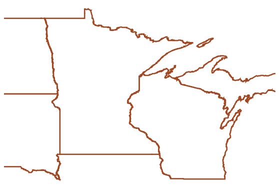
COMPREHENSIVE HOUSING MARKET ANALYSIS

Rochester, Minnesota

U.S. Department of Housing and Urban Development | Office of Policy Development and Research | As of August 1, 2006

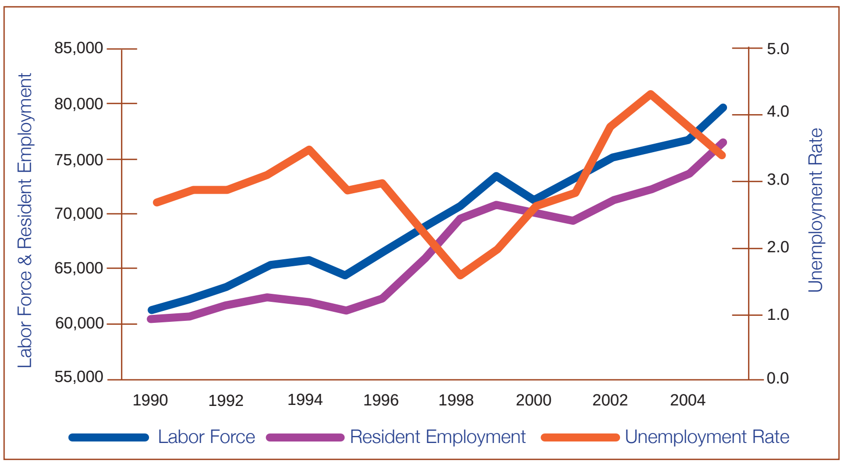


Economic Conditions

Historically, the economy of the Rochester HMA has tended to follow employment trends at the Mayo Clinic and IBM, which together account for nearly 40 percent of employment in the HMA. The Mayo Clinic is a world-renowned medical facility with 30,000 employees conducting research and serving more than 320,000 patients annually. The IBM plant, completed in 1958, currently employs 4,500 workers who are primarily engaged in research and development, supercomputer design and assembly, and customer service. The economy has a long history of expansion, with especially rapid job increases occurring in the latter years of the 1990s. Job growth since 1990 has led to increases in population and the number of households in the HMA and to additional in-commutation from outside the HMA. See Figure 1 for trends in labor force, resident employment, and unemployment and Table 2 for a list of major employers in the HMA.

During the 1990s, employment expanded significantly in the education and health services sector, led by the Mayo Clinic, and in the retail trade sector. In response to the expanding population and economy, employment in the construction sector increased substantially. Homebuilding was especially strong during the decade but had to compete for resources with a surge in commmercial construction, led by a major expansion of the Mayo Clinic from 1997 to 2004. At IBM, employment reached 8,000 workers in the early 1990s; in 1993, however, 1,900 workers were laid off. These layoffs, combined with other cutbacks and plant closings, limited gains in manufacturing sector jobs during the 1990s to 0.4 percent annually. Employment in the manufacturing sector peaked at 13,200 jobs in 1998. Further layoffs at IBM and Benchmark Electronics, Inc., a producer of electrical equipment, and closures of other plants brought employment in the manufacturing sector for the most recent 12-month period to fewer than 10,000 jobs.

Figure 1. Trends in Labor Force, Resident Employment, and Unemployment Rate in the Rochester HMA, 1990 to 2005



Source: Minnesota Department of Employment and Economic Development

Table 2. Major Employers in the Rochester HMA

Name of Employer	Employment Sector	Number of Employees
Mayo Clinic	Health Services	30,000
IBM Corporation	Manufacturing	4,500
Rochester Public Schools	Government	2,150
Olmsted County	Government	1,180
Olmsted Medical Center	Health Services	1,000

Sources: Rochester Area Economic Development, Inc.; estimates by analyst

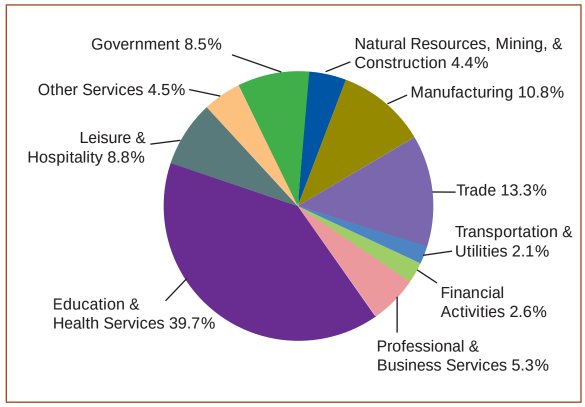
This figure represents less than 11 percent of total employment in the HMA during the period compared with more than 18 percent in 1990 and 17 percent in 2000. Figure 2 shows the percentage of change in each employment sector in the HMA since 2001.

Overall, employment increased by an average of almost 1,500 jobs, or 2.3 percent, annually from 1990 through 1999. The expansion was especially rapid in the last 4 years of the period, starting in 1996, when covered employment increased by an average of almost 3,350 jobs, or 4.8 percent, annually. This rapid expansion put strains on both the labor market and the housing market. The impact on the housing market was reflected in 2000 by vacancy rates of only 0.7 percent for owner-occupied housing and 3.9 percent for rental housing.

Job growth in the HMA has slowed somewhat since the 1990s. From 2000 through 2005, the annual gain in covered employment averaged a little more than 1,180 jobs, or 1.4 percent. For the 12 months ending July 2006, however, covered employment increased by 1,900 jobs, or 2.2 percent, compared with the previous 12 months.

The healthcare industry dominates the local economy, with the education and health services sector accounting for more than 39 percent of total jobs and 84 percent of the total job increase in the HMA for the 12 months ending July 2006. Employment in the leisure and hospitality sector, which primarily serves patients of the Mayo Clinic and their families, also has been expanding rapidly. This sector now represents almost 9 percent of all jobs in the HMA (see Figure 3).

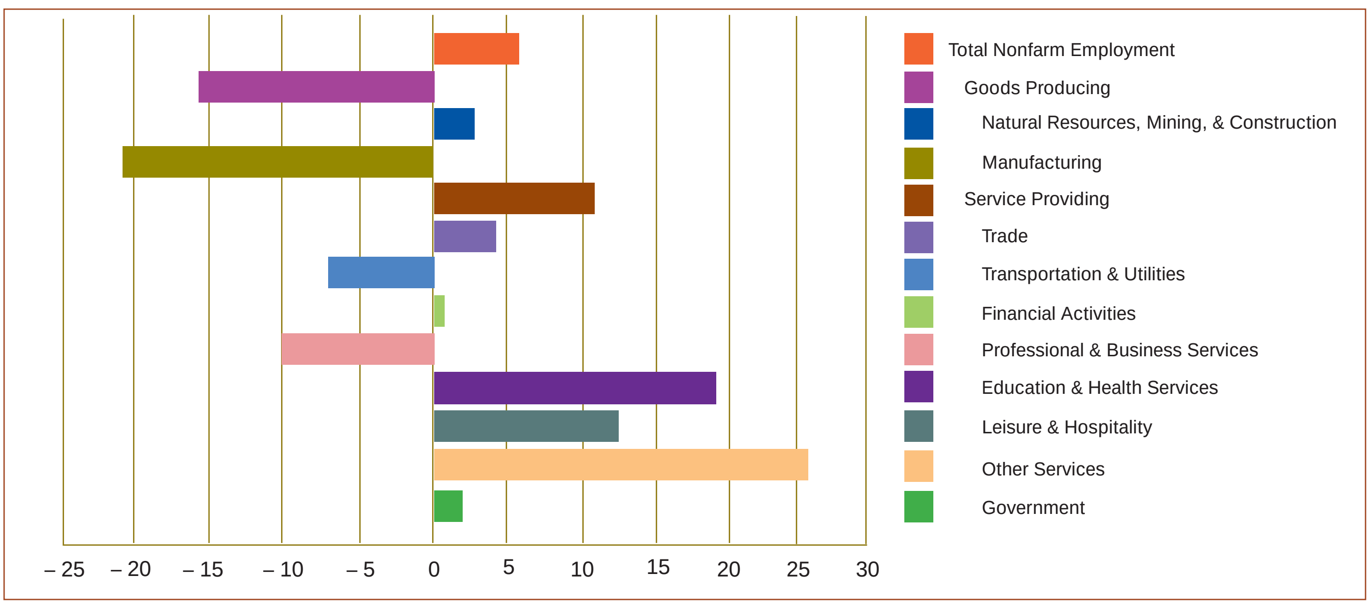
Figure 3. Current Employment in the Rochester HMA, by Sector



Notes: Based on 12-month averages through July 2006. The information sector is included in the other services sector.

Source: Minnesota Department of Employment and Economic Development

Figure 2. Sector Growth in the Rochester HMA, Percent Change, 1990 to Current



Notes: Current is based on 12-month averages through July 2006. The information sector is included in the other services sector.

Source: Minnesota Department of Employment and Economic Development

In-commutation is a major economic factor in the area. Starting in 1990, covered employment has been increasing at a considerably faster pace than the labor force and resident employment have. The relatively greater availability and affordability of housing outside Olmsted County, yet within reasonable commuting distance of jobs in the county, has stimulated growth in nearby counties. According to a 2003 study by the U.S. Census Bureau, 22 percent of workers employed in the city of Rochester were living outside the HMA. The percentage of workers commuting into the HMA has been increasing and, along with in-migration, will likely continue to play a vital role in the growth of the local economy. The forecast indicates that 1,520 jobs will be added annually in the HMA during the next 3 years. Table 3 provides data on covered employment in the HMA for the two most recent 12-month periods.

Table 3. 12-Month Average Employment in the Rochester HMA, by Sector

Employment Sector	12 Months Ending July 2005	12 Months Ending July 2006	Percent Change
Total Covered Employment	87,850	89,750	2.2
Goods Producing	13,800	13,600	– 1.4
Natural Resources, Mining, & Construction	3,850	3,975	3.1
Manufacturing	9,950	9,650	– 3.1
Service Providing	74,050	76,150	2.8
Trade	11,650	11,950	2.5
Transportation & Utilities	1,850	1,850	0.3
Financial Activities	2,300	2,350	1.8
Professional & Business Services	5,000	4,775	– 4.4
Education & Health Services	33,950	35,600	4.9
Leisure & Hospitality	7,800	7,925	1.8
Other Services	3,925	4,075	3.4
Government	7,575	7,625	0.6

Notes: Numbers may not add to totals due to rounding. Based on 12-month averages through July 2005 and July 2006. The information sector is included in the other services sector.

Source: Minnesota Department of Employment and Economic Development

Population and Households

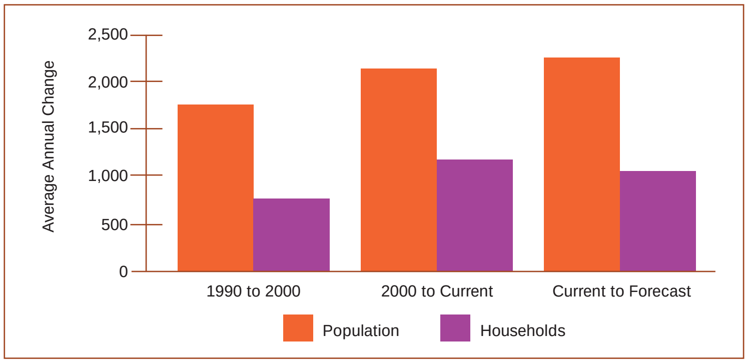
During the 1990s, the population of the Rochester HMA increased by an annual average of 1,780, or 1.6 percent a year, reaching 124,277 in 2000. The city of Rochester, accounting for almost 85 percent of the increase, had a population of 85,806 in 2000. From 2000 to the current date, the average annual increase in population in the HMA was 2,140, or 1.7 percent (see Figure 4). Net natural increase (resident births minus resident deaths) has accounted for about 60 percent of the population expansion since 1990 (see Figure 5). International migration has accounted for approximately 78 percent of all in-migration in the HMA since 1990. A major draw is the strong local economy, which provides a variety of employment opportunities, especially in the health services sector.

The nonhousehold population increased by an average of almost 60 a year from 1990 to 2000 to reach a total of 3,110 in 2000. Gains in the number of residents in group homes and the number of inmates in correctional facilities made up the primary increase and more than offset losses in the number of residents in nursing homes, which resulted in part from a growing preference for alternative care. These nonhousehold population trends have persisted since 2000 and are expected to continue during the 3-year forecast period.

As a result of expected increases in employment and the labor force, the population of the HMA is expected to expand by 1.7 percent a year from a current estimate of 137,800 to 144,700 during the 3-year forecast period.

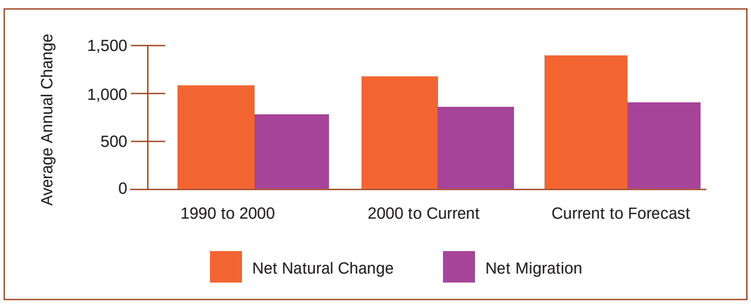
During the 1990s, the number of households increased by an average of nearly 780, or 1.8 percent, a year. From 2000 to the current date the number of households increased annually by more than 1,100, or 2.2 percent. The number of households is forecast to expand by almost 1,025 annually and reach more than 57,900 over the next 3 years.

Figure 4. Population and Household Growth in the Rochester HMA, 1990 to Forecast



Sources: 1990 and 2000—U.S. Census; current and forecast—estimates by analyst

Figure 5. Components of Population Change in the Rochester HMA, 1990 to Forecast



Sources: 1990 and 2000—U.S. Census; current and forecast—estimates by analyst

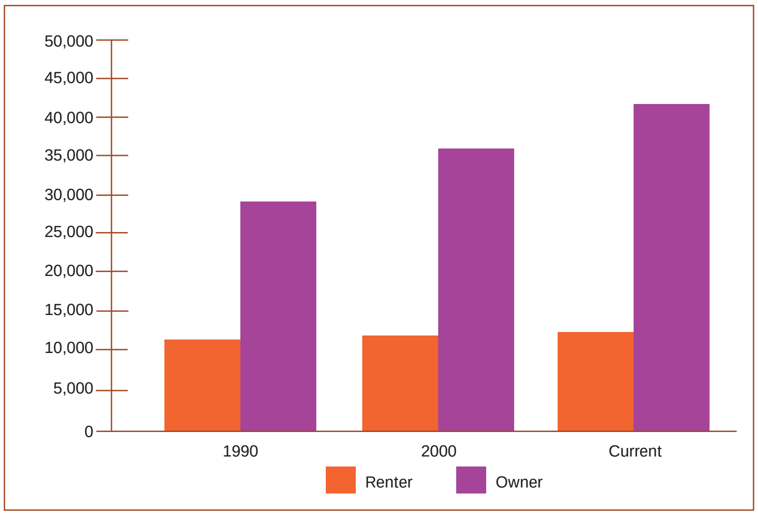
Housing Market Trends

Sales Market

The vacancy rate for sales housing in the Rochester HMA was 1.1 percent in 1990. Since 1990, more than 90 percent of net additions to the housing inventory have been sales units, and the share of owner households has risen from 72.4 percent of total households to 78.3 percent (see Figure 6). During the late 1990s, rapid increases in employment and population and a major shift in housing preference from rental to owner-occupied created demand for sales housing beyond the capacity of home builders to fully respond. The sales housing market tightened and the sales vacancy rate declined to 0.7 percent in 2000.

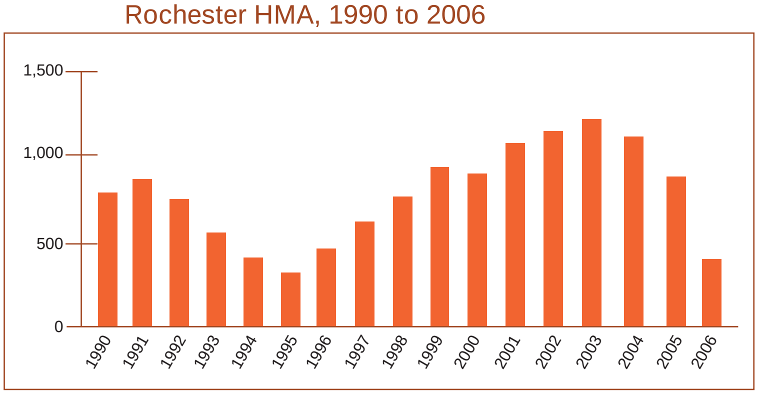
Since 2000, the sales housing market has returned to more balanced conditions; the current vacancy rate is 1.1 percent. Following the 1996-through-1999 period of rapid employment growth, job gains slowed and the construction of sales housing increased. In the late 1990s, new housing supply was not keeping up with demand, and only 735 single-family homes on average were permitted in the HMA from 1996 through 2000 (see Figure 7). From 2001 through 2004, the number of building permits issued for single-family homes averaged more than 1,240 a year. Production levels of single-family housing declined to 859 units in 2005 and 747 units for the 12 months ending July 2006. The increase in supply that occurred during the early part of the decade helped ease the tight market conditions as indicated by the current balanced market vacancy rate, a return to longer periods of time on the market for existing homes, and the recent slowdown in the construction of new homes. In Rochester, homes were on the market for an average of only 39 days in 2000 compared with 98 days in 2005.

Figure 6. Number of Households by Tenure in the Rochester HMA, 1990 to Current



Sources: 1990 and 2000—U.S. Census; current—estimates by analyst

Figure 7. Single-Family Building Permits Issued in the Rochester HMA, 1990 to 2006



Notes: Includes single-family units. Includes data through July 2006.
Source: U.S. Census Bureau, Building Permits Survey

The average sales price of an existing home in Rochester escalated from $120,500 in 1998 to $157,700 in 2000. This escalation represents an annual increase of nearly 15 percent. From 2000 to 2005, while the average number of existing homes for sale more than doubled, the annual increase in the average home sales price slowed to more than 5 percent, reaching $198,550 in 2005. Annual sales volume in Rochester declined from 2,040 units in 1998 to 1,900 units in 2000. Since 2000, the level of home sales has increased, totaling 2,165 units in 2001, 2,315 in 2003, and 2,400 in 2005.

Although newly constructed single-family starter homes, townhomes, and condominiums can be purchased for as little as $150,000, typical prices for new single-family homes start at $225,000. New homes are being built throughout Rochester but primarily in the northwest and southwest quadrants of the city.

A golf course community is currently under construction in the city of Byron. The development was originally expected to include 750 homes; most of the units are single-family units priced from $250,000 to $1 million and the rest are townhomes and condominiums with lower sales prices. Construction at the development began in 2001. Strong demand for housing in this community has prompted developers to acquire 100 additional acres to expand the development, which is scheduled for completion by 2010. As of the current date, 106 units have been built and 107 have been sold.

A demand for 2,900 sales units is estimated for the 3-year forecast period. See Table 4 for estimated demand by price range for new market-rate sales housing during the forecast period.

Table 4. Estimated Demand for New Market-Rate Sales Housing in the Rochester HMA, August 1, 2006 to August 1, 2009

Price Range ($)		Units of Demand	Percent of Total
From	To		
150,000	175,000	470	15.7
175,000	200,000	490	16.9
200,000	225,000	390	13.2
225,000	250,000	270	9.3
250,000	275,000	310	10.7
275,000	300,000	130	4.4
300,000	325,000	130	4.5
325,000	350,000	110	3.6
350,000	400,000	200	7.0
400,000	500,000	140	4.9
500,000	850,000	130	4.6
850,000	1,000,000	60	2.0
1,000,000	and higher	85	3.1

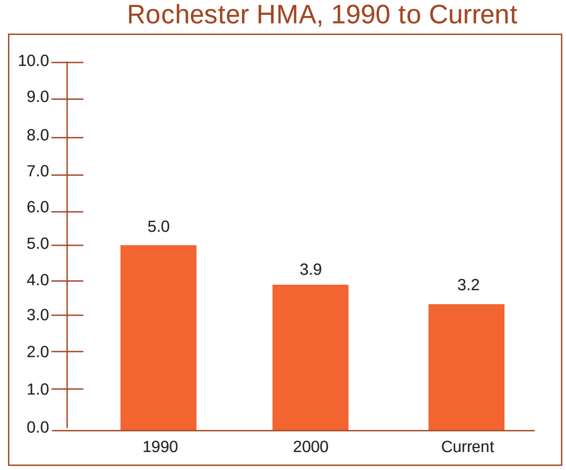
Source: Estimates by analyst

Rental Market

Conditions in the rental housing market are balanced to tight. The current rental vacancy rate is slightly more than 3 percent, down from 5 percent in 1990 and 3.9 percent in 2000 (see Figure 8). Growth in employment and population in the late 1990s created a demand that builders did not anticipate and could not respond to rapidly enough to prevent shortages in rental housing. Builders and developers increased the production of rental housing, with the number of multifamily units permitted increasing from an annual average of 211 for the 8-year period from 1990 through 1997 to 369 in 1998 and 482 in 1999. The additional completions could not reach the market as rapidly as needed, however, partly because of materials and labor market shortages as the construction industry met competing demand for commercial properties, especially in the Mayo Clinic expansion, and sales housing. The market softened in the early 2000s as a result of a slowdown in the economy that began in 2001, an increase in the number of renters becoming homeowners, and an increase in apartment construction. Building permits were issued for 660 multifamily units in 2000 and 483 units in 2001. By 2003, the rental vacancy rate reached 8.4 percent.

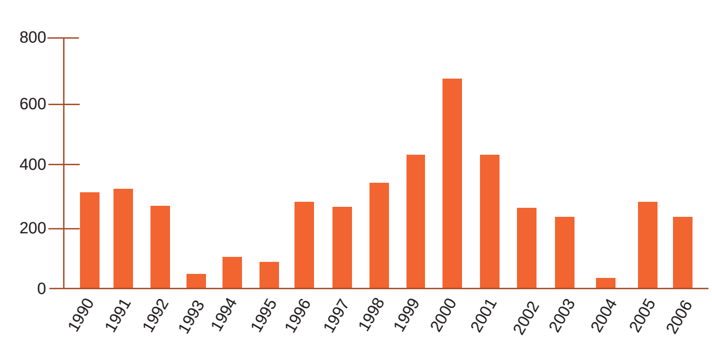
After 2001, construction activity, as measured by building permits, returned to more normal levels, averaging about 200 multifamily units annually from 2002 through 2005 (see Figure 9). Only 64 multifamily units were permitted in the 12 months ending July 2005, but the number of multifamily units permitted increased to 445 in the 12 months ending July 2006. A major component of the increase in development activity is a large, high-end project located within 2 miles of the Mayo Clinic's Saint Marys Hospital; the project is scheduled for completion in the spring of 2007. Through July 2006, 80 of the 276 planned units have been completed, with rent-up proceeding quickly. First Homes, an initiative of the Rochester Area Foundation, is active in developing affordable rental housing and has completed 313 affordable rental units in and near the HMA as of the current date. Rents for newly constructed apartments average $875 for one-bedroom units, $925 for two-bedroom

Figure 8. Rental Vacancy Rates in the Rochester HMA, 1990 to Current



Sources: 1990 and 2000—U.S. Census; current—estimates by analyst

Figure 9. Multifamily Building Permits Issued in the Rochester HMA, 1990 to 2006



Notes: Includes all multifamily units in structures with two or more units. Includes data through July 2006.

Source: U.S. Census Bureau, Building Permits Survey

units, and $1,050 for three-bedroom units. Based on anticipated household growth and current market conditions, estimates indicate a demand for 740 new rental units during the 3-year forecast period. See Table 5 for estimated demand for new market-rate rental housing, by unit size and rent level, during the forecast period. Also, see Table DP-1 at the end of the report for additional summary data on important housing market variables from 1990 to the current date.

Table 5. Estimated Demand for New Market-Rate Rental Housing in the Rochester HMA, August 1, 2006 to August 1, 2009

0 Bedrooms		1 Bedroom		2 Bedrooms		3 or More Bedrooms	
Monthly Gross Rent ($)	Units of Demand	Monthly Gross Rent ($)	Units of Demand	Monthly Gross Rent ($)	Units of Demand	Monthly Gross Rent ($)	Units of Demand
550	30	680	320	880	290	1,065	100
600	25	730	280	930	240	1,115	90
700	20	780	260	980	220	1,165	80
750	15	830	230	1,030	200	1,215	70
850 and higher	10	880	210	1,080	170	1,265	55
		930	170	1,130	140	1,315	50
		980	140	1,180	120	1,365	45
		1,080	120	1,280	100	1,465	30
		1,180	95	1,380	65	1,565	25
		1,280	75	1,480	45	1,665	15
		1,380 and higher	60	1,580 and higher	30	1,765 and higher	15

Notes: Distribution above is noncumulative. Demand shown at any rent represents demand at that level and higher.

Source: Estimates by analyst

Data Profile

Table DP–1.9 [illegible]

	1990	2000	Current	Average Annual Change (%) 1990 to 2000	Average Annual Change (%) 2000 to Current
Total Resident Employment	61,125	70,700	77,225	1.5	1.4
Unemployment Rate (%)	2.7	2.7	3.3		
Covered Employment	64,719	82,659	89,730	2.5	1.3
Total Population	106,470	124,277	137,800	1.6	1.7
Total Households	40,058	47,807	54,850	1.8	2.2
Owner Households	29,012	36,304	42,950	2.3	2.7
Percent Owner (%)	72.4	75.9	78.3		
Renter Households	11,046	11,503	11,900	0.4	0.5
Percent Renter (%)	27.6	24.1	21.7		
Total Housing Units	41,603	49,422	56,800	1.7	2.2
Owner Vacancy Rate (%)	1.1	0.7	1.1		
Rental Vacancy Rate (%)	5.0	3.9	3.2		
Median Family Income	$43,196	$61,610	$73,850	3.6	2.9

Note: Median family income data are for 1989, 1999, and 2006.

Sources: U.S. Census Bureau; U.S. Department of Housing and Urban Development; Minnesota Department of Employment and Economic Development; estimates by analyst

Data Definitions and Sources

1990: 4/1/1990—U.S. Decennial Census

2000: 4/1/2000—U.S. Decennial Census

Current date: 8/1/2006—Analyst's estimates

Forecast period: 8/1/2006–8/1/2009—Analyst's estimates

Demand: The demand estimates in the analysis are not a forecast of building activity. They are the estimates of the total housing production needed to achieve a balanced market at the end of the 3-year forecast period given conditions on the as-of date of the analysis, growth, losses, and excess vacancies. The estimates do not account for units currently under construction or units in the development pipeline.

For additional data pertaining to the housing market for this HMA, go to http://www.huduser.org/publications/pdf/CMARTables_RochesterMN.pdf.

For additional reports on other market areas, please go to www.huduser.org/publications/econdev/mkt_analysis.html.

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This analysis has been prepared for the assistance and guidance of the U.S. Department of Housing and Urban Development (HUD) in its operations. The factual information, findings, and conclusions may also be useful to builders, mortgagees, and others concerned with local housing market conditions and trends. The analysis does not purport to make determinations regarding the acceptability of any mortgage insurance proposals that may be under consideration by the Department.

The factual framework for this analysis follows the guidelines and methods developed by HUD's Economic and Market Analysis Division. The analysis and findings are as thorough and current as possible based on information available on the as-of date from local and national sources. As such, findings or conclusions may be modified by subsequent developments. HUD wishes to express its appreciation to those industry sources and state and local government officials who provided data and information on local economic and housing market conditions.