MARKET REPORT

MULTIFAMILY

Minneapolis-St. Paul Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

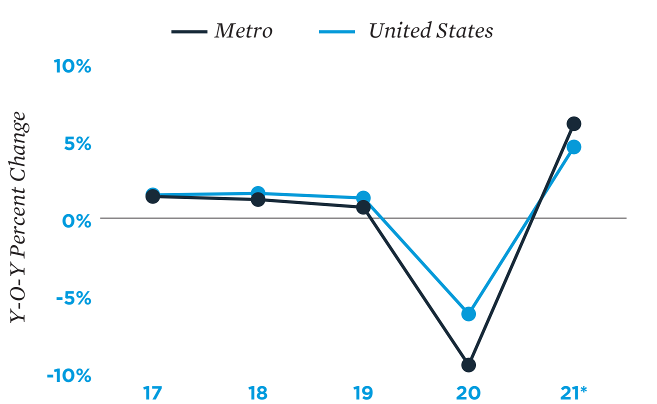
3Q/21

Rising Homeownership Costs Refocus Residential Demand on Upper-Tier Apartments

Pandemic hurdles begin to dissipate. Apartment segments more impeded by the health crisis and surge in unemployment are turning the corner as jobs are added and the economy reopens. In the second quarter, Class A vacancy declined by 120 basis points. Prior to this, availability in the tier had risen in six consecutive quarters. The stronger performance can be partially attributed to the single-family housing market. Minneapolis-St. Paul's median home price was up nearly 23 percent year over year in June, which in turn has bolstered upper-tier apartments' appeal as a cost-effective alternative. The recovery in downtown locales is also gaining traction as desirable urban amenities like shops and entertainment have reopened and more young adults are finding jobs in these settings. Central St. Paul posted a vacancy contraction of 280 basis points in the second quarter while Downtown Minneapolis-University had a 80-basis-point ease.

Large construction pipeline may temper the pace of recovery. Apartment completions in the metro will notch a 20-year high in 2021, which could present additional obstacles in the recoveries of a few submarkets. The fastest annual inventory expansion of 4.5 percent will take place in South Minneapolis-Richfield, a locale where vacancy was up year over year in the second quarter. Supply in North Minneapolis will also grow by more than 4 percent this year, though availability here was down from June of 2020. Local stock enlargements will exceed 3 percent in Downtown Minneapolis-University and Uptown-St. Louis Park as well, places where vacancy was up at least 100 basis points year over year.

Employment Trends



** Forecast*

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

Multifamily 2021 Outlook

113,000 JOBS
will be created

EMPLOYMENT:

Following the reduction of 194,700 personnel in 2020, the market will grow its worker count by 6.1 percent this year. The unemployment rate was 4.0 percent in June, up from 2.9 percent before the pandemic but still well below the national level.

8,200 UNITS
will be completed

CONSTRUCTION:

Completions in 2021 will grow metro inventory by 2.8 percent as the annual delivery volume exceeds the trailing-five-year average by about 3,000 units. By comparison, supply in the U.S. will expand by 2.1 percent this year.

0 BASIS POINT
change in vacancy

VACANCY:

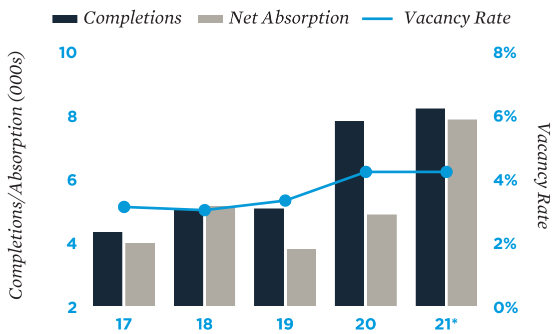
Greater demand for rentals will be equalized by the influx of new supply, keeping the vacancy rate firm at 4.2 percent in 2021. Availability in Minneapolis-St. Paul had risen in each of the prior two years, including a 90-basis-point jump in 2020.

3.9% INCREASE
in effective rent

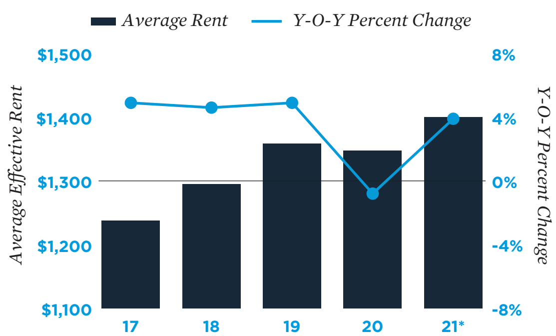
RENT:

The average effective monthly rent will move up to $1,400 as the market takes positive strides to make up lost ground after rent fell by 0.8 percent in 2020. Strengthening demand coupled with a wave of new luxury apartments will provide a boost.

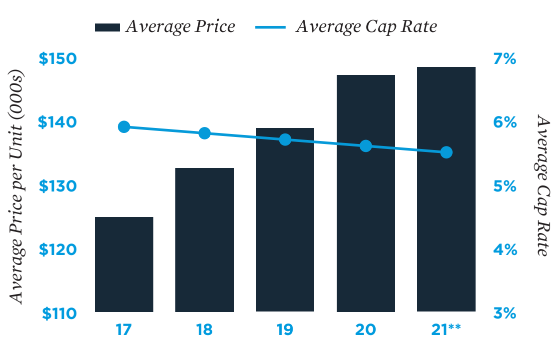
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

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

IPA Multifamily

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Price: $250

2Q21 — 12-Month Period

CONSTRUCTION

8,863 units completed

- Builders finalized roughly 2,600 more units during the past year ending in the second quarter than in the previous 12-month period. As of July, nearly 15,200 additional rentals had broken ground.
- In the past four quarters the Burnsville-Apple Valley and Uptown-St. Louis Park submarkets had stock enlargements greater than 5 percent.

VACANCY

30 basis point increase in vacancy Y-O-Y

- Availability in the metro tightened from 4.7 percent in March to 4.0 percent in June as net absorption in the second quarter surpassed 4,000 units for the first time in five years.
- Vacancy in the suburbs rose 20 basis points year over year to 3.7 percent, contrasting the national suburban 70-basis-point decline.

RENT

0.3% decrease in the average effective rent Y-O-Y

- Stunted by a 4.2 percent annual reduction in Class A rates, the metro's mean effective monthly rent retreated to $1,368 in June. Class A rates grew 2.0 percent in the second quarter, though, signaling momentum.
- The average rent in the Downtown Minneapolis-University area abated in each of the past five quarters, down 14.5 percent during that span.

Investment Highlights

- Minneapolis-St. Paul remains a top priority for investors as historically strong fundamentals outweigh near-term hurdles. Deal flow during the past 12 months ended in June jumped by one of the largest margins among major U.S. markets. The expanded buyer pool contributed to assets trading for higher prices and lower cap rates on average. The mean per unit cost was $148,000, while the average cap rate for assets traded during the past four quarters ended in June was 5.5 percent.
- Assets in the Outlying St. Paul locale, which encapsulates neighborhoods north of the city core between Interstate 94 and State Highway 36, traded four times as often in the past four quarters as in the previous year. This was primarily attributed to several large portfolio deals of Class C apartments. Lower-tier complexes here trade below the market average at roughly $120,000 per unit.
- Buyers concentrating on higher-quality buildings are setting their sights on western suburbs like Maple Grove, Plymouth and Shakopee. Entry costs here for Class A/B apartments often exceed $150,000 per unit with top-tier properties sometimes doubling that price point.