

3Q23

Minneapolis-St. Paul Office Market Overview



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Market Observations



- Minneapolis benefits from the stability and vitality of a strong headquarters economy, home to 14 firms on the Fortune 500 list, the most per capita in the U.S. for a major metropolitan area. In addition, there are more than 320 Fortune 1000 companies with a local presence.
- Minneapolis-St. Paul is a global leader in biotechnology and biomedical research, with deep roots in agriculture, food exports and water technology, and has one of the highest concentrations of banks and financial talent of any major metropolitan area.
- The region has a historically low unemployment rate, currently 60 basis points lower than the national rate. The unemployment rate is 3.2% as of August 2023, compared with a low of 2.0% in April 2022 and 11.7% in May 2020.



- Best Buy has made 600,000 SF of space available for lease within its expansive 1.5-million-SF corporate campus in Richfield. The complex has a 215,000-SF communal amenity area that includes numerous dining and coffee options.
- While the investment sale market remains slow, Spear Street Capital bought the 2022-built RBC Gateway tower from developer United Properties for \$225 million. The sale marks 2023's largest to date and included 525,000 SF of office space, a ground floor lobby and an underground parking facility with 296 stalls.
- SICK, a German sensor manufacturer, finalized the acquisition of land in Bloomington, close to the Mall of America. They will commence construction on a 144,000-SF office building in 2024, close to an existing production and logistics facility the company operates.
- UnitedHealth Group has opted not to renew its lease at its 345,000-SF headquarters building in Minnetonka. The company's C-suite executives are among the employees relocating from Minnetonka to the Optum campus in Eden Prairie during the first half of 2024.



- Quarterly net absorption was negative 979,222 SF, contributing to a year-to-date total of over 1.6 million SF. Much of this negative absorption was concentrated in the Southwest, due to Best Buy's listing of 600,000 SF at its corporate campus. Since the onset of the pandemic, the highest negative absorption was recorded in the third quarter of 2021, exceeding 1.9 million SF, and positive absorption was only observed in the first quarter of 2022 when RBC Gateway was completed.
- The vacancy rate including sublease space has risen to 17.3%, from 16.4% in the second quarter of 2023. The highest vacancy rate is 22.8% in the Minneapolis CBD, in contrast to suburban submarkets, where overall vacancy rate is notably lower at 14.4%.
- Following a 1.4% decrease in the second quarter of 2023, the first decline in asking rents since the onset of the pandemic, rental rates declined 3.2%. It's important to note that overall rental rates remain elevated, while concessions are substantial and increasing, particularly in the Minneapolis CBD.



- In a positive sign for future office space utilization, businesses continue to mandate or strongly encourage their employees to return to the office. In September, Xcel Energy declared a mandate for its employees to be in the office for a minimum of three days a week, including the 2,000 employees that work at the company's office in the Minneapolis CBD. Also of note are national tech firms, such as Apple, Google, Meta and Zoom, actively encouraging their employees to return to in-person work.
- Our estimates indicate companies that have renewed or signed leases since the onset of the pandemic are, on average, reducing occupancy levels by around 20% as they embrace hybrid work strategies. Among office space users, a significant portion haven't yet gone through the process of reevaluating their space requirements, which is typically triggered by events like lease expirations or early termination options. Because of this, we anticipate a sustained decrease in overall demand for office space over the next few years as companies reevaluate their needs. This trend should stabilize by 2026.
- Pace of sales will remain slow in future quarters due to high interest rates and uncertain fundamentals.

1. Economy
2. Leasing Market Fundamentals

3Q23

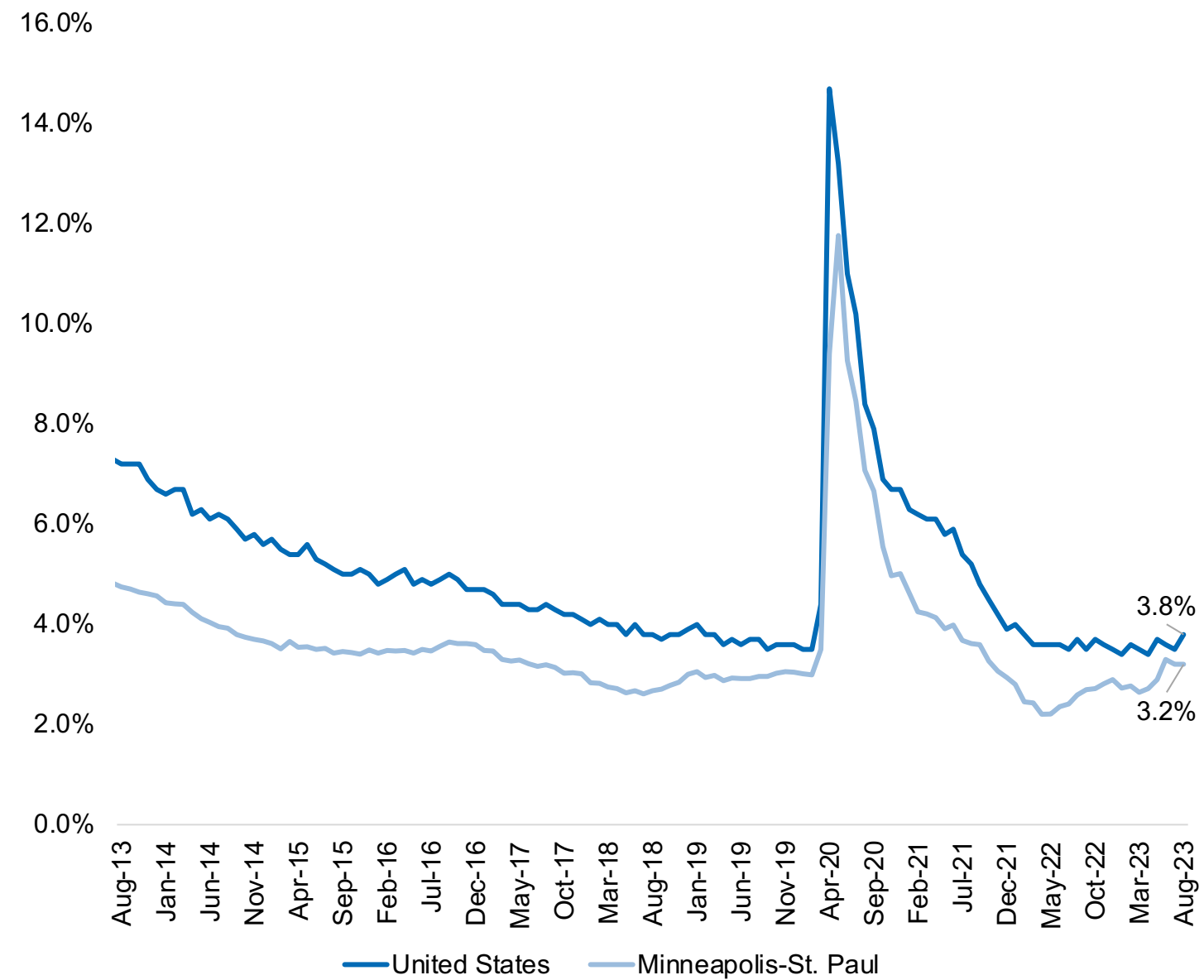
Economy



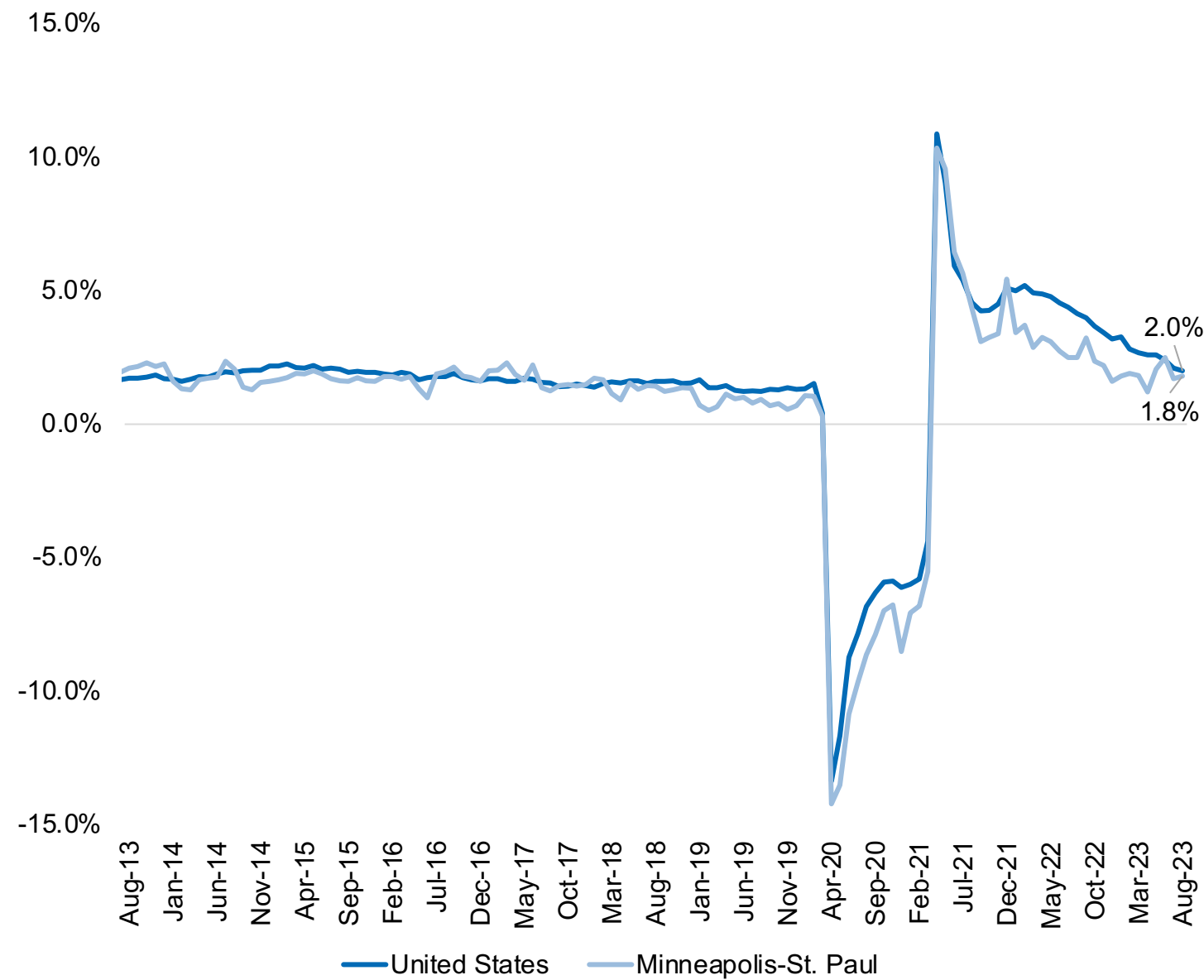
Minneapolis-St. Paul's Total Employment Continues to Increase

The region added 35,400 jobs since August of 2022; the unemployment rate remains lower than the national rate, at 3.2%. Total nonfarm employment is 22,400 jobs above February of 2020.

Unemployment Rate, Seasonally Adjusted



Nonfarm Payroll Employment, Non-Seasonally Adjusted, 12-Month % Change

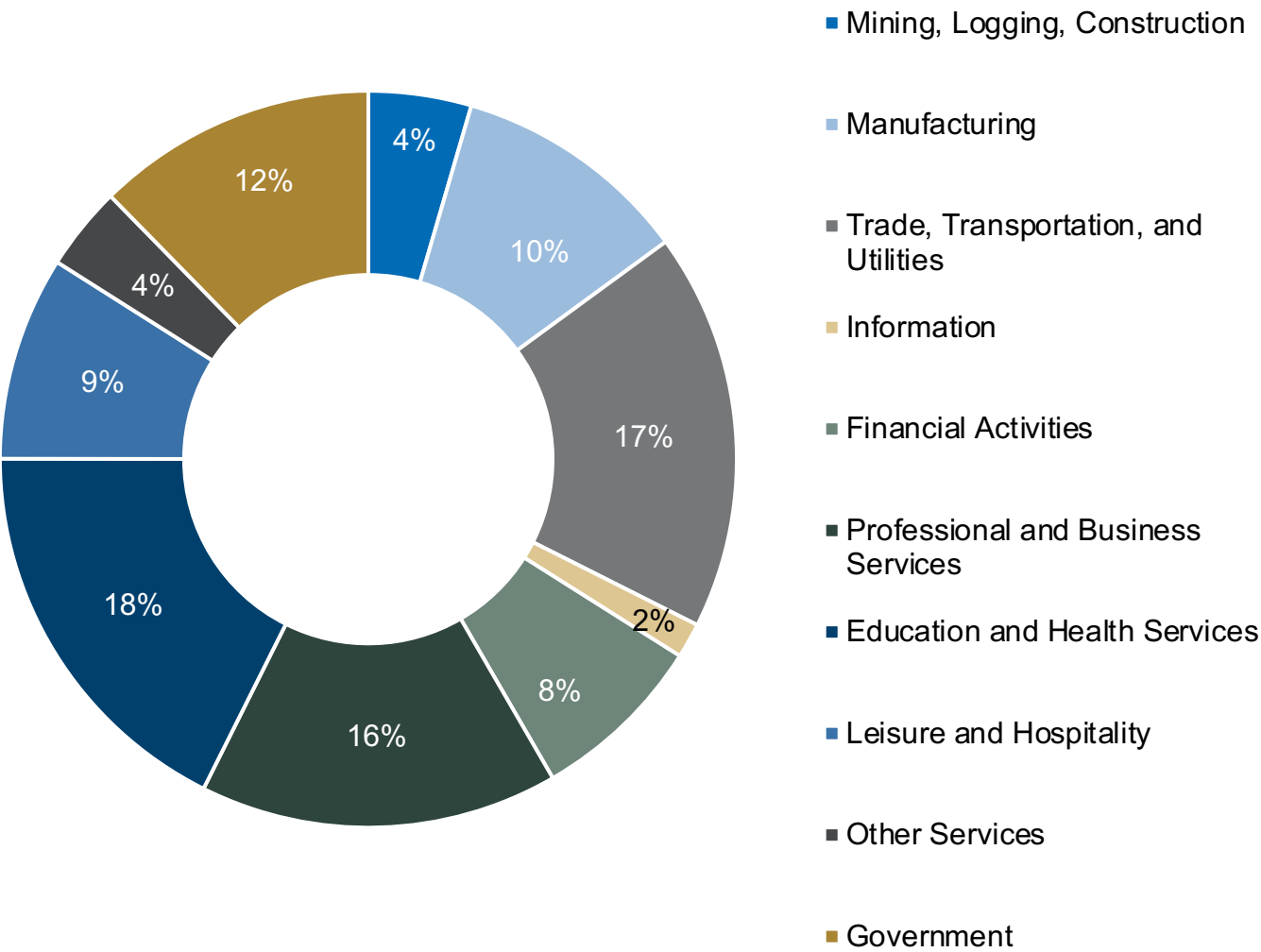


Source: U.S. Bureau of Labor Statistics, Minneapolis-St. Paul

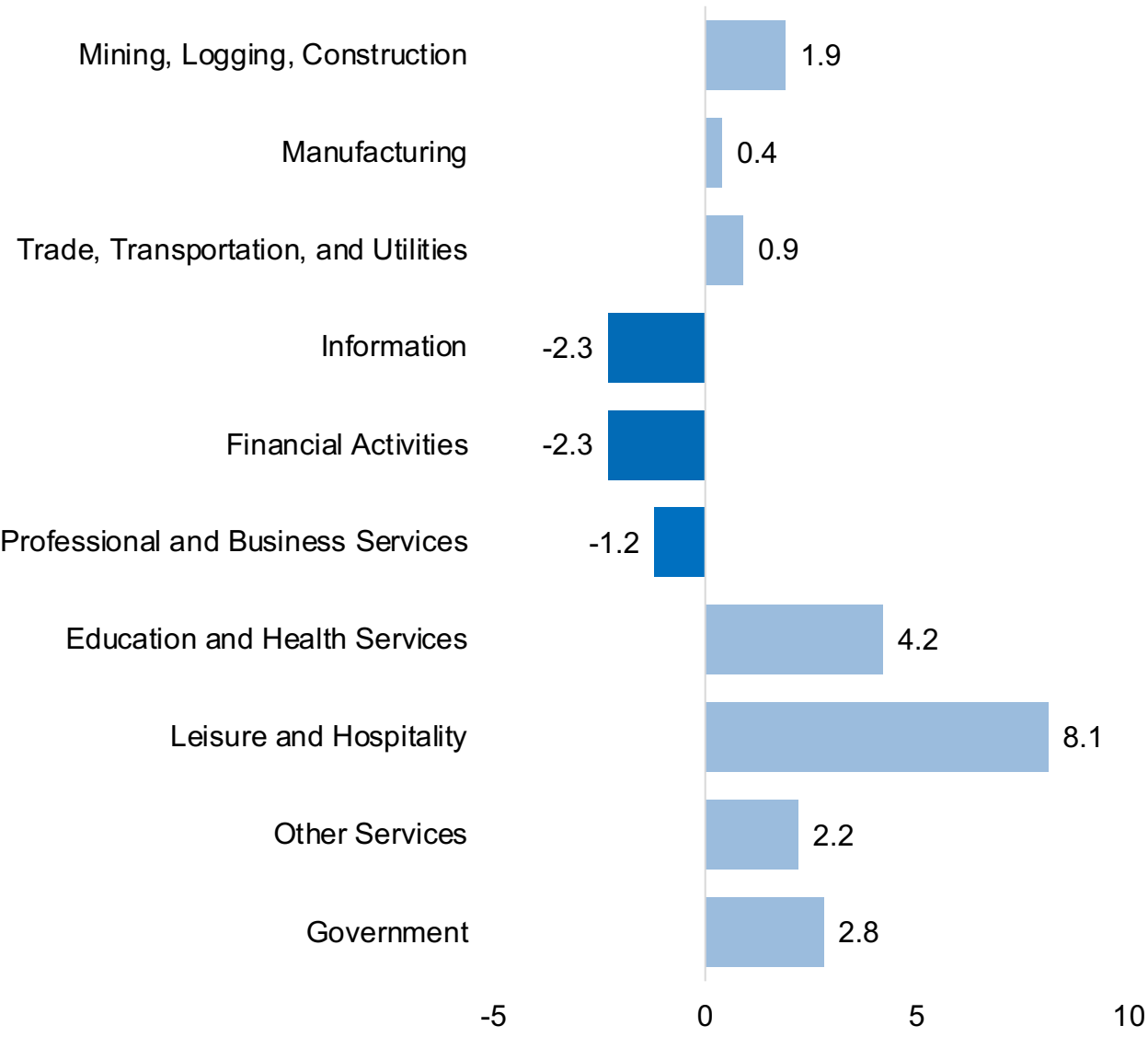
Office-Using Employment Lags While Leisure and Hospitality Sector Grows

Employment in the leisure and hospitality sector continues to thrive, driven by a shift in consumer spending preferences from goods to experiences. Information, financial activities and professional and business services are the only sectors that have seen a decline in jobs.

Employment by Industry, August, 2023



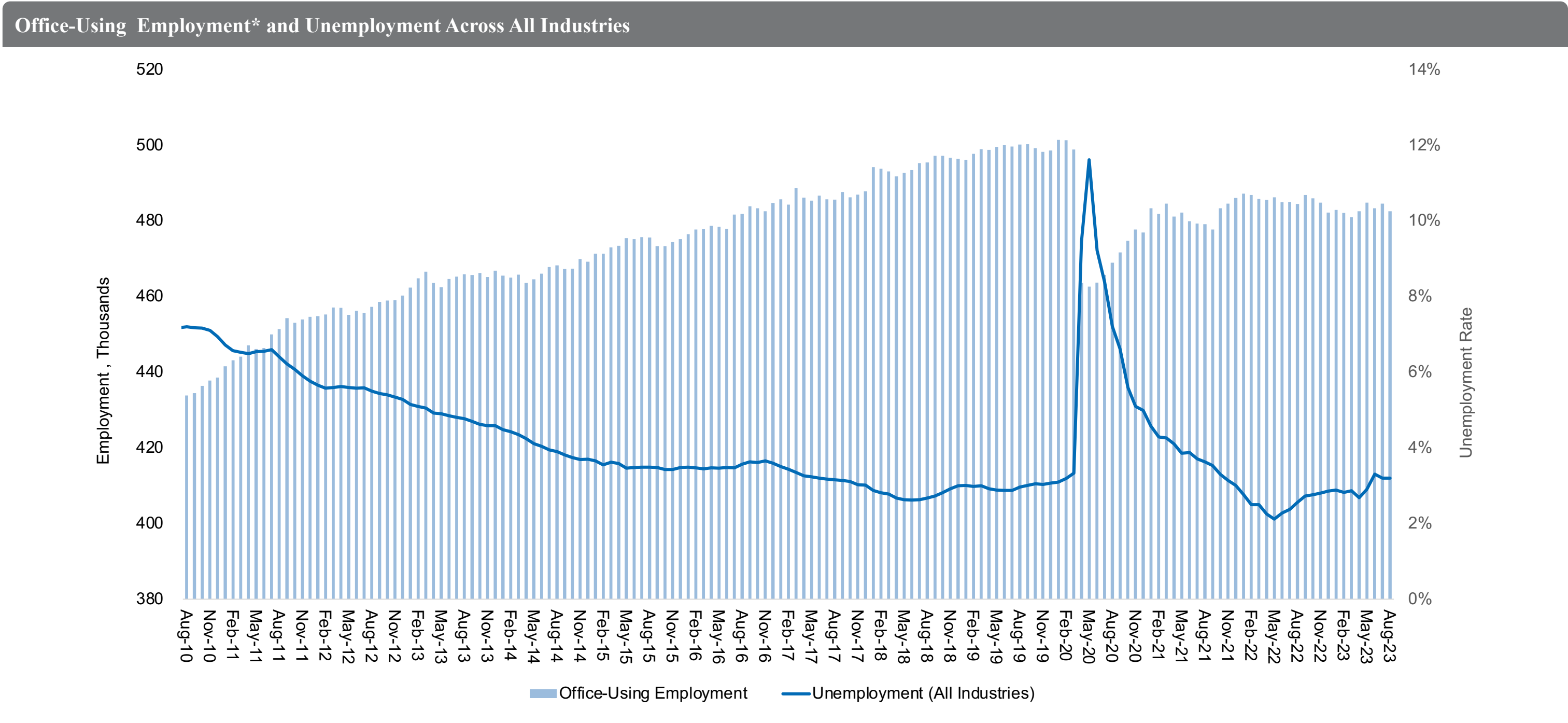
Employment Growth by Industry, 12-Month % Change, August, 2023



Source: U.S. Bureau of Labor Statistics, Minneapolis-St. Paul

Minneapolis-St. Paul Office-Using Employment Struggles to Reach Pre-Pandemic Levels

The employment sectors that utilize office spaces, including professional and business services, information and financial services, are all experiencing ongoing declines.



Source: U.S. Bureau of Labor Statistics, Minneapolis-St. Paul
*Office-using employment includes employment in the following industry sectors: Professional & Business Services, Financial Activities and Information.

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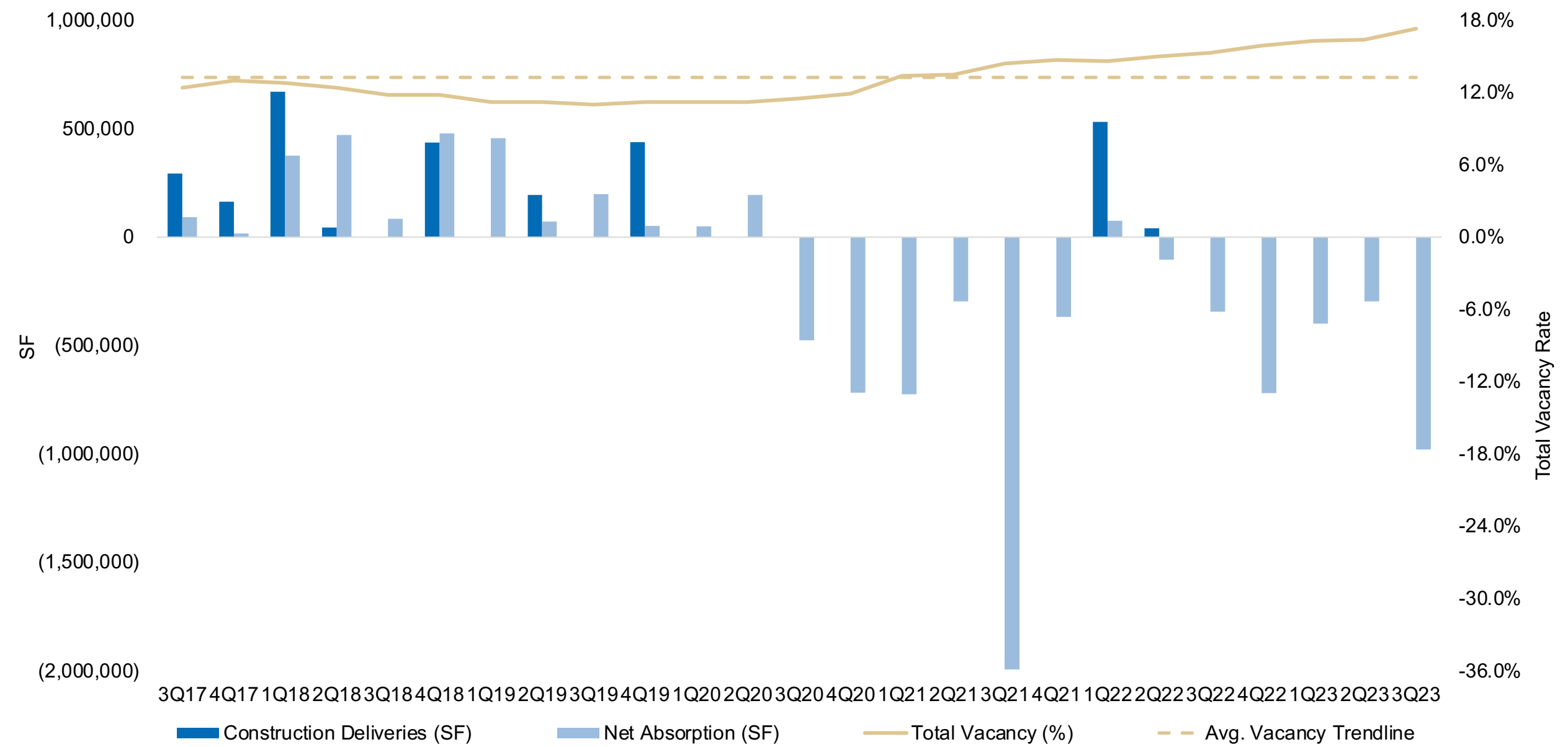
Leasing Market Fundamentals



Quarter 3 Negative Absorption at 2nd Highest Since the Start of the Pandemic

Best Buy listed 600,000 SF of space at its corporate headquarters in Richfield, accounting for more than 60% of the negative absorption during the quarter. Overall vacancy reached 17.3%.

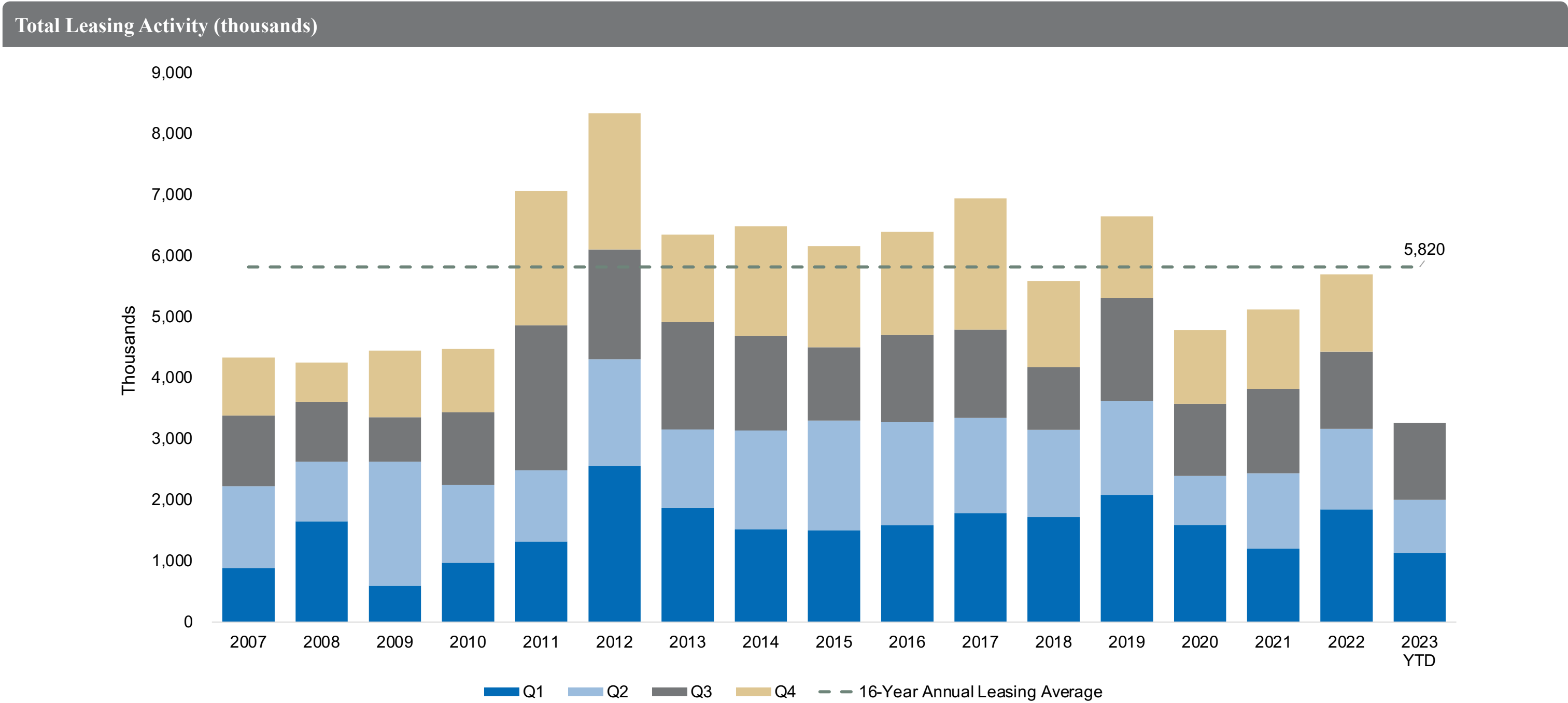
Historical Construction Deliveries, Net Absorption, and Vacancy



Source: Newmark Research, MNCAR, Costar

Leasing Activity Occurring but Most Companies Reducing Occupied Space

Activity is occurring as companies make longer-term decisions by either committing to new office spaces or renewing for longer terms. Most are reducing the amount of space they occupy.

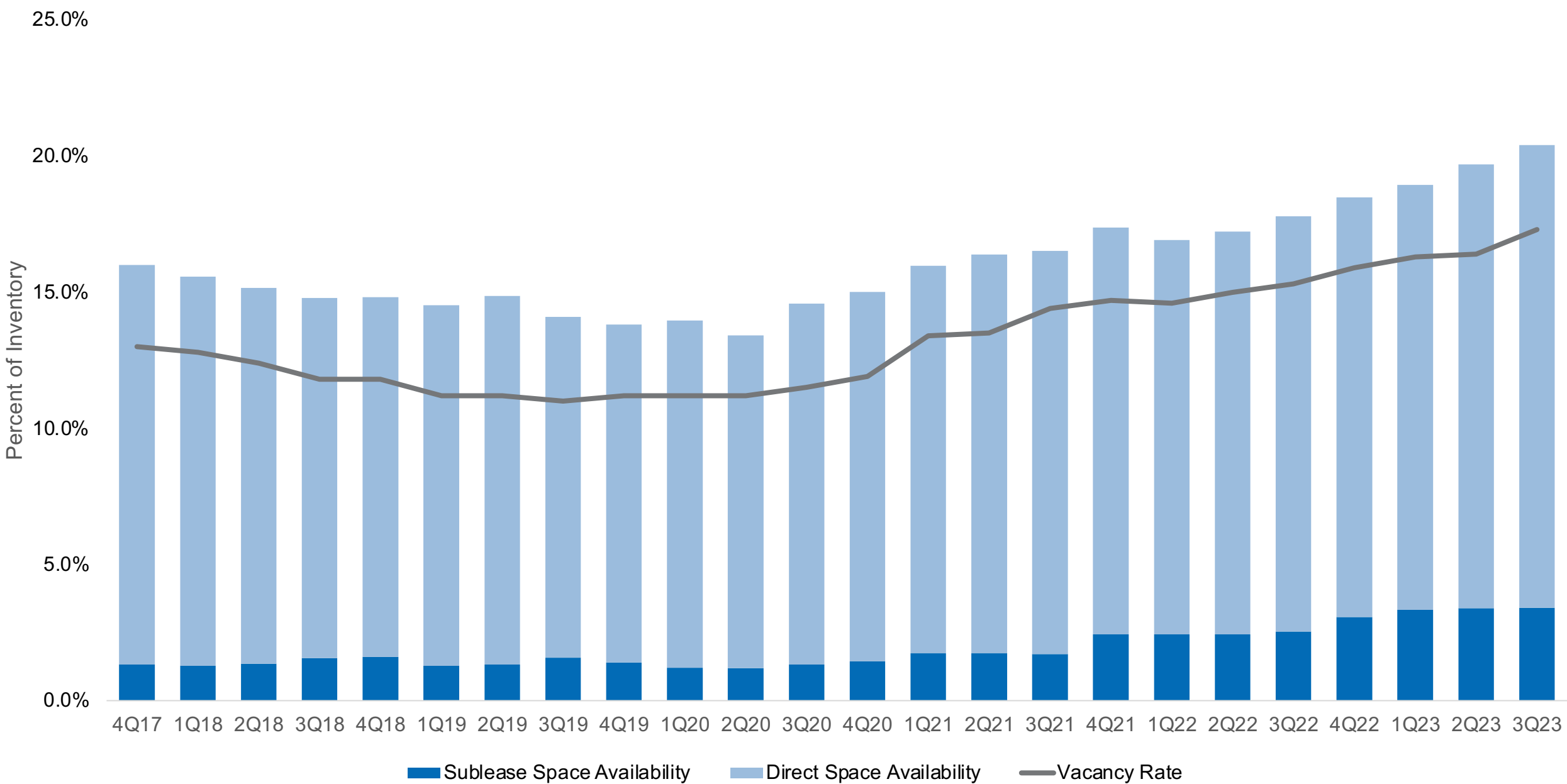


Source: Newmark Research, CoStar

Sublease Space Availability Continues to Increase

Led by corporate consolidations and a downsizing trend, the presence of sublease space remains a significant contributing factor in the vacancy rate.

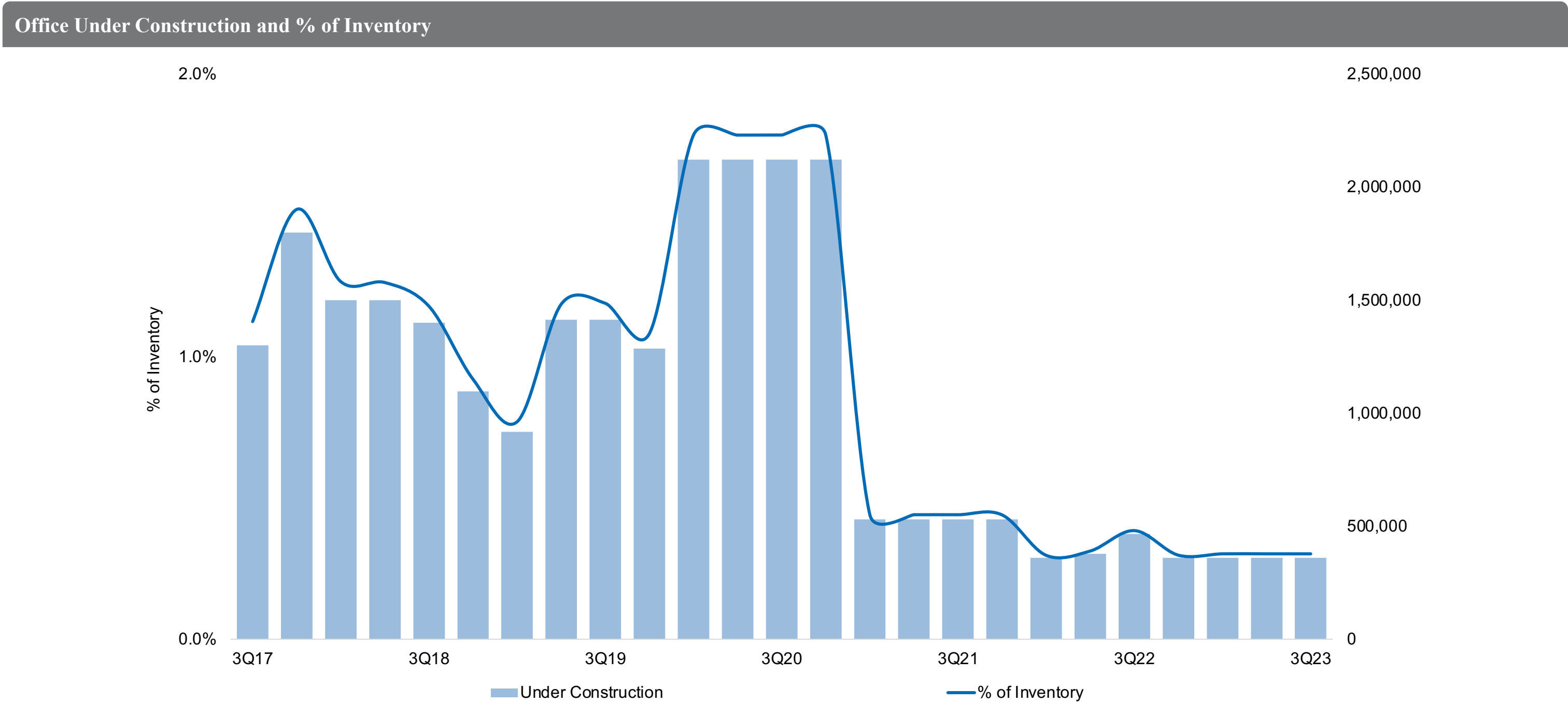
Available Space as Percent of Overall Market



Source: Newmark Research, MNCAR

Drop in Office Demand Limits New Construction

Given the ongoing decrease in demand for office space, future construction is not expected to exacerbate vacancy rates.

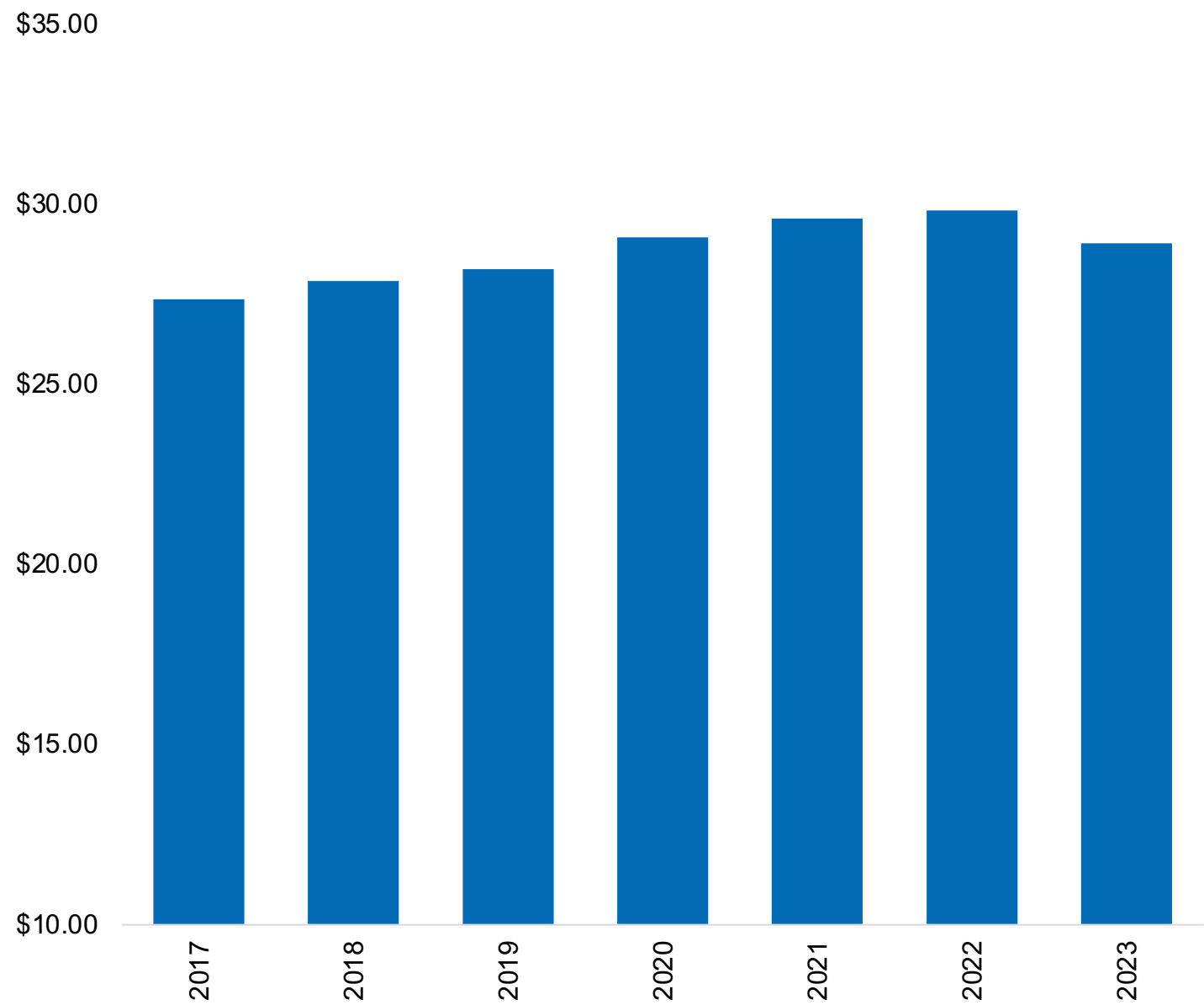


Source: Newmark Research, MNCAR, Costar

Quoted Rental Rates See a Decrease

After steadily increasing since the pandemic despite reduced demand, quoted rental rates began decreasing in the 2nd quarter and continued with a 3.1% drop this quarter. Effective rates, which take into account concession packages, are considerably lower, reflecting the real cost of leasing office space.

Office Average Asking Rent, \$/SF, FS



Year-over-Year Asking Rent Growth Rate

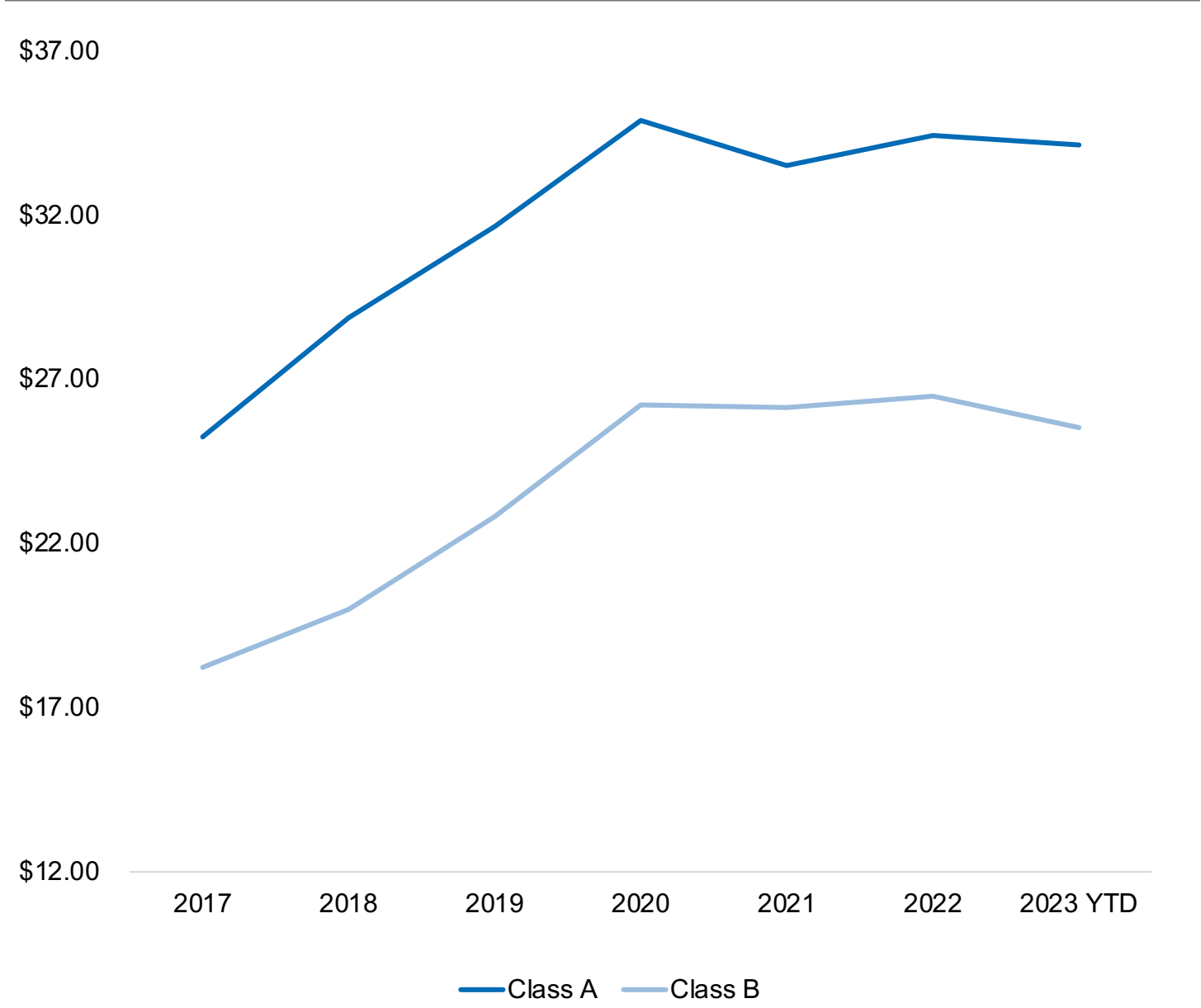


Source: Newmark Research, CoStar

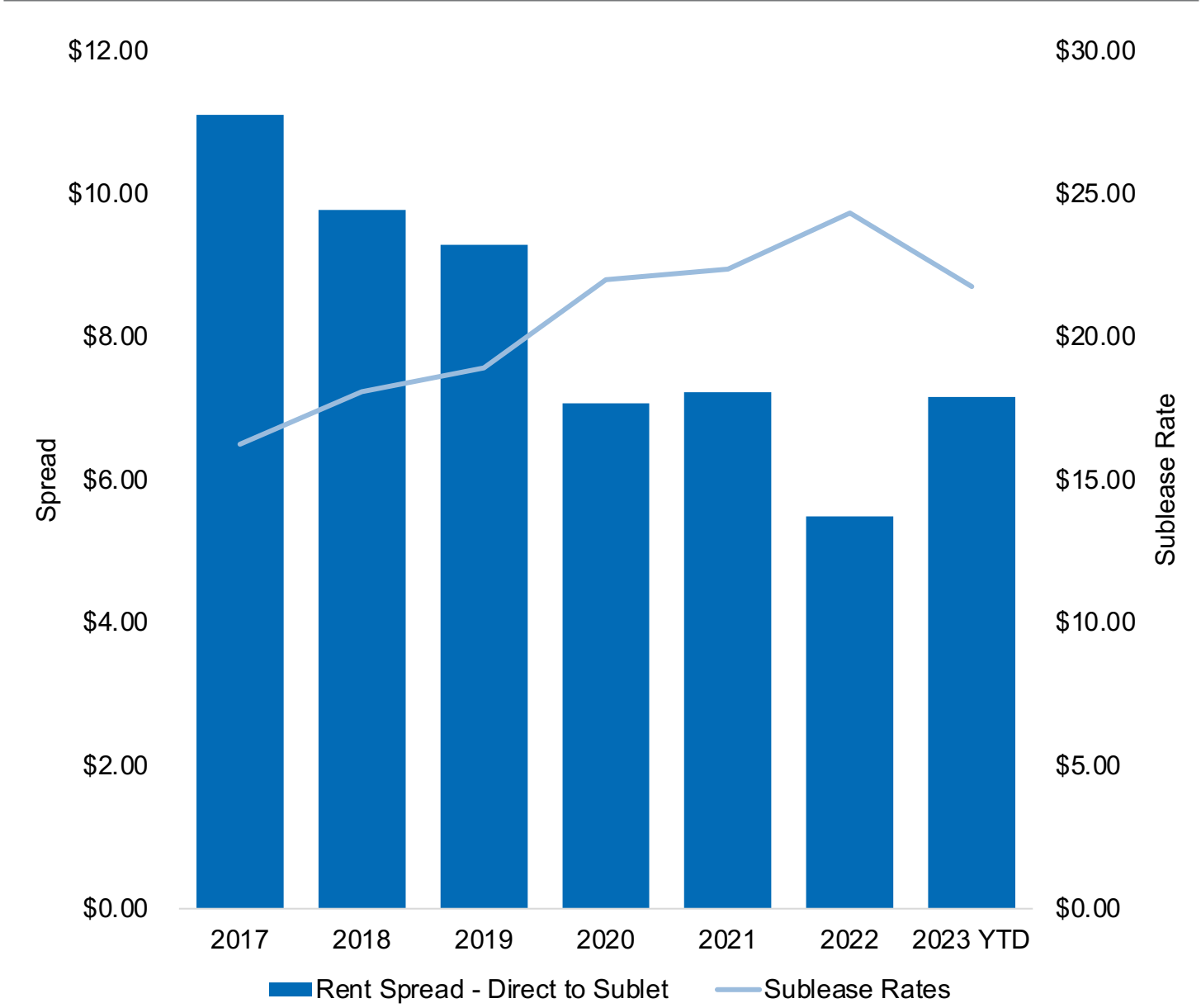
Class A Decreases Slightly; Class B Properties Decrease More Significantly by 3.6%

There is strong demand for the highest-quality properties. As a result, these properties are quoting the highest overall rates.

Class A and Class B Asking Rents



Sublease Rates



Source: Newmark Research, CoStar

Tenants Committing to Larger Subleases

Despite the continued prevalence of sublease availabilities, there has been an increase in activity among these spaces, with several significant subleases being signed during the current quarter.

Notable 3Q23 Lease Transactions				
Tenant	Building(s)	Submarket	Type	SF
Forward Edge/Lockheed	Midway Innovation Center - sublease	Northeast	New	68,308
NetSPI	Steelman Exchange - sublease	Mpls CBD - Northloop	New	60,000
WSB	Golden Hills Office Center	Golden Hills Office Center	Renewal	52,000
Polaris	Northland Corporate Center	Northwest	New	54,000
Circle K	6000 Clearwater	Southwest	New	39,385
Redpath	Securian Center	St. Paul CBD	Renewal	33,690
HSOA/Berkshire Hathaway	7500 Flying Cloud Dr - sublease	Southwest	New	20,927
Zimmerman Reed	IDS Center	Mpls CBD - Core	Renewal	15,736
Grant Thornton	Steelman Exchange	Mpls CBD - Northloop	New	15,000
Nexstar	Minnesota Center - sublease	Southwest	New	13,491
KLJ Engineering	Grand Oak Office VII	Southeast	New	13,149
Dedicated Financial	Shoreview Corporate Center	Northeast	New	12,930
Sezzle	The Dayton's Project	Mpls CBD - Core	New	11,498
Greater MSP	Osborn270	St. Paul CBD	New	10,000
Gopher Sport	Centennial Lakes Office Park V	Southwest	New	9,355
Associated Bank	IDS Center	Mpls CBD - Core	New	6,252

Source: Newmark Research, MNCAR

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