

Executive Summary

Twin Cities Commercial Real Estate Market Begins to Show Signs of Recovery

The Twin Cities commercial real estate market showed signs of recovery in 2011, with vacancy declining across most property types amid some signs of an improving economy. Market-wide, vacancy declined to 15.2% for direct space (17.6% overall across all property types)—reversing a three-year slide that saw direct space vacancy go from 11.5% in 2007 to 15.9% in 2010. The market recorded 1.6 million square feet of positive absorption, breaking a two-year skid that brought the market deep into negative territory.

BULK INDUSTRIAL DRAWS INVESTOR INTEREST

Large national investors showed significant interest in Twin Cities industrial properties in 2011, particularly newer bulk/warehouse product. The number of investment sales in bulk industrial properties was the highest seen in the Twin Cities in more than a decade, including at least 10 high-profile deals. Institutional investors are again looking closer at investment opportunities in the Twin Cities, including well-positioned grocery-anchored retail centers and multi-family properties.

DEAL-MAKERS DELIGHT IN OFFICE MARKET

Large office space users were active in the Southwest submarket, which posted 456,000 sf of positive absorption for the year, its highest number in more than a decade. The overall Twin Cities market experienced 484,000 sf of absorption. Class A property owners were the main beneficiaries, and increased demand for class A space was also evident in the West and Minneapolis Central

Business District (CBD) submarkets. Investment activity continued to rebound in the office sector in 2011, resulting in more than \$800 million worth of sales volume. Several significant transactions closed in the second half, and the pipeline of potential deals is relatively robust going into 2012.

MULTI-FAMILY CONSTRUCTION BOOM UNDERWAY

Resurgent demand for rental housing is fueling a boom in new multi-family apartment construction in the Twin Cities. Developers added approximately 900 new market-rate units in 2011 and another 1,300 units are slated for completion in 2012. Rental rates are rising in the face of rapidly declining vacancy rates, giving developers reason to invest in new construction. Much of the apartment development is taking place in urban areas such as the Minneapolis CBD and the Uptown area in south Minneapolis.

RETAIL PROPERTIES BENEFIT FROM MEDICAL SPACE USER DEMAND

Healthcare providers have been locating patient-friendly primary care and specialty practice clinics in high-profile retail sites, taking both existing second-generation retail space and also building new locations on land adjacent to existing centers. Retail center owners are more open to accommodating medical space users given existing market conditions.

Vacancy among all retail property types is 8.4% for direct space, down from 9.8% at year-end 2010. Major retailers are expanding in the Twin Cities area, fueling an

uptick in construction activity. Regional mall space is at a premium, as evidenced by an overall vacancy rate of 1.3% among the area's eight such properties.

OUTLOOK

Construction projects will be more numerous in 2012. Retail alone will see about 1 msf of new construction in 2012, led by big-box retailers. More multi-family projects are in the works as demand for rental units is expected to continue to grow. The market will likely also see more construction of large, single-user bulk/warehouse distribution facilities to meet the needs of users who cannot find the space they need in the current inventory.

The office and industrial leasing markets are expected to experience solid growth in demand in 2012, mostly in the second half of the year. Investors may broaden their search for more Twin Cities opportunities in 2012, while the supply of lender-owned office properties put back on the market for sale will also likely increase. Well-positioned retail centers can anticipate improvement in demand, including from some medical space users.

MORE ONLINE

More information by submarket and/or product type, including:

- Vacancy, absorption and rental rates
- Transaction activity
- Investment sale activity
- Projections for the next 6-12 months