CBRE

Net absorption turns positive as development and investment sales stall

▲ 20.0%
Total Vacancy Rate

▲ 23K
SF Net Absorption

▶ $31.95
FSG / Lease Rate

▼ 2.1M
SF Under Construction

▼ 1.0M
SF Leasing Activity

Note: Arrows indicate change from previous quarter.

MARKET SUMMARY

- Leasing activity dipped in Q4 2022 with a little over 1.0 million sq. ft. of leases transacted, bringing the year-to-date total to 4.5 million sq. ft.
- The office development pipeline stalled in Q4 2022 with no properties breaking ground, and only Vectra Bank's 127,000-sq-ft. headquarters delivering in the Southeast submarket.
- Positive net absorption of 23,300 sq. ft. in Q4 2022 brought the annual total to just negative 2,600 sq. ft., a considerable improvement from 2021's total of negative 2.1 million sq. ft.
- Annual sales volume totaled $2.5 billion, dipping only 2.7% year-over-year.
- Total vacancy increased slightly, rising 60 basis points (bps) year-over-year to 20.0%.
- Sublease availability increased 12.0% quarter-over-quarter and 39.9% year-over-year to 6.1 million sq. ft., breaking the record high of 5.4 million sq. ft. set last quarter.
- The overall average direct asking lease rate experienced minimal change, decreasing 0.4% quarter-over-quarter and increasing 0.5% year-over-year to $31.95 per sq. ft. FSG.

FIGURE 1: Downtown vs Suburban Market Statistics

	NRA (SF)	Total Vacancy Rate (%)	Sublease Availability (SF)	YTD Net Absorption (SF)	Direct Asking Rent ($/SF/YR FSG)	Under Construction (SF)
DOWNTOWN						
Class A	12,221,435	21.5	858,148	137,699	48.66	704,036
Class B	14,461,452	30.0	1,279,953	(519,336)	38.38	-
Class C	3,977,682	34.6	69,119	(53,221)	29.67	-
Total	30,660,569	27.2	2,207,220	(434,858)	39.68	704,036
SUBURBAN						
Class A	41,170,761	18.9	2,409,482	(355,427)	30.99	1,367,626
Class B	39,058,597	17.7	1,273,107	710,145	26.98	-
Class C	10,371,359	12.0	175,661	77,505	21.90	-
Total	90,600,717	17.6	3,858,250	432,223	28.43	1,367,626
METRO TOTAL	121,261,286	20.0	6,065,470	(2,635)	31.95	2,071,662

Source: CBRE Research Q4 2022

Vacancy

Total vacancy rounded out 2022 at 20.0%, an increase of 60 basis points (bps) year-over-year. Throughout the course of the year, vacancy remained principally consistent, only increasing 10 to 20 bps in each of the past three quarters. Although vacancy rates are not climbing drastically, they remain elevated as Denver continues to face an ever-evolving office landscape and economic headwinds.

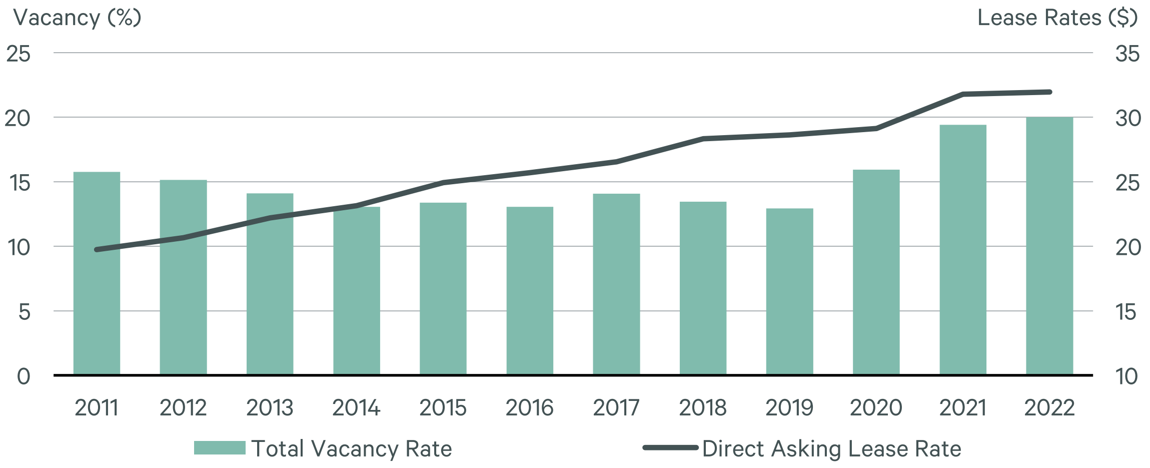
Vacancy among Class B properties reached 21.0% in Q4 2022, as these lower-quality, less amenitized assets are seeing tenants optimize their office spaces and flock to higher-quality space. Without a significant rebound in tenant demand or capital improvements, these buildings will continue to inflate overall vacancy. Office conversion projects were a relatively prominent discussion in 2022 and could be a feasible option in addressing some of the market's underutilized office space. The Downtown submarket vacancy rate increased 330 bps year-over-year to 27.2%, the largest increase by submarket in 2022. Vacancy rates in Cherry Creek, a high-demand suburban submarket, decreased 220 bps year-over-year to 8.3%, the lowest in the Denver metro.

Sublease Availability

Sublease availability rose 12.0% quarter-over-quarter and 39.9% year-over-year to 6.1 million sq. ft., breaking the previous record of 5.4 million sq. ft. set in Q3 2022. Throughout the year, companies have been listing space for sublease due to cost precautions, cutting underutilized space and to buy time to redefine their real estate needs. The technology industry was the largest contributor to sublease availability this year, as hybrid work is a more viable option in this specific industry and headcount reductions have been more widespread in lieu of the current economic landscape.

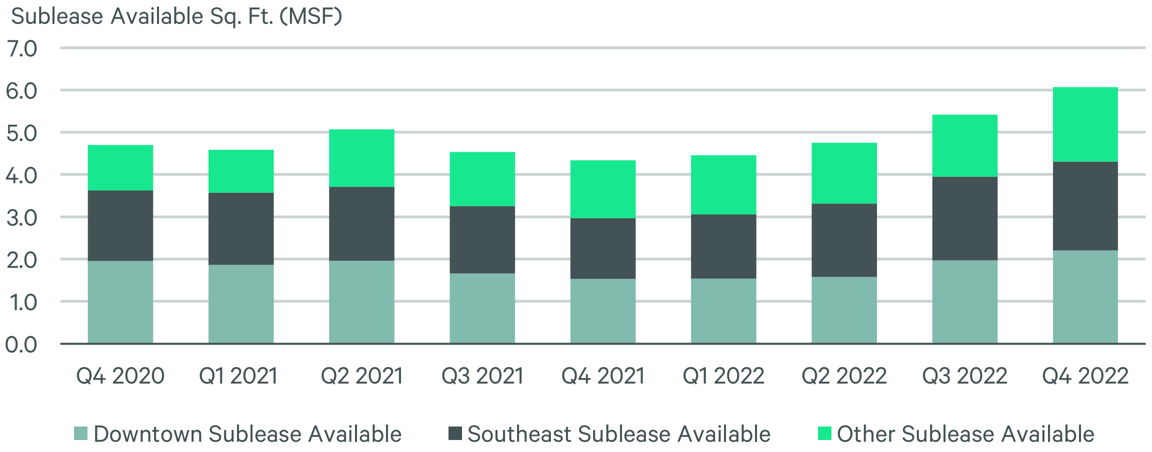
Class A properties accounted for 3.2 million sq. ft. of sublease availability, an annual increase of 34.6%. Notable Class A subleases that were listed in 2022 include: Jacobs Engineering (206,000 sq. ft.), Robinhood (119,000 sq. ft.) and Western Union (100,000 sq. ft.). The Downtown and Southeast submarkets have the most sublease availability with 2.2 million sq. ft. and 2.1 million sq. ft., respectively, and combined account for 71.7% of the market's total sublease availability.

FIGURE 2: Total Vacancy and Lease Rate



Source: CBRE Research Q4 2022

FIGURE 3: Sublease Availability



Source: CBRE Research Q4 2022

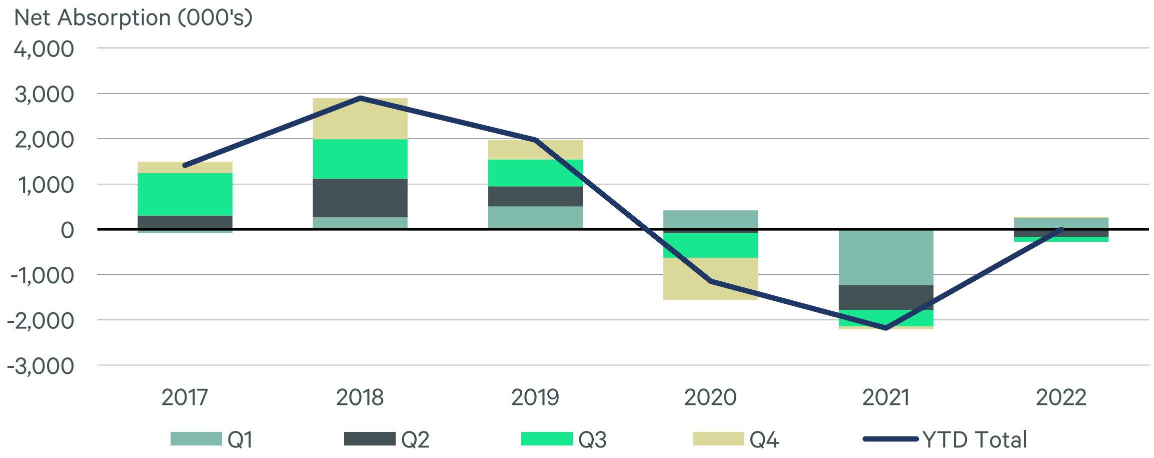
Net Absorption

Metro Denver recorded positive 23,300 sq. ft. of direct net absorption in Q4 2022, bringing the annual total for 2022 to just negative 2,600 sq. ft.. This is a significant improvement from the negative 2.1 million sq. ft. absorbed in 2021. Class B properties ended the year with a total of 191,000 sq. ft. of positive absorption – the only class type to finish the year in positive territory. This is largely due to Boom Supersonic occupying 287,000 sq. ft. in Q1 2022, which moved the needle immensely as no other property saw a move-in that large in 2022. Positive net absorption among Class B properties was offset by negative 218,000 sq. ft. of net absorption in Class A properties. This large Class A negative absorption can partially be explained by Starz downsizing by over 200,000 sq. ft. in Q4 2022, moving-out of 8900 Liberty Circle and into 6363 S Fiddlers Green Circle. Denver's largest submarkets, Downtown and Southeast, both posted significant annual improvements. Downtown recorded a total of negative 435,000 sq. ft., up from negative 1.2 million sq. ft. in 2021. The Southeast had positive 215,000 sq. ft. of net absorption in 2022, an impressive improvement from the negative 723,000 sq. ft. recorded in 2021.

Average Asking Lease Rates

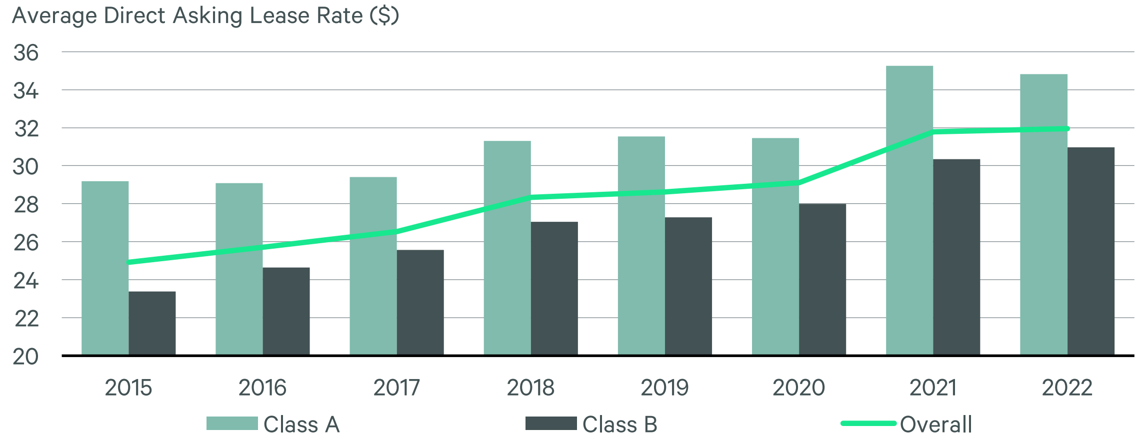
The overall average direct asking lease rate remained consistently flat throughout 2022, increasing only 0.5% year-over-year to $31.95 per sq. ft. FSG. Even with elevated vacancy rates, most landlords are holding firm and keeping rates steady as Denver has yet to see a drastic drop in asking rates during the current cycle. Also, with the construction pipeline relatively slow, average rates are not being driven upward by new premium product delivering onto the market. Both Class A and B direct average asking rates posted annual decreases, with Class A rates dropping 1.2% to $34.83 per sq. ft. FSG and Class B rates dipping 2.0% to $30.96 per sq. ft FSG. The Downtown average asking lease rate still ranks the highest at $39.68 per sq. ft. FSG, but the Cherry Creek and Boulder submarkets closely follow with asking rates of $37.72 per sq. ft. FSG, and $37.23 per sq. ft. FSG., respectively. Although Downtown boasts the highest asking rate, it has remained flat year-over-year, while Cherry Creek and Boulder's average rates saw annual increases of 9.3% and 2.2%., respectively.

FIGURE 4: Net Absorption



Source: CBRE Research Q4 2022

FIGURE 5: Average Asking Lease Rate



Source: CBRE Research Q4 2022

Development Activity

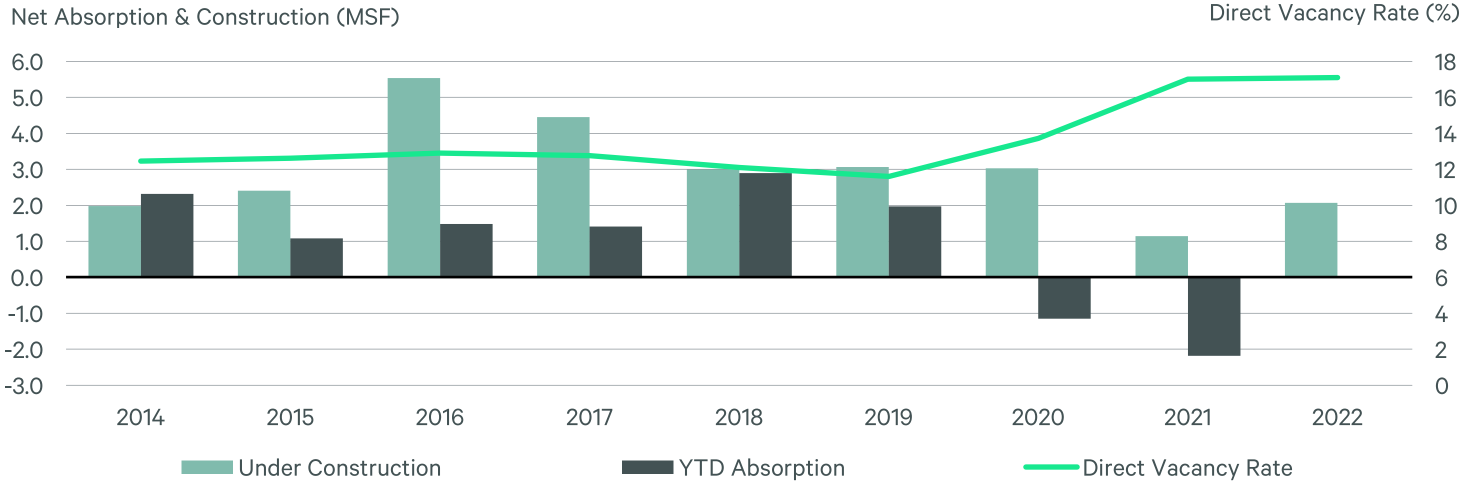
In 2022, the development pipeline saw ten properties spanning 1.5 million sq. ft. break ground and five new deliveries totaling 550,000 sq. ft. This year had a strong first half for development, but as the year progressed, development activity slowly stalled. In Q4 2022, no new properties broke ground across the entire Denver metro. Heightened vacancy, lower demand and the lack of debt availability have been roadblocks to development. These factors will most likely hinder the development pipeline in the coming quarters.

Despite the slowdown, there is still 2.1 million sq. ft. under construction across thirteen properties in metro Denver. The Boulder and Cherry Creek submarkets each have four projects underway for a total of 394,000 sq. ft. and 183,000 sq. ft., respectively. The largest project under construction is 1900 Lawrence in Downtown's Mid-CBD district. The 700,000-sq.-ft. property captured its first lease in Q4 2022 and is slated to deliver in Q4 2024.

Vectra Bank's new 127,000-sq-ft. headquarters officially delivered this quarter in the Denver Tech Center. Vectra Bank is occupying nearly three of the building's four floors, with roughly 35,000 sq. ft. available for lease.

Looking towards 2023, there are multiple projects that are slated to deliver in the first half of the year barring any construction complications. Several notable projects that are underway include: The Current River North (238,000 sq. ft.) in RiNo and 200 Clayton (70,500 sq. ft.) in Cherry Creek.

FIGURE 6: Construction, Net Absorption & Direct Vacancy



Source: CBRE Research Q4 2022

FIGURE 7: Notable Projects Under Construction

PROPERTY NAME	Property Size (SF)	Submarket	Preleased (%)	Spec/BTS	Est. Completion
1900 Lawrence	704,000	Downtown	4.3	Spec	Q4 2024
The Current River North	238,000	River North	20.7	Spec	Q1 2023
T3 RiNo	230,000	River North	0.0	Spec	Q3 2023
Paradigm River North	200,000	River North	38.4	Spec	Q2 2024
Boulder 29	154,000	Boulder	0.0	Spec	Q4 2023

Source: CBRE Research Q4 2022

Leasing Activity

Over 1.0 million sq. ft. was leased in metro Denver this quarter, bringing the 2022 total to 4.5 million sq. ft. On an annual basis, leasing volume was down 20.5% from the 5.7 million sq. ft. of transactions seen throughout 2021. Even though the number of transactions in 2022 and 2021 were comparable, leasing activity dipped this year due to an increase in downsizes amongst tenants. This year, larger tenants, especially those facing lease expirations, looked to reduce their office footprint as a cost saving measure and to occupy higher-quality space.

Class B properties' annual leasing volume decreased 38.7%, while activity in Class A properties dropped 6.1%. Even though leasing volume was less abundant in 2022, the percentage of Class A space leased increased, exemplifying the prominence of the flight-to-quality trend. Class A properties accounted for the majority of leasing volume in 2022 with 2.8 million sq. ft., or 62.2% of activity. In 2021, Class A properties still recorded the most transactions, but accounted for only 53.0% of total leasing volume.

Downtown leasing volume was down 38.4% year-over-year in 2022, while suburban activity only dipped 8.9%. The more dramatic decline in the Downtown submarket could allude to one emerging trend to watch: the effort to reduce employee commute times. Shorter commute times, especially to premium suburban office buildings, is one avenue employers are exploring to help attract workers back to the office.

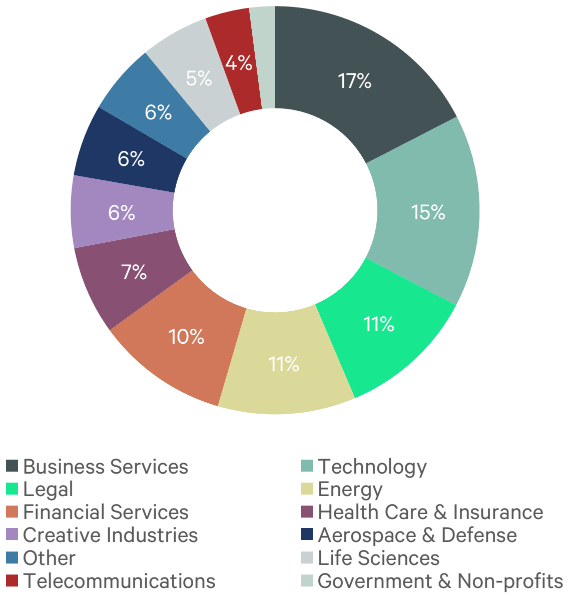
2022 leasing activity among traditional office-using sectors outperformed the volume transacted in 2021. Business Services had 786,000 sq. ft. of leases signed this year, up 30.6%, while Legal leasing volume increased 25.0% annually with 492,000 sq. ft. transacted. Comparatively, leasing activity amongst the Technology sector dipped 46.9% year-over-year.

FIGURE 8: Notable Q4 2022 Lease Transactions

TENANT	Industry	Location	Submarket	Lease Type	SF
Antero Resources	Energy	201 Fillmore	Cherry Creek	New Lease	132,000
E.W. Scripps	Telecommunications	2323 Delgany St	River North	New Lease	86,000
Ball Aerospace	Aerospace & Defense	10075 Westmoor Dr	Northwest	Renewal	83,000
Southwest Research Institute	Aerospace & Defense	1301 Walnut St	Boulder	New Lease	63,000
Anglo Gold	Other	6363 S Fiddlers Green Cir	Southeast	New Lease	33,000

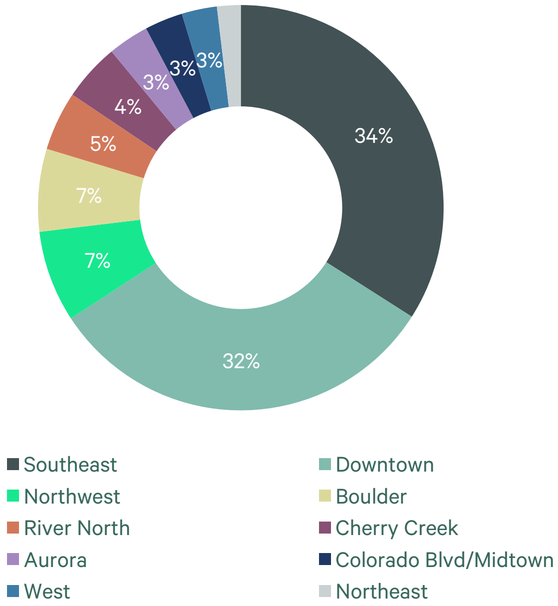
Source: CBRE Research Q4 2022

FIGURE 9: Leasing Activity by Industry Type (Q1 2022– Q4 2022)



Source: CBRE Research Q4 2022

FIGURE 10: Leasing Activity by Submarket (Q1 2022– Q4 2022)



Source: CBRE Research Q4 2022

Investment Trends

Investment activity stalled in the fourth quarter of 2022, with only nine properties trading hands at a total volume of $95.3 million (average price per sq. ft. $112.07). With interest rates continuing to rise in the second half of the year to mitigate high inflation, many investors have moved to the sidelines, tanking sales volume. Yearly sales volume rounded out to $2.5 billion, an annual decrease of just 2.7%. Strong investment sales in Q2 2022, and the sale of Flatiron Office Park for $625.1 million, helped soften slower investment activity in the latter half of 2022. Given the expectations of a relatively moderate recession approaching, the decrease in sales volume is not surprising, but office assets are fairing less favorably than other asset types due to their weaker fundamentals.

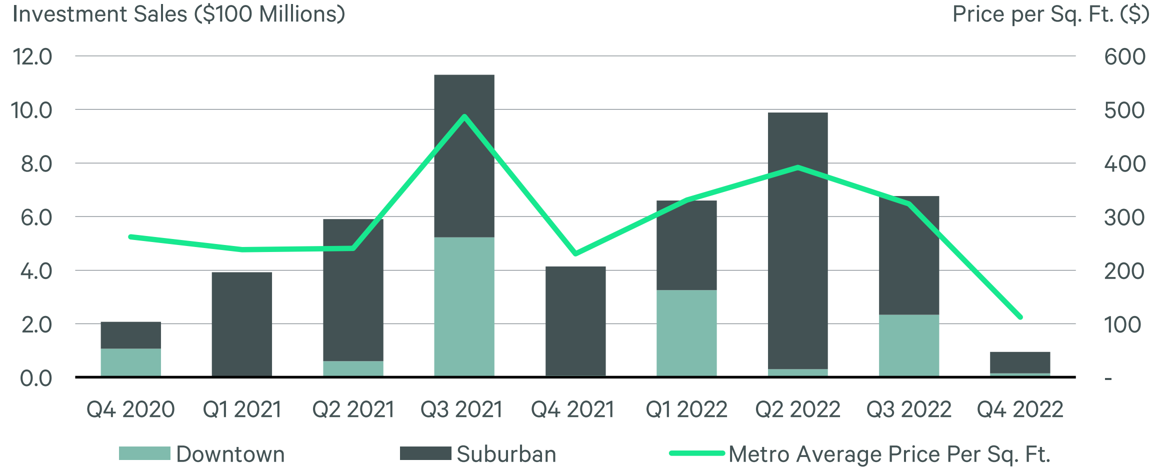
Due to the extenuating economic circumstances, there were not many notable sales in Q4 2022. The largest sale was 16401 E Centretech Pkwy in the Aurora submarket, which traded hands from Easterly Government Properties to NGP Group for $16.7 million or $143.46 per sq. ft. The suburban submarkets saw the majority of activity, while the Downtown submarket had only one transaction in the last quarter of the year. Goldman Sachs and Unico Properties sold The Denver Club Building (518 17th St) to Westside Investment Partners for $14.5 million ($52.80 per sq. ft.).

Employment

The Fed Funds Rate reached its highest level in five years in December 2022 amidst stubbornly high inflation, which has moderated slightly in recent months but continues to be supported by high food, housing and labor costs. While a recession appears imminent in 2023, wider expectations are of a more moderate slowdown. Higher costs of capital and the impact on corporate earnings are encouraging cost cutting that will trim employment levels, directly impacting consumer confidence and savings rates but ultimately leading to an anticipated, accelerated decline in inflation.

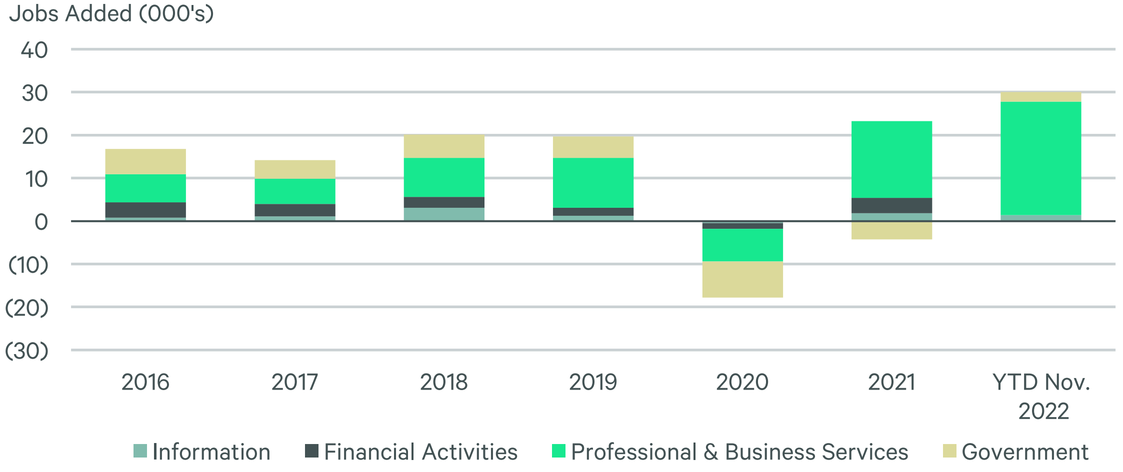
Total non-farm employment in metro Denver increased 4.2% through November on an average year-to-date basis, gaining 70,900 jobs. Office-using employment—including jobs in the information, financial activities, professional and business services, and government sectors—grew by 4.0%. Professional and business services, which represents 46% of office-using jobs, posted 8.0% growth and has added 26,400 jobs year-to-date. Metro Denver's unemployment rate declined slightly in November to 3.2% and is down 130 basis points year-over-year from 4.5%.

FIGURE 11: Investment Sales



Source: CBRE Research Q4 2022

FIGURE 12: Office-Using Employment Growth



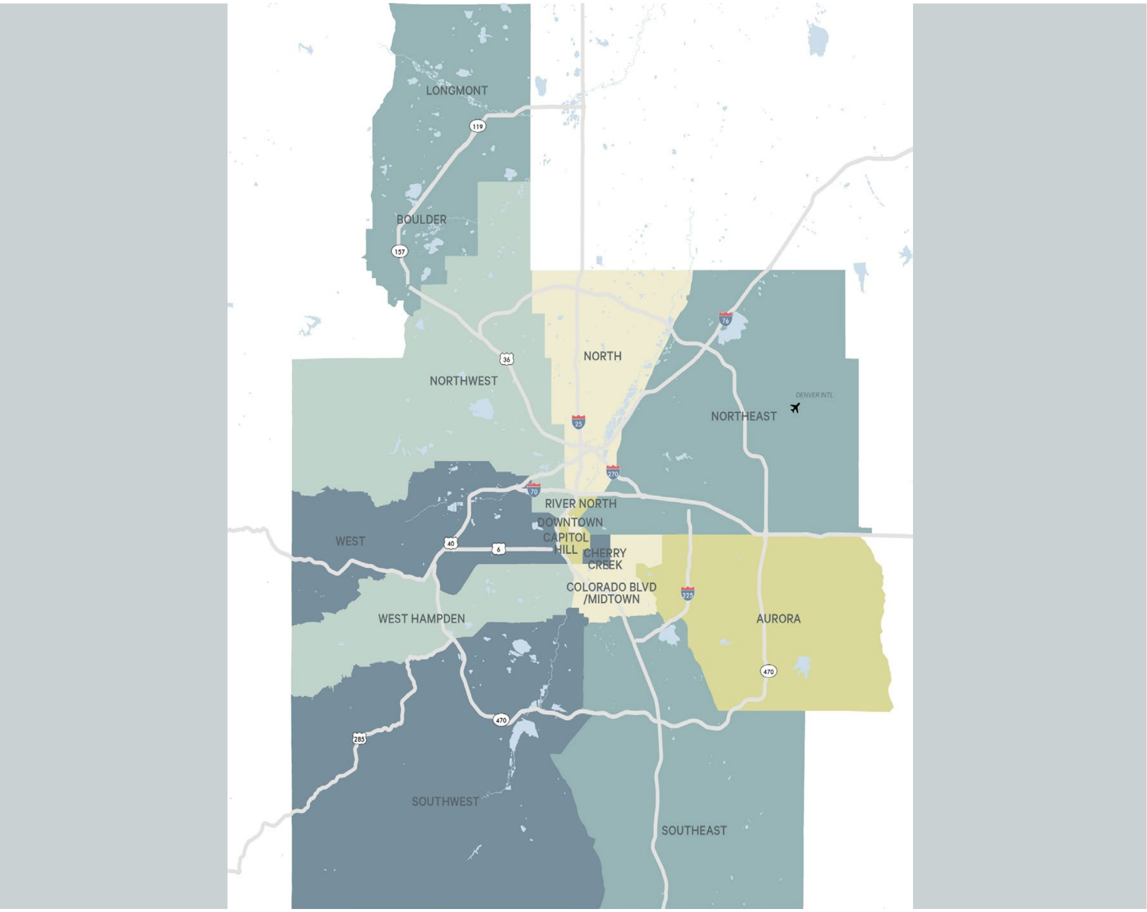
Source: U.S. Bureau of Labor Statistics, December 2022

FIGURE 13: Market Statistics by Submarket

SUBMARKET	NRA (SF)	Total Vacancy Rate (%)	Sublease Availability (SF)	Under Construction (SF)	Average Lease Rate ($./SF/YR FSG)	Q4 Net Absorption (SF)	YTD Net Absorption (SF)
Aurora	5,726,099	17.9	52,492	-	21.50	(131,097)	(192,104)
Boulder	7,093,125	14.4	370,803	394,080	37.23	(73,043)	(18,228)
Capitol Hill	2,440,567	21.5	258,523	-	30.27	20,476	(19,090)
Cherry Creek	2,733,665	8.3	15,308	280,548	37.72	16,008	70,860
Colorado Blvd/ Midtown	6,608,989	17.8	181,075	-	27.72	45,650	219,518
Downtown	30,660,569	27.2	2,207,220	704,036	39.68	13,551	(434,858)
Longmont	850,557	6.7	12,489	-	22.52	(2,511)	(9,030)
North	2,985,854	16.7	35,230	-	23.63	11,944	(1,313)
Northeast	1,198,063	16.6	105,133	-	27.47	1,256	42,706
Northwest	8,379,144	17.2	220,615	33,000	28.99	(67,768)	(50,820)
River North	2,054,403	32.7	267,346	659,998	47.38	(2,471)	77,059
Southeast	37,246,633	18.8	2,095,792	-	27.91	158,443	215,952
Southwest	5,531,656	13.6	25,171	-	25.53	4,976	38,934
West	6,721,865	17.0	206,384	-	25.80	27,290	91,010
West Hampden / Alameda	1,030,097	18.8	11,889	-	19.88	604	(33,231)
METRO TOTAL	121,261,286	20.0	6,065,470	2,071,662	31.95	23,308	(2,635)

Source: CBRE Research Q4 2022

Market Area Overview



CBRE Offices

Downtown Denver

1225 17th Street, Suite 3200
Denver, CO 80202

Denver Tech Center

5455 Landmark Place, Suite C102
Greenwood Village, CO 80111

Boulder

2755 Canyon Boulevard, 1st floor
Boulder, CO 80302

Fort Collins

3003 E. Harmony Road, Suite 300
Fort Collins, CO 80528

Colorado Springs

102 South Tejon Street, Suite 1100,
Colorado Springs, CO 80903

Survey Criteria

Includes all office buildings 10,000 sq. ft. and greater in size, excluding owner-user, in Adams, Arapahoe, Boulder, Broomfield, Denver, Douglas and Jefferson counties. Buildings which have begun construction as evidenced by site excavation or foundation work.

Contacts

Peyton Pellington
Research Analyst
+1 303 583 2017
peyton.pellington@cbre.com

Ryan McCauley
Research Analyst
+1 303 824 4710
ryan.mccauley@cbre.com

Jonathan Sullivan
Research Manager
+1 303 824 4230
jonathan.sullivan@cbre.com

CBRE