TREND report

Highlights from Pima County Real Estate Research Council's First Zoom Meeting on COVID-19 Impact

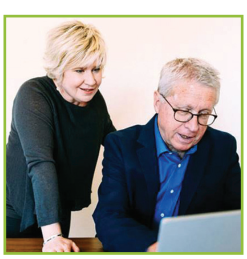
James B. Marian CCIM, MRE • published in the June 2020 issue

Did you hear a strange rumble in the morning a few weeks back? It was the great Roy Drachman, rolling over in his grave, as the Pima County Real Estate Research Council conducted its first ever quarterly meeting via ZOOM presentations by eight local real estate experts about the impact of COVID-19 on their businesses to date. Back in the early 1960's Roy, along with several other legendary real estate executives (such as Jim Sellers), had the foresight to form the Council, which is rumored to be the oldest, municipal real estate research organization in the nation. Think about it. Close to 60 years of uninterrupted local real estate research. Thanks again, Roy!!

Here is a summary of what our eight experts said:

Rosey Koberlein, CEO, Long Realty The residential real estate market was off to a great start in 2020, with excellent sales activity and rising prices. Then COVID-19 hit, local Long offices closed to the public, and pending contract activity fell by 30%. But surprisingly, things quickly turned around. For the past five weeks, pending contract activity has soared, and is now at a high for the year. Listing inventory for the under $500,000 price range is now under 1.7 months, which helps explain why many properties are receiving multiple offers, with some over the asking price. But wait, there's more good news. Google recently published that Tucson was the nation's #1 marketplace in terms of web-based residential searches pre- COVID to now, with a whopping 165% gain!! Low interest rates should keep demand levels high.

Randy Agron, VP, A.F. Sterling Initially, COVID-19 impact resulted in a 30% national drop in new home sales and a 34% decrease in new home starts. Here in Pima County, 218 single family housing permits were pulled in April, compared to 335 permits in April of 2019. Recently, there has been a significant uptick in both activity and buyer confidence. Homebuying traffic may be down, but almost all current Buyers are very serious Buyers, with less window-shoppers. A shortage of trade workers continues and the time to construct a home has increased approximately 30 days since COVID-19 began to impact the marketplace. Most in the business are cautiously optimistic about the future.



Jerry Hawkins and Kim Cole, Hawkins-Cole Hospitality The Hospitality market was off to a fantastic start this year, with occupancies in excess of 80%. By March, occupancies fell to below 30% and daily rates dropped by at least 20%. With Tucson International airport traffic down 95%, little if any turnaround is expected before October. All proposed projects are now on hold. However, construction continues on four local hotels. Food and beverage income are close to zero, which typically contributes from 30-50% of total hospitality income. No new local, regional, or national meetings are expected to be planned for 6–12 months. Unlike the past recession, Lenders appear to be much more willing to work with Owners. Some are offering 6–12-month forbearance periods.

Ross McCallister, CEO, McCallister Companies McCallister Companies owns and manages 5800 units in Arizona, Texas, and Oklahoma. When COVID-19 hit, the company immediately reached out to all tenants. The result has been a 95% rent collection level in April and, to date, 88% in May. Some tenants have gone on payment plans. The company's Tucson portfolio has performed the best with collection rates of 98% and 96% respectively. Major operational changes such as contactless apartment showings, application processing, and even minor apartment repairs where staff zoom sessions instruct tenants how to make repairs, have been surprisingly successful and well received. Special unemployment benefits have had a positive impact. However, future unemployment trends are a major concern. Nationally, class C projects have suffered the most, and class A the least.

Alex Hardie, Office Broker, Buzz Isaacson Realty The pre-covid marketplace was good, with declining vacancy rates. Overnight, leasing activity went to zero. To date, vacancy rates have increased in Tucson from 7.9% in April 2019 to 8.9%. The future is hard to predict. Some see many companies downsizing and/or increasing square footage per employee from 125 SF per employee back to 200 SF per employee. The immediate focus is on employee health and intense cleaning. Longer term, Landlords will look to technology such as touch-less access and improved HVAC systems and design. Depending on the industry, more shift work may evolve.

Rob Glaser, Industrial Broker/Principal, Cushman & Wakefield|PICOR Tucson's industrial market is comprised of approximately 44 million square feet.

- Half of this is owner-occupied, and half is "for lease" inventory.
- The vacancy rate at the end of the first quarter was 6.1%
- Of the 2.7 million square feet vacant, 52% is in space over 35,000 square feet in 11 properties, many with high degrees of functional obsolescence.
- The majority of the overall "for lease" inventory is in small bays under 10,000 square feet, currently 95% occupied and leased to small businesses. This is the segment of the market that we think is most vulnerable.

Commentary from two of the largest Business Park owners in Tucson:

- EastGroup: 848,000 square feet, is 99% occupied, has 13 tenants in seven buildings—don't anticipate losing any tenants.
- Presson Equity: 1,216,000 square feet, 92% occupied, 469 tenants in 14 Business Park Properties—have lost seven tenants to date and expect to lose twice that many over the next few months. They anticipate their occupancy will drop to 90%. In 2009, their occupancy dropped to 84.5%.

Factors that will positively influence industrial properties locally and may bolster Industrial as the strongest commercial asset:

- Amplification of e-commerce
- Need for last mile delivery
- Retail relocations—who needs to be on Main Street? Food prep and delivery as an example.
- Relocation of manufacturing—near and reshoring including expansion and relocation activity in Sonora, Mexico
- U A Tech transfer prospects
- Raytheon's recent $2 Billion contract
- 5G technology and development which is gaining some momentum in Tucson
- Continued Mining industry growth
- And to leave you on a high note, expansion of the Marijuana industry

Melissa Lal, President, Larsen Baker With a portfolio of 57 properties of which 80% is retail, Larsen Baker's occupancy rate was 93% in mid-March. That rate has not changed as of mid-May, although they have drafted 100 rent modifications, including 30 extensions and 60 deferrals. Approximately 60% of rents were collected in April and to date, 70% have been collected in May. Surprisingly, 8 new retail leases have recently been executed. All local Banks and Life Companies have been open to possible loan forbearance. The firm has retained a consultant to deal with CMBS servicers who have not been as cooperative so far. The firm is confident of the future with a loan-to-value ratio of only 49%. The next 3–6 months will be critical for many tenants as some work to re-work business plans. Unfortunately, many small businesses will close, forcing both landlords and brokers to become even more creative deal-makers.

Jeannie Nguyen, VP, National Bank of Arizona From 2015 into 2019, the Fed increased interest rates five times. Then in 2019, with an anticipated slow down, rates were decreased. Needless to say, COVID-19 changed life for all loan officers. Some borrowers have made deferral requests. Banks were flooded with PPP loan requests which resulted in 24/7 work schedules. National Bank of Arizona processed 5000 loans, averaging $42,000 per loan approval. However, the Bank is still processing round two requests, which will bring the national PPP loan total to over four billion dollars. At this time, there is some uncertainty with loan forgiveness requirements and constraints. A slow and steady rebound is expected.

Due to a lack of time, land was not discussed and so here are a few insights I can offer. The bad news is that other than fully improved residential lots, demand for raw land is close to zero. The good news is that to date and to my knowledge, very few existing land escrows have been canceled. What has changed is that National Home Builders have requested (and received) extensions from Sellers. Currently, they will not risk putting up non-refundable dollars and they will not close on existing transactions (again, other than fully improved lots). Builders want to be positioned to close on land deals as soon as the market is ready. Personally, I have several multifamily and commercial parcels currently in escrow, and again, Buyers so far, continue to spend planning and engineering dollars, but will not close at this time. Needless to say, demand for land will not return until the word absorption returns to our vocabulary.

The Council will meet (or ZOOM) together on August 20th at the Tucson Association of Realtors. Results of an updated research report on Pima County's residential marketplace will be presented That presentation was scheduled for our May meeting. As luck would have it, all research for the report was completed just before the COVID-19 disruption started, instantly leaving research results obsolete. The Council is honored to have Lucinda Smedley, *TRENDreport* publisher and Principal of Real Estate Consulting Groupy, leading all residential research efforts. To register for the meeting or for membership information, visit pcrerc.com.

Jim Marian is a founding Partner and designated broker for Chapman Lindsey Commercial Real Estate Services LLC. He is also an MRED adjunct lecturer and faculty member at the University of Arizona. He can be reached at jbm@ccim.net.