TREND report

Update: Multifamily Construction in Southern Arizona

Jim Tofel • published in the September 2023 issue

Southern Arizona's multifamily construction market has remained robust through the first half of 2023. While new multifamily construction starts have dropped significantly in other markets, Southern Arizona has thus far been immune to this slowdown.

The high inflation that plagued the construction industry in 2021–2022 has eased this year. Although costs in some areas, including electrical and HVAC, continue to rise, other trades, such as framing and drywall, have seen a small correction. Overall, we have been able to hold prices on projects that were bid out at the end of last year.

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Financing is now the biggest challenge facing the construction industry. As interest rates continue to rise, lenders are becoming more risk-averse. They are adding requirements on new projects, including reduced loan-to-value. These changes have made it more difficult to begin construction on projects, increasing the likelihood of last-minute project cancellations. For example, a developer told me last year that for every 0.1% interest rate increase, he had to generate an additional $300k in equity to build a 200-unit apartment project.

The second biggest issue in the construction industry is the electrical trades. New federal tax credits for electric vehicles and solar panels have increased demand for electrical gear and components, creating a significant backlog—typically between 12 to 20 months. Builders rely on just three suppliers for electrical gear, and they all have first-in, first-out production requirements. This is causing construction delays as long as three to six months on most projects.

Electrical-related problems may escalate next year if the proposed 2024 building codes, including the International Energy Conservation Code (IECC), are adopted by our local jurisdiction. As drafted, the 2024 code includes the following requirements:

- 75% of parking spaces must be EV charging-capable, and 20% must provide EV charging.
- Projects must allow for the installation of solar panels, which will require master metering, large distribution panels, and associated wiring.
- Projects must be built to accommodate future battery storage systems.
- Energy monitoring of R-2 occupancies, which will require the addition of sub-meters.
- Demand response HVAC, water heaters, and lighting controls.
- Energy recovery ventilators in all apartments larger than 500 SF.
- Increased insulation and building tightness.

Including all these requirements in local building codes could add between $15k to $25k per apartment to the construction cost. If you are considering a new multi-family project, I strongly encourage you to submit plans prior to the adoption of the 2024 code.

Southern Arizona developers have been progressing with their projects despite our current challenges. As we advance, we anticipate that new starts will proceed slower through the remainder of the year and into 2024. Because projects typically last 18–24 months, many construction trades would not feel this slowdown until 2025 and 2026. We would expect a 5–10% correction in construction costs at that point.

Jim Tofel is Managing Member with Tofel Dent Construction, and has over 250 multifamily projects to his credit. Jim's passion for providing housing opportunities for those less fortunate has propelled Tofel Dent Construction to being one of the leading affordable housing general contractors in Arizona and New Mexico. With Jim's leadership in the large multifamily project categories, including high-density market rate, senior living and mixed-use projects, Tofel Dent Construction is proud to have completed many successful projects. He can be reached at jtofel@tofeldent.com.