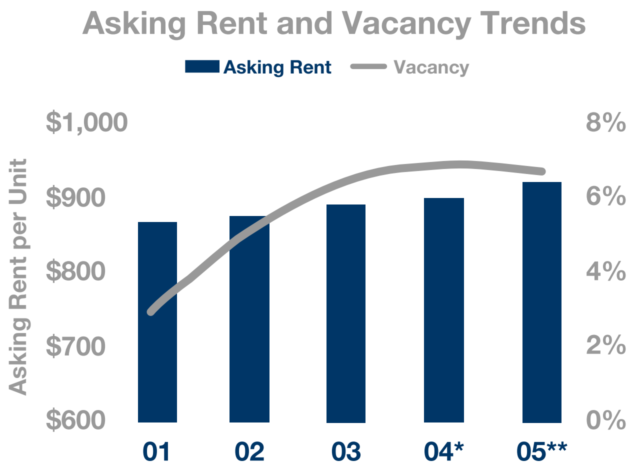
Minneapolis-St. Paul



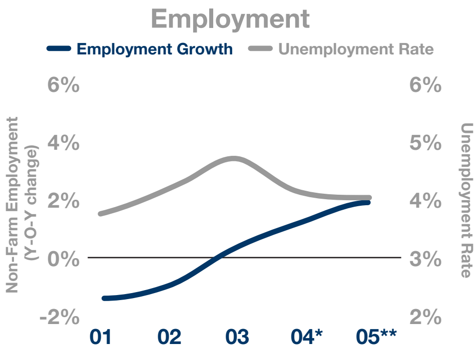
Condo Development Craze puts Apartments on the Back Burner

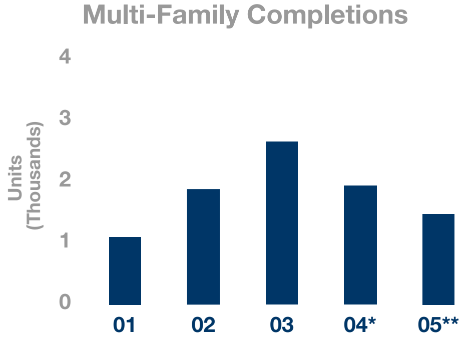
Improving economic conditions are fueling demand in the Minneapolis-St. Paul multi-family housing market, but the growing popularity of condos will continue to sap demand from the apartment market in 2005. Thanks to low interest rates and a reviving job market, entry-level homes are in short supply. This has prompted many builders to switch from apartment development to condos. The hot housing market has proven detrimental to the apartment sector, which ended 2004 with vacancy up 50 basis points at 6.8 percent. Despite the softened conditions, owners managed slight increases in rents and the gross revenue per unit. This trend will continue in 2005, with a few submarkets expected to outperform. The Anoka County submarket bounced back from a wave of move-outs in early 2004, and is expected to end 2005 with vacancy down 40 basis points, at 4.4 percent. The submarket is benefiting from healthy population growth, especially in the prime renter age group of 18 to 24 year olds. The Northeast submarket is experiencing substantial improvement, especially in the luxury apartment sector, as the number of retirees in the area increases. Overall, vacancy in the Northeast submarket ended 2004 down 70 basis points, at 5.5 percent, with expectations for another 50 basis point decline in 2005.

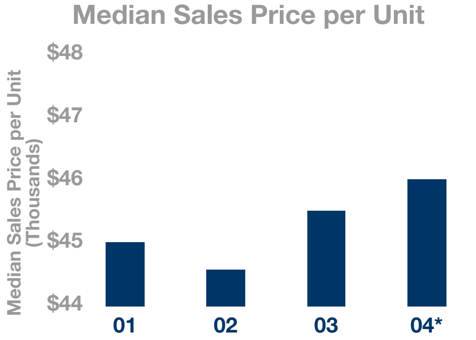
Apartment buyers will continue pursuing properties in the region, and investment activity is forecast to pick up in 2005 due to improving economic conditions and a dip in vacancy. Stronger fundamentals will allow values to continue rising in 2005, after growing 1 percent in 2004. Underperforming Class C properties in Anoka County and in the Northeast are likely investment targets as Class C vacancy in these submarkets is expected to be the lowest in the region, at sub-4 percent.

- ▲ Rent Forecast: Improved rent growth is forecast for 2005, after a minimal gain last year. Many of the positions being created are low-end retailing or tourism-industry jobs, which will boost demand at local apartments and give owners the ability to achieve asking rent growth of 2.5 percent, pushing the average to $918 per month.
- ▲ Investment Forecast: The growing popularity of condos will prompt many Class A apartment owners to start the conversion process or sell, given the profit per unit is much higher for condo-mapped properties.

- ▲ 2005 NAI Rank: 20, Up 3 Places. Rising home prices, below-average vacancy and a limited supply pipeline pushed Minneapolis into the top 20.
- ▲ Employment Forecast: Local employers are forecast to add almost 37,000 workers in 2005. Growth amounted to 1 percent in 2004, a gain of 17,260 positions.
- ▲ Construction Forecast: The focus on condo development has caused apartment construction to dwindle. Completions in 2005 will total 1,400 units, 450 fewer than were delivered in 2004. Most of the new apartments are being built in St. Paul, where nearly 700 units are slated for completion.
- ▲ Vacancy Forecast: Stronger job growth and rising mortgage rates will help alleviate the adverse effects that the booming condo market is having on apartments. Vacancies are expected to decline by 20 basis points this year, to 6.6 percent, representing the first improvement in five years.







* Estimate ** Forecast

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