MARKET REPORT

Multifamily

Denver Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

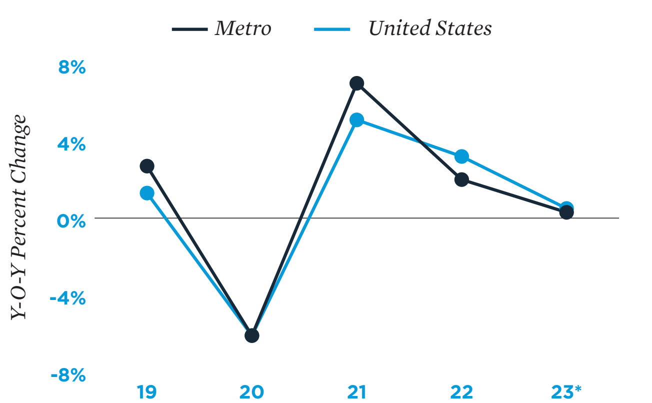
2Q/23

Development Requirements Alter Growth Trajectory as Commuters Identify the West

RiNo headlines record construction pipeline. Prior to the approval of newly-enacted affordability regulations, multifamily development in the central business district fell dramatically amid uncertainty surrounding the city's ruling. This resulted in downtown Denver welcoming its lowest number of new units in nearly a decade last year. Effective last July, apartments built within the city of Denver must now allocate 8 to 10 percent of units as affordable. Although this likely slows urban construction in the long-run, developers will increase inventory by the fastest pace on record during 2023. The RiNo neighborhood welcomes more than one-third of downtown units and 13 percent of the metro's total deliveries this year. Proximity to nightlife and sporting venues draws popularity among young professionals and should keep promoting growth here. A slowed long-term pipeline, however, could put a lid on expanding vacancy downtown.

Front range suburbs flourish. As development requirements downtown weigh on the long-term pipeline, suburban migration likely continues. Since the reshuffling of housing preferences in 2020 and 2021, renters continue to identify western neighborhoods this year offering suburban amenities with urban proximity. The Arvada-Golden and Wheat Ridge areas are well-positioned for commuting professionals, many of which take advantage of Class A rents well below the segment's downtown average. This has led to a local vacancy rate that undercuts the metro mean, although eased employment and household income growth may temper demand in the near-term.

Employment Trends



** Forecast*

Sources: BLS; CoStar Group, Inc.; RealPage, Inc.

Multifamily 2023 Outlook

5,000 JOBS
will be created

EMPLOYMENT:

Downward pressure on the tech sector continues in 2023, contributing to the metro's loss of 1,000 jobs within traditionally office-using industries. This decline, paired with a waning economic outlook, results in an employment growth rate of just 0.3 percent.

12,000 UNITS
will be completed

CONSTRUCTION:

The metro adds its largest unit count on record in 2023. Following reduced uncertainty around affordability requirements downtown, an influx of submissions prior to the ordinance's effective date contributes to this notable delivery slate.

90 BASIS POINT
increase in vacancy

VACANCY:

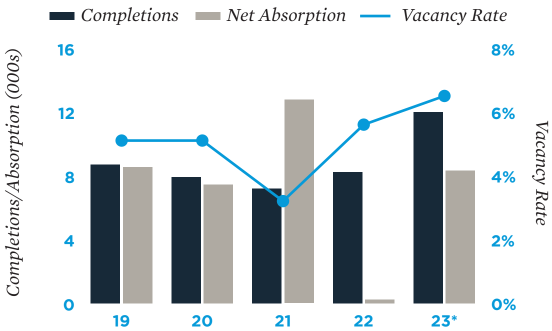
A record development pipeline and dwindled consumer sentiment result in vacancy expansion in 2023. By year-end, the rate will sit at 6.5 percent. This will be 150 basis points above the metro's 10-year average.

3.0% INCREASE
in effective rent

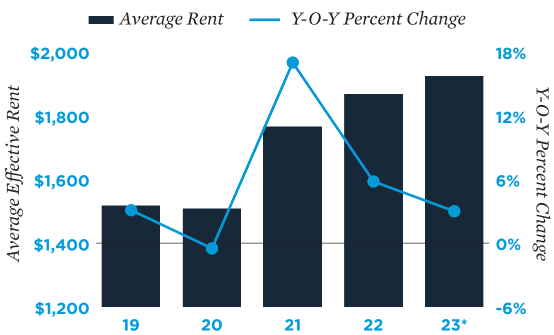
RENT:

Following a near-24 percent jump from 2020 through 2022, rent growth slows this year amid notable vacancy increases metrowide. By year-end, the average effective rate in Denver reaches $1,924 per month.

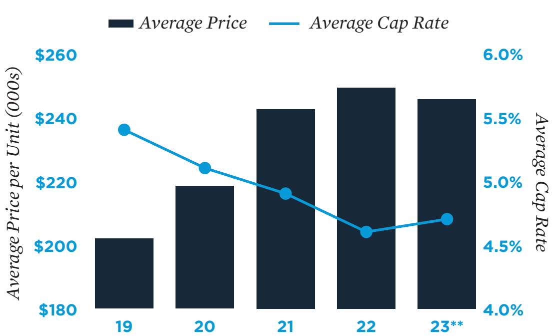
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 1Q*

Sources: CoStar Group, Inc.; Real Capital Analytics; RealPage, Inc.

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1Q 2023 - 12-Month Period

CONSTRUCTION

8,894 units completed

- Adding 1,300 more units than the previous 12-month period, Denver's inventory expansion totaled 2.8 percent year-over-year in the first quarter.
- A number of 200-plus-unit developments proximate to Interstate 70 near Green Valley Ranch were delivered this past year as developers continue to expand housing options north of Aurora.

VACANCY

290 basis point increase in vacancy Y-O-Y

- Strong apartment demand resulted in a historic-low vacancy rate of 3.0 percent in the first quarter of 2022. Since then, increased construction activity and slowed household formation have pushed the rate to 5.9 percent.
- Class A vacancy in Westminster recorded compression over the previous four quarters, the only submarket to do so.

RENT

4.3% increase in the average effective rent Y-O-Y

- Gains eased from their record pace experienced in early 2022. This year's modest increase brought the average effective rent to $1,856 per month.
- The Highlands Ranch and Westminster submarkets highlight areas with notable Class A rent growth. Amid vacancy rates at least 30 basis points below the market average, these locations had rent gains above 20 percent.

Investment Highlights

- New affordability regulations for development downtown may have contributed to the submarket's uptick in transaction velocity over the previous 12 months. Though institutional grade capital has remained largely on the sidelines in recent quarters, an elevated count of additions this year could benefit the Class A acquisitions landscape in the second half of 2023 as builders start to identify exit strategies.
- Denver's average cap rate entered the second quarter as the highest among all major Rocky Mountain metros. Decompression in the opening quarter of the year, combined with rebounding in-migration and home ownership difficulties, should support rising investor confidence, despite elevated interest rates challenging yields experienced over the previous two years.
- Colorado recently ranked as one of the nation's leading states in rent payment fulfillment for assets smaller than 50 units, with nearly 90 percent of renters meeting their obligations. As an added benefit to higher yields than nearby metros, this should continue to draw out-of-state investors, after accounting for nearly half of transactions during the previous yearlong period. Meanwhile, recently-enacted property transfer tax increases in Los Angeles may draw an expanded share of California investors here.