

REVITALIZING REAL ESTATE

Regional Pros Assess the Commercial and Housing Sectors – and See a Brightening Horizon

By Catherine Conlan

For many commercial real estate firms in the Duluth area, the past couple of years have been ones to forget. But to hear them talking about the next couple of years – those could be some to remember.



GREG FOLLMER - REAL LIVING MESSINA & ASSOCIATES

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“2008 and 2009 were some of the worst years I’ve ever seen,” said Greg Follmer of Real Living Messina & Associates. “And as much as I’ve seen good results in 2010, it’s still pretty soft...[but] I think the turnaround is here. That’s the way I see it.”

Commercial real estate – the buying, selling and leasing of office, retail and light industrial space, as well as hotels, restaurants and managed multifamily units – stumbled shortly after the collapse of the residential single-family home real estate market several years ago. But Follmer and others believe that signs of life are returning to other kinds of real estate.

“During the good times, we didn’t really have the boom that other communities have recognized, so we are in a position that we are not suffering as big a bust that others have realized,” said Sandy Hoff of F.I. Salter Co., Inc. “All in all, our market has been reasonably stable, especially in the Duluth area. There is clearly softness in the market, and it’s a result of a difficult banking and lending environment. It’s difficult to secure financing for new projects, and that creates challenges for new projects.”

Follmer said that while banks might be more circumspect about lending, he hasn’t seen it disrupt too many deals. “I have noticed that a couple banks have to hang onto more money now; it’s more closely watched,” he said. “But there are plenty of institutions lending, and I think that’s maybe it – you’ll see more select lending. There’s not as much risk on speculative purchases. There will be again someday, but right



ANDY WEYRAUCH - SHIPROCK MANAGEMENT

now there’s no need to.”

In the recovering market in the Duluth area, Follmer said there are some hot spots for retail and services: “The hottest section of town is the Miller Hill Mall [area], east downtown between Lake Avenue and 12th Avenue East, and even as far as 21st Avenue along London Road. But if you were off the beaten path, you’re struggling.”

He said health care was seeing some good gains. “The biggest, best thing in town to me is a lot of medical tenants – home health care companies,

health service companies, that sort of thing,” Follmer said. “They’re a huge benefit to the downtown area. They are the single biggest ‘pops’ that there are. I get a lot of calls on that and am filling spaces with it. Tenants that have that kind of business generally find that they can pay the bills.”

Residential rentals are also doing well. “The rental market in Duluth is very strong and stable – it’s a good market in terms of residential apartments,” said Andy Weyrauch of ShipRock Management. “Five or six

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or seven years ago, there were waiting lists for people who wanted to take up residence here. The paradigm has shifted ... the city has as many people looking for apartments as there are apartments available, and I think that is because we've had more rentals come on board."

Nevertheless, that doesn't mean there weren't some bad times. "It slowed down for sure," Weyrauch said. "But multifamily [residences] is a pretty strong market. Normally, when someone wants to sell, there are people ready to buy them. A lot of people who have owned them for a long time

even pass them on to their children; the turnover there is very slow."

Mike Edmunds of Edmunds Co. Real Estate, Sales & Development, LLP agreed. "Our senior subsidized housing building in Woodland is full, as well as our Mount Royal Pines units ... we have a couple other buildings we purchased just off Elizabeth Street a couple years ago, and they're pretty close to 100 percent," he said. "We've been down to Florida a couple times, and we're not even close to the boom that they experienced - and we're not even close to the bust that they have now." The industry here, he said, "has

experienced a 15 to 20 percent decline versus a 50-60-70 percent decline - and we're picking up again. I think the worst feels over."

The downturn in other industries has had an effect on real estate here. "Hospitality might be hit a little harder than other segments" of real estate because of the downturn, Hoff said, "just because both tourists and business travelers are traveling a bit less. We've held up in this market better than other communities, and that's a testament to the operators here, which are positioned well in this market."

Conversely, when other industries start rising again, that can help real estate, Follmer noted. The area has positioned itself well after the previous downturn in the 1980s, he said, and "we're doing a lot to improve on that, with the development at the DECC, work at the industrial seaport that gives the opportunities for high-paying labor, and with all the mines up and running on the Iron Range - that's really good. When all mines are



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up, that's a huge indicator. Tourism as well. There will be really good things in the next 10 years."

New development could perk up in the coming years, too. "There's still some optimism for a few people looking at developing projects," Weyrauch said. "With the armory, people are looking at turning that into a student facility and moving full force on that ... the city recently put in new planning and zoning stuff that just got passed, putting together certain areas where complexes could be built. There are a lot of favorable things right now. Interest rates are low, construction

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costs are low; all the forces are lining up for somebody to develop."

Again, however, it will depend on the banks and their underwriters: "If you go to a bank with a new restaurant or apartment building or retail project, they're looking at every project with a much higher level of scrutiny, and you may need to have more equity or cash in your project, and you certainly need to have very solid financials backing the investor group," Hoff said. "And even with all those things in place, you still may not be able to secure financing very easily in this market. The good news is, I believe that's going to change."

And while it's impossible to make predictions about almost anything in the current economy, many of the thoughts about the coming years are cautiously optimistic.

"Cautiously optimistic? We would support that," Edmunds said. "Definitely, from the residential standpoint, we are more optimistic this year than last year."

"In 2010, we'll work through some of the challenges," Hoff said. "We'll see a lot more activity in 2011."

Follmer agreed: "I've seen an awful lot of transactions, mostly small and local - small businesses are seeing younger [owners] leasing spaces, small businesses doing stuff and I really think it's here. 2010 is going to be a great year and you can probably look forward to make your money over the next 10 years." **D**

Catherine Conlan is a Two Harbors, Minn.-based writer who covers Northeastern Minnesota economic topics.

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