, there has been pressure on construction pricing to keep up with this increased demand.

Materials: We are currently seeing steel prices increase by $30 to $70/ton or a 30% increase in the cost of the raw materials. In addition to steel, lumber prices have risen at the fastest pace in over 70 years. Concrete has also been affected as well due to a national fly ash shortage. (Fly ash is an additive in concrete that helps lower the price but without affecting the strength.) So, we are not only seeing price increases in materials but also delays in the supply and delivery of materials needed, which affects construction schedules and final costs of construction. Delivery drivers and factory workers are out sick with COVID, dramatically increasing supply line delivery times.

All of these factors have been impacting the cost of projects. In March we thought the impact of COVID would keep pricing flat this year and slow the escalation seen in the industry over the past four years. I am now projecting 2% to 4% escalation for 2021 in the cost of building.

Insurance: Who would have thought the insurance industry could radically affect our business, but I was amazed at just that while doing a cost analysis for a recent project. The owner wanted to explore using a concrete frame in lieu of a wood frame for a multi-family project. By going to a "non-combustible" structure, the Builder Risk policy was *1/10* the price of going with wood frame. In addition, the ongoing yearly cost of insuring that wood frame building was also *10 TIMES HIGHER*. When you capitalize the savings in insurance, which for this project was a net operating expense savings of $265,000, at a 5% cap rate, the owner could justify an additional $5.3 million in project value and more than cover the $2.4 million dollar premium of switching to concrete.

The Bright Side: There is a bright side to this picture. There are a significant number of large projects completing in the first half of 2021 that should help alleviate some of the labor pool shortages and have an easing effect on local pricing. I have seen several procurement results posted lately that indicate a competitive approach amongst general contractors to securing backlog for the second half of 2021 and beyond. Hopefully, this will keep pricing escalation in check and allow the developers to stay within their pro-forma budgets and keep the industry moving forward.

I am hopeful my crystal ball will become clearer this next year as we hopefully emerge from this horrible pandemic quickly and we can begin to forecast construction trends with some certainty. Until then, hang on. Stay informed and talk to your builder and architect early in the process to remove as much risk as possible from the equation.

David Ollanik is the Project Director for Sundt Construction's Tucson Office. He has 31 years of experience in the construction industry. David is a University of Arizona graduate and is actively involved in many service organizations in Southern Arizona including serving on the board of the Metropolitan Pima Alliance. He can be reached at deollanik@sundt.com.

COMMERCIAL PROPERTY FINANCING UPDATE

» continued from page 22

center at 55% leverage on a 21 year fully amortizing loan at a rate in the mid 3's, with a different life company. And we recently closed a refinance loan for Green Valley Village at 70% of value. Loans on strip centers with strong rent collections occupied by essential service tenants are also available from banks, life insurance companies, conduits, and debt funds for transitional loans.

Bridge lenders are stepping in to write short term senior loans designed to provide capital to complete a sponsor's business plan, and are writing mezzanine loans to bring leverage up to 75–85% of cost. Rates on the mezzanine loans are generally around 10%–14%. Life companies have stepped into the bridge lending arena, providing a lower cost reliable option for borrowers.

Lenders are geared up to write more loans in 2021 than 2020. We believe leverage will remain modest at 65% of value or less until the fear of a double dip recession is gone. Tucson is in demand by our lenders. Churchill plans to place more Southern Arizona CRE loans, and is seeking to hire a loan producer. If you know someone who may fit, please refer them.

Meanwhile, we will happily ring out 2020 and bring on 2021!

Cindy Hammond is Founder and President of Churchill Commercial Capital, headquartered in Scottsdale, with over 25 years of experience in Capital Markets, primarily in Arizona. The Churchill Commercial Capital team has closed over $3 billion in commercial real estate financing over a 25 year period. Cindy can be reached at chammondchurchillcc@gmail.com.

» by Joe Snapp

About this same time last year, I was asked to write an article on Finance. Well, considering that article was about Black Swan events and given what some might call the Mother of all Black Swan events (COVID-19) happening shortly thereafter, you can imagine I'm a little hesitant to write one again! I'm not saying I'm a soothsayer but let's just say that I prefer to keep things a bit more positive this time.

"In the long run, I think Arizona benefits. Vitamin D (sunshine), outdoor activities, year-round outdoor dining, and room to roam all lead to growth. Rising in-migration is expected to push Arizona's population above 7.5 million people sometime in 2021. This despite the fact that fewer Americans are moving than at any point in more than 70 years."

That's not to say that positive things have not come out of the pandemic. Napolean Hill, an American author and philosopher once said, "*Every adversity carries with it the seed of equal or greater benefit.*" Certainly, there are plenty of folks and businesses who might argue with that, especially those in the hospitality (especially full service, destination hotels), airlines, tourism, and restaurant industries. Or, I imagine, even a drycleaner. It's just one of many examples of a domino effect that I don't think we all fully understand or appreciate. As employees work remotely in ever increasing numbers, the need for dry cleaning has to diminish. How many are adhering to the "dress to impress" mantra? Most Zoom or GoToMeeting calls are from the neck or chest up. But getting back to and in keeping with the saying that adversity carries with it the seed of equal or greater benefit, the leisure wear and pajama industry must be winning.

Borrowers are winning. Borrowers are benefitting. Seems every week a new record low is set for residential mortgage rates. Commercial rates too. I know that going into 2020 I never thought we would see rates decrease. In fact, everyone was talking about the exact opposite. Yet, here we are at the end of 2020 and a Borrower can easily find rates in the low 4%'s and even the 3%'s. These low rates have definitely helped propel the residential market (both new builds and resale value). As for anyone purchasing or refinancing an income producing property they have definitely seen their cash flow benefit.

In the long run, I think Arizona benefits. Vitamin D (sunshine), outdoor activities, year-round outdoor dining, and room to roam all lead to growth. Rising in-migration is expected to push Arizona's population above 7.5 million people sometime in 2021. This despite the fact that fewer Americans are moving than at any point in more than 70 years. Those who are moving are abandoning major urban centers at the fastest rate in over 20 years as they relocate to the suburbs. And who has more sprawling suburbs than Phoenix? This while our neighboring state of California saw its lowest population growth since 1900 according to a December 2020 report for the state's Department of Finance. A coincidence perhaps? Specifically, according to Moody's Analytics, Tucson has been named among the top 10 cities best positioned to thrive following the pandemic. The report argues that the generation growing up today may recall the impact of the COVID-19 crisis and be more likely to pursue careers and live in less-densely-packed places. Tucson is the only Arizona city in the top 10 list, joined by locations like Washington, D.C.; San Jose, California; and Salt Lake City, Utah.

Finally, in an odd way, Banks win. Unlike previous economic downturns or trying times, Banks were given tools to help. The Payroll Protection Program (PPP) was a huge success. This program allowed businesses to stay afloat. It really made a difference. This process also allowed Banks to again really get to know their customers and, in some instances, get new ones as some customers were unable to obtain a PPP from their existing lender. COVID Deferral programs for both commercial and residential loans also proved beneficial. Allowing payment deferrals proved a huge benefit for those in need.

I really don't know what the future brings but I do know that working together, helping each other, we will be stronger.

Joe Snapp is Senior Vice President at Foothills Bank, a Division of Glacier Bank. A lender in Tucson since 2002, he has 25 years of commercial real estate lending experience including CMBS originator and DUS lender for Fannie Mae. He holds a BA from Boston University and an MBA from University of Denver. Joe can be reached at joe.snapp@foothillsbank.com.

» by Matt Thrasher

When I addressed the issue of Arizona's hospitality sector in the August TREND Report, I ended the article with a quote from OpWest Development's Tyler Kent who stated that: "There is no doubt Arizona's economy will recover. Even despite the pandemic, our state has seen some of the strongest population growth in the country. We see that driving the overall market growth for years to come." Fortunately for us, Mr. Kent has largely been proven right.

While there is no doubt that Arizona has suffered many of the same pandemic-induced economic troubles as the rest of the Nation, we can nevertheless look forward with optimism to 2021 as the beginning of a complete recovery. At the time I am writing this article, there are two approved vaccines and a fresh federal COVID-19 economic relief package has just been passed by the House and Senate. These two factors should bolster Arizona's already-occurring recovery and drive us forward into a near-term complete recovery.

To analyze Arizona's current commercial real estate (CRE) recovery, I chose to shift away from the hospitality sector and to the multifamily housing sector. I will first focus on the national CRE multi-family housing market, and then narrow the focus to Arizona's two major markets: Phoenix and Tucson.

National Trends

The significant trend to highlight at the national level is US GDP contraction. According to Moody's Analytics, US GDP should contract much less than was initially expected by many large institutions such as the IMF. Moody's predicts a US GDP contraction of less than 3% for 2020 and positive GDP growth in 2021. While any contraction in GDP is a bad thing, this is nowhere near as bad as predictions made this past summer of an 8% contraction. In fact, this contraction is smaller than the 3.8% contraction of the January 2008 to June 2009 period of the Great Recession. However, Moody's is quick to point out that despite this "rosy" GDP outlook, the US has still not recovered 9.4 million of the jobs that it has lost since the beginning of the pandemic. This disparity between job loss and GDP strength is likely largely due to government fiscal and monetary support.

Moving the CRE specifically, CRE transactions have begun to show signs of the same economic recovery evidenced by the GDP contraction figures. While overall year-to-date transactions are down significantly (50–60% depending on sector), third quarter transactions are up 10% over second quarter transactions which indicates some recovery stirring. While this gives rise to some optimism, given that larger economics trends often take some time to show up in the CRE markets, the CRE market in 2021 may struggle to recover their pre-COVID-19 transaction numbers.

The national multifamily sector is now also reflecting the overall economic troubles of the Nation. While it did take time for negative trends to materialize, in the third quarter, national apartment vacancies increased to about 5% and effective rents fell by 1.9%. While the 1.9% decline in effective rents may not sound significant, it is the worst quarter-to-quarter decline since the metric began being tracked in 1999. Thus, for 2020 as a whole, Moody's expects a 2.8% decrease in effective rates for the year, and for rents overall to decrease for 2021. Despite these negative trends, the vacancy rates will still be less than the vacancy rates seen following the Great Recession (8.1% in 2010). Moody's points to a 30% decrease in new apartment completion in 2020 for this lower vacancy rate. The multifamily productivity seemly shifted to industrial projects where warehouse and distribution construction has increased by about 30% during 2020.

Arizona Trends

Justifying the optimism of Mr. Kent's opening statement, Arizona's multifamily sector has shown resilience throughout 2020. Overall, Arizona has replaced 46% of the jobs lost during 2020. As I discussed in the August TREND Report, this total job loss was less than that experienced by many other states. Arizona's resilience is likely due to its industry diversity and high-skilled job market which contains companies such as the popular stock trading app Robin Hood (which added jobs in Phoenix in 2020). However, one trend highlighted by the Arizona Multihousing Association, is the uneven effect this pandemic has had on Arizonans. In Tucson for instance, lower-income earners have taken the brunt of the economic hardships, while higher-paying employers such as ADP, Raytheon, and Caterpillar have actually added jobs throughout 2020. This disparity is reflected in the shift in renters away from downtown Phoenix with its higher rents to the southeast Valley suburbs with cheaper options and space for home offices.

Reflecting these strong job numbers, Phoenix rents have remained strong and have in some instances actually gone up in 2020. In fact, one highlight in Arizona's multifamily housing sector is detached single family rental communities. These rental communities have shown strong demand as more units have entered the market. Additionally, in the Valley, 2020 will bring near-record levels of new apartments entering the market (9700 units), with more under development. This strong development likely reflects Arizona's growth in high-income jobs.

While Arizona has shown resilience and a characteristic toughness, we have not been totally immune from larger national trends. Accordingly, we should not expect a full recovery to 2019 year-end figures until 2022. Further, complete recovery will largely depend on the ability of the country to roll out an effective, safe vaccine and for governments to feel comfortable lifting restrictions. Regardless, Arizona's multifamily sector has remained strong throughout this crisis and in many cases has actually seen in increase in production, rents, and demand.

In sum, these factors lead us to only one conclusion: optimism in the face of a difficult period in our state's history.

Sources:
The Winds of Change: US Multifamily and Commercial Real Estate in 2021, Moody's Analytics
Apartment News, November/December 2020, Arizona Multihousing Association.

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» by Lucinda Smedley

As we close the books on the insanity of 2020, we are eager to ring in the new year which already promises to be a more uplifting one with an end to the pandemic within reach. We are hugely grateful to our contributors who have shared their expertise in this year's finance issue including Jodi Bain of The Bain Law Firm; Eric Freeman of Beach Fleischman; Caroline Janjić of Iridius Capital; Scott Stovall of National Bank of Arizona; Kevin Prouty, Tim Prouty, Brian Prouty, and Theresa Witz of CBRE Debt and Structured Finance Group; Ryan Johnson of Son Property Management; George W. Hammond, PhD of the Economic and Business Research Center in the Eller College of Management at the University of Arizona; David Ollanik for Sundt Construction; Cindy Hammond of Churchill Commercial Capital; Joe Snapp of Foothills Bank; and Matt Thrasher of Thrasher Law Offices. We are also grateful to include two new contributors in this issue—Sophia Gonzalez of Startup Tucson; and Suzanne Droubie, the newly elected Pima County Assessor, who has indicated that she will be providing regular updates for us to include in coming issues.

Closing 2020 with some good news, as discussed by Eric Freeman, Congress passed the Consolidated Appropriations Act on December 21st, 2020 which was signed into law by the President on December 27th, 2020. In addition to providing $900 billion in stimulus relief for the COVID-19 along with a $1.4 trillion omnibus spending bill for the 2021 federal fiscal year and preventing a government shutdown, the Consolidated Appropriations Act provides for $284 billion in funding to the Small Business Association for first and second PPP loans to businesses. This is really good news for small businesses.

Good news for Tucson—As discussed by Sophia Gonzalez, Startup Tucson's Remote Tucson pilot program received an overwhelming response. During the one month application period, from early November to December, the Remote Tucson website saw 4,000 visitors and received over 500 applications from 39 states across the country! About 60% of all applicants identified as "boomerangs"—individuals that lived in Tucson previously either growing up or attended college here. This indicates that as times have changed with COVID, prior members of our community are looking to return and contribute to Tucson's growth.

First Quarter 2021 Industry Events

March 4, 2021, 8–10am Pima County Real Estate Research Council will hold its First Quarterly Meeting which will feature a presentation by Sara Baker of Baker, Peterson, Baker & Associates on the findings from the Development Incentives Study that she is undertaking in partnership with Metropolitan Pima Alliance. Register at pcrerc.com.

March 26, 8am–12pm Join IREM, Southern AZ and Central AZ CCIM Chapters for a VIRTUAL Economic Forecast Event featuring KC Conway, Chief Economist for CCIM, and moderated by Pete Bolton of Pete Bolton Co. Register at https://southernazccimchapter.com/meetinginfo.php?id=24&ts=1608661570.

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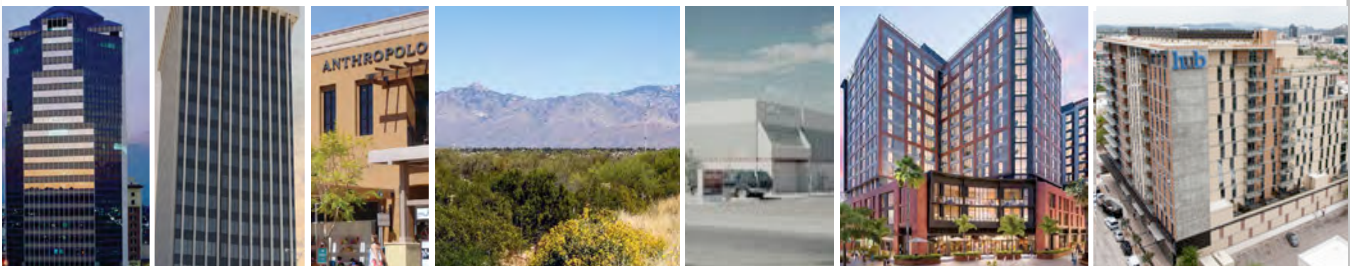

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