

# COMPASS



## INVESTMENT & CAPITAL MARKETS

JANUARY 2021

### Second Half Rebound Experienced Unevenly Across Asset Classes

Overall transaction volume in the Twin Cities in 2020 was down nearly 29% from the previous year, though debt and financing became more accessible through the second half of the year after the initial pause in response to the arrival of COVID-19. Pricing and capital availability, however, were not uniform across property types as investors sought stability and predictability from assets earmarked for allocation. Assets catering to industries most impacted by COVID-19 remained a challenge as pricing gaps persisted while buyers and sellers grappled with disparate pricing discovery caused by slowdowns in transaction and leasing activity. By contrast, pricing and underwriting for assets geared toward more stable or growing industries, such as retail wholesale and last-mile distribution, or multi-family and medical office product, were relatively unchanged.

TWIN CITIES INVESTMENT SALES In Millions (Rolling 12 Month Total)			Source: Real Capital Analytics
PROPERTY TYPE	2019 SALES VOLUME	2020 SALES VOLUME	PSF/UNIT
Hotels	\$400.52	\$64.85	\$52,878.01
Multifamily	\$1,676.43	\$1,326.69	\$173,200.34
Industrial	\$1,702.06	\$1,573.95	\$85.03
Office	\$1,780.10	\$921.58	\$141.00
Retail	\$617.89	\$522.73	\$158.61
<b>TOTAL</b>	<b>\$6,177.01</b>	<b>\$4,409.81</b>	<b>\$107.15</b>

#### ACTIVITY SHIFTS TO SUBURBAN MULTIFAMILY

For the seventh consecutive year in the Twin Cities, multifamily investment sales surpassed \$1 billion in total deal volume. First-ring suburban markets attracted increased attention from investors and developers alike in the second half of the year. Average rents in the suburbs were up 2.5% year-over-year, and with relatively stable employment levels through the year, the suburban vacancy rate remained at 3.2%, according to Marquette Advisors. A confluence of negative factors in the downtown markets, on the other hand, led to a temporary pause in activity, though investors and developers expect a snap back particularly with office users returning to in-person work in the CBD as vaccines are distributed.

#### DEMAND FOR INDUSTRIAL PRODUCT LIFTS RENTS AND PRICING LEVELS

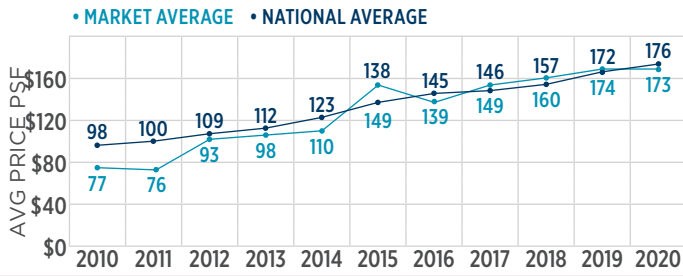
The investment sale market for industrial assets remained active with more than \$1.2 billion in 2020 sales finalized by year-end. As the ownership structure in the market shifted further from predominantly local ownership, leasing fundamentals changed, and buyers looked to capitalize on ongoing rent growth. Portfolios continued to command premium pricing and push cap rate compression. Investors have shown a willingness to stretch on pricing and geography for portfolios as an effective mechanism to deploy capital, drive rent growth and control market share. A highlight of year-end deals was the Opus portfolio sale, which consisted of two recently completed speculative construction projects: Arbor Lakes Corporate Center in Maple Grove and Dodd Road Business Center in Eagan. The assets were 98% leased with 15% office finish and achieved watermark pricing for the asset class.

#### OFFICE INVESTORS FOCUS ON PREDICTABILITY AND SECURITY

Overall transaction volume remained below 2019 totals as investors and owners continued to navigate general underwriting and pricing discovery disparities associated with limited data available through the COVID-19 pandemic. Quality assets offering the stability of lease term and credit remained in high demand, and investors have also shown an interest in acquiring value-add assets in attractive suburban submarkets with good fundamentals. Financing vehicles became more accessible through the second half of 2020 in preparation to meet anticipated pent-up demand for office assets throughout the Twin Cities. With COVID-19 vaccines being distributed, a pathway to repopulating office towers and re-engaging employer leasing and space needs is beginning to appear. The emergence of more datapoints and positive rent collections are expected to promote a significant increase in activity through 2021, especially in the latter half of the year.

**MULTIFAMILY SALE MARKET**

Source: Real Capital Analytics



**INDUSTRY SHAKE-UP SLOWS RETAIL INVESTMENT SALES**

With vacancy rates rising at year-end 2020 and more fallout in the retail sector expected in the first half of 2021, investment sales remained relatively muted in the Twin Cities. Debt markets have opened back up for the retail asset class at favorable rates, and centers comprised of users that have been less impacted by COVID-19 have attracted the most interest to date. With just 17 unique transactions during the second half of 2020, there are still relatively few datapoints to gauge pricing in the market. The auction sale of Burnsville Center represented the outlier example in the market of a distressed asset acquisition.

**STEADY ACTIVITY FOR MEDICAL OFFICE SALES AND DEVELOPMENT**

The Twin Cities medical office market recorded steady investment sales activity in the second half, spurred by demand from established ownership groups as well as new capital entering the market. The more measured pace of off-campus development activity, which has been a long-term trend in the Twin Cities, continued during the second half as Davis began construction on the ±78,000-sf Xchange Medical project in St. Louis Park with lease commitments in place. The relatively limited supply of for-sale product in the market has contributed to the strong pricing support that stabilized assets have experienced when coming to market. In the second half, for example, Montecito Medical purchased the fully-leased Ridges Pondview in Burnsville for nearly \$300 per square foot (psf), marking the group's first acquisition in the Twin Cities.

**ON SLOW ROAD TO RECOVERY, HOTELS NAVIGATE PRICING DISCOVERY**

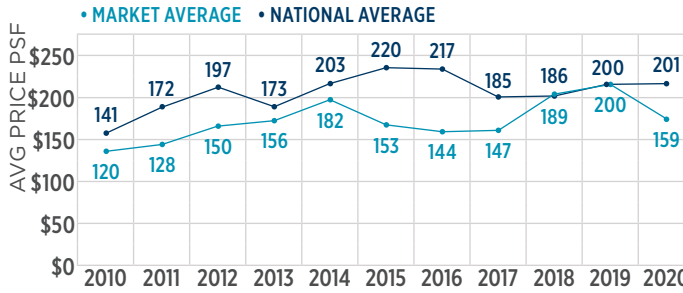
The hotel asset class has experienced a prolonged slowdown in investment sales as the hospitality industry has navigated the pandemic. A notable exception that traded in the Twin Cities during the second half is the Bloomington Doubletree. Vinayaka Hospitality purchased the 568-room property for \$46,000 per room and announced plans for major renovations. There is significant capital waiting to deploy in the asset class, including residential and governmental buyers that have continued to be active pursuing hotel opportunities. A bid-ask spread is expected to persist as buyers and sellers evaluate factors such as the rate of demand recovery, how the second relief package will affect the industry, and the broader economic recovery and vaccine rollout.

**OUTLOOK**

Although segments of the finance market re-engaged in the second half of 2020, a successful roll-out of vaccines on a national level will be required to get back to the robust environment of 2019 and early 2020. Positive signs continue to emerge as corporate credit markets have generally recovered with effective yields at or below 2019 levels and CMBS delinquency rates stabilized. Although pricing disparities remain in certain asset classes, investor sentiment is generally positive and national and international debt and equity continues to accrue on the sidelines.

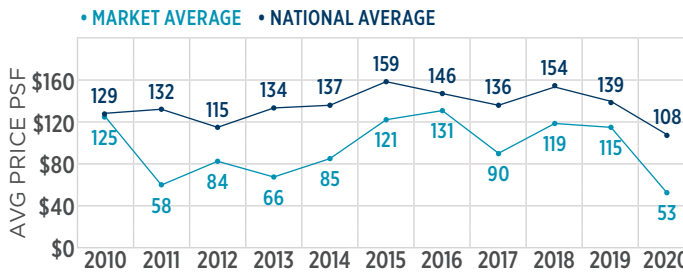
**RETAIL SALE MARKET**

Source: Real Capital Analytics



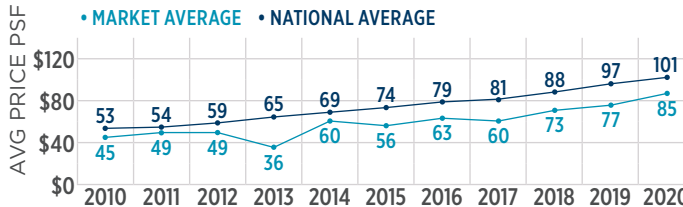
**HOTEL OFFICE MARKET**

Source: Real Capital Analytics



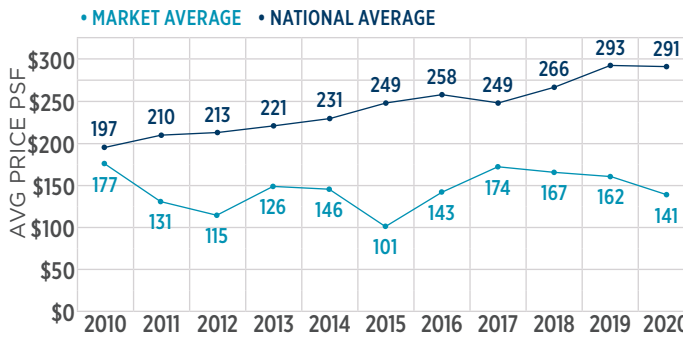
**INDUSTRIAL SALE MARKET**

Source: Real Capital Analytics



**OFFICE SALE MARKET**

Source: Real Capital Analytics



**THE COMPASS REPORT**

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3500 American Blvd W Suite 200  
 Minneapolis, MN 55431  
 +1 952 831 1000  
[cushmanwakefield.com](http://cushmanwakefield.com)