

...away, and with six roads a day, adding on 10 barrels each

seeing a lot of this," he said.

At the water depot at Love's

The truck weighed in at more than 113,000 pounds —

suming task of truck-weight enforcement.

Sunday morning, chugging down Route 200 near the

Maya Rao • 612-673-4210

# Low rural rents stymie housing supply and job growth

◀ **RENTS** from A1 to build apartments in these towns without subsidies.

"It's definitely sticking our necks out, and chasing good money after bad," said Smedsmo, who also owns the AmericInn in Roseau. "I hope we can make it fly financially."

In Roseau, the presence of 300 temporary Polaris workers punctuates the need for homes, and the company says it could hire 200 more if enough housing were available.

Smedsmo's project should break even, barely, but only with \$325,000 from a state pilot grant program and \$460,000 from the city of Roseau, he said.

Without the grants and a loan from the city, he would have to charge about \$1,200 per month in rent to bring in enough to cover the mortgage and property taxes. Most apartments in Roseau rent for around \$600.

Construction projects face the same math in parts of Iowa, South Dakota and Kansas. Rents aren't high enough to support apartment construction, said Cam Saunders, who lives in Grand Rapids, Minn. He has developed and sold apartment buildings across northern Minnesota, and owns 48 units in Thief River Falls.

"The main problem is the cost of construction and what you can get for rent in these smaller communities," Saun-

ders said. "Wages aren't there to support what it costs to build apartments."

The reason for low rents in Roseau, where wages have grown in recent years, is a matter of debate. City officials say the problem is not worker pay, but a complex mix of factors involving the size of the city and the rents people are accustomed to paying.

But Rodger Tinjum, the Detroit Lakes appraiser who put a \$2.2 million value on Smedsmo's project, said the problem is low wages.

"It's all economics, and there's only so much income out there," Tinjum said. "There's a certain amount of money that people can afford for their housing."

## Healthy wages

If any small town in rural Minnesota has high enough wages to support new apartments, it should be Roseau.

The city, closer to Winnipeg than to Minneapolis, is home to Polaris Industries, the maker of snowmobiles and ATVs whose factory is on the southwest side of town. Marvin Windows & Doors is to the east in Warroad. Mat-tracks, another manufacturer, is to the west in Karlstad.

Polaris turned a \$377-million profit in 2013 and employs 1,650 people in town. Wages are growing twice as fast in Roseau County as the state. Average weekly pay is \$955,

a 38 percent jump since 2010.

Textbook economics would suggest the town is ripe for apartment development. Supply is low, demand is high and wages are on an upward trend.

But Smedsmo's project is almost 30 percent funded by the government. And the other big apartment project in town, 40 units proposed by Sand Companies of St. Cloud, will be partly income-restricted and dependent on tax credits and state grants. Sand Companies hopes to break ground this spring, but has struggled to get the project going.

## Size, culture matter

To make an apartment project work, a developer needs a pool of potential tenants with similar incomes and budgets. But Roseau's size — population 2,600 — means there aren't a lot of people at any particular income level. That increases the risk of prolonged vacancies, which can wreak havoc for a landlord.

Also, construction costs are high because so many contractors folded in the economic downturn and others are drawn to projects in North Dakota, said Todd Peterson, the city of Roseau's development coordinator.

Developers with no subsidy and 20 percent down would need to charge about \$1,100 to \$1,300 per month to get a worthwhile return in town, Peterson said.

Smedsmo wants to charge around \$800 for a two-bedroom apartment. That might be a stretch for an assembly worker starting at \$14.25 per hour at Polaris, but easily within reach for higher-skilled workers and two-income couples.

Still, appraisers and bankers are skeptical, because few renters in town are paying that much today.

This is not primarily because of wages, Peterson said.

Median pay in northwest Minnesota, at \$15.73 per hour, is 26 percent less than the \$19.92 median in the Twin Cities. But the city-rural gap in rents people pay is far larger. Average rent in the Twin Cities is \$1,090 for a two-bedroom unit, compared to roughly \$600 per month in Roseau or Thief River Falls, an 81 percent gap.

For some reason, Roseau renters historically pay a lower percentage of their income toward housing than renters in the Twin Cities, and low rents have been stubborn.

Owners are reluctant to raise rents, so the value of new construction is driven downward, said Paul Vitrano, vice president of global government relations for Polaris Industries.

"Ultimately, rents will need to increase or new construction will continue to be constrained," Vitrano said.

The city of Roseau is trying

to do something about this.

The city owns 24 townhouses where a two-bedroom unit costs \$645 per month and a three-bedroom unit costs \$705 per month. Officials plan to raise rents on the units by \$50 in January, hoping to drive up prices in the local market to encourage developers like Smedsmo.

"We are doing it because we need to move the market to where it needs to be, then see where the actual resistance is," said Peterson. "When do we lose residents who say 'We can't afford that?'"

Until small towns prove that people in them will pay higher rents, bankers won't touch apartment projects without a huge down payment or government grants.

And the problem of low rents makes profits on rural apartment projects so negligible that investors don't want to get involved, even if they do have the money for a massive down payment.

"If you make \$10,000 on a \$100,000 investment, you're happy," said Terry Kriesel, a commercial real estate banker at Bremer Bank in the Twin Cities. "If you make \$10,000 on a \$500,000 investment, you're not happy."

## One company towns

And developers are wary of towns with one dominant employer, who could have a few rough years and lay people

off, or even conceivably leave town.

"If Digi-Key moved out tomorrow, everybody'd be hurting as far as occupancy," said Saunders, who built 48 units in Thief River Falls in the 1970s and still owns them. "When you have a major employer in any of these small towns, it's a big factor, going to take a risk to build apartments."

## Civic motivation

To Smedsmo, it's about more than just numbers.

If he wanted to get into apartments purely for business reasons, buying an existing property would have made more sense. But he wanted to try to help solve the housing problem.

The hometown company, the inventors of snowmobiles, are his "bread and butter" customer.

Last week, he helped unload upstairs joists from a semi-trailer at the construction site for the building, called Parkland Place. The frame of the central hallway is now discernible on the ground floor.

"We wouldn't be here without Polaris, so we've got to do something to help our town and our industry," Smedsmo said. "Other communities would kill for industry like this."

Adam Belz • 612-673-4405 Twitter: @adambelz