

Market Highlight: Minneapolis/St. Paul

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Though the federal government and some economists point to indicators suggesting the recession is over, in the Minneapolis/St. Paul metro area stories of layoffs, bankruptcies and foreclosures still far outnumber those of corporate expansions, new development and investment transactions. Commercial real estate, the cycles of which typically lag the overall economy by 6 to 12 months, is still in the midst of negative absorption, declining property values and the inaccessibility of credit. Despite current conditions, there are examples of business occurring as usual and patient optimism for opportunities ahead.

Development

A few development projects are moving forward, bucking the challenges of securing acceptable debt and reconciling project costs with market expectations to justify a return. Doran Companies recently broke ground on Sydney Hall, a six-story, 125-unit student housing project located near the University of Minnesota. This \$36 million project has been in the works for more than 2 years as Doran worked through planning and financing hurdles. It ultimately received financing through the Private Bank of Chicago, which, along with \$10.8 million of its own capital, made the project possible. Now under construction, Sydney Hall is scheduled to be open for students in August 2010.

Medical and medical-related industries have been a bright spot for development in the Minneapolis/St. Paul metro area. UnitedHealth Group recently expanded into a new 350,000-square-foot office building in Minnetonka. North Memorial and Fairview partnered on the new 90-room Maple Grove Hospital, set to open at the end of the year. Additionally, the University of Minnesota is currently building the new 227,000-square-foot Amplatz Children's Hospital in Minneapolis, which will open in 2011.

Retail development is virtually non-existent in the metro area. The projects that are going forward are primarily infill or property repositioning. Stonehenge USA recently closed on a former Ethan Allen store in Eagan and has begun demolition and reconfiguration of this 20,000-square-foot, single-tenant retail building into a 14,400-square-foot, multi-tenant center. Scott Tubman, a development consultant for Stonehenge, said the project's success was largely due to its tenant makeup. Stonehenge has 83 percent of the project pre-leased with one 2,500-square-foot space remaining.

An example of repositioning is the sale of a 107,000-square-foot office/warehouse building for reuse as a Hmong market on St. Paul's Eastside. The building is located at the intersection of two major thoroughfares, but it lacks the access and visibility typically associated with retail development. Its main advantage is its location at the epicenter of St. Paul's Hmong population. The new owners plan to build 300 stalls in the building, which will be leased to vendors selling various types of food and merchandise. The seller provided contract for deed financing. Prior to the sale, few industrial companies expressed interest in the property.

One important driver of future development in the Minneapolis/St. Paul metro area will be public transit. The Northstar Commuter Rail, which runs 40 miles from Big Lake to Minneapolis' central business district (CBD), is set to open this month. Additionally, construction begins next summer on the Central Corridor

Light Rail line that will connect the St. Paul and Minneapolis CBDs via Washington and University avenues. Other drivers for future development include a continued increase in the demand for LEED-certified or "green" buildings and the impact in Minneapolis around both Target Field (opening for the Twins' 2010 season) and a potential future Vikings stadium on the Metrodome site (still in negotiations for the 2012 football season).

Sales

Two large obstacles have caused a significant decline in the number of commercial properties trading hands in 2009: a bid-ask gap that exists with sellers valuing property higher than buyers and a difficulty in obtaining debt financing on acceptable terms. Significant amounts of capital are sitting patiently on the sidelines, awaiting opportunities from lenders or distressed sellers. Local entrepreneurs, with both knowledge of the market and relationships within that market, are poised to acquire quality assets when the opportunity arises. Ned Abdul of Swervo Development Corporation recently took advantage of the described situation when he closed on the Northland Corporate Center in Brooklyn Park for \$1.3 million. Swervo purchased this 200,400-square-foot, three-story office building from Allied Capital REIT Inc. Abdul was selected as the buyer for the property because he was an all-cash buyer and able to close quickly.

Leasing

General contractors typically provide a good gauge of a market's leasing activity, as they are involved in tenant renovations. Plymouth-based Bainey Group Inc. has seen a 40 percent revenue decline in 2009. According to Chuck Bainey, they will book more business in fourth quarter 2009 than any of the previous three quarters. Much of that work is preparing buildings and vacancies to be "tenant ready." With the supply of vacant space outclipping demand, aggressive and responsive landlords, those focused on maintaining/increasing occupancy and willing to meet the market will fare better than others.

Recent leases include the consolidation of Buffets Inc., the entity behind Old Country Buffet restaurants, into 43,000 square feet with Wellington Management Inc. in Eagan for 10 years. Buffets selected this location because it required minimal improvement to meet their needs, and the landlord assisted with the costs associated with relocating.

Also, Acosta Sales and Marketing, a food-marketing firm, agreed to 10-year lease with United Properties for a 67,000-square-foot build-to-suit lease in Eden Prairie. Acosta will move in next summer, following construction of the stand-alone building, which is phase two of the Staring Lake Corporate Center. John McCarthy, the NorthMarq Capital broker who represented Acosta, said this site was selected as the most cost-effective consolidation option for Acosta in the Eden Prairie area.

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