Twin Cities Commercial Real Estate Market Moves into Recovery Mode

The Twin Cities commercial real estate market is emerging from one of the worst economic downturns since the 1930s with renewed growth in space demand and increased investment sales activity.

Vacancy is down to 15.3% for all property types. The market posted 1.1 million square feet of positive absorption, putting the Twin Cities on track for the first full year of positive absorption since 2008.

INVESTORS REDISCOVER TWIN CITIES

Investment capital is returning to commercial real estate, and the Twin Cities market is seeing the effects. Large institutional investors are aggressively pursuing the best-located, stabilized, Class A assets. There is also an increasingly active base of investors, national and local, for both deeply distressed assets and the better-quality properties with an issue or two such as a high vacancy rate or near-term rent roll exposure.

RETAILERS HAPPILY BOXING THEMSELVES IN

Vacancy at community retail centers tumbled to 7.1% on the heels of 210,000 sq. ft. of positive absorption as retailers selectively backfilled about a dozen of the best-located empty big-box and junior-box spaces. Overall vacancy is 8.8%, its lowest level since 2008. First-half absorption totaled a positive 134,000 sq. ft., with losses in the neighborhood and specialty retail properties countering gains among community retail centers and regional malls.

OFFICE MARKET ROLLS FORWARD

Long and slow as it may ultimately be, the Twin Cities office market took its first steps toward recovery in the first half. The market saw 324,000 sq. ft. of positive absorption, which helped whittle the overall vacancy rate down to 19.2%—still high, but down from 19.9% at year-end 2010.

INDUSTRIAL SPACE DEMAND SLIDES INTO GEAR

Demand for industrial space picked up during the first half, resulting in 542,000 sq. ft. of positive absorption—the market's first positive absorption report since 2008. Bulk warehouse properties are seeing the most activity, and large users are back scouting the market for space.

RISING TIDE OF RENTERS PUMPS UP MULTI-FAMILY MARKET

The metro area's apartment rental market is booming. Vacancy tumbled to 3.1%, a five-year low, and the rush to rent has given landlords leverage to raise their rates and eliminate costly concessions. Demand is strong at all pricing levels. Absorption is currently outpacing development, although several new projects are in the pipeline.

MEDICAL OFFICE MEASURES UP

Medical office space users are taking a measured approach to expansion, both in the leasing and new construction segments of the market. New on-campus construction is very selective, as the industry continues to deploy capital conservatively. The first half saw 90,000 sq. ft. of positive leasing absorption, mostly attributable to the new Two Twelve Medical Center in the Southwest submarket.

LAND DEMAND STARTING TO PERCOLATE

The market saw one large industrial land transaction, which involved a national REIT, during the first half, and other sites are under consideration by buyers who see a pending shortage in well-positioned office warehouse and bulk warehouse industrial properties. In-fill sites within the core market remain in high demand.

ON THE HORIZON

The Twin Cities could see an additional 2 million square feet of positive absorption in the next six months, making for a full-year total of 3 million square feet of absorption. That would be the highest absorption number since 2007, when the market absorbed 4 million square feet of space. Much of this is already booked.

While the space markets are certainly seeing increased levels of activity, the actual flow of new transactions looks to be thinner for 2012 than what's projected for 2011. The slow job growth projected for next year likely means 2012 will look a lot more like 2002—a recovery year from a deep recession that generated 1.5 million square feet of positive absorption in the Twin Cities. ■

MORE ONLINE

Find more information by submarket and/or product type, including:

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