

The Emergent Value of Third City Markets

**Ranking and Evaluating 20
Under-the-Radar Markets in America**



A GRACEADA PARTNERS REPORT

Primary markets—New York, Chicago, Los Angeles—are still the dominant investment destination for institutional investors in the United States

They are long standing economic hubs that have stood the test of time over the last century. But, the pandemic has shifted how some people work, and this led to an uptick in people moving from primary markets and dispersing to secondary and tertiary cities in the U.S. The growth of secondary markets like Austin, Charlotte and Sacramento—the phenomenon and growth of what Graceada Partners refers to as the outpost economy—was only the beginning of this paradigm shift. The emergence of viable assets within third city markets have led institutional investors to further analyze these tertiary regions. Using industry data and an internal Graceada Partners formula to rank cities based on criteria ranging from cost of living to quality of life to home values, this report will detail the top 20 third city markets in the United States that could be poised for more investment attention in the coming quarters.

As America's population grows by roughly one million people each year, that doesn't necessarily mean that city centers will grow at the same rate. The decade of the 2020s is expected to bring the U.S. population 5% higher, but not all cities and states will see the same growth. Not all cities are created equal. While some states in the Midwest such as Illinois and Michigan will be on the lower end of this growth, there are emerging tertiary markets in those states witnessing population growth above state averages. States like Arizona and Texas are on the higher end of this population growth. Certain cities—regardless of their population projections over the next decade—are showing signs of opportunistic rent-to-income ratios and positive standards of living. [Deloitte](#) notes that “the residential sector continued its strong and stable run, buoyed by a competitive homebuying market and increasing consumer interest in single-home rental properties.”

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American population trends and movement of people reflects many things including values, affordability, and quality of life. There is a desire among people to pursue places where the grass is greener and embedded in the American dream is the spirit of people on the move. From the Gold Rush to the Great Migration and the modern Work-and-Live-Anywhere Movement during the pandemic, groups of people have been on the move for various reasons.

Modern migration taking place in the U.S. is centered on affordability and perceived quality of life. People are looking for cities with relatively lower rent or mortgage payments where they can cultivate a better work/life balance. For some, that means moving out of primary and even secondary markets into tertiary ones. There is an interesting trend of people and growth in what can be considered “third city markets,” defined generally as a city with 100,000 to 200,000 residents within several hours drive or a short plane ride from a major hub. These third city markets—hereby referred

to as TCMs—are paving the way for a more geographically diffused economy. There is some momentum toward certain TCMs and away from certain primary and secondary markets, particularly in the Heartland, the Southwest (the Cactus Belt), and portions in the Pacific Northwest and Mountain West (Western Interior).

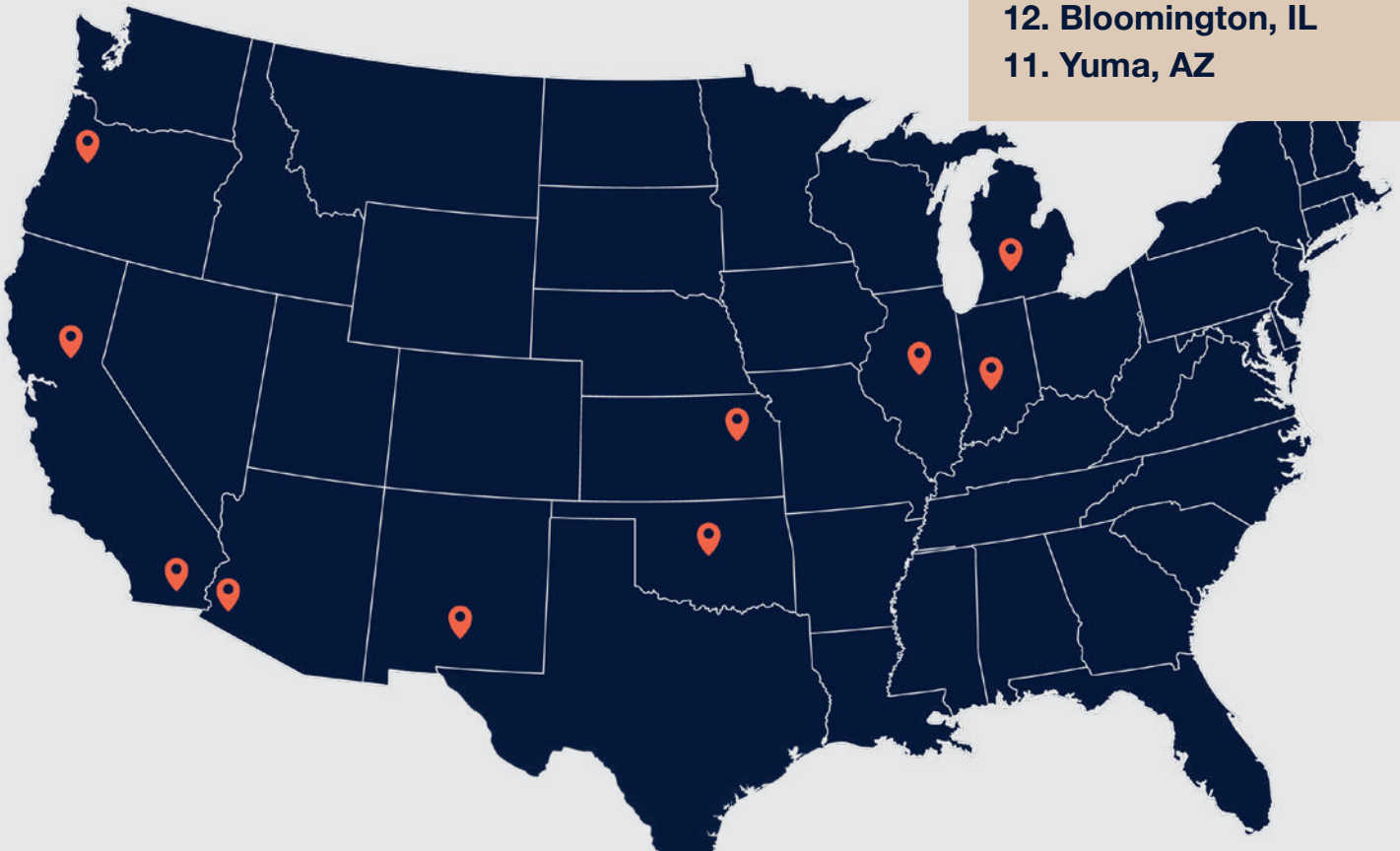
The Gravitational Pull Towards Third City Markets

With the dispersion of remote and gig workers away from major metropolitan areas and the increasing interest of investments in non-primary markets, second and tertiary markets are primed for incredible growth given the trends of the past few years. Nathan Metheny, the co-founder of [Wealth Rise Capital](#), said that “Healthcare and education are typical industries supporting tertiary markets which can be viewed as a main factor to the stabilization.” He went on to say that these micro-economies were recession resilient because of their financial growth and diversification. In Graceada Partners’ first ever ranking

of third city markets, we looked at more than 65 target markets across the U.S. that broadly fit our definition of a TCM.

From there, we compiled a list detailing the top 20 TCMs based on key criteria such as renter value, rent growth potential, and purchase value collected using CoStar, as well as quality of life measurement using AARP data. We also evaluated U.S. Census data to track population growth in regions. Our overall formula provides a comprehensive, unique measurement of the top 20 TCMs in the United States that may hold the most value for residents looking to move there and investors looking to build a portfolio in those areas.

- 20. Kalamazoo, MI**
- 19. Yuba City, CA (North)**
- 18. El Centro, CA (South)**
- 17. Topeka, KS**
- 16. McMinnville, OR**
- 15. Norman, OK**
- 14. Bloomington, IN**
- 13. Las Cruces, NM**
- 12. Bloomington, IL**
- 11. Yuma, AZ**



While a handful of TCMs had higher than average vacancy rates compared to the national environment, El Centro and McMinville had vacancy rates at 1.6% and 1.2%, respectively. Despite not being higher on the Top 20 List, they showed signs of growth that could lead these tertiary markets.

How an uptick in TCM growth could impact some secondary and primary markets

Given the rise of the concept of “Zoom towns,” TCMs will become appealing to those in proximity to a secondary or primary market. “By the end of 2020, 48% of Americans expressed an interest in living in small towns,” according to a [recent Twingate study](#) evaluating the “Zoom town” phenomenon, a reference to boomtowns of the 1800s that sprung up around newly discovered economic opportunities. Some of the growth of TCMs come from working professionals moving there remotely. This, in turn, creates demand for housing. And the influx of people creates more demand for consumer-facing businesses to support the influx of new residents (grocery stores, restaurants, gyms, etc.) which also need to hire.

Several years removed from the start of the pandemic, Americans are still rethinking where they want to reside as more employers create or make permanent work from home. As a result, some real estate investors may consider re-examining the markets where people are moving as viable investment opportunities.

Secondary markets will still be valuable for homebuyers, renters, and investors. TCMs will experience a similar, but less

pronounced, trend in the coming years. Part of this will be due to expansion from secondary markets into TCMs, as well as tertiary markets offering a greater opportunity-to-cost ratio than living in a nearby larger market. Yuba City, for example, may become one of these “Zoom towns” as former Bay Area or Sacramento residents move into this tertiary market. As the Gig Economy becomes more widespread, cities like Yuba City and other locations in Northern California may experience a piqued interest among institutional investors looking for opportunistic, long-term investments outside of San Francisco or the state’s capital.

Competitive secondary markets are driving some people to TCMs

As noted in Graceada Partners’ [Rise of the Outpost Economy report](#), office demand is increasing, financial rebirths are occurring in traditionally working-class cities, and the increase of untethered workers will propel professionals into less expensive geographic areas that still have a competitive edge in terms of living standards. This was true of workers leaving primary markets towards secondary markets, and also representative for those relocating from primary or secondary markets into tertiary markets. A more globalized world and interconnected financial community decentralizes where untethered workers choose to live. Simply put, more people have the luxury of living and working wherever they want. Yuma, Arizona—a border city equidistant from San Diego and Phoenix—is an example of this. Yuma is a TCM that shows considerable potential in a state that is projected to

grow by 12% between now and 2030 and is on our list of top 20 TCMs.

Except for a few outliers, average rent for many TCMs is in the \$900s. The states of New Mexico, Arizona, and Washington are expected to rise in population throughout the 2020s by over 10% each. With more people moving to these states and seeing the value in the TCMs within, we expect demand to continue to grow.

More competitive tertiary markets may catch the eye of investors who have traditionally not considered such markets. According to [Wealth Management](#), “Traditionally, larger institutional investors have been wary of the greater risk and reduced liquidity in smaller metros, as well as the challenge of being able to place capital at scale. However, many smaller metros are posting strong growth, which has been further fueled by the pandemic and remote working.”

Some major markets are witnessing a surge in population and increasing housing or development costs which make them unattainable for many people with smaller budgets. Take Seattle as an example. The average rent in Seattle is \$2,334 according to RentCafe, which is more than \$1,000 above the national average. However, Yakima, Washington is geographically close to Seattle while being far less expensive (roughly half the rent cost compared to the Emerald City). This makes Yakima appealing to workers who may be fully remote, or only need to show up to their Seattle office a few times a week.

Money speaks volumes, but quality of life is also quite relevant

Affordability is key, but quality of life has a value all on its own. Some of the high-performing cities on our list of TCMs made the cut not because they had the lowest rents or home prices, but because they offer both affordability and a high quality of life. La Crosse, Wisconsin for example—which is in the top 10—had the highest AARP Livability Index Score in the Top 20, coming in at 64. An AARP livability

score above 50 is impressive, but those ranked in the 60s and 70s are stellar.

Pueblo, Colorado, No. 8 on our list, has a price per unit for a one-bedroom of \$95,100, making it the only city in the top 10 with a five-figure value. Additionally, Colorado's population is expected to increase 14% by the time of the 2030 census. This state growth, coupled with Pueblo being a mere 40-minute drive from Colorado Springs and 90 minutes from Denver, showcases the likelihood that this TCM will continue to climb in value

and desirability from both residents and investors.

Looking at the top TCMs in the nation reveals multiple trends. It shows how smaller markets with a high quality of life can and are attracting new residents and retaining others who may have otherwise decided to leave in a different way. Here are five of the leading trends, exemplified in the top TCMs.



TREND 1:

Third City Markets are becoming an increasingly popular place to live and will grow as a place to live and invest in the next decade

Echoing the success and growth of fast-growing larger markets like Atlanta, Salt Lake City, and Austin, TCMs will find themselves seeing spillover from primary and secondary markets, creating accelerated prosperity and population growth in top TCMs with a higher quality of life. As shown in primary markets like San Francisco during the pandemic, many individuals began relocating inland to areas in and around Sacramento. This migration has led to further outpost economies in northern California, boosting the attractiveness of cities like Redding, California, No. 3 on our list of top TCMs. The [Milken Institute](#), in its 2022 “Best-Performing Cities” list even ranked Redding as the 4th best economic small city within the United States in 2022. This was a considerable improvement from Redding’s 2021 rank of 63rd on their list. Idaho Falls,

also on our Top 20 list of TCMs, was right behind Redding on the Milken Institute’s analysis, coming in respectively at fifth in Milken’s 2022 analysis, and sixth on our assessment.

With these trends and indicators in mind, some niche real estate investors may consider investment opportunities in attractive TCMs that wouldn’t have been on their radar only a handful of years ago. Our analysis reveals three major regions of the U.S. that hold many of the top 20 TCMs. These regions are the Heartland, the Cactus Belt, and the Western Interior. Colloquially, these regions typically fall into the Midwest, Southwest, and the Western U.S., respectively. TCMs in these regions appear to be well positioned to grow and attract more residents, potentially more than other American regions like New England or the Deep South. While

primary markets will continue to thrive, these emerging third city markets could become more competitive in their respective regions. Furthermore, some of the top 20 TCM cities on the list may witness rapid expansion that elevates their positioning as a city in America. For example, Raleigh, North Carolina, was roughly 200,000 people in the year 1990, and 30 years later finds itself more than doubled in population at over 450,000. Raleigh, a market with relative affordability and a thriving tech industry has brought in significant real estate investment.

Redding, CA



TREND 2:

Third City Markets offer increasingly more value to residents compared to some secondary markets

One of the top appeals to TCMs for residents is the general lower cost of living compared to larger markets in the U.S. Monthly rent costs and mortgage costs compared to average income in these markets demonstrates that they are particularly attractive for people looking for value.

Three cities in the top 5 TCMs have an average rent price below \$1,000. Compare this to Austin, Texas, one of the fastest growing secondary markets in the nation, where cost of living has skyrocketed of late and an average

apartment is now over \$1,800 per month. While some people will be able to justify the higher cost of living with higher comparable salaries, the reality is that average salaries in many primary and secondary markets simply aren't high enough compared to the low housing cost to income ratio of TCMs. The rent-to-income ratio in Bloomington, Illinois, is only 13%; it is under 20% in 8 out of the top 20 TCMs.

The buying power of renters and homeowners in these communities will be higher, making them more enticing

than nearby secondary markets with substantially higher rent costs. This enhanced value, leading to heightened demand for more affordable rentals, could equate to long term rent growth in cities such as Cheyenne, Wyoming, Rapid City, South Dakota, and Redding, California.



Bloomington, IL City Hall

TREND 3:

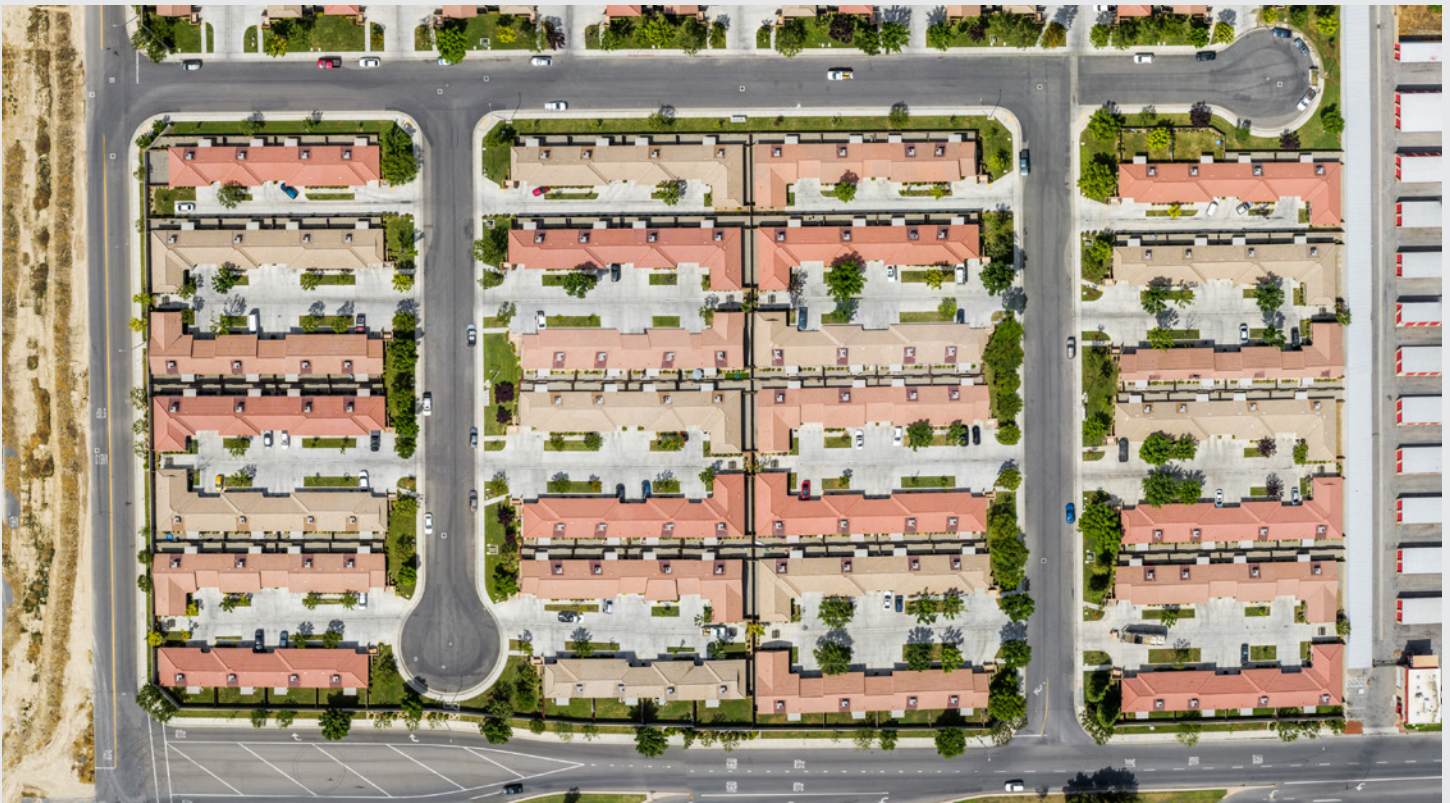
Multifamily properties are becoming increasingly expensive in secondary markets, which opens opportunities in TCMs

Parents with school-age children are moving away from large cities because of the pandemic. Analysis from the [Economic Innovation Group](#) published in July 2022 notes that 68% of large urban counties witnessed a decline in population during the pandemic and families with young children left in relatively large numbers. From July 2020 to July 2021, the number of children under five years of age in large urban counties (with a

population of at least 250,000 people) fell by 3.7% in one year. Regardless of their reasoning—whether it be lockdowns, cost of living, or quality of life—these families are settling into tertiary markets because of shifting priorities among some members of the American middle class.

The result of high inflation and a lack of space to build new multifamily properties in primary and secondary

markets are paving the way for America's middle class to be more dispersed across the country than was the case in the previous few decades. This is illustrated in some of the vacancy rates within the TCMs found on the Top 20 list, with Cheyenne, Rapid City, La Crosse, Bakersfield, Yakima, McMinnville, and El Centro all having vacancy rates below 2% as of late 2022.



A multifamily property acquired by Graceada Partners in 2022 based in Bakersfield, CA

TREND 4:

Industrial growth is creating expansion in some TCMs

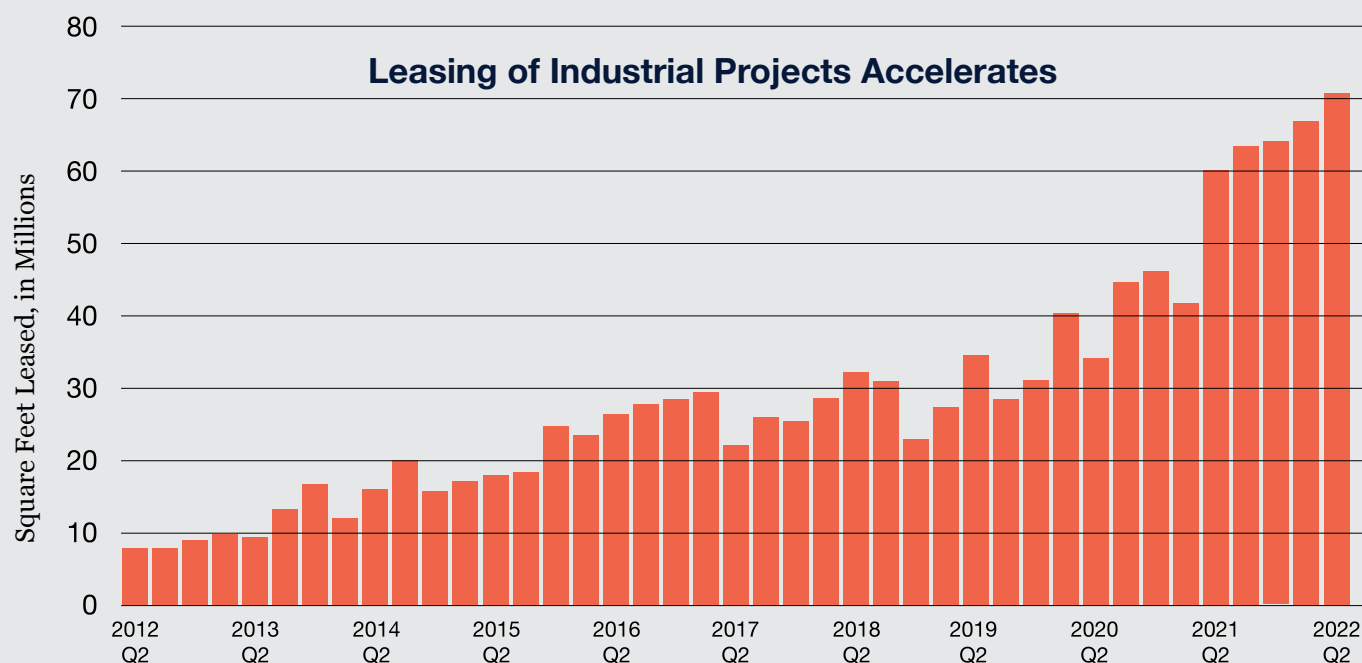
Nationwide, industrial real estate is witnessing strong demand, with industrial leases up 14% year-over-year with strong demand overcoming market uncertainty, [according to CoStar](#).

The industrial real estate sector in TCMs is a landscape ripe for growth—one of the benchmarks of potential upside in a third city market is the construction and addition of a major warehouse, like an Amazon facility. This is the case in Bakersfield, California, No. 9 on the list of top TCMs, where Amazon built a Fulfillment Center completed in 2019. Salem, Oregon—which found itself just outside the top 20 TCMs in our analysis—also had an Amazon Fulfillment Center open in 2019. The presence of Amazon facilities in some ways parallels areas that had

the railroad running through them in the late 1800s. A place connected by railroad received faster mail and more industrialized materials than an area far out of reach from the locomotive tracks. Being near a train station helped those regions gain prominence through expedited industrialization. Similarly, an Amazon warehouse brings job opportunities and better business delivery services while also creating opportunities for ancillary businesses supporting Amazon. It also can create demand for housing for the additional workforce needed.

[Globe St reported on Amazon's increasing footprint](#) in late 2021, noting that it has been on track to create 120 million square feet of warehouse space annually. In this

article, Graceada Partners' co-founder Joe Muratore noted that “Amazon distribution centers are anchoring industrial parks. When Amazon brands a spot and shows up, others want to be near it. Cities provide roads and infrastructure to support that. And it's happening largely in tertiary cities. This is wonderful for tertiary markets.” With more industry, there may be incentives for stronger infrastructure in TCMs. It's the concept of a perpetual cycle: local economic growth leads to better infrastructure, which leads to industrial investment projects, which leads to more local economic growth, and so on.



Leasing of Under Construction or Proposed US Industrial Properties

Source: CoStar, August 2022

TREND 5:

Companies recruiting in TCMs can build stronger company culture and diversity as populations expand and work environments shift

A company based in Denver, Colorado, that promotes itself as having a hybrid work environment may seek out talented employees in places like Pueblo, Colorado. Whether it's Pueblo residents that have lived there most of their lives or newcomers from a few months ago, companies in traditional office settings will be able to expand their employment pool. They will have a hiring advantage over those that require their workers to be in the office five days a week. Better selection of happy people in their desired living situation will open the doors for companies having more diverse candidates based across their state, region, and the nation.

Due to more flexible work arrangements, companies continue to expand their reach by hiring employees in secondary and tertiary markets. This could extend to new offices that act as satellites of central headquarters, as well as fully or partially remote workers. Recruiting in growing TCMs opens the door to prospective employees who may be unable to afford living in the city where the business's primary office is located. Increasingly hybrid and remote positions based in primary markets like San Francisco or secondary markets like Portland, Oregon, can recruit in TCMs located within a few hours—the talent in those TCMs can come into an office several times a month because they are

close enough while also enjoying a higher quality of life in the respective TCM they live in.

[According to Dice](#), Topeka, Kansas, saw one of the greatest shifts in new tech hirings in the summer of 2022—only a few hundred less people than San Francisco's new tech worker additions. For tech startups to remain competitive in the market, bringing in fresh perspectives is a quintessential strategy. Companies capable of shifting their workforce towards a hybrid or fully remote environment will have many advantages that traditional always-in-the-office companies will not be able to compete with.



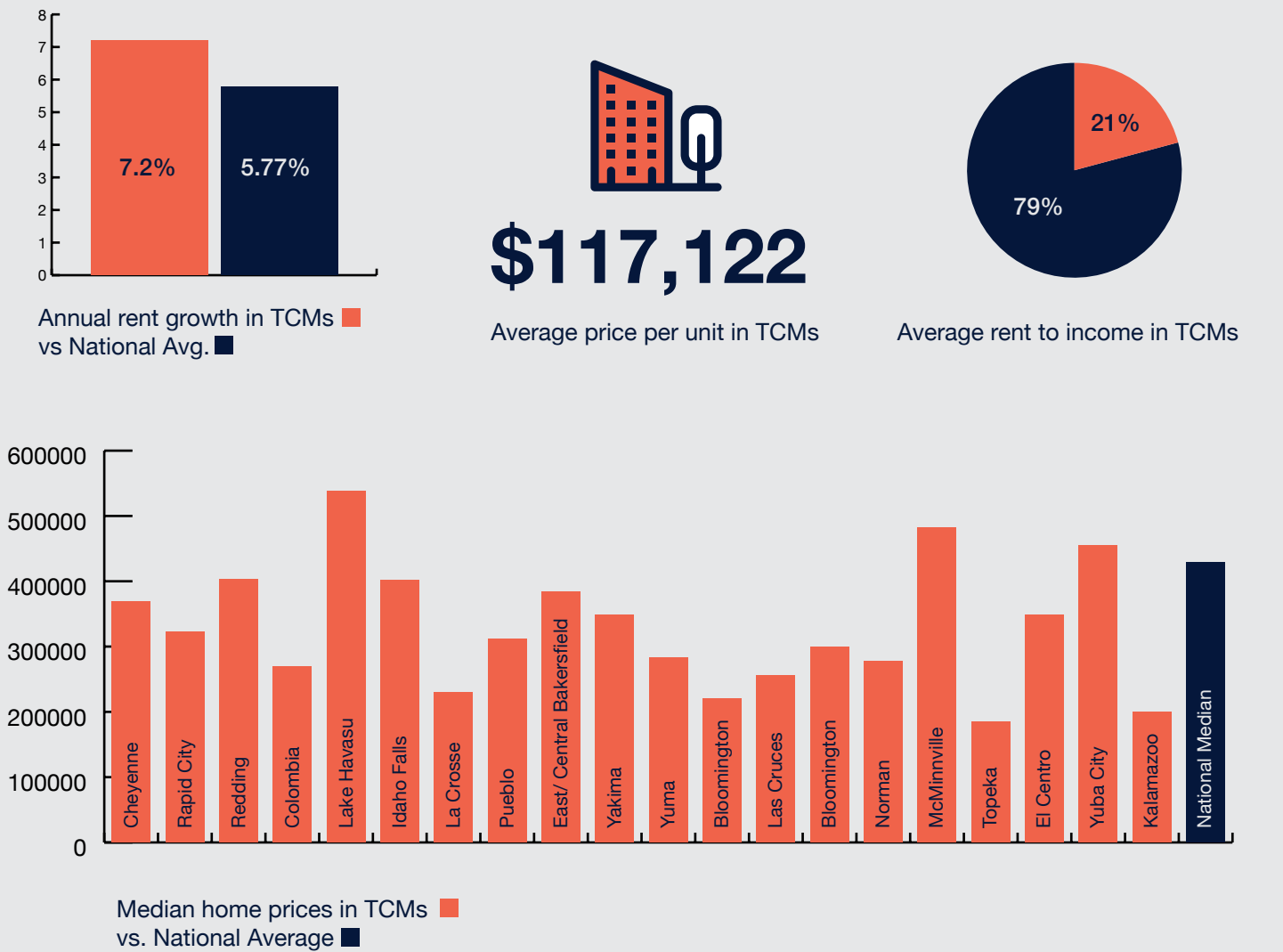
Looking ahead at potential opportunities in TCMs

Real estate investors who analyze some of the current trends of growth and affordability in TCMs may find an opportunity to grow their portfolios in a burgeoning TCM. With the higher interest rates ushered in in 2022 and a cooling housing market in some markets in the next year—along with potentially inflated home prices in some of the fastest-growing secondary markets—TCMs may be a place where investors and residents alike find the next frontier of value.

Some of the cities on our top 20 list may not become as profitable or viable for institutional investors as the real estate climate naturally shifts. Cities in New England or the Deep South may hold better financial opportunities than the ones analyzed. Demographic shifts, corporation migration, birth rate, vacancy rate, and numerous other factors will contribute to America’s tertiary markets’ success. However, this list serves as an indicator to the types of cities well positioned for growth in value in the foreseeable future. Comparing low median home prices and higher-than-average incomes is one example. Viewing

a low vacancy rate as it compares to a higher-than-average annual rent growth may indicate that a tertiary market offers a better quality of life. These and other contributing factors will continue to shape how potential residents and investors view the viability of America’s third city markets.

Data Snapshot



Data Table

	Vacancy	Avg. Rent	Annual Rent Growth	Avg. Income	Rent to Income	Median Home Price	AARP Score
Cheyenne, WY	1.3%	\$882	5.6%	\$63,235	17%	\$369,421	54
Rapid City, SD	1.6%	\$1,176	9.9%	\$53,760	26%	\$322,144	56
Redding, CA	2.0%	\$1,026	4.4%	\$56,098	22%	\$402,481	54
Colombia, MO	2.3%	\$949	9.10%	\$63,670	18%	\$270,000	51
Lake Havasu, AZ	2.7%	\$895	8.6%	\$55,887	19%	\$537,500	44
Idaho Falls, ID	2.4%	\$1,146	9.7%	\$56,590	24%	\$401,597	55
La Crosse, WI	1.4%	\$1,013	2.7%	\$66,767	18%	\$230,000	64
Pueblo, CO	2.2%	\$992	6.3%	\$42,902	28%	\$311,260	51
Bakersfield, CA	1.8%	\$1,066	9.2%	\$65,687	19%	\$384,077	41
Yakima, WA	1.7%	\$936	5.1%	\$48,220	23%	\$348,803	50
Yuma, AZ	3.0%	\$992	12.4%	\$52,183	23%	\$283,645	40
Bloomington, IL	2.4%	\$957	5.6%	\$85,630	13%	\$219,900	59
Las Cruces, NM	3.2%	\$960	11.0%	\$46,500	25%	\$256,047	41
Bloomington, IN	3.2%	\$1,115	7.7%	\$63,018	21%	\$299,900	53
Norman, OK	6.1%	\$935	7.20%	\$67,160	17%	\$277,117	50
McMinnville, OR	1.2%	\$1,200	5.5%	\$54,254	27%	\$482,326	58
Topeka, KS	9.1%	\$824	5.90%	\$67,161	15%	\$185,000	54
El Centro, CA	1.6%	\$962	4.4%	\$47,366	24%	\$348,548	45
Yuba City, CA	2.5%	\$1,090	4.7%	\$60,910	21%	\$455,477	48
Kalamazoo, MI	3.1%	\$1,105	8.4%	\$62,517	21%	\$199,900	53