MARKET REPORT

Multifamily

Minneapolis-St. Paul Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

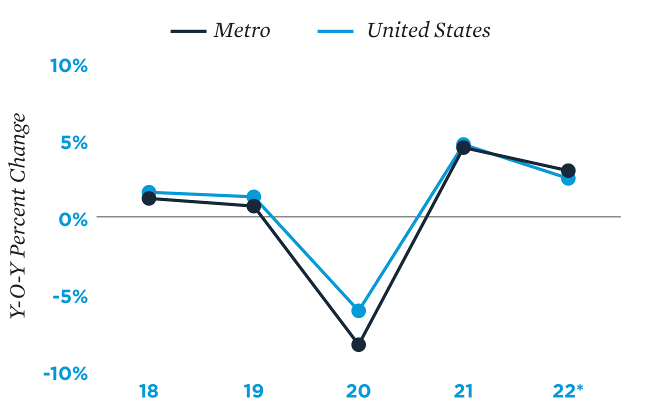
2Q/22

Rent Control Reshuffles Development; Downtown Makes Headway

Builders react to rent control. In November 2021, voters passed legislation to cap annual rent increases at 3 percent in St. Paul, one of the strictest ordinances in the nation as it applies to new construction. In response, building permits in the city plummeted by more than 80 percent during the November through January period, according to the U.S. Department of Housing and Urban Development. Just as many builders have turned away from St. Paul, they have ramped up construction plans in other parts of the Twin Cities. Multifamily permits in Minneapolis climbed more than 65 percent during that same span. An additional 11,000-plus units are already underway in the market, excluding St. Paul. Push back from developers and operators prompted a senate bill aiming to retroactively overturn the measure, but the policy remained in place as of April.

Downtown Minneapolis moving in the right direction. Rental demand in the urban core of Minneapolis was disproportionately impacted by the health crisis and coinciding shift to remote work. The submarket had a vacancy rate 150 basis points higher than any other area in the metro, entering April at 6.3 percent; however, tailwinds are building, with availability easing 110 basis points during the past year. The vacancy moderation should continue in 2022 as more firms bring workers into the office, boosting the allure of nearby living options. Wells Fargo and U.S. Bancorp announced hybrid returns to the office in the first quarter of 2022.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.; RealPage, Inc.

Multifamily 2022 Outlook

58,000 JOBS
will be created

EMPLOYMENT:

The Minneapolis-St. Paul metro had an extremely low unemployment rate, at 2.7 percent in March 2022. This could limit hiring activity, producing a smaller job addition relative to last year. Nonetheless, the personnel count grows by 3.0 percent in 2022.

8,500 UNITS
will be completed

CONSTRUCTION:

Inventory growth exceeds 2.5 percent for the third straight year; however, the 2022 volume will be roughly 700 units below last year's. Locations that will add the most new space include South St. Paul-Eagan, Anoka County and Downtown Minneapolis.

10 BASIS POINT
increase in vacancy

VACANCY:

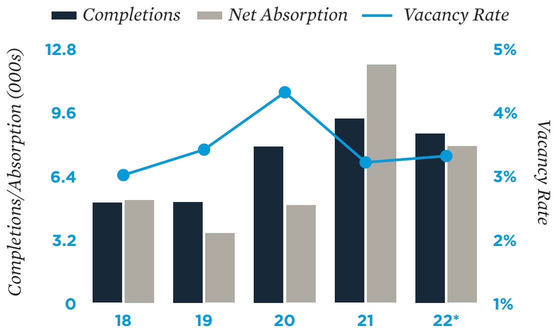
Vacancy ticks up to 3.3 percent, as net absorption measures 600 units short of completions. Despite the mild rise in availability, the rate will be low by historical standards. The metro recorded an average vacancy level of 3.6 percent from 2010-2020.

3.9% INCREASE
in effective rent

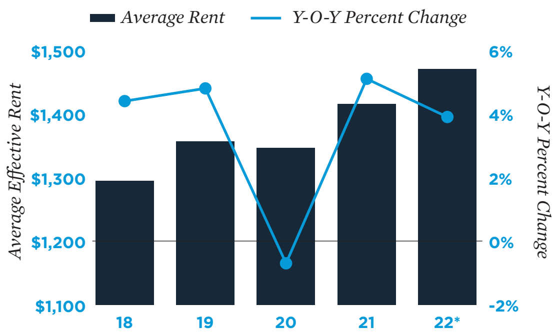
RENT:

Rent growth falls short of last year's 5.1 percent elevation, with the average effective rate moving up to $1,471 per month. Annual rent hikes that trail results for other low-vacancy metros are typical in the Twin Cities.

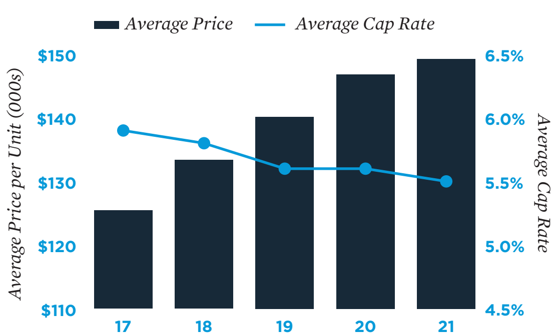
Supply and Demand



Rent Trends



Sales Trends



* Forecast

Sources: CoStar Group, Inc.; Real Capital Analytics; RealPage, Inc.

IPA Multifamily

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Price: $250

1Q 2022 - 12-Month Period

CONSTRUCTION

9,772 units completed

- The past four quarters ended in March were an active development period, beating the previous yearlong total by almost 2,000 units delivered. Six different submarkets had 3-plus percent stock expansions during that span.
- More than 1,200 units are projected to finalize in Anoka County in 2022, growing the submarket's stock by about 4.5 percent this year.

VACANCY

130 basis point decrease in vacancy Y-O-Y

- After peaking at 4.7 percent in the first quarter of last year, vacancy in the Twin Cities dropped to 3.4 percent in March 2022. Suburban availability descended near 3.0 percent and could hold there.
- In March 2022, vacancy rates in all three apartment tiers were within 10 basis points of their respective pre-pandemic marks.

RENT

7.1% increase in the average effective rent Y-O-Y

- Rent gains during the past 12 months reversed the 2.1 percent contraction logged from April 2020 through March 2021. The metro's average effective rent was $1,439 per month in the first period of 2022.
- Amid higher than normal vacancy, the Downtown Minneapolis-University area recorded the market's slowest annual rent gain, at 3.9 percent.

Investment Highlights

- Trading activity surged last year, with deal volume exceeding both 2020 and 2019. Despite this lift, the average sale price grew by the smallest amount in 10 years, inching up to $149,300 per unit in 2021. As rental metrics in the suburbs were strong during the pandemic, while performance lagged in the urban core, investors focused heavily on outlying areas, where prices tend be lower on average.
- Exemplifying the trend of buyers expanding their searches outward, Pierce and St. Croix counties in Wisconsin noted significantly higher levels of trading over the past few quarters. Suburbs including Hudson and River Falls attract local private investors, often targeting Class B and C buildings with fewer than 100 units. First-year returns in the low-to-mid-6 percent band are recorded for these types of trades.
- Out-of-state buyers from the east and west coasts have been active participants in the market in early 2022, as they seek higher returns than those found in their home markets. Class A apartments in suburbs west and south of Minneapolis, like Minnetonka and Burnsville, are intriguing amid strong household formation. Prices for luxury suburban assets in these areas often exceed $250,000 per unit.