MARKET REPORT

Retail

Minneapolis-St. Paul Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

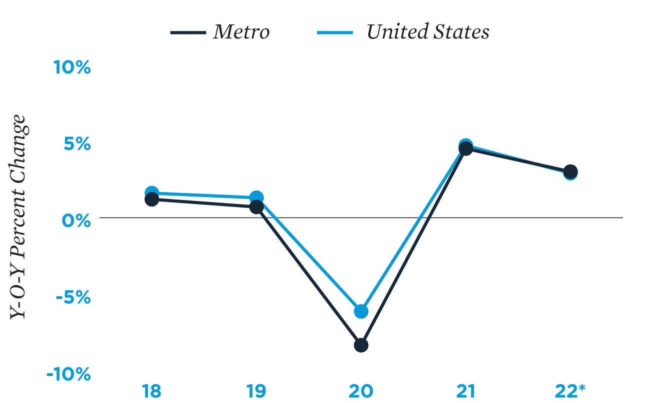
3Q/22

Availability Tightens Across the Twin Cities; Positive Fundamentals Helping St. Paul Recover

Vacancy compresses in nearly every submarket. Historically low unemployment and above-average consumer spending backed strong positive absorption in each of the last four quarters ending in June, totaling over 1.3 million square feet — the largest amount in that span since 2016-2017. Heightened leasing during this period resulted in strong year-over-year vacancy compression in most of the metro's submarkets. Locales experiencing significant vacancy drops consisted of Maple Grove, Southdale, St. Paul and West St. Paul, all of which had triple-digit declines year-over-year in the second quarter. Of these submarkets, Maple Grove is the only one to have lower than pre-pandemic vacancy, irrespective of its noteworthy construction pace, with local inventory increasing by 0.5 percent.

Downtown St. Paul still recovering. Availability below 2 percent amid positive absorption throughout 2018 and 2019 fortified a very strong retail landscape in St. Paul's urban core, prior to the pandemic. However, the submarket has faced pronounced challenges during the health crisis, and fundamentals are still working their way back. The rebound is gaining headway with vacancy here dropping 250 basis points over the yearlong period ended in June to 4.8 percent, with tenants absorbing a net of 160,000 square feet during that span. Limited construction has helped direct expanding retailers to vacant space. Given St. Paul's positive apartment metrics of vacancy compression, net absorption and rent growth, increased foot traffic and retail spending should bolster its retail recovery.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Retail 2022 Outlook

58,000 JOBS *will be created*

EMPLOYMENT:

Job growth continues in the Twin Cities, with unemployment falling to its lowest point on record of 1.6 percent in July, before inching up to 1.7 percent in August. Payrolls will increase 3.0 percent by year-end, as expansion slows compared to 2021's pace.

450,000 SQ. FT. *will be completed*

CONSTRUCTION:

For the second consecutive year, completions in the metro will fall below 1 million square feet, a trend that had been maintained for the previous seven years. Single-tenant space makes up the majority of the active pipeline at roughly 75 percent.

40 BASIS POINT *decrease in vacancy*

VACANCY:

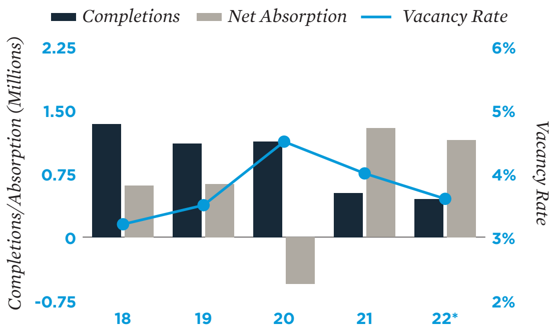
Backed by over 1.1 million square feet of anticipated net absorption, availability will decline to 3.6 percent. Tight conditions will continue in downtown-adjacent suburbs, as additions work to catch up to demand.

5.4% INCREASE *in asking rent*

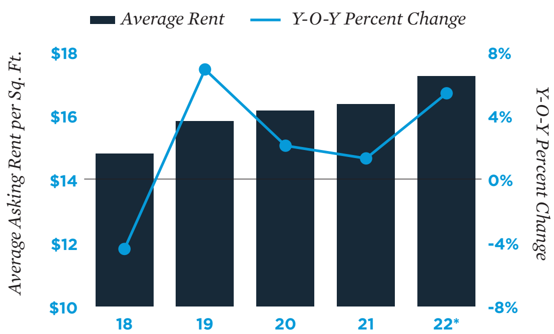
RENT:

Little vacancy in the market will continue to drive higher rent on available space during the second half of the year. The average asking rent in the market is set to rise to $17.25 per square foot, 9.0 percent higher than the year-end 2019 figure.

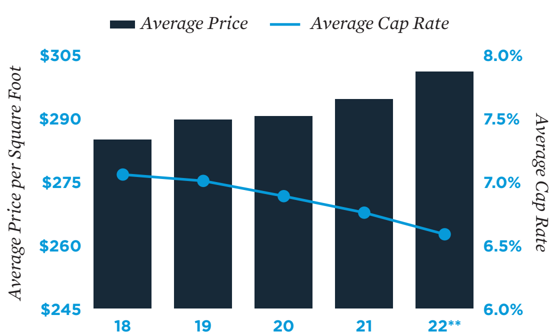
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

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Price: $250

2Q 2022 - 12-Month Period

CONSTRUCTION

514,000 sq. ft. completed

- Completed space in the last 12 months ending in June fell short of the 600,000 square feet mark for the first time since midyear of 2012.
- The Eagan submarket had the most space go online in the past year, as over 90,000 square feet was completed. This was followed by Wright County, with more than 64,600 square feet of additional inventory.

VACANCY

50 basis point decrease in vacancy Y-O-Y

- For the fourth consecutive quarter, vacancy in Minneapolis-St. Paul compressed year-over-year, falling to 3.8 percent at midyear.
- Low completions have supported continued vacancy contraction in multi-tenant space. The segment recorded a 160-basis-point decline to 5.4 percent in June, yet the rate is up slightly from the first quarter.

RENT

5.7% increase in the average asking rent Y-O-Y

- Properties in several affluent suburbs, such as Eagan, Woodbury and Coon Rapids, have reported above-market rent growth, as have St. Paul and Brookdale, where household density is high.
- Multi-tenant asking rent jumped 11.4 percent on average in the second quarter, its biggest year-over-year increase since the start of 2020.

Investment Highlights

- Trade velocity across the Twin Cities expanded roughly 25 percent in the yearlong period ending in June, as total transactions approached their highest point on record. This increase in trades was mostly due to multi-tenant deals jumping over 50 percent during the year, while single-tenant acquisitions held consistent.
- With transaction velocity rising, paired with record-low interest rates in the second half of 2021, dollar volume jumped over 75 percent across all retail properties and 130 percent in multi-tenant assets. This correlated to a 20-basis-point compression in the average cap rate for both asset types, while the multi-tenant price per square foot expanded 4 percent compared to single-tenant growth of 2 percent.
- The Rosedale and Woodbury submarkets welcomed the highest number of transactions over the past year ending in June. Of these trades, roughly 45 percent had an out-of-state buyer, as coastal investors look to Minnesota for more affordable entry costs and higher yields. Coon Rapids, on the other hand, experienced the largest decline in trades of any submarket, down over 40 percent as triple-digit vacancy hikes in the second half of 2021 deterred investors. Stabilizing availability this year may shift sentiment.