HVS

MARKET REPORT

Market Intelligence Report 2013 Minneapolis

AUGUST 12, 2013

Fortune 500 companies, universities, and a thriving arts and culture scene drive commercial, meeting and group, and leisure demand to Minneapolis hotels, which have experienced a solid recovery over the past two years.

Minneapolis and neighboring St. Paul show many signs of a strong recovery from the recent economic downturn. Healthcare, finance, and consumer goods companies are thriving in the Twin Cities. Nineteen Fortune 500 companies are based in the metro area, seven of which appear on Forbes' 2012 list of largest private companies. Area universities provide the market with an educated workforce, and with a student body of more than 50,000, the University of Minnesota boasts one of the largest enrollments in the U.S. Recent accolades from major organizations and publications speak to Minneapolis' high quality of life, and a thriving arts and dining scene placed Minneapolis on Travel + Leisure's list of "Hottest Travel Destinations" for 2013. Together, these attributes make Minneapolis a powerfully attractive destination for leisure, commercial, and meeting and group travelers.

Economy Update

The following table illustrates historical and projected employment, population, and income data for the overall Minneapolis market.

HISTORICAL & PROJECTED EMPLOYMENT, HOUSEHOLDS, POPULATION, AND HOUSEHOLD INCOME STATISTICS

Year	Total Employment	% Chg	Office Employment	% Chg	Industrial Employment	% Chg	Households	% Chg	Population	% Chg	Household Avg. Income	% Chg
2000	1,756,830	—	544,777	—	344,924	—	1,151,110	—	3,003,500	—	$98,516	—
2001	1,734,370	(1.3) %	537,656	(1.3) %	327,000	(5.2) %	1,166,070	1.3 %	3,038,160	1.2 %	98,610	0.1 %
2002	1,720,130	(0.8)	537,185	(0.1)	314,845	(3.7)	1,177,700	1.0	3,064,220	0.9	100,659	2.1
2003	1,725,200	0.3	540,971	0.7	309,747	(1.6)	1,189,520	1.0	3,091,510	0.9	104,310	3.6
2004	1,748,000	1.3	544,673	0.7	312,757	1.0	1,200,980	1.0	3,118,180	0.9	111,101	6.5
2005	1,778,600	1.8	556,988	2.3	314,087	0.4	1,213,840	1.1	3,148,070	1.0	112,301	1.1
2006	1,788,170	0.5	562,692	1.0	314,231	0.0	1,229,500	1.3	3,183,140	1.1	117,647	4.8
2007	1,792,770	0.3	563,085	0.1	311,273	(0.9)	1,245,140	1.3	3,216,510	1.0	122,266	3.9
2008	1,767,930	(1.4)	559,468	(0.6)	302,953	(2.7)	1,259,570	1.2	3,247,340	1.0	122,229	(0.0)
2009	1,687,130	(4.6)	540,783	(3.3)	274,827	(9.3)	1,272,880	1.1	3,273,810	0.8	115,186	(5.8)
2010	1,707,330	1.2	549,877	1.7	277,787	1.1	1,289,470	1.3	3,300,050	0.8	120,934	5.0
2011	1,729,630	1.3	558,828	1.6	285,721	2.9	1,307,780	1.4	3,337,650	1.1	123,620	2.2
2012	1,753,650	1.4	574,139	2.7	285,277	(0.2)	1,327,550	1.5	3,378,140	1.2	126,955	2.7
Forecasts												
2013	*1,785,650*	*1.8 %*	*583,068*	*1.6 %*	*288,397*	*1.1 %*	*1,346,820*	*1.5 %*	*3,413,370*	*1.0 %*	*$128,632*	*1.3 %*
2014	*1,839,010*	*3.0*	*596,560*	*2.3*	*294,971*	*2.3*	*1,365,760*	*1.4*	*3,447,220*	*1.0*	*134,430*	*4.5*
2015	*1,881,630*	*2.3*	*608,000*	*1.9*	*301,317*	*2.2*	*1,386,680*	*1.5*	*3,478,790*	*0.9*	*140,448*	*4.5*
2016	*1,916,470*	*1.9*	*618,735*	*1.8*	*305,818*	*1.5*	*1,406,600*	*1.4*	*3,509,360*	*0.9*	*146,506*	*4.3*
2017	*1,942,290*	*1.3*	*629,465*	*1.7*	*306,688*	*0.3*	*1,425,860*	*1.4*	*3,541,620*	*0.9*	*150,848*	*3.0*
Average Annual Compound Change												
2000 - 2012		(0.0) %		0.4 %		(1.6) %		1.2 %		1.0 %		2.1 %
2000 - 2007		0.3		0.5		(1.5)		1.1		1.0		3.1
2007 - 2010		(1.6)		(0.8)		(3.7)		1.2		0.9		(0.4)
2010 - 2012		1.3		2.2		1.3		1.5		1.2		2.5
Forecast 2012 - 2017		*2.1 %*		*1.9 %*		*1.5 %*		*1.4 %*		*0.9 %*		*3.5 %*

Source: REIS Report, 4th Quarter, 2012

Of the roughly 1.8 million persons employed in Minneapolis, 33% are categorized as office employees and 16% as industrial employees. Total employment decreased by an average annual compound rate of -1.6% during the recession of 2007 to 2010, followed by an improvement of 1.3% from 2010 to 2012. By comparison, office employment reflected compound change rates of -0.8% and 2.2% during the same respective periods. Total employment is anticipated to expand by 1.8%, and office employment by 1.6%, in 2013. Total employment is expected to improve at an average annual compound rate of 2.1% for the period of 2012 through 2017, and office employment is forecast to improve by 1.9% on average annually during the same time frame. Household average income is forecast to grow by an average of 3.5% annually between 2012 and 2017.

The following table highlights major employers with operations based in the Minneapolis-St. Paul metropolitan area.

MAJOR EMPLOYERS

Firm	Number of MN Employees
Target Corporation	30,773
University of Minnesota	25,166
Allina Hospitals and Clinics	23,869
Wells Fargo	20,000
Fairview Health Services	19,594
UnitedHealth Group	18,000
3M	15,000
HealthPartners	11,001
US Bancorp	10,883
Park Nicollet Health Services	8,342

Source: 2013 Business Information Guide - Twin Cities Business Magazine

The healthcare sector is heavily represented in the list above, and the metro area is also home to high-profile companies such as Cargill, Best Buy, General Mills, and Target, the area's largest employer. SuperValu announced that approximately 600 Eden Prairie-based employees would be laid off later this year, and Best Buy will be laying off 400 employees in the Minneapolis suburb of Richfield. Nevertheless, growth is occurring at other local companies, including UnitedHealth Group and General Mills, and the relocations of Pinnacle Airlines and other new companies to the local market are anticipated to offset some of these job losses.

The following table lists unemployment figures in the greater Minneapolis area, as well as the state and nation as a whole, from 2002 to 2011.

UNEMPLOYMENT STATISTICS

Year	County	MSA	State	U.S.
2002	4.4 %	4.4 %	4.5 %	5.8 %
2003	4.6	4.7	4.9	6.0
2004	4.4	4.4	4.6	5.5
2005	3.8	3.9	4.2	5.1
2006	3.6	3.8	4.1	4.6
2007	4.2	4.4	4.7	4.6
2008	4.9	5.1	5.4	5.8
2009	7.5	7.9	8.0	9.3
2010	7.0	7.3	7.3	9.6
2011	6.0	6.3	6.4	9.0
Recent Month - Dec				
2011	5.2 %	5.5 %	5.8 %	8.5 %
2012	4.8	5.1	5.4	7.8

* Letters shown next to data points (if any) reflect revised population controls and/or model re-estimation implemented by the BLS.

Source: U.S. Bureau of Labor Statistics

Unemployment in Minneapolis remains well below the national level, a fact attributable to the city's diverse economic base, which ranges from healthcare to banking to manufacturing. Unemployment increased in 2008 and more dramatically in 2009, a result of the recent recession; however, rates for 2010 and 2011 illustrate an improving trend. Data from the most recent comparative period reflect a continuing decline in unemployment.

Office Space Market Update

The following table details the Minneapolis-St. Paul area's office space statistics, which are important indicators of a market's propensity to attract commercial hotel demand.

OFFICE SPACE STATISTICS – MARKET OVERVIEW

Submarket	Inventory Buildings	Inventory Square Feet	Occupied Office Space	Vacancy Rate	Average Asking Lease Rate
1 Midway	52	3,854,000	3,002,300	22.1 %	$18.80
2 St. Paul CBD	28	5,094,000	3,759,400	26.2	19.34
3 Dakota County	100	4,353,000	3,404,000	21.8	18.55
4 Washington Cty	40	1,512,000	1,143,100	24.4	17.87
5 SW/NE Scott Cty	200	20,309,000	16,592,500	18.3	23.70
6 Minneapolis CBD	136	27,177,000	23,236,300	14.5	22.84
7 West/Northwest	159	11,881,000	9,706,800	18.3	23.17
8 Northeast	64	3,620,000	2,859,800	21.0	18.45
9 Anoka Cty	21	611,000	458,900	24.9	17.61
Totals and Averages	**800**	**78,411,000**	**64,163,100**	**18.2 %**	**$22.11**

Source: REIS Report, 4th Quarter, 2012

Of the greater area's more than 78 million square feet of office space, the Minneapolis CBD houses the largest inventory with the lowest vacancy rate and commands the second-highest average asking lease rate; the Southwest Minneapolis/NE Scott County submarket boasts the highest lease rate. With CBD parking rates reportedly above the national average, suburban areas like Brooklyn Park and Minnetonka are becoming popular locales for corporate expansions.

The following table illustrates historical and projected trends for office space statistics for the overall Minneapolis-St. Paul market.

HISTORICAL AND PROJECTED OFFICE SPACE STATISTICS – GREATER MARKET

	Minneapolis Market						
Year	Available Office Space	% Chg	Occupied Office Space	% Chg	Vacancy Rate	Asking Lease Rate	% Chg
2000	72,272,000	—	65,918,000	—	8.8 %	$23.36	—
2001	74,931,000	3.7 %	64,603,000	(2.0) %	13.8	22.50	(3.7) %
2002	75,645,000	1.0	61,961,000	(4.1)	18.1	21.70	(3.6)
2003	75,809,000	0.2	61,029,000	(1.5)	19.5	21.01	(3.2)
2004	75,508,000	(0.4)	61,099,000	0.1	19.1	20.92	(0.4)
2005	75,996,000	0.6	61,734,000	1.0	18.8	20.62	(1.4)
2006	76,127,000	0.2	63,155,000	2.3	17.0	21.03	2.0
2007	77,079,000	1.3	65,436,000	3.6	15.1	21.72	3.3
2008	78,014,000	1.2	64,950,000	(0.7)	16.7	21.89	0.8
2009	78,297,000	0.4	63,006,000	(3.0)	19.5	21.81	(0.4)
2010	78,324,000	0.0	62,819,000	(0.3)	19.8	21.61	(0.9)
2011	78,292,000	(0.0)	63,582,000	1.2	18.8	21.79	0.8
2012	78,411,000	0.2	64,162,000	0.9	18.2	22.11	1.5
Forecasts							
2013	*78,911,000*	*0.6 %*	*64,888,000*	*1.1 %*	*17.8 %*	*$22.55*	*2.0 %*
2014	*79,433,000*	*0.7*	*65,697,000*	*1.2*	*17.3*	*23.28*	*3.2*
2015	*80,288,000*	*1.1*	*66,828,000*	*1.7*	*16.8*	*24.12*	*3.6*
2016	*81,265,000*	*1.2*	*68,328,000*	*2.2*	*15.9*	*25.17*	*4.4*
2017	*82,450,000*	*1.5*	*70,165,000*	*2.7*	*14.9*	*26.13*	*3.8*
Average Annual Compound Change							
2000 - 2012		0.7 %		(0.2) %			(0.5) %
2000 - 2007		0.9		(0.1)			(1.0)
2007 - 2010		0.5		(1.4)			(0.2)
2010 - 2012		0.1		1.1			1.2

2010 - 2012	0.1	1.1	1.2
Forecast 2012 - 2017	*1.0 %*	*1.8 %*	*3.4 %*

Source: REIS Report, 4th Quarter, 2012

The inventory of office space in the Minneapolis market increased at an average annual compound rate of 0.7% from 2000 through 2012, while occupied office space contracted at an average annual rate of -0.2% over the same period. The onset of the recovery is evident in the 1.1% average annual change in occupied office space from 2010 to 2012. From 2012 through 2017, the inventory of occupied office space is forecast to increase at an average annual compound rate of 1.8%. Available office space is expected to increase by 1.0%, resulting in an anticipated vacancy rate of 14.9% as of 2017, the lowest level realized since 2001.

Major developments in Minneapolis include the new Green Line light rail, which will connect Minneapolis and the University of Minnesota campus with Downtown St. Paul; the new line is scheduled to open in 2014. In addition, Vikings Stadium will be demolished and rebuilt in the Downtown East neighborhood; the Vikings are scheduled to play in the current stadium through 2013. The ease in metro travel, in addition to the upgraded sports facility, is expected to boost visitation to the greater metro area.

Hotel Construction Update

The 500-room Radisson Blu opened on March 15, 2013, on the south end of the Mall of America (MOA). This is expected to be the last large hotel to enter the market until the potential opening of a Downtown convention hotel, which is currently being evaluated. Additional hotels are planned in Bloomington, including an upscale hotel at Bloomington Central Station and a full-service hotel as part of Phase II of the MOA expansion. Smaller hotels are also proposed in Bloomington, Minnetonka, and Downtown Minneapolis, including a boutique hotel on 1st Avenue. While several new hotels are expected to enter the market in the coming years, the percentage increase to the overall market supply will be minimal.

Outlook on Market Occupancy and Average Rate

Occupancy remained relatively stable between 2011 and 2012 in the metro area, and average rate grew by approximately 3%. The growth in rate resulted in a RevPAR level comparable to that realized between 2007 and 2008, indicating that a market recovery is taking hold. Based on group bookings, year-to-date travel trends, and changes in supply, HVS anticipates that market occupancy will be relatively flat in 2013, followed by slight increases in 2014, 2015, and 2016 to a stabilized level of 63%. Given strong mid-week demand throughout the year, strong weekend demand during the summer months, and the entrance of some new upscale supply, average rate growth for the metro area is expected to rise above inflationary levels for the next several years.

Recent Hotel Transactions

The following table lists hotel transactions in Minnesota from April of 2010 through December of 2012.

REVIEW OF HOTEL TRANSACTIONS

Property Name	City	Rm. Count	Date of Sale	Price Paid	Price Per Room
Sheraton St. Paul Woodbury	Woodbury	150	December-12	$13,400,000	$89,333
Comfort Inn Lakeville	Lakeville	54	November-12	$1,800,000	$33,333
Hotel Minneapolis Autograph Collection	Minneapolis	222	October-12	$46,000,000	$207,207
DoubleTree by Hilton Suites by Hilton Minneapolis	Minneapolis	229	September-12	$28,761,942	$125,598
Le St. Germain Suite Hotel	Saint Cloud	103	September-12	$6,200,000	$60,194
AmericInn Walker	Walker	37	July-12	$1,150,000	$31,081
Days Inn Burnsville	Burnsville	84	July-12	$1,515,000	$18,036
Country Inn & Suites Eagan	Eagan	78	July-12	$4,200,000	$53,846
Cambria Suites Maple Grove	Maple Grove	129	June-12	$7,150,000	$55,426
Comfort Inn Brooklyn Center	Brooklyn Center	60	June-12	$2,050,000	$34,167
Embassy Suites St. Paul Downtown	St. Paul	208	May-12	$14,030,224	$67,453
Quarterdeck Resort	Nisswa	44	April-12	$2,250,000	$51,136
Days Inn Bloomington West	Bloomington	141	March-12	$3,900,000	$27,660
Ramada Mall of America Airport	Bloomington	255	December-11	$14,400,000	$56,471
University Hotel Minneapolis	Minneapolis	304	August-11	$20,750,000	$68,257
Hyatt Place Minneapolis Eden Prairie	Eden Prairie	126	July-11	$9,525,000	$75,595
AmericInn Ham Lake	Ham Lake	52	April-11	$1,450,000	$27,885
DoubleTree by Hilton Bloomington Minneapolis South	Minneapolis	564	January-11	$20,000,000	$35,461
Motel 6 Rochester	Rochester	86	January-11	$1,000,000	$11,628
Motel 7	Fergus Falls	17	December-10	$540,000	$31,765
Fifth Avenue Inn & Suites	Rochester	62	October-10	$3,700,000	$59,677

Grand Hotel Minneapolis	Minneapolis	140	September-10	$33,000,000	$235,714
Nicollet Inn	Burnsville	144	July-10	$3,500,000	$24,306
Hilton Minneapolis	Minneapolis	821	June-10	$155,500,000	$189,403
Hotel Minneapolis Autograph Collection	Minneapolis	222	May-10	$21,000,000	$94,595
Homewood Suites by Hilton Minneapolis Mall of America	Bloomington	144	April-10	$18,000,000	$125,000
Radisson Bloomington by Mall of America	Bloomington	403	April-10	$39,100,000	$97,022
Crossings Inn & Suites Becker	Becker	68	April-10	$1,750,000	$25,735

In addition to the sales listed above, the Crowne Plaza and DoubleTree in St. Paul were purchased for an undisclosed amount in March of 2013 by the Mille Lacs Band of Ojibwe. The former Comfort Suites in Downtown Minneapolis was purchased in October of 2012 for an undisclosed amount by an affiliate of Hyatt Hotels; this property is scheduled for renovation and conversion to a Hyatt Place by the summer of 2013, at which time Summit Hotel Properties will acquire the asset. The recent sales of the Comfort Suites and the Hotel Minneapolis Autograph Collection indicate the attractiveness of the market for institutional investors. Another Downtown property, the Hotel Ivy, is actively being marketed for sale. Brokers convey confidence in Minneapolis' hotel market given the diversity of the area's economy and the quick recovery of occupancy following the recession, as well as a highly educated workforce and low unemployment levels in the city.

Conclusion

Expansions at local corporations and a drop in office vacancy to levels below those of 2005 both bode well for the continued economic growth in the greater Minneapolis market. Market-wide occupancy has shown stability in the last calendar year, and average rate growth has surpassed inflationary levels for the last two years. Given current demand trends and anticipated supply additions in the market, average rate is anticipated to surpass pre-recessionary levels in 2013. Together, these developments and forecasts provide for an optimistic outlook for the Minneapolis hotel market in the near term.