MID-2016
SIOUX FALLS, SD
MARKET OUTLOOK REPORT

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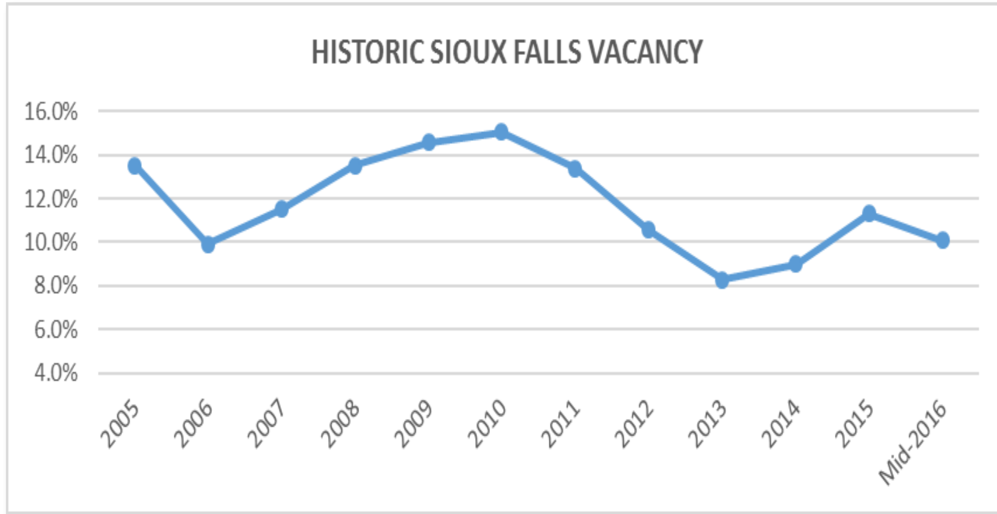
Bender
COMMERCIAL

OFFICE MARKET
ANDI ANDERSON, SIOR

By mid-2016, Sioux Falls entire office market consisted of approximately 14,320,187 square feet of space. This figure includes both owner and owner-occupied buildings. However, buildings that are entirely leased by an owner do not truly affect the market's rental rate, hence it is removed in this report when examining the market. This criteria left 7,652,228 square feet of tenant-occupied space, an increase of nearly 70,000 square feet in the past six months. The overall vacancy of the Sioux Falls office market decreased from 11.3% at the end of 2015 to 10.1% by mid-2016.

Central Business District. The CBD did not add any inventory to the market in the first six months of 2016, however, this segment did see over a percentage point decrease in its vacancy rate, from 9.3% to 8.2%. The asking lease rates in this market decreased slightly to $13.45/sq. ft. from $14.00. This decrease was due to the increase vacancy in the Class B/C space.

Suburban Market. The entirety of the 70,000 square foot increase in the Sioux Falls office market occurred in the suburban segment. This increase was due to four conversions from owner-occupied and one newly constructed 35,000 square foot office building in the southwest area of Sioux Falls. The conversions brought with it new vacant space, however this segment still had a slight decrease in its vacancy rate, 11.4% from 12.2% The majority of this decrease was found in the Class A buildings. The average asking rate for Class A space increased approximately $0.30/sq. ft. in the past six months, while the Class B/C space went down nearly $1.00 per square foot.



OFFICE MARKET SURVEY RESULTS	CBD	CLASS A CBD	CLASS B/C CBD	SUBURBAN	CLASS A SUBURBAN	CLASS B/C SUBURBAN	TOTAL
INVENTORY	**2,326,937**	691,399	1,635,539	**5,325,91**	1,609,422	3,715,869	**7,652,228**
VACANCY	**191,689**	37,097	154,590	**609,942**	129,647	480,295	**801,629**
VACANCY RATE	**8.2%**	5.5%	9.4%	**11.4%**	8.1%	12.9%	**10.1%**
NET ABSORPTION	**23,643**	(9,899)	33,542	**99,214**	69,168	30,046	**122,857**
ASKING AVERAGE RENTAL RATE (NNN)	**$13.45/SF**	$14.80/SF	$13.15/SF	**$12.00/SF**	$13.75/SF	$11.05/SF	**$11.70/SF**

RETAIL MARKET

REGGIE KUIPERS, SIOR

At year end, I predicted the retail sector was at its peak in the real estate cycle. I admit, based upon the fundamentals that we study, I was probably a year early, but do anticipate that we are at the top of our market in 2016.

"The road to success is always under construction" - *Arnold Palmer*

Well, Arnold, so is the retail sector in Sioux Falls!

In the first six months of 2016, the city of Sioux Falls has issued over $34.2 million in building permits for retail construction (compared to $31.6 in 2015 and $11.4 in 2014). We will continue to see explosive retail growth in 3 core areas of our city:

1) **Dawley Farm**: New construction in 2016 includes Aldi, First Bank & Trust/ Coffea and Deuces Casino. There will be additional announcements in the third quarter for more financial and medical services. Dawley is poised for continued growth.

2) **85th & Minnesota**: New construction in 2016 includes the opening of Walmart, Schulte, Subaru, Burger King and some speculative strip malls. There will be additional announcements by year end for more retail (financial, food, medical, services users).

3) **Lake Lorraine**: New construction in 2016 includes the Sioux Falls Ford complex. We anticipate several big retail announcements in the second half of 2016 around Lake Lorraine and some additional automotive services along 26th Street.

ACTIVE TENANTS

<u>2016 Retail Observations:</u>

- **Large Restaurant Sales**—Minerva's, Foley's, Outback, Dairy Queen, Pourhouse have sold in 2016.
- **At the Peak?** The fundamentals appear to be in line with the peak expectations. However, there is some pent up demand/projects with the reclassification of the floodplain. Retail sector will likely taper slightly in the next 12 months.

<u>Predictions:</u>

- Retail construction will surpass $45 million by end of 2016, which will be the highest in Sioux Falls history.
- Big retail announcements coming to Lake Lorraine by year end
- In the next 12-24 months, some restaurants will close in Sioux Falls due to the explosive growth of the same store concepts within the market.

RETAIL MARKET SURVEY RESULTS

SECTOR	TOTAL SF	VACANCY RATE	ASKING PRICES (NNN)
Mall Area	588,242	5.4%	$12.00 - $30.00/SF
57th Street & Louise Avenue	164,328	2.5%	$17.00 - $24.00/SF
57th Street & Western Avenue	92,774	10.2%	$15.00 - $17.00/SF
Dawley Farm / East Sioux Falls	175,911	3.3%	$14.00 - $24.00/SF
69th Street & Western Avenue	53,985	7.5%	$14.00 - $16.00/SF
69th Street & Minnesota Avenue	64,462	2.8%	$14.00 - $16.00/SF
26th Street & Marion Road/Lake Lorraine	99,346	8.7%	$12.00 - $17.00/SF
Total	**1,239,048**	**5.3%**	

TRENDS TO WATCH

RENTS ↑

CONSTRUCTION ↑

VACANCY ↑

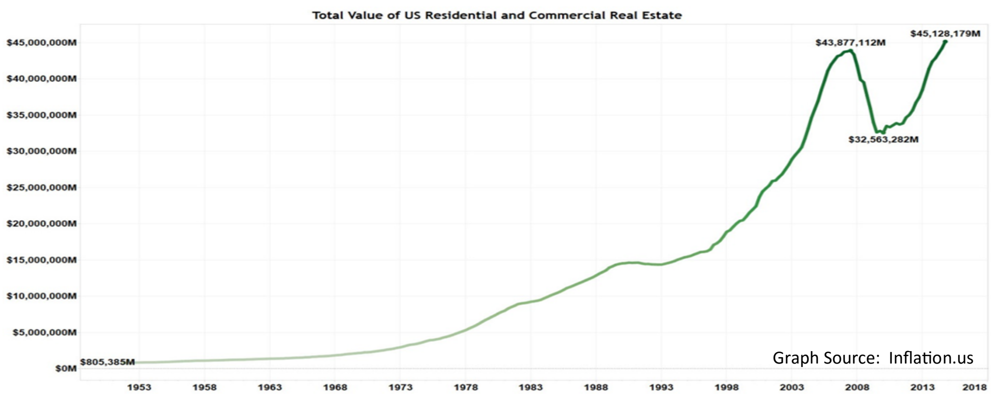
DOWNTOWN MOMUNTUM
(Lewis Drug, PAve, Keller's)

BANK ACTIVITY
(Great Western Bank - Home Federal Bank)
(New Banks Coming to Sioux Falls)

INVESTMENT REPORT
NICK GUSTAFSON, CCIM

Global Search for Yield in Low Environment

Investors are entering their 8th year of decision-making in a low interest rate environment. Savers have been penalized by low returns in savings, money markets and bonds while investors in the stock and real estate markets have been largely rewarded with a strong rebound in stock market and real estate valuations since 2009.



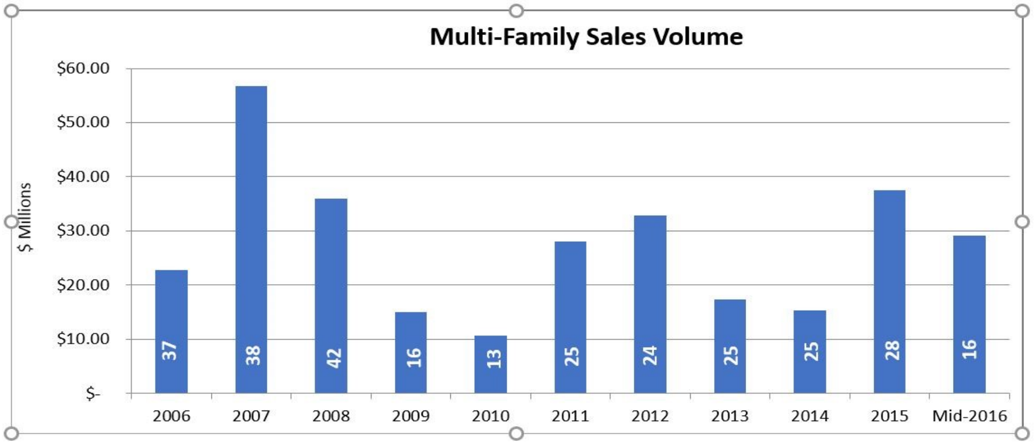
The challenge investors face in 2016 is navigating through a yield landscape that has been defined by a decades long influence of cheap money.

During the early aftermath of 2009 to 2011, confidence in real estate investing was low, balance sheets were under siege and low interest rates were often ignored by real estate investors as the circled the wagons and conserved cash through the downturn.

Investors started to dip their toes in the water locally once again in 2011 and found great deal and motivated sellers. Over the last four years, leasing has been strong across all asset classes and the pool of motivated sellers has largely dried up. Good deals have become increasing hard to find.

All that said, real estate continues to be an attractive option for investing.

This month in Fortune, Cond King Bill Gross was quoted, "Negative returns and principal losses in many asset categories are increasingly possible unless nominal growth rates reach acceptable levels. I don't like bonds; I don't like most stocks; I



don't like private equity. Real assets such as land, gold, and tangible plant and equipment at a discount are favored asset categories."

Sioux Falls

Multi-family. Multifamily has been on of Sioux Falls' most vibrant asset classes for many years. Developers continue to increase new unit construction as the city continues to grow and absorb new units.

Investors continue to seek multifamily deals as sales volume has surged year-to-date over last year's transactions, albeit 60% of this gaudy number is two large transactions between an out-of-state buyer and seller.

Retail & Office. Investors continue to scour retail and office assets for investment deals. Based on market data, I believe the number of sales and volume will be down over last year at this point. Most of the deals in these asset classes so far this year are owner occupant driven. This is largely an inventory issue as there is a large number of able and willing investment buyers in the market at this time.

Conclusion. There is a tremendous demand for good investment properties as evidenced by the amount of quality of buyers right now. Any property owners that are considering selling in the next five years should seriously consider taking profits now. Buyers are continuing to be aided by aggressive lenders and historically low interest rates. It remains a good time to buy and a good time to sell.