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Founders Properties' Wade Lau: Don't expect the Twin Cities industrial market to lose its momentum anytime soon

By Dan Rafter, Editor

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Still strong. That's the best way to describe the industrial market in the Minneapolis-St. Paul market.

What's behind this strength? Ecommerce is still fueling much of the demand for industrial space. Companies still need distribution centers across the country to deliver their products and warehouse space to store it. And they are looking for these spaces across the country, including in the Twin Cities.

At the same time, the push to bring manufacturing back to the United States is inspiring more companies to open industrial facilities in the country, providing another boost to industrial demand.

While the Twin Cities market isn't a big distribution market, because of its location, the Minneapolis-St. Paul region is still seeing strong demand for industrial space.

We spoke with Wade Lau, president and chief executive officer of Minnetonka, Minnesota-based real estate investment management company Founders Properties, about the resilience of the local industrial market and what the future might hold for it.

Here is some of what he had to say.

What makes industrial properties, in the Twin Cities area and across the country, such a good asset type for investors?

Wade Lau: The investment characteristics are really solid. Vacancies have held up well over the long term. It's an investment that cash flows, unlike office, which doesn't cash-flow particularly well.

But there are also strong tailwinds, strong megatrends, that are benefitting industrial. Ecommerce is still a big driver of industrial demand. The need for last-mile warehouse space is not slowing. That trend

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Twin Cities metro area scores another big industrial lease: Schimberg Co. opens first location in Minnesota

By Dan Rafter, Editor

The suburbs surrounding the Twin Cities continue to attract new tenants looking for industrial space. An example? Just look at a recent lease in suburban Woodbury.

Schimberg Co., a regional pipe, valves and fittings supply company headquartered in Cedar Rapids, Iowa, recently opened its first Minnesota location with a new lease in the Royal Gateway Commerce Center in Woodbury. Schimberg becomes the first occupant in the commerce center's Building B.

What attracted Schimberg to the building? John Young, vice president- advisory with Forte Real Estate Partners, represented the company in its search for the right site. He said that several factors attracted Schimberg to the Woodbury location.

One of the most important? The quality of the workforce in and around the region.

"Officials with Schimberg believed that they would have a great workforce from eastern Minnesota and western Wisconsin," Young said. "That was a big factor for them. And it's a workforce particular to the industry, people who know how to run heavy equipment and drive a truck. Schimberg knew that it could attract those employees to this Woodbury location."

Schimberg also found the right building, Young said. Royal Gateway Commerce Center Building B features 28-foot clear heights, something that was critical to Schimberg. The higher clear height allows Schimberg to do their racking properly and efficiently, Young said.

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line will continue. A product needs three times the amount of warehouse space if it goes through the ecommerce channel as it needs if it is sold in a store. Companies will continue to need that warehouse and distribution space.

Then there is the push for onshoring and reshoring. The reinvestment in this country in manufacturing is real, and that, too, is increasing the demand for industrial.

Those are two important megatrends that help make industrial such a strong asset class. We do think this is a good time to invest in industrial real estate.

Ecommerce certainly got a push during COVID. But the growth of ecommerce was taking place long before the pandemic, right?

Lau: Definitely. The rise of ecommerce has almost been a straight line. It started in the early 2000s that ecommerce sales were steadily accounting for a greater percentage of all retail sales. COVID accelerated the growth of ecommerce, but the rise of ecommerce sales has been a very steady trend line up for a long time.

How strong is the reshoring trend?

Lau: The reshoring and onshoring activity have been steady. There has been significant investment from governments through the CHIPS Act. That has spurred significant investment in manufacturing around the country. Manufacturing has become a bigger piece of the industrial market. Manufacturing still accounts for a smaller percentage of industrial space than distribution facilities and warehouses. But it accounts for a bigger percentage of the demand for industrial space today than it did several years ago.

Here in Minneapolis, our friends at Opus are building the big build-to-suit in Maple Grove for a manufacturing entity. That's an example of the sort of investment in manufacturing that is happening.

How strong is the industrial market in the Twin Cities?

Lau: The industrial sector is performing well here. Relative to other cities, we have a low vacancy rate. It is sub-5%. That is positive. Development has tailed off, as it has in most markets, and most of the new development that is taking place is build-to-suit. We are seeing more build-to-suit than speculative development.

The amount of institutional ownership has grown in Minneapolis significantly. Link Logistics, for example, owns a significant amount of industrial space here. These larger institutional owners have helped boost industrial rents in the market.

We are not a large distribution market. We have some regional distribution, but Minneapolis doesn't have that two-day travel to most of the country that markets like Chicago, Indianapolis or Columbus can claim. Overall, though, the numbers are good in our industrial sector. Rents are still growing and vacancy rates are low. Demand for industrial space in the Twin Cities market remains strong.

Another thing to consider: Not all Midwest cities are seeing population growth. Minneapolis still has good population growth. We like Minneapolis as a good place to invest. We have meaningful investments here.

Wade Lau
(Photo courtesy of Founders Properties.)

When do you think we might see more spec industrial construction in the Twin Cities market?

Lau: The relationship between rents and new construction costs must be in the right balance. The capital needs to be available. The banks with the run-up in interest rates three years ago really slowed their lending to almost a trickle. That's meaningful because banks account for 40% to 50% of the debt capital in real estate. They got out of the business and that slowed development. For us to see more spec, the banks will need to come back stronger than they have so far.

We also need to see a little bit more industrial space get absorbed. The banks coming back will create more transaction activity. That will solidify values and will help developers underwrite the value of their properties.

Do you think we'll see more investment sales in the industrial market this year?

Lau: Investment sales activity has been slow. But it has been getting better. The banks coming back will help with this, too. The liquidity question is a big deal. When you take that much debt capital out of the system, you will see fewer transactions. The financial environment is unpredictable now, too. There is a little pause out there in investment sales as investors wait to see how everything settles out.

But I'm very optimistic that over the course of the next 12 to 24 months we will see investment sales pick back up. Of course, every time it looks like we're going to get there, something crops up and it doesn't happen. But I am hopeful that transaction activity will go up as the year unfolds.

What attracts investors to the Twin Cities?

Lau: Our metro area has a lot of strengths. Growth is one thing. We are seeing population growth. That means more employees and shoppers. Growth matters. We also have an educated workforce. That makes a difference, too. There is transportation and manufacturing infrastructure already in place here. You are not starting from a dead stop when you are developing something here. You are not trailblazing here.

Are there any new or planned industrial developments in the Twin Cities area that you are excited about?

Lau: There are a number. The interesting one that everyone is watching is the redevelopment of the Thomson Reuters campus in Eagan. That will be a fascinating project to watch. It is going to be big. It's also in a great location. Eagan is a great location. We are seeing this phenomenon elsewhere, where owners are converting large, older office campuses into industrial uses. That is interesting. It's a way for developers to get at infill sites. There are some real advantages if you can develop an infill site, to get your buildings closer to population centers.

The strongest submarkets in the Twin Cities are the infill markets. There is investment going on in existing buildings, too, with developers boosting the functionality of these older properties. That is happening in a lot of the infill areas, particularly when it comes to light manufacturing. Infill space is attractive to those kinds of companies.