MARKET REPORT

Multifamily

Minneapolis-St. Paul Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

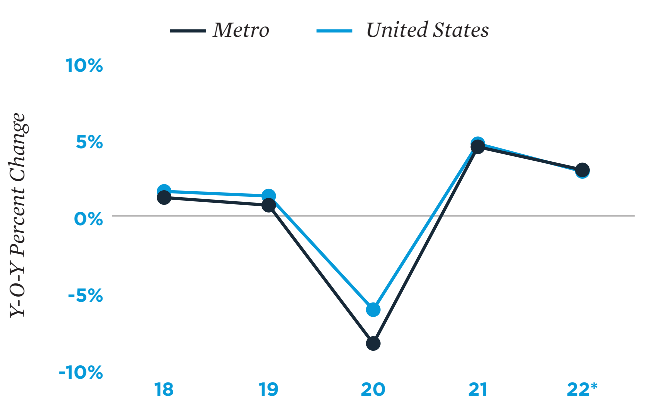
3Q/22

Return to Office Calls for Internal Migration; Development Shifts in Wake of Rent Control

Demand gravitates back to Minneapolis. The metro experienced its lowest unemployment rate on record at 1.7 percent in the second quarter this year, a positive signal for rental demand. Home to six Fortune 500 companies, Minneapolis has a greater prevalence of higher-paying opportunities and office-based employers than St. Paul. As more firms bring workers back into the office, employees that were taking advantage of remote work will likely seek living options closer to their jobs. This may have contributed to the sharp Class A/B vacancy drops recorded during the first half in Bloomington, South Minneapolis-Richfield and Uptown-St. Louis Park. Conversely, demand for upper- and mid-tier rentals in Central and East St. Paul slowed during the opening six months, as some residents likely migrated across the Twin Cities.

Construction accelerates in Minneapolis. Stimulated by rent control legislation passed late last year, construction starts and proposals in the St. Paul submarkets have plummeted. The diminished incentive to build here with rent caps applying to new construction, coupled with a growing labor force and renter pool in Minneapolis, is shifting development. The active pipeline is already starting to show this, with roughly 5,550 units underway in greater Minneapolis compared to 3,500 units in St. Paul. The impacts of rent control in St. Paul are beginning to be seen, as year-over-year effective rents in Central St. Paul rose 2.4 percent, while Minneapolis saw rates grow 10.7 percent during that span.

Employment Trends



* Forecast

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

Multifamily 2022 Outlook

58,000 JOBS
will be created

EMPLOYMENT:

Following the metro's historically low unemployment rate in the second quarter, job creation is set to slow. This will ease employee additions to a 3 percent increase by the end of 2022, helping return total employment to the 2 million mark.

8,300 UNITS
will be completed

CONSTRUCTION:

Inventory in the Twin Cities will grow by 2.7 percent in 2022, as more than 3,500 units are anticipated to go online in the second half of the year. Of these new units, the majority will arrive outside of the St. Paul metro amid rent growth cap concerns.

90 BASIS POINT
increase in vacancy

VACANCY:

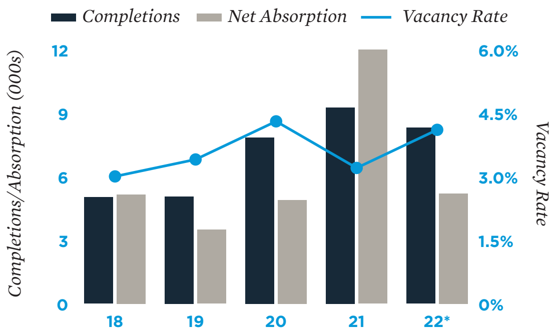
The Twin Cities will start to experience a cool off in demand as construction starts to catch up. Breaching the 4 percent mark by the end of the year, vacancy will exceed that of pre-pandemic levels.

5.1% INCREASE
in effective rent

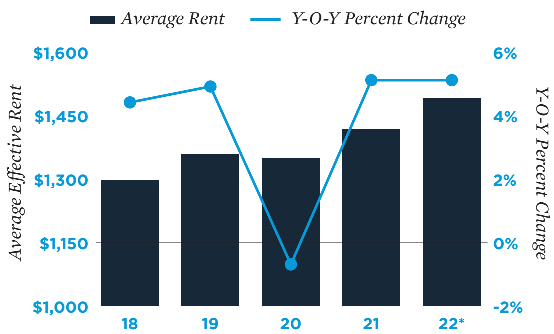
RENT:

Effective rents will continue to grow at an above-average rate in 2022, about matching the pace of last year. Recovered employment and demand have helped boost rent growth, as it nears $1,500 per month on average.

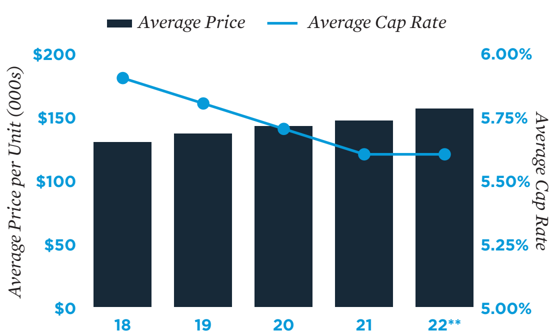
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

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

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2Q 2022 - 12-Month Period

CONSTRUCTION

10,492 units completed

- The Minneapolis metro continued to ramp up construction during the 12 months ending in June, making up roughly two-thirds of all new units.
- The South Minneapolis-Richfield submarket had the most amount of inventory growth, adding 6.7 percent over the past four quarters.

VACANCY

40 basis point decrease in vacancy Y-O-Y

- Vacancy was down year-over-year in the second quarter of 2022, however, the drop was smaller in magnitude than in the prior four quarters.
- The South Minneapolis submarket experienced the largest decline in vacancy year-over-year at 170 basis points, followed by the Bloomington and Uptown-St. Louis Park submarkets, each with 150 basis points.

RENT

7.3% increase in the average effective rent Y-O-Y

- Escalating rent growth over the previous four quarters brought the average effective rent to its highest point on record at $1,418 per month.
- Minnetonka, a western submarket of Minneapolis, continues to show high demand as year-over-year rent growth persists into the double digits in the second quarter of 2022.

Investment Highlights

- Transaction velocity in the Minneapolis-St. Paul metro held steady over the last 12 months ending in June, compared to the same period in 2021. Total dollar volume, however, increased over 75 percent between the two periods. This correlates with the return of well-capitalized investors, who often concentrate on larger-scale suburban apartments and upper-tier complexes in the urban cores, contributing to the higher dollar volume metric.
- Institutions continue to increase their positions in the metro, due to strong yields, economic growth and renter demand, fostering positive sentiment. This is reflected in the 8 percent year-over-year hike in the average price per unit to $156,100. Nonetheless, this mean price point is still more than 10 percent below nearby Chicago, capturing the focus of some regional institutions. The average cap rate in the Twin Cities metro remained unchanged at 5.6 percent, which is significantly lower than Chicago's mid-6 percent mean.
- Record-low unemployment and a rising median household income have boosted investor optimism in the urban areas of the market. The Class A vacancy rate in Downtown Minneapolis-University came down 50 basis points over the past year, yet remains the highest in the metro. Institutions will ramp up activity as top-tier vacancy here realigns with 2019 levels.