Yardi® Matrix

Twin Cities: Healthier Than Ever

Multifamily Report Summer 2017

Occupancy Rate Tops Nation

Investors Eye Class B, C Suburban

Developers Target Core Submarkets

Market Analysis

Summer 2017

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Strong Demand Augments Occupancy Rate

A strong job market has kept the economy on sound footing in Minneapolis–St. Paul, sustaining one of the lowest unemployment rates in the country, at 3.5% as of June. The healthy economy and strong multifamily fundamentals should continue to attract investors and developers to the metro.

The education and health services sector is leading growth, having added 20,000 jobs year-over-year through June. The area's health-care industry—led by Fortune 500 companies that include powerhouse UnitedHealth Group, as well as St. Jude Medical, which Abbott recently acquired—is bound to remain a constant source of new employment. World-renowned Mayo Clinic is the anchor partner in the $5.6 billion Destination Medical Center project in Rochester. At the same time, the University of Minnesota and the University of St. Thomas enroll more than 60,000 students, feeding a deep talent pool.

Multifamily demand remains strong—especially for market-rate apartments—and has led to rising rental rates and the highest occupancy rate among major U.S. metros, at 97.7% as of July. However, the roughly 6,500 units slated to come online this year are bound to alleviate some of that demand in the short term. In the 12 months ending in July, rents in the metro rose 4.0%, well above the 2.6% national average. Just shy of $1,200, Twin Cities rent still trails the $1,350 U.S. average. These fundamentals have led Yardi Matrix to project rent growth of 3.9% in 2017.

Recent Twin Cities Transactions

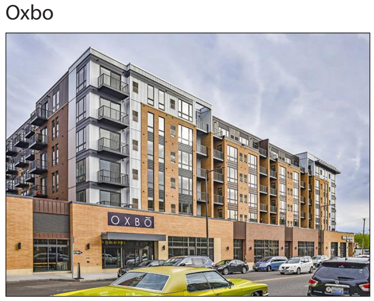
Arrive Eden Prairie

City: Eden Prairie, Minn.
Buyer: FPA Multifamily
Purchase Price: $85 MM
Price per Unit: $167,323

The Penfield

City: St. Paul, Minn.
Buyer: LaSalle Investment Management
Purchase Price: $66 MM
Price per Unit: $257,874

Oxbo



City: St. Paul, Minn.
Buyer: Investors Real Estate Trust
Purchase Price: $62 MM
Price per Unit: $321,990

The Quinn at Plymouth

City: Plymouth, Minn.
Buyer: Mesirow Financial
Purchase Price: $54 MM
Price per Unit: $180,233

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On the cover: Photo by Yin Yang/iStockphoto.com

Rent Trends

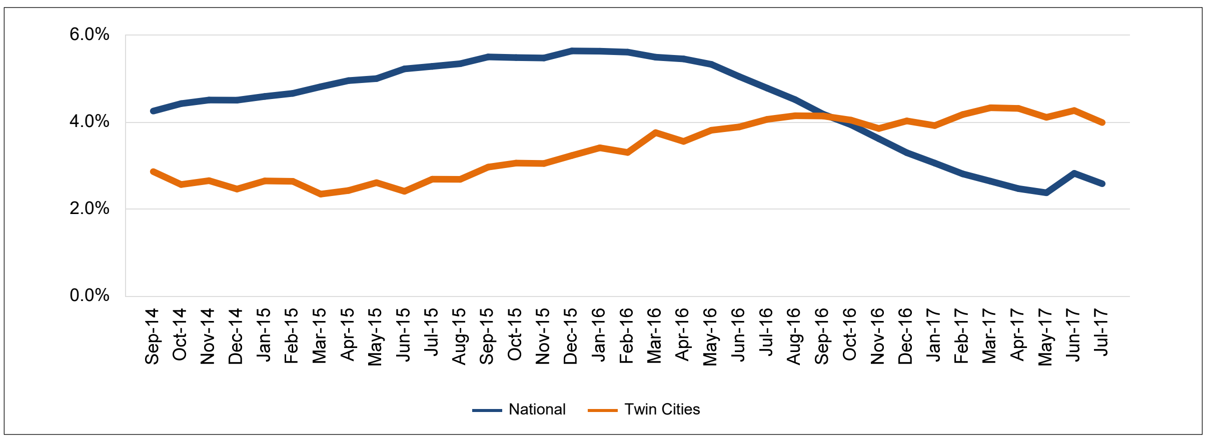
- Minneapolis–St. Paul rents rose 4.0% in the 12 months ending in July, well above the 2.6% national rate. The average rent in the Twin Cities was $1,199, some $150 dollars below the U.S. average. A healthy population growth rate, an increase in the prime, renter-age cohort of young workers and a low number of completions in 2016 has helped keep rents rising at a consistent rate, bucking national deceleration.

- The working-class Renter-by-Necessity segment led rent gains, with a 4.4% increase to $1,041. The segment has performed consistently throughout this cycle. Meanwhile, rents in the Lifestyle sector rose by 3.3%, reaching $1,568.

- Among submarkets, Cambridge (12.0%), St. Paul–West Side (10.1%), Lakeville (9.3%), St. Paul–Summit Hill (8.7%) and Eden Prairie (8.4%) saw the largest rent increases.

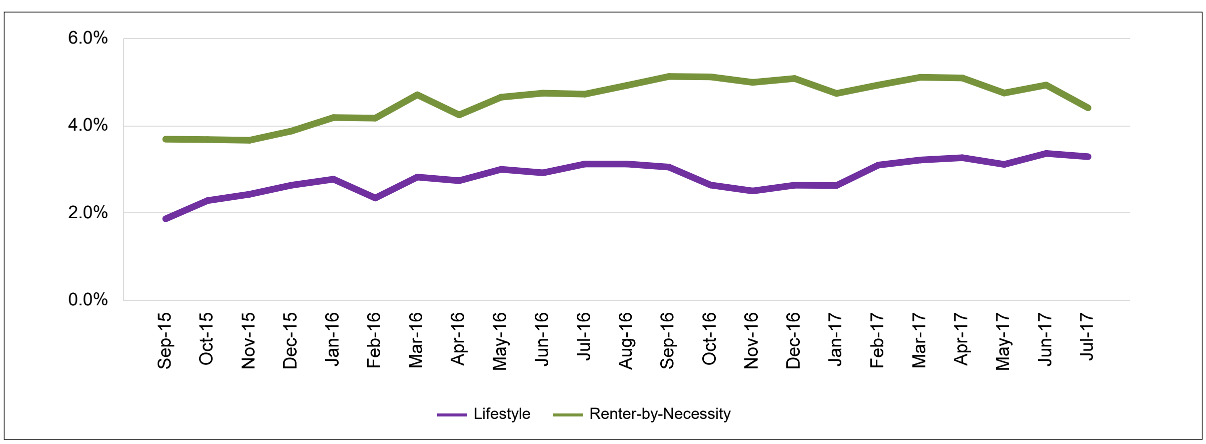
- Occupancy for stabilized properties was 97.7% as of July—the highest of any major U.S. metro—and is expected to remain high for the foreseeable future. Demand is also likely to stay elevated in the near future as well, although the upcoming wave of completions should partially put a damper on growth, at least in several core areas. Yardi Matrix forecasts rents will increase by 3.9% in 2017.

Twin Cities vs. National Rent Growth (Sequential 3-Month, Year-Over-Year)



Source: YardiMatrix

Twin Cities Rent Growth by Asset Class (Sequential 3-Month, Year-Over-Year)



Source: YardiMatrix

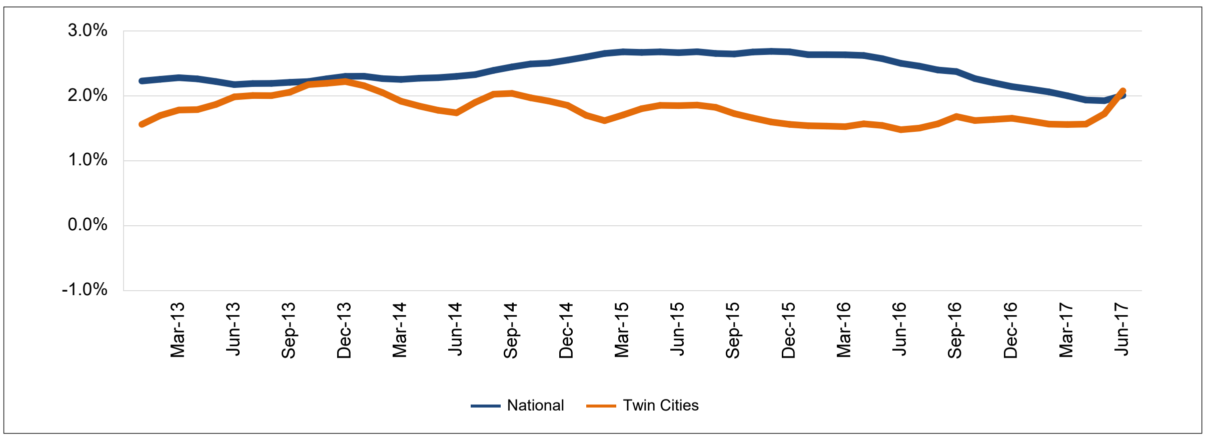
Economic Snapshot

- The Twin Cities added 67,200 jobs in the year ending in June, a 2.1% year-over-year gain, roughly on par with the U.S. average. Anchored by large employers based in the area—including the Mayo Clinic, 3M, Target and UnitedHealth Group—the metro's economy continues to diversify, adding high-paying jobs at a fast pace. At 3.5% as of June, Minneapolis-St. Paul has one of the lowest unemployment rates among large U.S. metros.

- Education and health services led gains, adding 20,000 jobs in the 12 months ending in June. The sector's strong performance results largely from the area's high concentration of established health-care companies and facilities, as well as by a strong student population, with University of Minnesota alone enrolling more than 50,000 students. The metro's health-care and biotech industries will most likely remain a stable source of new employment as Destination Medical Center, a $5.6 billion long-term plan spearheaded by the Mayo Clinic, aims at turning Rochester into a powerful innovation hub.

- As the metro is adding well-paid jobs at a fast pace, Class A properties continue to drive the Twin Cities office market. According to Colliers International, roughly 350,000 square feet of Class A space was absorbed in the second quarter of this year, most of it in Minneapolis' Central Business District, with Amazon and Ryan Cos. among the list of tenants taking more space.

Twin Cities vs. National Employment Growth (Year-Over-Year)



Sources: YardiMatrix, Bureau of Labor Statistics (not seasonally adjusted)

Twin Cities Employment Growth by Sector (Year-Over-Year)

		Current Employment		Year Change	
Code	Employment Sector	(000)	% Share	Employment	%
65	Education and Health Services	359	16.7%	20,000	5.9%
60	Professional and Business Services	341	15.9%	12,200	3.7%
40	Trade, Transportation and Utilities	386	18.0%	6,800	1.8%
90	Government	268	12.5%	6,500	2.5%
30	Manufacturing	219	10.2%	6,400	3.0%
70	Leisure and Hospitality	206	9.6%	5,300	2.6%
15	Mining, Logging and Construction	96	4.5%	4,900	5.4%
55	Financial Activities	149	6.9%	2,300	1.6%
80	Other Services	86	4.0%	2,200	2.6%
50	Information	40	1.9%	600	1.5%

Sources: YardiMatrix, Bureau of Labor Statistics

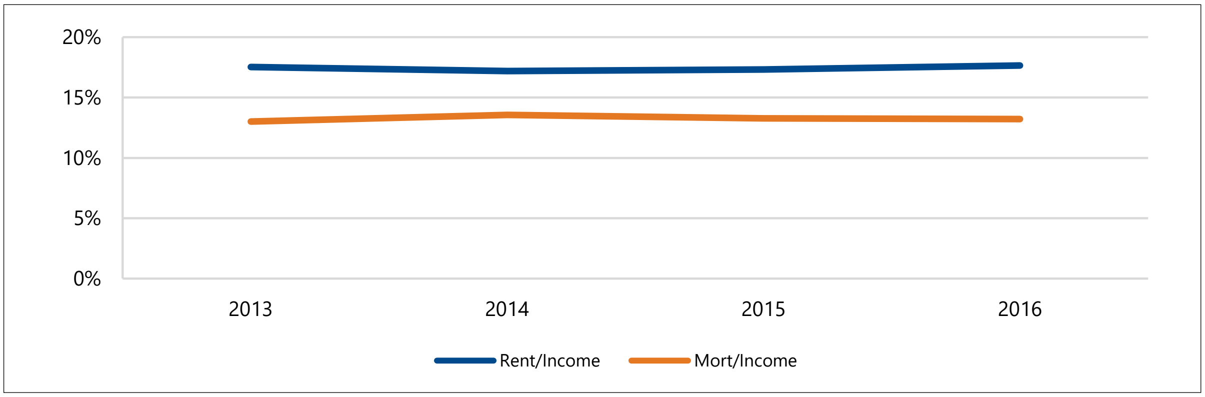
Demographics

Affordability

- The median home price has been rising steadily over the past five years, reaching a cycle high of $219,039 in 2016. However, owning continues to be the more affordable option, as the average rent accounts for roughly 18% of the metro's median income. Meanwhile, the average mortgage payment comprises only 13%.

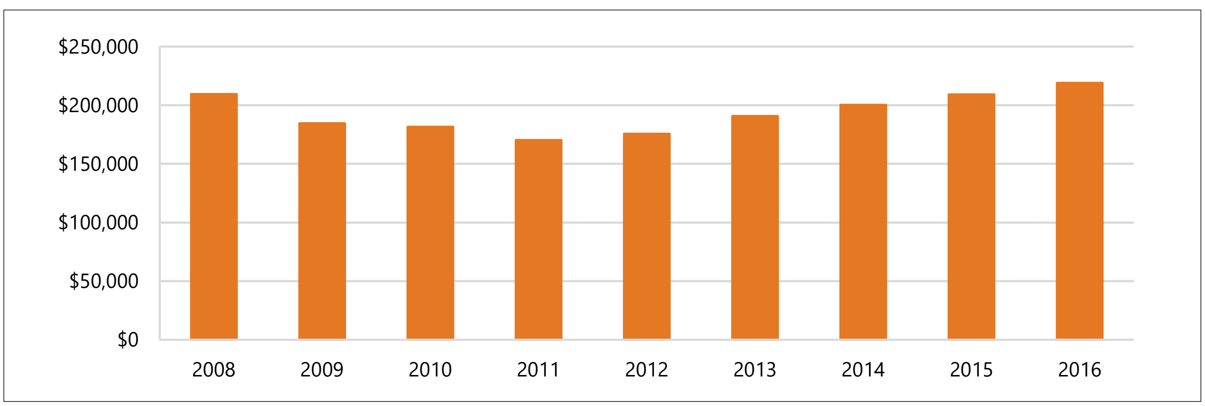
- Last year, The Greater Minnesota Housing Fund launched the NOAH Impact Fund, which aimed to raise $25 million to preserve the affordable status of 1,000 units for another 15 years. It managed to raise $32 million, of which $3 million is coming from Hennepin County. The initiative aims at buying Hennepin County housing units to keep them affordable, thus protecting low-income residents from involuntary displacement.

Twin Cities Rent vs. Own Affordability as a Percentage of Income



Sources: YardiMatrix, Moody's Analytics

Twin Cities Median Home Price



Source: Moody's Analytics

Population

- The Twin Cities added 32,784 residents in 2016, a 0.9% increase, above the 0.7% national growth rate.

- The metro grew by more than 128,400 residents since 2012. This marks a 3.8% increase, 90 basis points over the U.S. rate.

Twin Cities vs. National Population

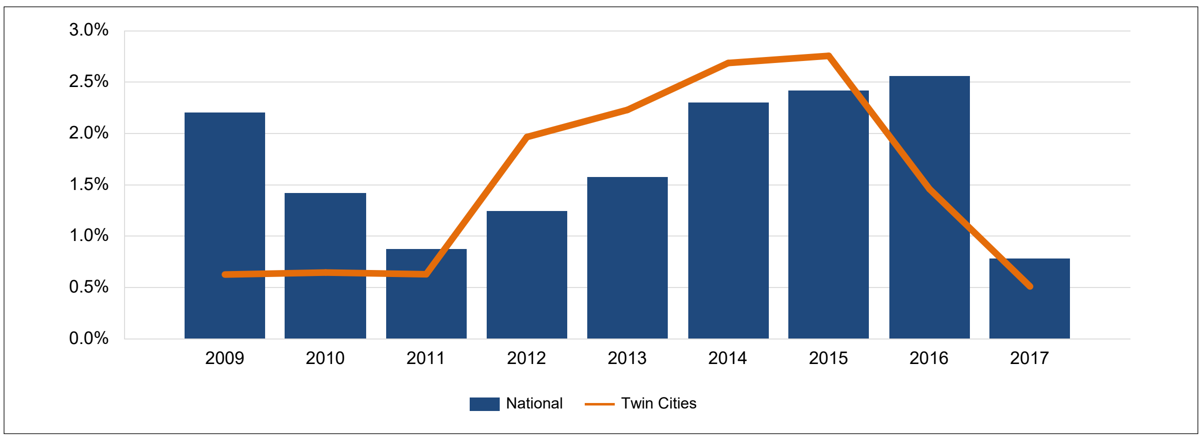
	2012	2013	2014	2015	2016
National	313,998,379	316,204,908	318,563,456	320,896,618	323,127,513
Minneapolis Metro	3,422,542	3,458,513	3,491,838	3,518,252	3,551,036

Sources: U.S. Census, Moody's Analytics

Supply

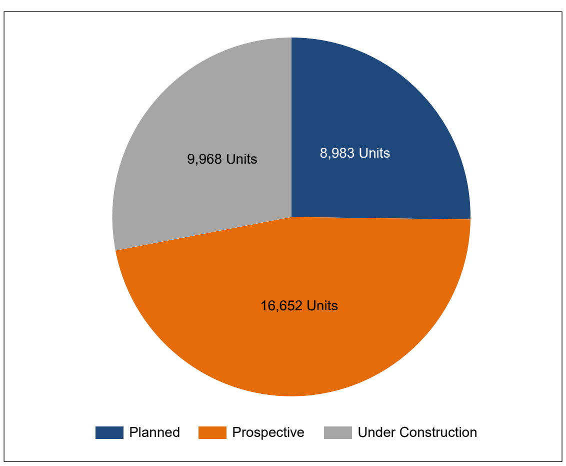
- Multifamily development in the Twin Cities is not keeping up with demand. As of July, only 721 units were completed in 2017, as compared to the 2,800 units that came online in 2016, marking a significant drop from figures for the previous three years.
- However, completions are bound to pick up, as nearly 10,000 units were under construction as of July. We expect the total number of completions to reach 6,500 apartments for the whole of 2017, partially alleviating the demand-side pressure. When taking into account planned and prospective units, the total pipeline in Minneapolis–St. Paul amounts to more than 35,000 units.
- Development is mostly concentrated in core submarkets due to young workers preferring transit-oriented apartments in urban areas that offer easy access to large employment centers. Three submarkets (Minneapolis–University, Minneapolis–Central and Golden Valley) had nearly 3,500 units under construction as of July.
- The largest development underway is Doran Cos.' 610 West, which is expected to deliver a total of 484 upscale units by July 2018. Located in Brooklyn Park, the $90 million property was 36.6% leased as of July.

Twin Cities vs. National Completions as a Percentage of Total Stock (as of July 2017)



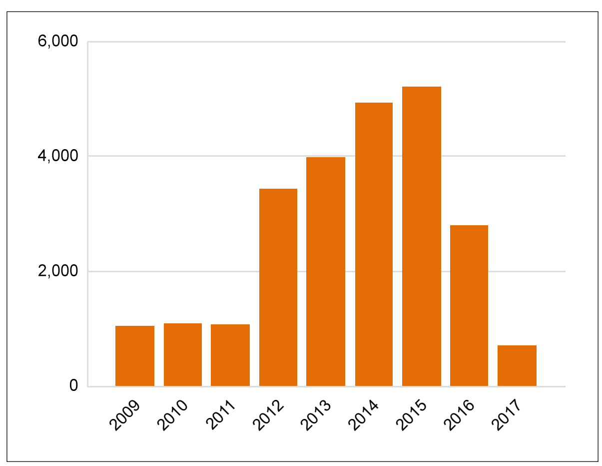
Source: YardiMatrix

Development Pipeline (as of July 2017)



Source: YardiMatrix

Twin Cities Completions (as of July 2017)

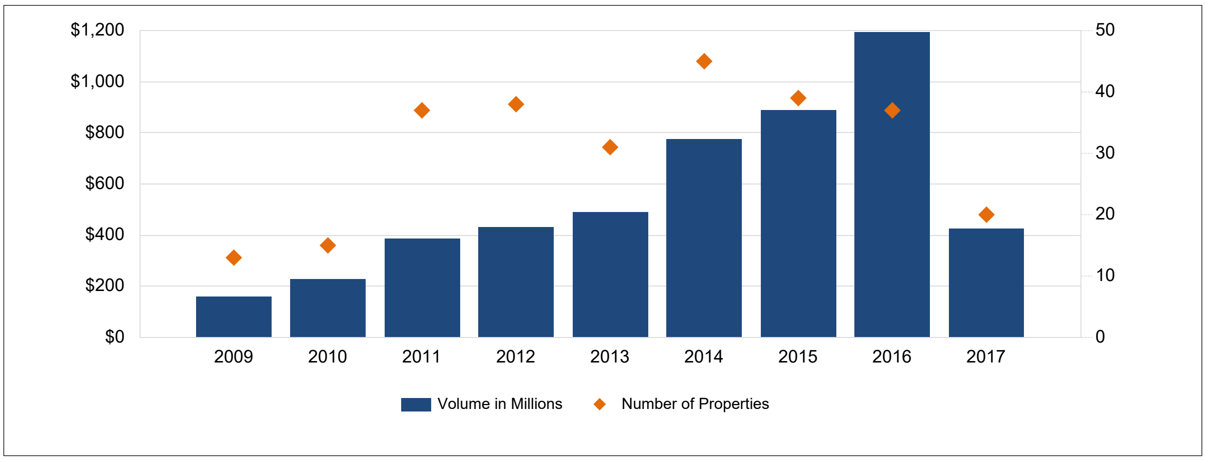


Source: YardiMatrix

Transactions

- Some $425 million in multifamily assets changed hands in 2017 through July, marking a slight slowdown after a cycle high of $1.2 billion last year. The average price per unit was $148,553 for 2017's first seven months, almost flat for the past two years and above the national average of nearly $133,000.
- Investors are focusing on Class B and C assets in suburban neighborhoods that feature strong occupancy rates and easy access to Minneapolis' core. Burnsville, Eden Prairie and Woodbury/Cottage Grove totaled some $340 million in sales in the year ending in July.
- The largest deal over the 12 months ending in July was FPA Multifamily's purchase of the 508-unit Arrive Eden Prairie for $85 million. Invesco Real Estate sold the asset for $137,332 per unit. Formerly known as Mark at Eden Prairie, the Class B property was completed in 1986.

Twin Cities Sales Volume and Number of Properties Sold (as of July 2017)



Source: YardiMatrix

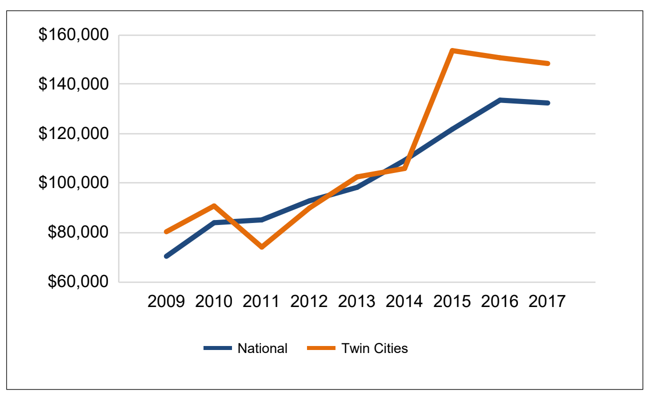
Top Submarkets for Transaction Volume[1]

Submarket	Volume ($MM)
Burnsville	159
Eden Prairie	103
Woodbury/Cottage Grove	76
Minneapolis–Central	71
St. Paul–Downtown	66
St. Paul–West Seventh	62
Apple Valley	61
Plymouth	54

Source: YardiMatrix

[1] From August 2016 to July 2017

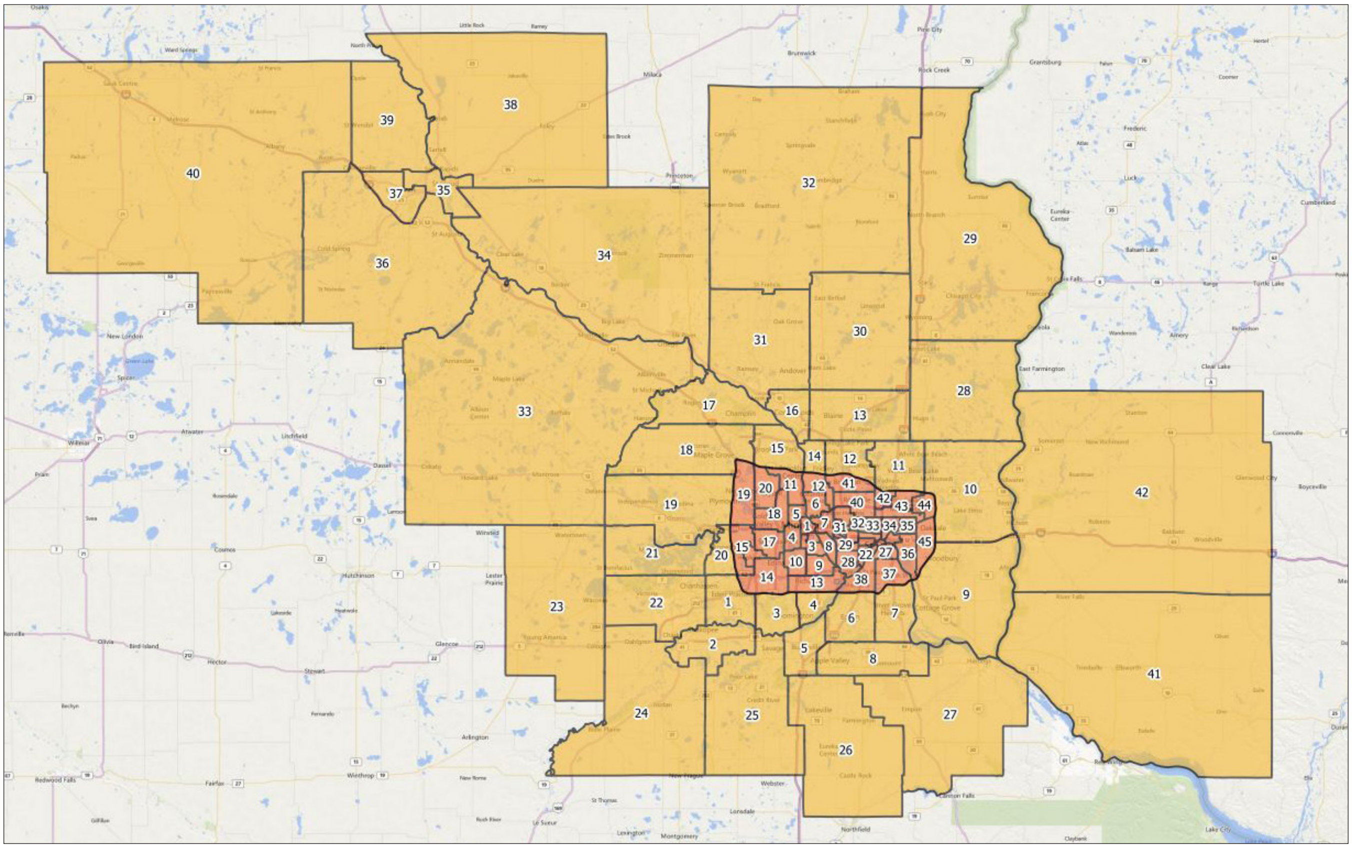
Twin Cities vs. National Sales Price per Unit



Source: YardiMatrix

Photo by jim kruger/iStockphoto.com

Suburban Twin Cities Submarkets

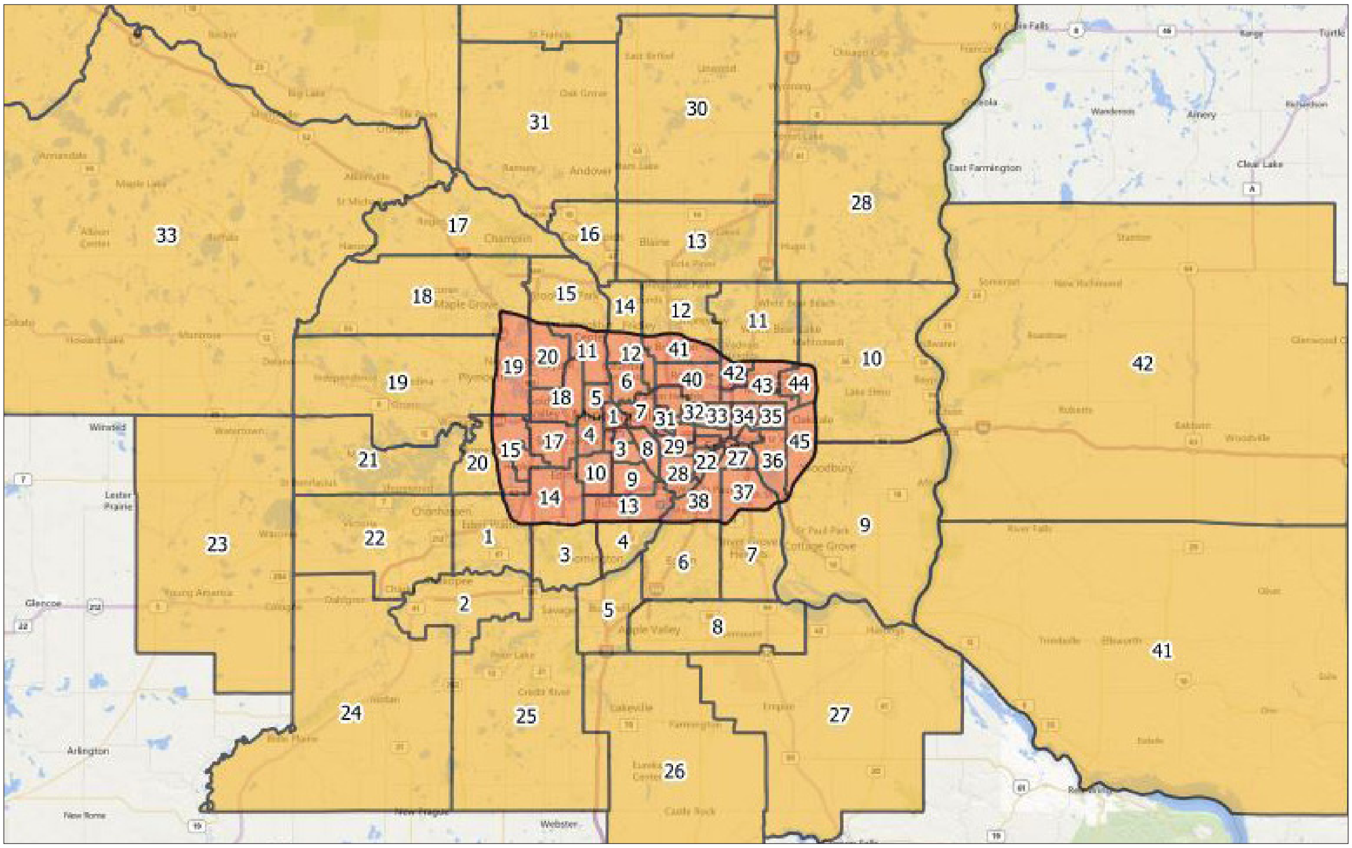


Area #	Submarket
1	Minneapolis–Central
2	Minneapolis–Phillips
3	Minneapolis–Powderhorn
4	Minneapolis–Calhoun Isle
5	Minneapolis–Near North
6	Minneapolis–Northeast
7	Minneapolis–University
8	Minneapolis–Longfellow
9	Minneapolis–Nokomis
10	Minneapolis–Southwest
11	Brooklyn Center/Camden
12	Columbia Heights
13	Richfield
14	Edina/Eden Prairie
15	Minnetonka

Area #	Submarket
16	Hopkins
17	St. Louis Park
18	Golden Valley
19	Plymouth
20	New Hope/Crystal
21	St. Paul–Downtown
22	St. Paul–West Seventh
23	St. Paul–Summit Hill
24	St. Paul–Summit University
25	St. Paul–Thomas Dale
26	St. Paul–Dayton's Bluff
27	St. Paul–West Side
28	St. Paul–Highland
29	St. Paul–Macaleste Groveland
30	St. Paul–Lexington Hamline

Area #	Submarket
31	St. Paul–St.Anthony
32	St. Paul–Como
33	St. Paul–North End
34	St. Paul–Payne-Phalen
35	St. Paul–Greater East Side
36	St. Paul–Sunray Battlecreek
37	West St. Paul
38	Mendota
39	Falcon Heights
40	Roseville
41	New Brighton
42	Little Canada
43	Maplewood
44	Oakdale–North
45	Oakdale–South

Urban Twin Cities Submarkets



Area #	Submarket
1	Eden Prairie
2	Shakopee
3	Bloomington–West
4	Bloomington–East
5	Burnsville
6	Eagan
7	Inver Grove Heights
8	Apple Valley
9	Woodbury/Cottage Grove
10	Stillwater
11	White Bear Lake
12	Mounds View
13	Blaine
14	Fridley

Area #	Submarket
15	Brooklyn Park
16	Coon Rapids
17	Champlin
18	Maple Grove
19	Plymouth
20	Minnetonka
21	Spring Park
22	Chaska
23	Wacoma
24	Jordan
25	Savage
26	Lakeville
27	Hastings
28	Forest Lake

Area #	Submarket
29	Chisago City
30	Andover
31	Anoka
32	Cambridge
33	Buffalo
34	Elk River
35	St. Cloud–North
36	St. Cloud–South
37	Waite Park
38	Sauk Rapids
39	Sartell
41	River Falls
42	Hudson

Definitions

Lifestyle households (renters by choice) have wealth sufficient to own but have chosen to rent. Discretionary households, most typically a retired couple or single professional, have chosen the flexibility associated with renting over the obligations of ownership.

Renter-by-Necessity households span a range. In descending order, household types can be:

- *A young-professional, double-income-no-kids household* with substantial income but without wealth needed to acquire a home or condominium;
- *Students*, who also may span a range of income capability, extending from affluent to barely getting by;
- *Lower-middle-income ("gray-collar") households,* composed of office workers, policemen, firemen, technical workers, teachers, etc.;
- *Blue-collar households*, which may barely meet rent demands each month and likely pay a disproportionate share of their income toward rent;
- *Subsidized households*, which pay a percentage of household income in rent, with the balance of rent paid through a governmental agency subsidy. Subsidized households, while typically low income, may extend to middle-income households in some high-cost markets, such as New York City;
- *Military households*, subject to frequency of relocation.

These differences can weigh heavily in determining a property's ability to attract specific renter market segments. The five-star resort serves a very different market than the down-and-outer motel. Apartments are distinguished similarly, but distinctions are often not clearly definitive without investigation. The Yardi® Matrix Context rating eliminates that requirement, designating property market positions as:

Market Position	Improvements Ratings
Discretionary	A+ / A
High Mid-Range	A- / B+
Low Mid-Range	B / B-
Workforce	C+ / C / C- / D

The value in application of the Yardi® Matrix Context rating is that standardized data provides consistency; information is more meaningful because there is less uncertainty. The user can move faster and more efficiently, with more accurate end results.

The Yardi® Matrix Context rating is not intended as a final word concerning a property's status—either improvements or location. Rather, the result provides reasonable consistency for comparing one property with another through reference to a consistently applied standard.

To learn more about Yardi® Matrix and subscribing, please visit www.yardimatrix.com or call Ron Brock, Jr., at 480-663-1149 x2404.

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