MARKET REPORT

Office

Denver Metro Area

IPA INSTITUTIONAL PROPERTY ADVISORS

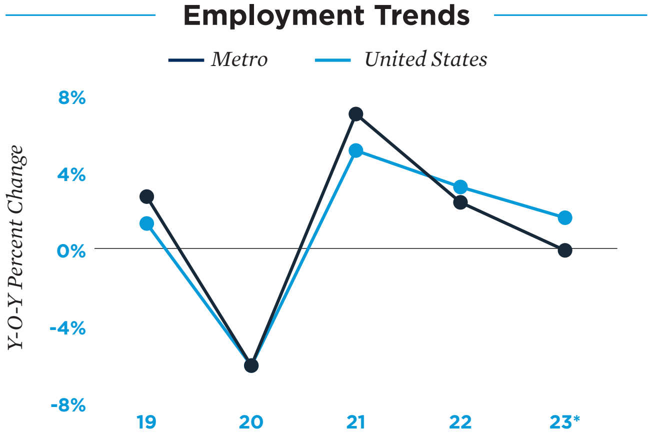
4Q/23

Bright Spots in Select Areas Spark Optimism, Though Marketwide Challenges Persist

Denver retains its status as a high growth market. This year's net in-migration total of 18,200 new residents will register as the metro's largest influx since 2016. A notable portion of these relocations are among 20- to 34-year-olds, allowing the demographic to expand by a five-year high 1.1 percent. This substantial increase is partially tied to a tight local labor market. As of July, Denver's unemployment rate held below 3 percent, well under its 3.9 percent decade-long average. Despite a net reduction over the initial seven months of the year, employment among traditionally office-using sectors was 5.2 percent above its 2019 headcount. Combined with a pullback in construction, this should benefit the metro's existing office stock, even as employers continue to encourage in-person and hybrid schedules.

Subleasing indicates vacancy spikes may subside. In the second quarter, Denver's total vacancy rate, when including space available for sublease, ranked as the fifth highest among major U.S. metros. However, when comparing markets based on the amount of space that does not have a lease attached, Denver has a better standing, ranking ninth. This indicates that, relative to other metros, more of Denver's marketed office space has a commitment in some capacity. Although vacancy continues to rise in the near-term, robust population growth trends and a tight labor market should supplement tenant demand down the line, particularly as the count of traditionally office-using positions remains above pre-pandemic levels.

Employment Trends



** Forecast*

Sources: BLS; CoStar Group, Inc.

Office 2023 Outlook

1,000 JOBS
will be lost

EMPLOYMENT:

Over the initial seven months of the year, the professional and technical services sector added a notable 6,500 jobs. Nevertheless, overall employment declined marginally, a theme consistent for the remainder of 2023.

825,000 SQ. FT.
will be completed

CONSTRUCTION:

Builders increase stock by less than 0.6 percent for the second straight year, below the 1.3 percent five-year annual average between 2017 and 2021. Nearly 80 percent of deliveries arrive in the second half of the year.

130 BASIS POINT
increase in vacancy

VACANCY:

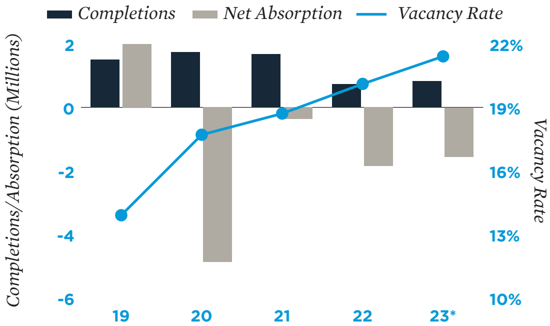
Supply additions notably outpace demand for a fourth consecutive year. The relinquishment of space recorded during 2023 maintains upward vacancy pressure as Denver's rate lifts to 21.4 percent by year-end.

0.4% DECREASE
in asking rent

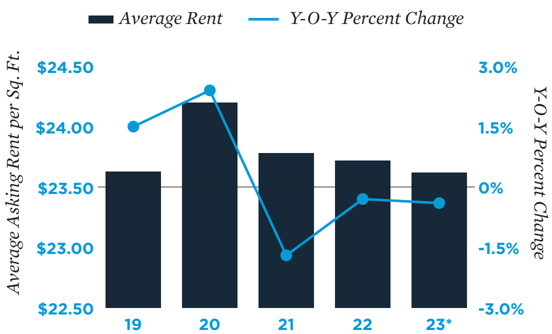
RENT:

Historically high vacancy requires some operators to lower asking rents to attract tenants. This reduces the metro's mean marketed rate to $23.62 per square foot by year-end. Still, this will be on par with the 2019 mean.

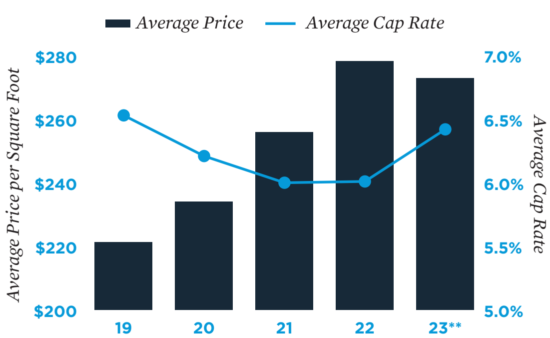
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 2Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

IPA Office
Al Pontius
Senior Vice President, Director
Tel: (415) 963-3000 | apontius@ipausa.com

For information on national office trends, contact:
John Chang
Senior Vice President, Director | Research & Advisory Services
Tel: (602) 707-9700 | jchang@ipausa.com

Price: $250

2Q 2023 - 12-Month Period

CONSTRUCTION
467,000 sq. ft. completed

- A minimal number of completions during the first quarter of the year contributed to the metro's modest, 0.3 percent rate of inventory growth over the 12-month period ending in June.
- About one-fourth of completions were accounted for in the Northeast Denver submarket, increasing local inventory by 2.6 percent.

VACANCY
180 basis point increase in vacancy Y-O-Y

- Northwest Denver noted a 50-basis-point compression to its Class B/C vacancy over the year ended in June. This was one of just two submarkets with at least 1 million square feet of stock to note a reduction.
- Overall vacancy in Southwest Denver, spanning Lakewood to Columbine, lowered 190 basis points to 9.3 percent.

RENT
1.0% decrease in the average asking rent Y-O-Y

- Total vacant stock expanded by 3.3 million square feet over the past year, resulting in the average asking rent declining to $23.69 per square foot.
- Despite the overall decline, six of the metro's 14 submarkets posted gains to their average asking rents. Broomfield's 5.8 percent advancement was the most pronounced as its rate reached $22.20 per square foot in June.

Investment Highlights

- Tighter underwriting guidelines, changing tenant priorities and increased debt costs translated to historically below-average transaction velocity in the second quarter. Sales activity, however, was up from the minimal recording made during the initial three months of the year. The base of deals within the $1 to $10 million price tranche is growing of late, with a notable portion of these trades located in the Southeast Denver area, encompassing Centennial and the Tech Center.
- A higher volume of institutional levels of capital is also being deployed in Southeast Denver. Although fundamentals here lag the market, large lease commitments are still being signed. Additionally, as firms across the metro continue to enact hybrid and in-person attendance requirements, and financing challenges ease, investor confidence should improve here.
- Rising cap rates suggest more buyers and sellers are coming to agreement. Over the yearlong period ended in June, the average first-year return among transacted properties lifted 40 basis points to 6.4 percent, its highest point since 2019. Higher yields and long-term tenant demand optimism may garner more investor confidence moving forward.