A Colorado Real Estate Journal Publication

March 2021

OFFICE & INDUSTRIAL Quarterly

Measuring the shadow cast by sublease space

The amount of shadow space, a portion of leased space that the tenant is not using, is challenging to measure because it is not officially marketed or tracked in industry databases. However, over the next year, it will impact vacancy rates as it comes to market.

As a year into the pandemic is quickly approaching, the commercial real estate industry in Denver and the rest of the economy are hopeful the pandemic signed a short-term lease and will not be renewing. With most employees working from home, many office users are taking this opportunity to reduce overhead. They saw their real estate footprint as the most obvious choice to downsize and coincidently listed a portion or, in some cases, the entirety of the space for sublease. Since Gov. Jared

Jared M. Balcavage
Research analyst, Transwestern

Polis announced the statewide stay-at-home order in late March of last year, 2 million square feet of sublease space was added to the market, nearly doubling the Denver market's sublease availability rate.

Following the oil price shock, massive layoffs and bankruptcies from companies across the metro area, sublease availabilities catapulted to the highest level in the past 20 years. The downtown market added over 800,000 sf of available sublease space since March, and the southeast market mirrored those levels, adding over 700,000 sf of available space to the bucket. While sublease availabilities have increased substantially over the past year, the reality of the situation is that a small number of major tenants (50,000-plus sf) account for the largest percentage of available sublease space. Of the 1.9 million sf of total sublease space listed downtown, major tenants of more than 50,000 sf account for 45% of the available sublease space. In the southeast, the situation is even more polarized, where major tenants of more than 50,000 sf account for 61% of the submarket's 1.7 million sf of available sublease space.

While we'd like to believe that the sublease availability rate will begin to taper off, this likely won't be the case for a while. Still, it is more likely that we will continue to see

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Letter from the Editor

Insights from national surveys

To help understand the national outlook, two associations, NAIOP and Society of Industrial and Office Realtors, released information from their January member surveys, which indicate sentiment for both asset classes.

Some good news:

- **Rent collections.** Rent collections improved across most sectors, including office, where 87% of respondents reported that 90% or more of their office tenants have paid rents in full and on time, which is the highest reported collection rate for office properties since April, when NAIOP first conducted its Coronavirus Impacts Survey.

- **Deal activity.** No surprise. There's been strong growth in industrial deal activity. Meanwhile, deal activity in the office sector "remains more robust than it had been before September," the NAIOP January Coronavirus Impacts Survey reported.
- **Rent relief.** Additionally, January saw the sharpest decline in rent relief requests from office tenants – only 19.7% of respondents reported that more than 10% of their tenants requested relief, the report states.
- **On-time transactions.** Across the board, on-time transactions increased in the fourth quarter, according to the SIOR Snapshot Sentiment Report. For office, 52% of all transactions are now on time, up from 38% the previous quarter; 74% of industrial transactions are on time, up from 51% in the third quarter.
- **Asking rents.** According to the SIOR report, asking rents are improving from the start of the pandemic across the board, but they still are nowhere near prepandemic levels and there's large variance between the gains for office and industrial.

However, some news remains starkly divided, based on asset type:

- **Confidence.** Industrial confidence continues to rise, now measuring a 6.9 out of 10. Office confidence continues to decline, now at its lowest confidence level of 4.7, the SIOR survey found.
- **Leasing.** "The difference before office and industrial leasing activity is extreme, with office specialists reporting 88% of lower leasing activity in Q4 versus only 34% for industrial," the SIOR survey reports.
- **Tenant concessions.** For industrial, 58% of the SIOR respondents said landlords had the bargaining power and were offering little to no concessions. Only 2% of office respondents felt the same.
- **Vacancy.** Likewise, only 22% of industrial specialists reported higher vacancy in the fourth quarter, while 60% of office respondents reported higher vacancy rates.

These surveys, in addition to the articles in this issue, support the claim that industrial already appears to be through the worst of the COVID-19 challenges. However, the road to recovery seems much longer for office.

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OFFICE — MARKET UPDATE

Denver's resilience will drive investment activity

Commercial real estate experts anticipate choppy waters for office investment sale activity over the next six months, as the world awaits widespread immunization. With immunization expected to bring the pandemic under control, rays of hope are shining down on the Denver metropolitan statistical area, and our team in Denver is confident the city will be a bright light coming out of the pandemic.

Corporate relocations from MSA to MSA and from central business districts to suburban communities, remote and flexible work environments, dedensification and wellness are all major themes, among others, affecting office investment in the future. Already in motion prior to the pandemic, these themes now are accelerating. Denver's office market stands to benefit from these changes, resulting in capital sources continuing to invest in assets in our city.

Denver is projected to rank in the top 10 for best cities to recover from coronavirus. The Mile High City always has been a highly resilient market. After the 2001 and 2008 downturns, Denver experienced significant job growth, growing by almost 79% combined. It is still one of the country's hottest markets, driven by leading metrics in population growth, a highly educated workforce and quality of life. Denver's job market has added 368,900 nonfarm employees across a diverse set of industries in the last decade, growing more than 23% since 2010, almost 1½ times the national average. This is important because job creation fuels future office demand.

Larry Thiel
Managing director, capital markets, JLL

Denver's population growth has continued to soar over the past decade, growing over 17%. Denver's population is 2.9 million today, and it is projected to grow to 3.1 million by 2025. A surge in in-migration could lead to greater future growth than projected; Colorado attracted 60,000 net new residents in 2020, which landed Denver in the top five cities across the U.S. for population gain in 2020.

Some companies are relocating from high-cost gateway cities to emerging markets throughout the Sunbelt and Mountain West. This major trend is due to availability and cost of talent, favorable personal income tax rates and pro-business governance. Denver is regularly identified as one of the nation's top markets for new corporate headquarter relocations and expansions due to the growing educated labor force, high quality of life and economic strength. Currently, Denver is home to 22 Fortune 1,000 companies and 10 Fortune 500 companies.

In its Better than Normal: Vision 2021 report, JLL Research projects Sunbelt and Mountain West markets to outperform gateway cities within 36 months, driven by increased adoption of distributed work models (hub and spoke) and continued office relocations. The MSA-to-MSA migration has proven to be more impactful on the overall U.S. office landscape than the CBD-versus-suburban office debate. In Denver, as occupiers analyze their talent demands and space needs, most could find that they do not need to choose a purely urban or purely suburban strategy; both have value and both environments can thrive in a post-pandemic Denver.

Jason Schmidt
Managing director, capital markets, JLL

Our team has been back in the office since June, with varying occupancy levels depending on when coronavirus cases were spiking in our state. We are fortunate our leadership endorsed this reentry because, like many growing organizations, our company culture is key. We anticipate most of the discussion about working from remote locations will have a minimal long-term impact on occupancy.

Humans are social animals who connect with each other to create progressive results. For certain roles, evaluating performance and measuring productivity is challenging in a virtual work environment. As soon as vaccines are widely distributed, our team expects office space demand to exceed prepandemic levels with pent-up demand and short-term renewals coming to expiration.

When JLL surveyed more than 2,000 office tenants for the Vision 2021 report, one theme is clear: Tenants expect their buildings to be focused on health and well-being. Even in the prepandemic environment, health and wellness were growing concerns for office tenants, but COVID-19 has accelerated this preference over the past year.

It stands to reason that healthy buildings in healthy environments will drive healthy returns. Selective tenants might require things like improved air-filtration systems and natural light. Owners should expect contactless security, elevator and access technologies to become standard tenant desires moving forward.

De-densification will play a role in overall employee satisfaction, as well as offsetting the partial work-from-home dynamic. A moderate uptick in employees working either permanently or mostly from home reduces overall desk needs, allowing space to be reimagined for new and innovative uses.

Pivoting to office investment activity, in 2020, office sales volume was down 19.5% in Colorado, and sale velocity was down 54.8%. Nearly 53% of the sales volume in 2020 occurred in the first quarter, with the rest of the year muted. Early in 2021, our team has noticed institutional capital's increased willingness to underwrite office assets, sig-

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OFFICE — MARKET UPDATE

Health crisis redefines submarkets attractiveness

Office workers are facing a new environment and reshaped daily routines. Some large tech firms have announced a full transition to remote work, raising questions over the future of the traditional office model. For the vast majority of companies, office space will remain essential to their operation, though many will adopt a more flexible model that allows for some days to be remote.

Uncertainties weigh on property performance. Companies put long-term commitments on hold as they await greater clarity, pushing the national office vacancy rate up. More sublease space will come to market at discounted rates as firms seek to offload unused space, particularly in denser downtown corridors and larger markets.

New realties are shifting buyers' concerns. The need for office space still is apparent and highly desired among the majority of workers, which will continue to attract investor attention. While it is more difficult to locate available assets and acquire lending, buyers are searching for properties designed for a post-pandemic world.

Smaller markets and suburban areas are poised to benefit from the shift in demand characteristics. The workplace will be more flexible. With reentry into the workplace still on the horizon, firms and employees are finding new ways to manage in a virtual world. It is estimated that about 37% of U.S. workers could plausibly do their jobs from home, which will lead

Brian C. Smith, CCIM, SIOR
First vice president, investments, and director, Healthcare Real Estate Division and National Office & Industrial Division, Marcus & Millichap

to a greater adoption of a hybrid model that allows for partial remote work. In a recent survey of office-occupying firms, 82% will allow partial remote work because employees are demanding more accommodations in an uncertain environment. Independent work can be done at home, while the office will be a space for collaboration and meetings. Offices will become larger to make more room for workers following 10 years of condensing the traditional private suite from roughly 250 square feet to just under 200 sf.

Secondary and tertiary markets are becoming popular. In the years leading up to the pandemic, employers were adding more office space in secondary and tertiary markets to access a larger talent pool and lower expenses. While most markets in the second quarter registered softening demand, some smaller metro areas remained more stable. The pandemic will accelerate the movement to smaller markets and suburban areas as businesses transition to a more decentralized hub-and-spoke model. This has been highlighted recently by

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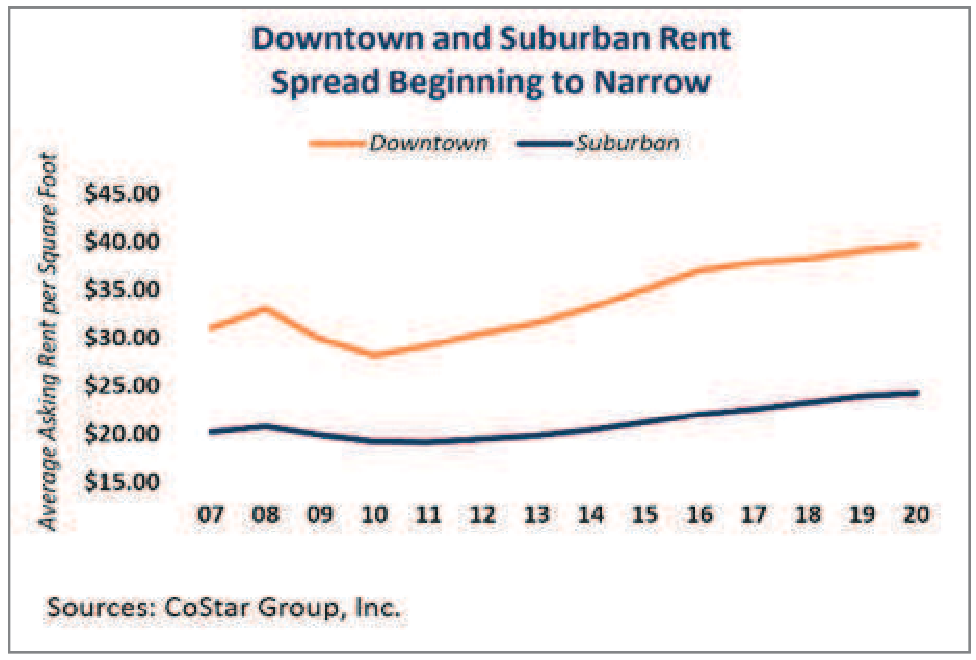
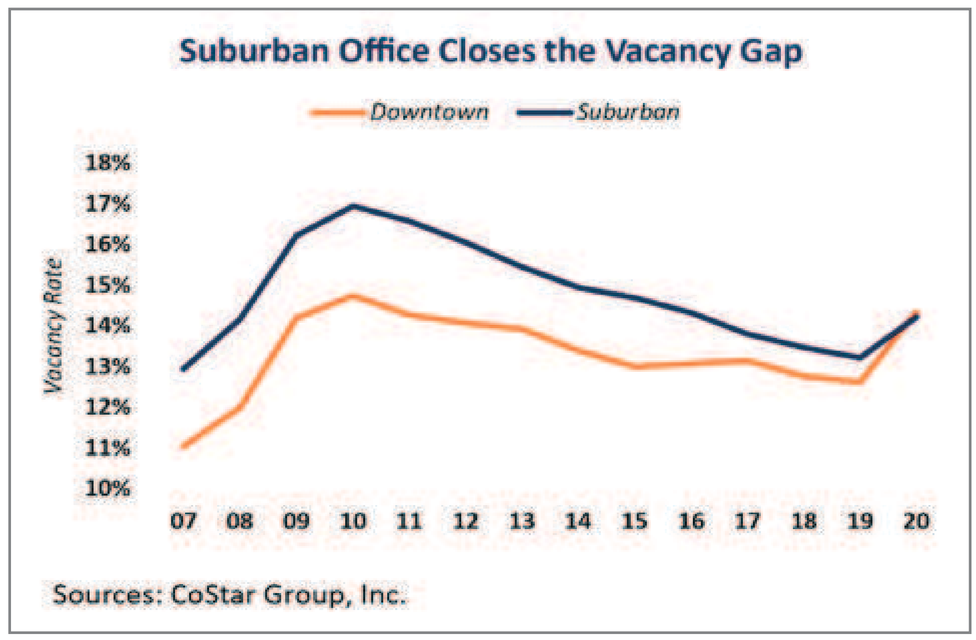


Sources: CoStar Group, Inc.



Sources: CoStar Group, Inc.

OFFICE — MARKET UPDATE

The sales market recovery is underway in Denver

COVID-19 dealt a significant blow to the sale market in commercial real estate, particularly the office and retail markets. Market activity was strong prior to the pandemic, and it seemed as though the market could not be slowed down. What COVID-19 reminded everyone is that major events can alter market dynamics seemingly overnight.

Darrin Revious
Senior adviser, Pinnacle Real Estate Advisors

One of the most important factors we are seeing in the quest to market recovery is increasing investor optimism. Furthermore, investors have shifted their focus from downside risk to upside potential. With increased capital waiting to be deployed, low interest rates and increased debt financing, investment is poised for a rebound in 2021. Last year was a year to forget for many in commercial real estate. With 2021 underway, the election over, the vaccine rollout underway (albeit slowly) and general impatience in the market, we now are seeing what market recovery looks like.

Markets like Denver that were performing better than most before the pandemic are seeing recovery sooner and faster than others. Despite an increase in sales, leasing and construction activity from last year, general activity in the market remains lower than before the pandemic began. According to the National Association of Realtors, dollar sales volume in commercial real estate is down 56% from the prior year. In order for sales, leasing and construction to rebound to prepandemic levels, social distancing measures will need to be relaxed so that restaurants, stores and public places can be full of people again. Of course, this should be done safely, with public health given the highest level of consideration. According to President Joe Biden, there will be enough vaccine doses for everyone to be vaccinated by May. If this happens, we can expect market recovery to accelerate by the third and fourth quarters of 2021, with full recovery hopefully happening sometime in 2022. The bottom line is the market will not fully recover until the pandemic is brought to an end.

Another important aspect of the market recovery in commercial real estate will be how the U.S. Federal Reserve behaves, and how large banks react and adjust to the new landscape. According to Kansas City Federal Reserve Bank President Esther George, "Strains on real estate finance currently appear contained." This is encouraging to hear, as recovery can only occur in this scenario. Programs like the Payment Protection Program have been effective in getting small businesses, nonprofits and event venues hit hard by COVID-19 the necessary support needed to stay afloat. Large government support programs like this have been successful in shifting a significant amount of the financial burden from business owners to the federal government. This shift also allows capital to remain with investors. It is estimated that there is more than $200 billion in investor capital waiting to be deployed for 2021.

In terms of the nuances of the sale and lease market recovery, COVID-19 undoubtedly has altered the way tenants, landlords, buyers and sellers are behaving. Jamie Gard, executive managing director at Newmark, said tenants have the leverage right now and they are pushing the envelope. "They are asking for less space in the short term, but does that mean they won't need it in the long term? Probably not," he said. "It would not be surprising to see them say in a year or two that they need more space because their employees are coming back."

This is not surprising, given that in the grand scheme of things COVID-19 is very much temporary. "User sales have been very strong with multitenant office investment properties much slower," Gard said. "The suburbs are recovering marginally faster than downtown, but downtown is improving. Short-term extensions are mounting up, which should lead to a better 2022."

Perhaps the group most affected by the pandemic are landlords, who are competing with an abundance of sublease space. Todd Roebken, executive managing director at Savills Studley, said, "Concessions are up, tenant improvements from landlords are up and there is still not much velocity. Landlords are going to need to get more aggressive because they are competing with a sizeable amount of significantly discounted sublease space. Will the market recover? Yes, but tenants will occupy 20 to 40% less than their original size and demand an option to contract and expand."

Although COVID-19's impact on the commercial real estate market has felt overwhelming, there is reason to remain optimistic. Real estate markets historically are cyclical, and major events have been overcome before. Despite the downturn, COVID-19 appears to be moving further into the rearview mirror. With an abundance of readily available capital, low interest rates and lots of pent-up demand, one can hope the recovery will lead to an even stronger market than what existed before the pandemic. While conditions will be somewhat different in terms of spatial needs, fewer common areas and maybe one or two fewer buffets, it is unlikely that the commercial real estate landscape will be fundamentally changed forever, as some have suggested. It is likely that more employees will be given the option to work from home, but that amount is expected to be negligible, and additional job growth likely would offset any noticeable impact. Denver remains one of the most desirable places to live, work and invest, and not even a pandemic can derail it. ▲

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COMMUNITIES OPEN FOR BUSINESS

EDC DIRECTORY

BOULDER ECONOMIC COUNCIL

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BROOMFIELD, CITY & COUNTY OF

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Targeted Industries: InfoTech, Finance/Asset Management, Global, Aerospace, Healthy Living/Foods and HealthTech. Community-focused targets include experience retailers and creative restaurants.

CHERRY CREEK NORTH BUSINESS IMPROVEMENT DISTRICT

Nick LeMasters
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303-394-2904
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Targeted Industries: Retail, restaurants, hotels, boutique office including legal, accounting, wealth management and residential uses.

COLORADO SPRINGS CHAMBER AND EDC

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Targeted Industries: Aerospace & Defense, Aviation Related & Specialty Manufacturing, Cybersecurity, Information Technology, Healthcare & Medical Technologies, Sports & Outdoor Recreation

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COMMERCE CITY ECONOMIC DEVELOPMENT

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Targeted Industries: DIA Technology, Advanced Manufacturing, Logistics and Distribution, Business and Professional Services, Retail/Hospitality/Leisure

DENVER SOUTH

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Targeted Industries: Aerospace/Aviation, Software and Electronics/IT, Health Sciences, Broadband and Internet, Engineering Services, Financial Services.

DOWNTOWN DENVER PARTNERSHIP

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Targeted Industries: Downtown has a strong and diverse concentration of industries, including: legal services, accounting, energy/natural resources, finance/insurance, engineering/architecture and broadcasting/telecommunications.

FOUNTAIN, CITY OF

Kimberly Bailey
Economic Development / Urban Renewal Director
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www.furaco.org
Targeted Industries: Manufacturing (*specialized "niche" advanced, food/AG*) - Transportation & Logistics - Homeland Security (*military, law enforcement*) - Entrepreneurialism - Renewable Energy - Motorsports Economy (*tourism & entertainment*)

GRAND JUNCTION ECONOMIC PARTNERSHIP

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JEFFERSON COUNTY ECONOMIC DEVELOPMENT CORP.

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LONE TREE, CITY OF

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THORNTON, CITY OF

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Targeted Industries:

WESTMINSTER ECONOMIC DEVELOPMENT

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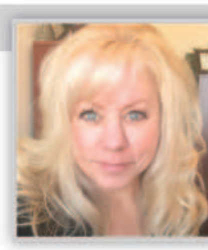
stroller@cityofwestminster.us
www.westminstereconomicdevelopment.us
Targeted Industries: Aerospace, Information & Technology, Life Sciences & Healthcare, Professional & Technical Services, Experiential Retail & Entertainment, Unique Dining



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If your community would like to appear in the EDC Directory, please contact Lori Golightly at lgolightly@crej.com or 303-623-1148 ext. 102.

OFFICE — OWNER INSIGHTS

How we're evolving to meet new leasing demands

As COVID-19 vaccinations are being rolled out, companies are trying to figure out their return-to-office plans. Many office workers have been working from home for almost a year. As a result, many companies are planning some type of flexible work policy if they did not have one prior to the WFH experience. Some companies are opting for a hybrid model where employees work the majority of days in the office and fewer days at home. Others are exploring the hub-and-spoke model, which includes a main "hub" with offices spread out closer to employees' homes.

Despite some advantages to WFH, the office continues to be the ideal place for collaboration, innovation and maintaining company culture. Granite Properties, owner and manager of five office buildings in Denver, conducted a return-to-office customer survey and received more than 3,200 responses from decision-makers and office employees in our buildings. The survey found that people miss the office camaraderie and creative energy that comes from being with their teammates and that they value the flexibility WFH allows. In addition, these companies said they want more workspace flexibility to help them run their businesses more efficiently and productively. We believe that going forward companies will be looking for flexible workspace solutions.

To meet the growing demand for flexibility, it will be important for office owners to adapt and help companies find the right office solutions. This is why we modified our leasing platform and integrated "evolve," a new menu of office and leasing solutions. Through

Stephanie Lawrence
Senior managing director, Granite Properties

this solution, we now offer a wide range of solutions, including conventional, on-demand, move-in-ready, short-term and coworking space. We also can support the hub-and-spoke model through partnerships with coworking firms.

The platform consists of the following solutions that companies can tailor to their individual needs:

■ **Create.** Many companies cannot wait for their employees to return to the office full time because they either miss it or because WFH isn't a feasible solution for them. Our company continues to offer leases of one to more than 10 years with this option. Customers can customize their offices to fit their brand. They also will have full access to the amenities, including fitness centers, conference rooms, food services, indoor lounges and outdoor workspaces. To accommodate the need for flexibility, customers can take advantage of our short-term and on-demand solutions as well.

■ **Ready.** Short-term office space has been popular with startups because it is harder for them to forecast how much space they'll need for the future. Short-term, one- to five-year, lease options provide startups with the flexibility to grow, downsize or move to a different market. Now that more companies are trying to figure out their flexible work policies, a short-term and fully furnished lease space can

An interior shot of Regency Plaza in Denver

be an attractive solution. This short-term Ready option allows customers to move in right away, furnished or unfurnished, with lease terms ranging from monthly to yearly.

■ **On-demand.** Now more than ever, companies are looking for collaborative office space with high-end amenities to encourage employees to return to the office. Through this option, customers have access to amenities in buildings across all markets. For example, when Denver customers travel to Dallas for business, they will be able to use any of the amenities, like fitness centers or conference rooms, at any Granite building in the Dallas area. The On-Demand program also supports customers interested in the hub-and-spoke model through partnerships with coworking firms. Through a program called G.O. Pass, customers can lease their primary space in a Granite building and establish a network of satellite offices at coworking locations to support remote employees.

We have spent this last year focused on the future of office space. We have listened and communicated with our customers, and taken this time to innovate and anticipate future needs. We have made our buildings healthier and safer in Denver, and portfoliowide, with our $10 million Inspire Wellness initiative. We have enhanced the air quality with Needlepoint Bipolar Ionization, retrofitted touchless fixtures in restrooms and improved outdoor workspace experiences. We are moving quickly to help our customers adapt to their changing business needs with our office leasing solutions. As we approach returning to the office, we believe that office owners who adapt to the changes and focus on flexibility, wellness and collaborative work environments will attract the greatest demand. ▲

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Office Properties Quarterly - Financing Sources Matrix

TYPE OF CAPITAL	SOURCE OF CAPITAL	EXPLANATION	RATES/SPREADS	LTV/COVERAGE	TERM	AMORTIZATION	FOCUS	TRENDS
LIFE INSURANCE COMPANY	• Insurance premiums • Annuity and GIC sales	• Non-Recourse • Longer-term fixed rate loan	2.75%-3.75%	• Up to 60% LTV • 1.50x Minimum DCR	5-30 Years	20-30 Years	• Downtown, urban locations or popular suburban office parks • Multi-tenant, traditional floor plates • Top tier tenants with good credit • Major metros & secondary markets (being more selective on secondary markets) •Diversified rent rolls with evenly distributed rollover	• Many of the life insurance companies have become more selective on office properties but that is starting to ease up • Lenders are digging further into the rent roll to understand each tenant business models and credit • Higher push for properties with credit tenants and term • Most competitive at lower to moderate leverage (50% - 55%) with strong sponsors • Typically targeting higher quality assets with better credit in the rent roll or assets with a staggered rent roll • Starting to target high-quality suburban office more due to impacts of COVID-19 on more urban areas • Interest reserves implemented on deal-by-deal basis
CONDUIT (CMBS)	• Sales of mortgage-backed securities through public markets	• Non-Recourse • Longer-term fixed rate loan	3.25%-4.25%	• Up to 65% LTV • 1.40x Minimum DCR • 9.0% Minimum Debt Yield	5, 7, & 10 Years	25-30 Years	• Downtown office • Suburban office • Single-tenant with structure • Secondary/Tertiary Markets	• Looking at office assets but being more selective with effects of COVID-19 •Higher emphasis on tenants' credit or loan structure around rollover • Interest reserve on a case-by-case basis; loans greater than 60% LTV will likely have a debt service reserve • Targeting acquisition or cash-neutral refinances in the current environment • Will consider full-term I/O on select office deals at LTVs of 55% or less
BANK	• Corporate Debt • Deposits	• Recourse (non-recourse becoming more available) • Shorter-term fixed and floating rate loans	3.25% - 4.25%	• Up to 65% LTV • 1.40x Minimum DCR • 9.5% Minimum Debt Yield	Up to 10 Years Fixed, Typical Max Term is 5-7 Years	25-30 Years	• All office assets • Value-add with guaranties • Secondary/Tertiary Markets	• Being more selective on asset quality given the current environment • Many banks focusing primarily on existing client relationships • Most competitive for Sponsors with established banking relationships and strong borrower history that are willing to accept recourse • Establishing a deposit relationship is becoming a requirement • Typically recourse loans, but non-recourse becoming more available to strong sponsors at lower leverage • More flexible (open) prepayment terms
DEBT FUND / BRIDGE LOAN	• Private Capital • Institutional Capital	• Non-Recourse • Shorter term bridge loans for acquisition and/or repositioning	L+375-550 bps spreads	• Up to 75% LTC • Going-in 1.0x DCR	1-5 Years (3+1+1)	Interest Only	• Value-Add Transactions • Recapitalizations	• Most lenders have a LIBOR floor of 25 or 50 bps • Being more selective on asset quality given the current environment • Pricing depends on leverage level, property quality, and Sponsor strength • Needs to have strong value-add business plan and story in place • Limited interest for non-cash flowing assets
MEZZANINE/ PREFERRED EQUITY	• Private Capital • Institutional Capital	• Junior financing secured by a pledge of, or participation in ownership interest	Mezzanine 8%-12%	• Up to 80% LTC • 1.10x DCR	2-10 Years	Interest Only (in most cases)	• All office assets • Value-Add Transactions • Recapitalizations	• Preferred equity offers higher funding than mezzanine, but at a higher cost • Minimum investment is typically $5MM but can start as low as $1MM when paired with senior position

DCR - Debt Coverage Ratio
DUS - Delegated Underwriter Servicer
LTV - Loan to Value Ratio
LTC - Loan to Cost Ratio
LIBOR - London Interbank Offered Rate
REIT - Real Estate Investment Trust

This information is intended to illustrate some of the lending options currently available. Other options may exist. While Essex Financial Group strives to present this information as accurately as possible, no guarantee is made as to the accuracy of the data presented, or the availability of the terms at time of application. Rates and terms are subject to change. Please contact one of our mortgage bankers for up to date rate and term information.

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Essex Financial Group - Recent Office Transactions

Canyon Point II
Golden, CO
$3,400,000 Permanent Loan
Life Insurance Company

Medici Office Portfolio
Aurora, CO
$18,500,000 Permanent Loan
CMBS

Boulevard 25
Denver, CO
$5,800,000 Permanent Loan
Life Insurance Company

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OFFICE — LEASING

Spec suites may be best option amid pandemic

Rick Roberts
General manager, Aberdeen Construction

Everybody loves spec suites. Landlords, tenants, asset managers, brokers – they're all on board. And why not? Spec suites always have been a durable, timely real estate option for tenants, especially in distressed cycles. COVID-19 is aggressively putting that claim to the test.

A speculative suite, or "spec suite," is a rentable office space built out by the landlord without a committed tenant to lease it. That is, all the design and construction of the suite is done at the front end before a prospective tenant begins the lease negotiation process. In "traditional" leasing it takes 80 to 120 days to build out any given space, and that's only after design approval, pricing and purchasing of finishes, and navigating through the construction documents with the architect.

Spec suites can have almost limitless variables but share a common theme: They're built to be move-in ready or nearly move-in ready to present prospective tenants with a far shorter search-to-lease timeline than traditional leasing can offer. In a market as uncertain as this one, spec suites may be the answer for tenants that require a fixed address in a space visually adaptive to their general requirements.

"The pandemic has affected every business differently," said Greyson Konkel, construction project manager with Stream Realty Partners, a commercial real estate firm working with owners, investors and tenants. "The common factor for many tenants today is that they need to adapt, sometimes very quickly, to changing conditions. Specs suites are ready to go. They offer that flexibility in size and design that allows tenants to hit the ground running."

They also offer a visual element that existing building spaces cannot. Existing suites or even ones in "white-box" condition offer few or no clues as to what the finished product might look like. Although software technology can produce stunningly realistic renderings of any given space, it's still not the real thing. There is no substitute for actually being in the space surrounded by those visual and tactile elements, even if design is on the simple side. And that's really the point.

A clean, basic aesthetic allows landlords to cast a wider net for potential suitors. Typically, those spaces should include a reception area, conference room, kitchen or break area, perhaps a few fixed offices and an open area for workstations. There are almost limitless variations on that collection, of course but, again, simplicity is what sells.

Spec suites can range in size from less than 1,000 square feet to several floors depending on a host of factors. Generally, the larger they are, the more potential complications exist, especially with COVID-19 distancing and hygiene requirements in place.

"The size of those suites is based largely on potential tenants in the area relative to how much vacancy exists in a particular building or development," Konkel said. "And there is the state of each building, the submarket location and any specific market conditions. Clearly people are chomping at the bit to get back into their buildings, but confidence is just not there yet." Some shaky market fundamentals reflect that sentiment.

Aberdeen Construction
Spec suites offer tenants a fast track to occupancy. Designs are usually clean and simple with a variety of architectural elements.

Metrowide, the office market absorbed negative 1.5 million square feet in the last quarter of 2020, a record low, according to CoStar Group. Vacancy took a hit as well rising from 15.8% to 17.4% in the fourth quarter, as all three building classes continue to struggle. Rates haven't yet begun to drop significantly, but landlord concessions like free rent and parking and more generous tenant improvement allowances are on the rise for the first time in years.

"Small spec suites are leasing quickly at this point in the COVID-19 frenzy," said Justin Rayburn, principal at Fountainhead Commercial. "We're seeing business owners ready and willing to kick-start their companies again, jumping on spec suites that are newly constructed and immediately available in the marketplace. The smaller spec suite option is giving those owners a chance to reduce their footprint and

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OFFICE — LEASING

Building managers: How square are your feet?

Becky Hanner
Principal, Commercial Asset Services

Building Owners and Managers Association's floor measurement standards are very well known throughout the commercial real estate industry. They are so well recognized that it is common practice to include a reference to BOMA floor standards in standard lease language. BOMA published the first office floor measurement standard in 1915, has updated the standard to maintain relevancy and has developed an entire suite of floor measurement standards, all of which are American National Standards Institute certified. It is no wonder that BOMA is known as the preeminent industry standard for calculating floor measurements for commercial real estate buildings. Yet, with all this validation, real estate executives often are circumspect about verifying building measurements or implementing revised calculations when a building is remeasured.

The square footages of buildings are ever changing. You might wonder how that can happen. It really starts with the original development of the property. The initial architectural plans of a building will state what the square footage of the structure will be, when developed. During the construction process, discrepancies can occur. A wall may have been constructed slightly off from the original plans, a footing might have to be altered due to site conditions, or the front entrance could have been recessed just a little more than initially anticipated. As a practical manner, when constructing a property, things can happen that may very well change the architect's original calculation of building square footage.

Over the years, spaces will get remodeled, cojoined, subdivided or portions of common corridors absorbed into tenant suites, among other types of building alterations. If the property is capping the load factor for market accommodation, then the measurements can be further altered, especially when market cap tolerance changes over the years and the building may amend the load factor as the market will accept in order to minimize the amount of space not captured as leasable. Real estate professionals may forget to update suite square footages when they are aware of spaces that have revised measurements or, when altering space configurations, they may attempt to estimated square footages according to what they feel is a fair calculation of a space. Any of these scenarios will skew building measurements. Over time this can add up to a considerable amount of discrepancy.

Square footage is the foundational measurement in commercial real estate. Tenants occupy usable square feet. Leases may be based on a capped rentable-square-foot basis. Building sales are noted on a gross-leasable-area basis. Lenders use square feet to pro forma potential gross rents. Construction costs are estimated on actual square-foot basis. Operating costs customarily are measured by a rentable square-foot basis. It seems to make sense that if square footage is the language of real estate, then a building owner would want to know a property's true measurement calculations.

Consider the actual case study where a building was purchased at the height of the economy and based on a given measurement. A subsequent downturn in the economy resulted in a large building vacancy. The owner had the building professionally measured and found 5% more space in the building, in this case, amounting to over 30,000 sf. This owner was able to reposition the property, then sell it without taking a loss that otherwise would have occurred.

Another true-life case study is the building that was purchased based on a given measurement. Since no plans were conveyed, the buyer had the building professionally measured to find the building had 3% less square feet than it purchased. In this case this amount equated to almost 6,000 sf.

A final example is a tenant audit. The last situation you wish to find yourself in is having a tenant inform you it had its space professionally measured and is demanding a refund on rent paid over the years. Not only do you have less recurring income, but also you potentially owe back rent and have a dissatisfied tenant.

It is important that the company you engage to measure the building fully understands the BOMA floor measurements so that accurate calculations will be received. Ensure to utilize the services of a true metrologist (measurement professional). Questions you may ask include:

- How many buildings and total square footage has the professional measured?
- Has the professional gone to court to testify on building measurements and what was the outcome?
- How long has the metrologist been providing floor measurements?
- What measurement methodology does the professional use?
- What deliverable will the metrologist provide so that you can verify accurate floor measurements and calculations?
- Can the professional provide recommendations from satisfied clients?
- Does the measurement professional safely store, update and maintain the floor plans and other related files in case there is an alteration to the property?

Once your building is measured and new calculations are provided, compare them to the current rent roll. You might find that suites or overall building square footage have increased or decreased from the size you previously had referenced. Once you have this information, your team can sit down and determine a strategy for implementation.

In conclusion, accurate measurement of a building provides the owner with factual data that is used to make critical decisions in the course of leasing, managing, buying and selling real estate. An implementation strategy of accurate calculations should be developed with the property owner and the leasing/management team. Part two of this series will outline best practices for implementation of new building measurements. ▲

OFFICE — TRENDS

3 office market trends to watch as year unfolds

After the roller-coaster year we experienced in 2020, we're all looking for a little bit more calm and predictability as we head further into 2021. Fortunately, with more clarity around the COVID-19 vaccine rollout and its impact on our daily lives, we can anticipate a year of recovery marked by change.

Andy Cullen
Managing broker, Tributary Real Estate

As job losses in various sectors around Denver continue to slow as businesses are allowed to return to something closer to prepandemic normalcy, there will be a rebound in the economy and office market, especially in the latter half of the year. As we try to navigate new reentry challenges, it's important to understand some key trends that will affect the workplace.

1. The rise of the hybrid model. In many respects, COVID-19 accelerated trends we already were experiencing in office real estate. Among them is the "hybrid model" of work, which can mean a few different things but generally refers to a combination of working from home and at the office. Many companies are realizing that employees enjoy working from home and can maintain productivity levels, and while some companies have decided to abandon their offices altogether, most employers will retain their office space in some form while perhaps allowing employees to work from home at certain times.

Some companies are considering rotating the days that employees work remotely in order to have fewer people in the office at once – a sensitivity that is likely to emerge in a post-COVID-19 world. This means that companies may choose to lease smaller spaces with desks more spread out. Those desks will be part of a "hoteling" approach, in which employees don't have a set desk but rather can touch down anywhere in the office. This will require new office management and employee guidelines, as well as an increased focus on sanitization in order to meet new standards for cleanliness where shared surfaces are concerned. Integrated technology and teamwork considerations also will come into play as this model becomes more popular to ensure consistency of corporate culture.

2. Tenant improvement challenges. Last March as the virus took hold, Colorado didn't order the shutdown of construction sites as other states did, although the economic situation that followed has created slowdowns for various types of building.

Most important to prospective tenants, there are delays in acquiring the permits necessary to complete tenant finishes as a result of permit staffs across the Front Range working remotely while using processes that were designed around face-to-face interaction. Some governmental agencies have had to furlough workers as a result of depressed tax collections that have affected their budgets. Tenants who want to remodel an office space before moving in should anticipate that these challenges are likely to continue in the near term as permit offices work to find ways around these challenges.

As companies determine how and when employees need to be in the office, one option could lead to smaller spaces with employees not having a set desk. This will require new office management and employee guidelines, as well as an increased focus on sanitization in order to meet new standards for cleanliness where shared surfaces are concerned.

Additionally, although some may have anticipated a dip in construction prices for tenant improvement, projections indicate that construction prices generally are likely to tick up as supply chain issues and demand for materials persist into 2021.

3. Market fundamentals will begin to shift. The economic fallout from COVID-19 significantly changed the trajectory of the commercial real estate market everywhere, metro Denver included. Millions of square feet of office space were placed on the sublease market in 2020, in the central business district in particular. This was the result of companies pulling back on leasing plans or vacating office space because of market conditions or uncertainty about the economic climate, but the increased availability of sublease space, which leases at a somewhat lower rate than direct space on average, created opportunity for tenants seeking to move or expand, particularly if they are in search of higher-quality space.

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OFFICE — TRENDS

Tweaking coworking models for the next generation

Once the fastest-growing disruptor in commercial real estate, coworking now fights for its life as the global pandemic continues the stress test on this modern concept. In Denver, like many cities, coworking was fueled by startups chasing rapid growth and needing flexibility along the way. The concept provided a great solution for customers by offering leases with flexible terms and sizes. "Need space for three more people? Just sign here." "Want to keep your office another three, six or 12 months? No problem, happy to have you."

Unfortunately, there were multiple problems with this business model and the global pandemic wasted no time revealing the Achilles' heel in the system. Does this mean coworking is dead and will leave empty blocks of space around Denver to become a scar on our rent roll? In short, the answer is "no" – if the concept pivots.

Just one year into the pandemic, the majority of coworking subtenants likely have seen their lease or membership expiration come up and, in many cases, have opted not to renew due to COVID-19 concerns and governments asking people to work from home. Now, industry leading coworking companies such as Industrious, Knotel and others are grabbing at lifelines by selling to traditional brokerage firms such as CBRE and Newmark. In addition, WeWork is rumored to be entertaining a SPAC merger amid its efforts to close four locations in Denver, a move reflective of its push to abandon leases worldwide. Here, more than 1 million square feet of coworking space currently is leased from a traditional landlord, with the plan to sublease to numerous smaller subtenants and turn a profit. Therein lies the issue; coworking in its first-generation form sought to lease space long term from traditional landlords at market rates, attempting to beat the market consistently on short-term deals with subtenants who often lacked credit history. The pitfalls of this first-generation model now have been fully illuminated, but the entire model is not necessarily flawed, just inefficient.

Reid Freeman
Vice president, Stream Realty Partners

As we already have established, the coworking customer has been a happy customer. When we ask these customers why they are satisfied with their experiences, the lists include reasons such as high-quality office space, modern fixtures, an array of amenities, flexible deals, concierge-level service, interaction with other companies in the workspace and convenience of the transaction process. Keep in mind, many of these users do not have full accounting departments or administration personnel. Often, the entrepreneur writing the code also is cutting the checks, and checks seem antiquated to these bright minds. Coworking platforms have long understood how to attract users and continued accommodating happy customers by accepting credit cards, removing complex language from their transactions and providing friendly faces to answer questions or show visitors to their destinations.

With these positive attributes, Denver's central business district will have an exciting opportunity to tweak the failed first-generation coworking models and lead the way toward downtown's rise in the next real estate cycle. With record high levels of sublease space in the market and coworking as downtown's largest tenant, the path to recovery for downtown office seems long and arduous. However, if we consider the successful aspects of the first-generation coworking model, we quickly see there is nothing stopping a traditional landlord from implementing these characteristics into their own properties. Collaboration between landlords, property managers and real estate agents could lead to the production of buildings that incorporate all of the positive characteristics that coworking operators would be sure to include, while eliminating the negatives of the first-generation coworking model. Additionally, this provides a means for landlords to further diversify their rent roll and strengthen the value of their asset. Yes, you take on the volatility of the rent roll specific to the coworking space, but when right-sized within the building's rent roll, that volatility starts to mimic an asset's market vacancy with upside.

Imagine if landlords pivoted to this second-generation coworking concept coming out of the global pandemic. As tenants abandoned leases, they quickly became fatigued by the work-from-home environment and currently are showing a desire to reenter the workplace. Utilizing a landlord agency operated coworking model could allow smaller tenants, as well as tenants relocating from other markets, to ease into the Denver office market through flexible deals in the adjusted coworking model. The landlord would then have better clarity concerning the coworking users in their building (previously a heavily guarded secret by coworking companies) and would be able to address their needs at the property more effectively. As these users grow and look to graduate from the coworking location and establish a private office location, the same landlord would have the opportunity to address those needs within their asset. This structure enables landlords to have stronger relationships with their customers, further diversify the size and term lengths on their rent roll, mitigate volatility, participate in the upside of successful coworking revenues and reduce turnover cost of small traditional office spaces. If properly executed, forward-thinking landlords could attempt to give coworking a second chance at life and gain the advantage over competitors who might be seeking to design-build or speculatively build small- to mid-sized traditional office spaces. ▲

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OFFICE — TRENDS

Embrace flexibility to build the office of the future

Design and construction trends always are evolving, sometimes more rapidly in specific sectors, which is what we are seeing with the office market now. Many offices along the Front Range still are experiencing reduced occupancy, anywhere from 30% to 50%, depending on the location. Given this reality, construction industry professionals need to evaluate and anticipate the workplace trends that will be in high demand, in both the short and long term.

While it's unclear how COVID-19-related changes to the office environment will develop over the next several years, we can be certain that offices will need to be able to adapt to serve future workers, whatever new or changing needs arise.

Flexible floor plans are a critical need, particularly now as employers work to accommodate changing density standards and distancing requirements. Similarly, cleaning systems – both for surfaces and the air – are being prioritized, all to keep offices clean and safe. The need for space that encourages collaboration and engagement remains high, although distancing guidelines are forcing designers to be creative and think outside the box to create more functional use than we've seen in the past.

We can't anticipate what the office market will look like once the pandemic is behind us, but we

Michael Brumley
Project executive, Kiewit Building Group Inc.

do know demand will be highest for offices that offer adaptable features with flexibility to evolve with the times. Construction industry professionals should prioritize these goals to build next-generation workspaces.

■ **Office features are changing with the times.** Kiewit currently is constructing a new regional complex for its Colorado-based staff in the city of Lone Tree. In the last year, several changes were made to ensure the campus includes offices equipped with the safety and design features required to support a healthy, efficient and thriving work environment.

Located in the master-planned community of RidgeGate, the project includes roughly 400,000 square feet of office space across two buildings along with a parking structure. Construction was well underway in 2020 when the industry saw an immediate reshuffling of priorities to accommodate safety features and density standards in the office environment as a result of the pandemic.

The adaptions made to Kiewit's regional headquarters are not unique; many, if not all, of our clients in the office market are prioritizing the same needs coming out of the pandemic, with similar demand for features that will help guarantee safe, flexible and collaborative workspaces.

John Hoffman, Kiewit Corp.

Office spaces can be reconfigured easily by using modular office wall systems like those pictured here inside Kiewit's regional headquarters in the city of Lone Tree.

■ **Trends in office features that will stick around following the pandemic.** With the sudden shift of density goals, open-space office concepts that provided high-density solutions might now fall short in supporting required distancing standards. Those in the construction industry are identifying ways to integrate suitable parameters of space that aim to keep employees safe, while still leveraging some of the benefits of the open office, like the potential for reconfiguration. This includes use of modular furniture and wall systems, and other semipermanent and flexible solutions to divide workspaces and configure high-, medium- and low-density environments depending on the need. Other COVID-19-related impacts to norms in how office spaces will be used – like increased telecommuting and heightened need for collaborative spaces – will emphasize the importance of flexible and adaptive floor plans.

Another important need is the cleanability and sterilization of

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Mothers' rooms make big impact in small spaces

Over the next 12-18 months, as workplaces transition back to in-person work from remote work, we will have the opportunity to rethink our workplaces. One thing that employers should consider is adding (or improving) mothers' rooms. Mothers' rooms – also referred to as nursing rooms or lactation rooms – are dedicated spaces in a workplace where breastfeeding employees can comfortably, conveniently and privately express breast milk while at work.

A 2019 survey conducted by the Society for Human Resource Management suggests that mothers' rooms are growing in popularity across the U.S., with nearly half of surveyed workplaces providing a mothers' room or similar space. This widespread recognition of working mothers in the U.S. workforce is a wonderful development! However, it does leave an estimated half of U.S. workplaces without any dedicated space for breastfeeding employees to express milk. Additionally, those numbers don't account for the quality of those spaces that employers have designated as a mothers' room.

As we approach this "reset" of office life, I encourage any employers who do not currently provide a mothers' room in their workspace to add one. Secondly, I encourage those employers who do provide mothers' rooms on site to investigate whether those rooms adequately serve the needs of their breastfeeding employees.

This second step is critical because I am certain that for many workplaces, "mothers' room" is

Kasia Bulkowski, AIA, NCARB, WELL AP
Architect, MOA Architecture

synonymous with "old storage closet that we cleaned out and added an armchair." (I am certain because this was my first mothers' room experience.) Why would an employer convert a storage room and consider this satisfactory? Part of the reason is due to how the law defines a mothers' room.

According to federal law, an employer must provide a "place, other than a bathroom, that is shielded from view and free from intrusion from co-workers and the public, which may be used by an employee to express breast milk." State law in Colorado expands on this, adding that an employer must make "reasonable efforts to provide a private space near the employee's work area for expressing breast milk, which cannot be a toilet stall."

Because this is law, the standard of care as an architect obliges me to inform my clients of this requirement when I am designing a work environment. Based on legal requirements, the most basic mothers' room offers privacy, is free from intrusion and provides seating, an elevated flat surface for equipment and an electrical outlet.

However, my approach as an architect always is to think beyond the basic requirements and consider the real needs of the building user. So, when working with a client in designing a new workplace,

MOA Architecture

A recently completed mothers' room in the Amy Davis Hospice Support Center

I nudge them to think beyond the basics and consider the ideal mothers' room. What do we add to the basic mothers' room to make it ideal? First, we add a food-prep sink for handwashing and washing pumping parts and bottles. This allows women to avoid any awkward kitchen moments with colleagues while washing up after pumping. Second, we add a small refrigerator for milk storage. Likewise, this means that breast milk stays out of the communal kitchen refrigerator. (Plus, this small refrigerator can be used by other employees for other temperature-sensitive items that likewise don't belong in the shared kitchen fridge.)

Then we take a close look at how the space provides privacy. For many women, the act of pumping breast milk requires visual and audible privacy and a relaxing setting, with the aim of reducing pumping anxiety. We can promote privacy by locating this space in an area of the office that is not highly trafficked, while still being accessible and convenient. Locking door hardware with an occupancy indicator allows women to feel safe from intrusion (and avoid the dreaded "door rattle"). Paying attention to lighting, finishes, artwork and other hardware (such as coat hooks) raises the quality of this space even further. The accompanying image offers a more complete overview of the systems, furniture, fixtures and equipment you would find in the ideal mothers' room.

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OFFICE — MARKET UPDATE

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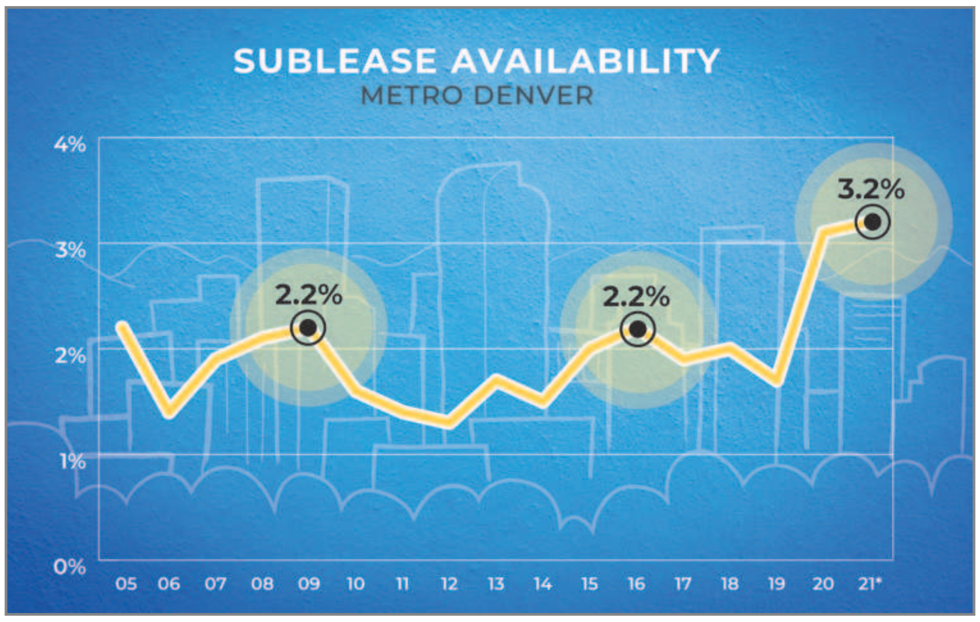
additional space added over the next year as the vacant shadow space transition impacts the market. Our firm defines shadow vacancy as a portion of leased space that the tenant is not using. While there is shadow space in most office markets, the volume has grown during the pandemic recession. Working from home has become the norm, and many tenants remain hesitant to return to an unsafe office environment. Shadow space is challenging to measure because it is not officially marketed or tracked in industry databases.

In order to understand the effect that shadow space will have on the market, it is important to focus on the major tenants in the market as they will have the most significant impact on the availability and move the needle substantially more. Major tenants like Newmont Mining, Checkr, Allstate and 2U already have taken steps to reevaluate their local footprint, offering an indication for the future of some of Denver's most significant contributors. Currently, the largest 5% of the downtown tenants make up 26% of the total leased space downtown, and in southeast Denver, the largest 5% of tenants account for



The sublease market in Denver from 2005-2021.

20% of the total leased space. Because shadow vacancy is scarcely tracked, sublease space often provides the best indication of the impact that shadow space will have on the future market. At current levels, a 5% reduction in space by major tenants would account for a 2.5% increase in the total availability rate downtown and a 2.7% increase in the southeast. A 10% reduction would result in 3.5% and 3.7% increases, respectively, and a 15% reduction would equate to a 4.7% increase in each markets.

The unquantifiable stock of shadow vacancy means that the market will experience less actual demand for space at least until occupancy restrictions are lifted, and likely lag growth for the foreseeable future. It is anticipated that sublease availability will increase through 2021 by way of a combination of bankruptcies and companies reassessing their space needs. We already have watched this trend come to fruition after notable companies like Ralph Lauren and Salesforce hit the front page of the news recently after they announced plans to decrease their corporate footprints, transitioning to flexible work schedules.

This being said, within crisis are the seeds of opportunity. Opportunities are abundantly available for growing office users to take advantage of discounted available space within their current buildings, and in some cases, sublease space may offer an opportunity for a user to try out a market before making a long-term commitment. Additionally, submarkets that previously posed a high barrier to entry now offer increased opportunity for new entrants to establish a presence. While the future of office space remains a bit of a blur, tenants focused on migrating to the Mile High City or maintaining a current footprint in Denver's real estate will find a discount that will pay dividends down the road. ▲

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Thiel

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naling the anticipated increase to full steam ahead for office investment as the first half of the year progresses.

Core investors favor single-tenant office assets with investment-grade tenancy on long-term leases, and they remain active in this space. The majority of noncore investors are focused on the highest-quality assets, with weighted average lease terms over six years in the most compelling submarkets. Expect many investors to maintain this defensive posture until the distribution of vaccines creates a point of herd immunity.

Select owners of transitional/unstabilized office buildings with some lease rollover risk are beginning to test the market. Fortunately, valuations are assisted by accretive debt options provided by debt funds that have reemerged and are quoting higher leverage and lower coupons than they have in the past nine months. Coupled with an anticipated flurry of leasing activity in the second half of 2021 from the reasons stated above, we are confident in Denver's resilience, particularly in the office market, during these disruptive times. ▲

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Smith

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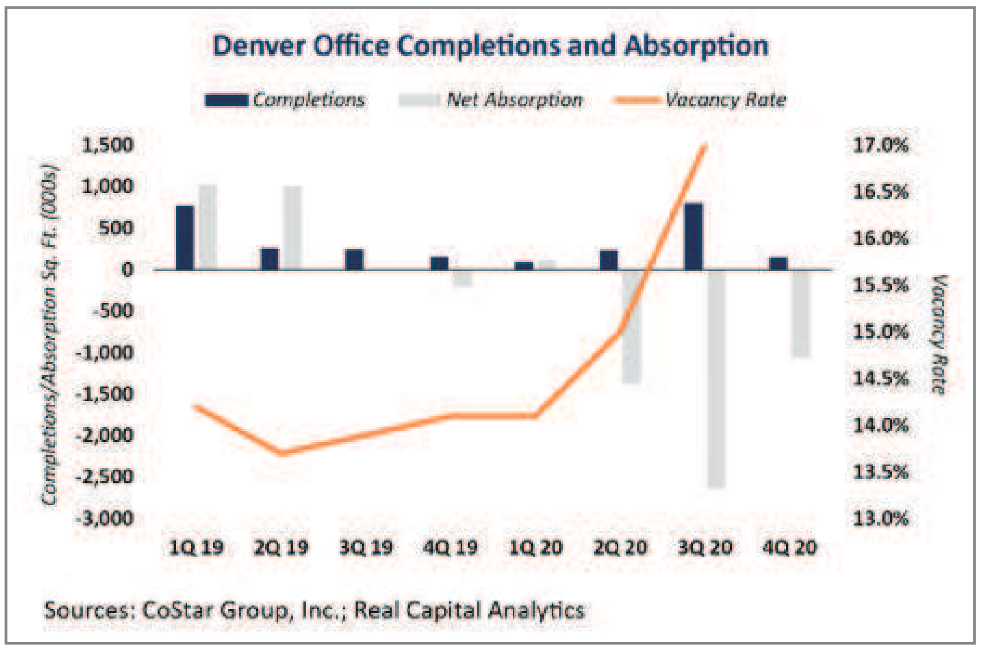

Sources: CoStar Group, Inc.; Real Capital Analytics

Amazon after it announced a greater commitment to Detroit, Denver, Phoenix and San Diego, which could act as a catalyst for other companies that are looking at expansions.

Suburban office is rivaling downtown office. A pullback in leasing pushed vacancy higher in central business districts and office space rates climbed in the suburbs. Suburban office construction has been more aligned with demand in recent years, maintaining stable performance and closing the vacancy gap with the urban core.

Large cities face an employer exodus. Primary markets are likely to face greater hurdles in the quarters ahead as companies reassess space needs and move to shore up financial reserves. More expensive markets like New York City, San Francisco and Seattle-Tacoma could take longer to recover, particularly with large tech companies giving their workers more freedom to work elsewhere. San Francisco could face more hurdles as the market has a higher share of startup firms that are unable to weather the crisis, resulting in available sublet space. Employers already were considering leaving larger markets due to high costs of living. The pandemic will strengthen this movement through its favoring of low-density, less expensive secondary markets.

Now, let's look at the Denver metro area specifically.

■ **Completions and absorption**. On a local level, supply additions will test demand in core submarkets. Office developments in downtown Denver and adjacent neighborhoods are positioned to place upward pressure on vacancy in the coming quarters. In fact, the central business district accounts for half of recently completed office space. Vacancy in the urban core has jumped, suggesting projects slated for delivery could struggle to secure tenants. Companies with provisional lease agreements also may pull out, similar to WeWork's passing on more than 200,000 sf.

■ **Price and cap rate trends.** Although office sales activity remains subdued, recent deal flow is promising. Suburban office properties have accounted for a high percentage of transaction volume.

- Average price per sf has increased to slightly over $212.
- Average cap rate fell slightly to 6.6%.
- Suburban Class B assets of less than 50,000 sf have upheld deal flow throughout the pandemic, while most of these transactions have closed for less than $200 per sf. ▲

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Roberts

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test how remote working may fit into the post-pandemic office philosophy."

At the very least, spec suites almost always are in a landlord's conversation when trying to reduce high vacancy in a distressed market, regardless of the cause. Yes, the pandemic is unprecedented, but landlord tactics essentially are the same in a correction cycle. So, the build-out of new spec product is not as risk adverse as other potential short-term investments may be. In any event, it looks like those risks are paying off.

"Numerous building owners rolled the dice and chose to proactively spend during the pandemic downtime to create high-end spec suites to attract new tenants and to retain existing occupants to their buildings," Rayburn said. "Those landlords now are showing a willingness to transact short-term deals of one to two years to land tenants who are likely to renew for a longer term within the first six to 18 months of their leases."

This is not a new idea. Landlords have employed spec suites as a highly successful office space model for at least a decade, and competition is fierce. Typically, landlords must compete for tenants in both existing and new buildings in the marketplace. And spec suites have served as a hedge against uncertain market conditions, but not a pandemic.

COVID-19 presents a whole other layer of challenges, and nobody can say when those will be diminished significantly. Additionally, construction prices are not coming down anytime soon. The construction industry has been dealing with manpower shortages and supply chain disruptions well before March 2020. Landlords can mitigate those types of risks by using economies of scale, when available, especially for long-lead items.

The win-win here is that spec suites are a nearly perfect match for smaller tenants not yet sure of their footing in this pandemic era. Landlords can offer spec suites as flexible, high-performing spaces to a wide range of potential tenants. For now, COVID-19 vaccines should inspire confidence in a market craving normalcy. And spec spaces can offer some measure of certainty in a fundamentally uncertain environment.▲

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Cullen

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The central business district has long driven office leasing activity in metro Denver, but since the pandemic set in, the area has struggled the most out of any submarket. That likely will improve as 2021 goes on. The Denver Tech Center also is picking up steam, along with the western part of the metro area. Micromarkets like Lower Downtown and River North are outperforming the CBD while Cherry Creek stood up to the pandemic's challenges better than nearly any other part of the market, likely thanks to a high concentration of well-capitalized financial companies with office space in that submarket.

As the vaccine rollout continues, driving the virus back and helping stir the economy back to life, now is the time for companies to reconsider the plans they shelved or reevaluate their decisions to pull back on office space. As the year goes on, we're likely to see leasing activity in the metro area increase even more, which will make it more difficult to find the same kinds of opportunities that are available now. ▲

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Brumley

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interior environments. From desktop surfaces to conference rooms to air filtration, technology-driven solutions and creative design are raising the bar on safety. Office workspaces are incorporating simple changes, such as increasing the efficiency of air filters (MERV rating) in heating and cooling systems to provide cleaner work environments. In addition, construction industry professionals also are looking to new technologies, such as needlepoint ionization, that can help neutralize pathogens and limit the spread of germs.

We'll also see an effort to reduce physical touch points within the workspace. Previously optional improvements – like touch-free sinks – are becoming the standard. Other touch points are being reduced by technology enhancements. For example, the prevalence of automatic doors and key cards for access throughout the office, and the integration of nonporous, antimicrobial materials like copper into the design are all helping to keep offices as clean and sanitized as possible.

While there are a number of interior trends to focus on, we also need to look outside the building to ensure the office's exterior environment is adding value for workers. In places like Colorado that typically experience an abundance of sunny days, there is tremendous opportunity to rethink and more fully leverage outdoor space. This includes the incorporation of outdoor seating, covered patios and extended balcony spaces that can be used as active workspace, accommodating meetings and providing employers with functional options to bring their work outside. Building technology and low-voltage systems also are being extended to these outdoor workspaces to help maintain connectivity and efficiency.

As construction industry professionals, we can look forward to seeing the demand for office space come back strong as we move out of the pandemic. It's a great time to take a step back and think critically to anticipate the needs from office users of the future to ensure the construction industry is poised to deliver when demand bounces back.▲

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Bulkowski

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Finally, the ideal mothers' room is a space supported by internal policies and practices. Any lactating mothers, who can expect to use it two to three times per day for a duration of approximately 25 minutes at each use, should be able to reserve the room. Office policy must prioritize the use of the room for lactation, while recognizing that when it's not utilized by nursing mothers, the room can serve other wellness purposes for all employees – changing clothes, taking private calls, meditating or even just having a quiet moment.

Depending on an organization's size, an employer may want to provide multiple rooms throughout the building. Property managers should consider a mothers' room as a building amenity, not unlike public restrooms. For larger buildings, property managers could even consider consolidating individual mothers' rooms into larger mothers' suites. These spaces might offer privacy with individual seating spaces with occupancy indicators and incorporate calming music. Such space can double as a nursing suite in case building users or visitors need a private space to attend to their child's needs. A restroom with a changing table within the suite or nearby would be encouraged.

The trends in mothers' rooms are positive, but there is a lot more that we can do as architects, designers, building owners and employers to ensure that we are valuing the contributions of working women in our organizations. Let's celebrate the great progress we have made, but keep an eye on the bigger picture. Let's aim to make mothers' rooms a part of every workplace program. ▲

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INDUSTRIAL PROPERTIES

2020: A tale of diverging markets in Northern Colorado

The High Country Beverage building in Johnstown at 2534 is being expanded to help meet growing demand.

Last year was a struggle for most people, either physically, financially, psychologically or some combination of all three. Vaccines are being rolled out nationwide, however slowly. 2021 should deliver a gradual return to normal but, according to our new president, not until Christmas. So, 2021 still will be challenging for individuals and their families and businesses. (At least we are not in Texas!)

In this article I will detail how the industrial and office markets performed in Larimer and Weld counties in 2020.

The industrial market in Larimer

Joe Palieri, CCIM
Senior adviser, NAI Affinity

County was very strong. Vacancy rates increased but still average only 4.4%. Lease rates grew another 2.5% to $10.18. That lease rate is skewed by larger leases at lower rates. If you are looking to lease industrial space under 20,000 square feet, it is difficult to find a base lease rate below $12-plus triple net. Almost 400,000 sf of new construction was delivered to the market in 2020. Larimer County had only 63,000 sf of negative net absorption, which is an impressive number given the almost complete economic shutdown from mid-March through the end of May and all the new construction. New construction will be just as strong in 2021 and demand does not seem to be slowing.

Larimer County industrial sales set a record of $160 million for approximately 2 million sf of improved property for the year. The average sale price for Larimer County reported by CoStar was $83 per sf. Three notable sales occurred that were significant and skewed the average sale price dramatically.

Building 4 at Centerra Industrial Park in Loveland was completed in 2018. It consists of 122,807 sf and was leased to Amazon on a 10-year contract in 2020. It sold to an investor for over $32.6 million ($266 per sf.)

Two other sales were on the opposite end of the spectrum: 815 14th St. SW in Loveland, the former Agilent Campus, now referred to as Rocky Mountain Center for Innovative Technology, and 3800 N. Wilson Ave., the Woodward Governor Loveland Campus. Woodward was purchased by Martin Lind's Water Valley devel-

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INSIDE

INDUSTRIAL — MARKET UPDATE

E-commerce boom shows no sign of slowing

Paul Kluck, SIOR
First vice president, Industrial & Logistics, Advisory & Transaction Services, CBRE

Overall, 2020 marked a record year for the U.S. industrial market due in large part to the increased e-commerce activity driven by COVID-19. Here in Denver, the industrial market emerged from 2020 resilient and healthy with strong deliveries, positive net absorption and a construction pipeline that again reached new highs. Confidence remains high as the market continued its streak of positive net absorption for the 43rd consecutive quarter.

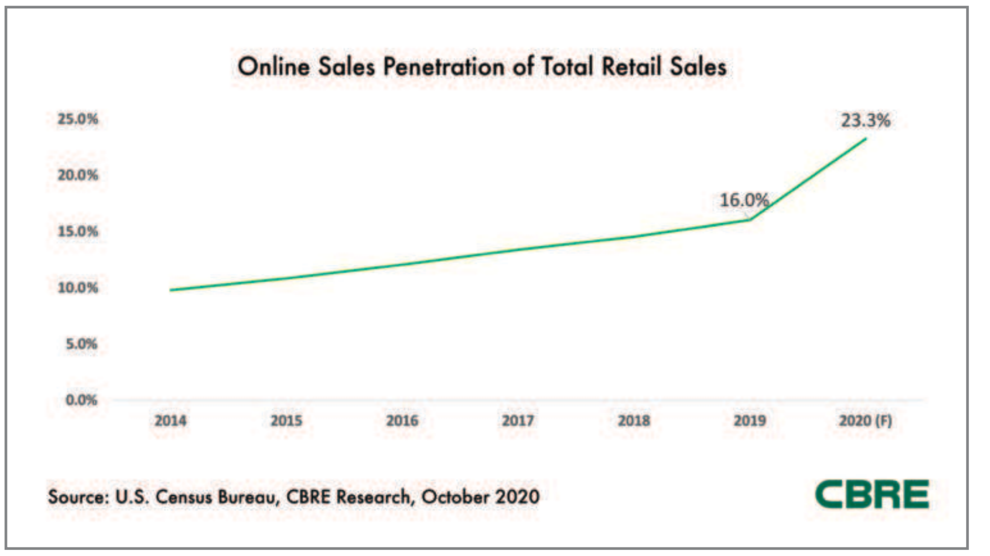
■ **Looking back at 2020.** The Denver industrial market reached record-high development with over 4 million square feet delivered in 2020 and construction activity rising to 8.2 million sf – the highest in over 20 years. Of the total volume of projects underway, 4.2 million sf (51.9%) is planned for speculative space, and 3.9 million sf (48.1%) is preleased. Notable projects underway include the 1 million-sf Lowes build-to-suit and the speculative 594,000-sf Stafford Logistics Center Building 1, both located in Denver's airport submarket.

Annual absorption activity reached nearly 3.4 million sf, a 14.9% increase year over year, in line with the 22% increase in quarterly net absorption. Overall annual sales volume increased 7.4% from 2019 to nearly $1.6 billion. The overall average price per sf remained stable year over year at $130 per sf.

Unsurprisingly, leasing activity was dominated by e-commerce users. In addition to the Lowes e-commerce distribution center, another well-known e-commerce company leased almost 1.5 million sf in Denver in 2020, and is building another 1 million sf at the Stafford Logistics Center and 3.6 million sf in Colorado Springs.

■ **Looking ahead in 2021.** Industrial became the most in-demand commercial property sector in the nation as e-commerce sales increased by over 40% due to COVID-19 restrictions. At a national level, demand for industrial buildings was strongest among mega-distribution facilities of 1 million sf or more, which was reflected in the average size of the nation's top 100 industrial deals in 2020, which topped more than a million sf. This is a significant jump over 2019's average of 887,594 sf. Across the country, there were 48 leases of 1 million sf or larger, a significant increase from the 29 leases of this size in 2019. E-commerce occupiers, companies that exclusively ship directly to consumers, led the country with 35 transactions totaling 37.3 million sf – nearly double the 18 signed in 2019.

Nationally, e-commerce will be a demand driver for the foreseeable future, along with the need to hold additional inventory onshore (known as "safety stock") to avoid supply disruptions like we saw as a result of the pandemic's disruptions in early 2020. As a result, even as life returns to normal, average transaction size likely will continue to increase in 2021.



But the good news for industrial will extend to Denver as well and the picture looks equally rosy due to several key factors:

• New construction – There seems to be no constraint to supply as over 10 million sf of spec construction is planned and will break ground as existing projects get absorbed.

• Resulting vacancy – Vacancy in the big-box distribution market will continue to climb because of these deliveries, but e-commerce demand is likely to continue to drive absorption.

• Lease rates – National and regional distributors will be required to be in Denver and will pay the going rate, driving lease rates up.

• Investment sales – Cap rates in gateway markets have dropped to undesirable levels. Every institution sees Denver as an opportunity to chase yield. This demand will lead to additional cap rate compression and increased sales prices.

When the pandemic began, there was endless speculation about how commercial real estate would be impacted, but as the situation began to become clear, the demand for e-commerce became an unrelenting driver for the industrial sector, a trend that shows no signs of stopping. While we can never be sure what the future holds, it's a safe bet that Denver's industrial market will continue to grow stronger in 2021 and, quite possibly, for much longer.▲

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INDUSTRIAL — MARKET UPDATE

Market fundamentals show industrial's strength

Simply put, the COVID-19 pandemic defined 2020. From business decisions to everyday life, the regulations and shutdowns that surround it have impacted our every action and will continue to do so for the foreseeable future. In 2020, Denver's red-hot real estate market stalled as tenants grew wary of the future, put real estate decisions on hold and even watched their businesses fail. But as office and retail product types have struggled, demand for industrial product has remained steady and, despite midyear pandemic-related hiccups, it ended the year strong. In this article, we will look at industrial metrics compared to other major commercial real estate product types and what they could mean for the future.

Vacancy in industrial product rose 50 basis points over the course of 2020, closing the year at 6.3% on an overall basis. This rise in vacancy was due to the delivery of new product as more than 4.4 million square feet delivered over the course of 2020.

Vacancy in office product rose 320 basis points over the course of 2020, closing the year at 17.7% on an overall basis. Contrary to industrial product, this increase was due primarily to the pandemic as sublease space increased by 91.9% over the course of 2020, closing the year with more than 3 million sf of sublease space vacant across the metro area, a figure that does not include anticipated additional shadow space. Only 1 million sf of new office product delivered during 2020, representing the lowest amount since the Great Recession. Retail product, as tracked by our firm, recorded similar rises in vacancy as community neighborhood strip product increased 160 basis points over the course of 2020 despite just 101,000 sf delivering across the metro area.

Tim Morris
Senior industrial research analyst, Cushman & Wakefield

Overall net absorption figures put this comparison in even starker contrast; over the course of 2020, industrial product recorded over 3 million sf of positive absorption while office product recorded negative 3.2 million sf and retail product recorded just shy of negative 1 million sf.

Comparing leasing activity across product types demonstrates similar results. Leasing activity across all industrial product types netted over 9.3 million sf. While activity stumbled in the second quarter, the market quickly recovered and a strong second half of 2020 brought activity near the 9.5 million-sf average of the prior five years. Leasing in office product recorded just over 5.8 million sf of activity during 2020, compared with a 9 million sf annual average over the prior five years. Retail product recorded a similar drop-off in activity as 1.9 million sf leased over the course of 2020 compared with a 2.8 million-sf average over the prior five years. Office users reassessed who needed to be in the office versus who could work from home and retail tenants were forced at first to close, then to overhaul how they served their customers. Industrial users, on the other hand, found that distribution requirements held steady and even grew as e-commerce surged during the pandemic. While it is impossible to predict the future for office and retail tenants, it is clear that, despite new hurdles, industrial users will continue to require space as Denver's population continues to grow.

Michael Coppola
Associate market director, Cushman & Wakefield

"We're keeping a close eye on new construction supply," said Cushman & Wakefield's Drew McManus, "but with the continued growth of demographics in Denver along with good market activity, the fundamentals of our market continue to remain sound and Denver's industrial market is set for another strong year."

These fluctuations in demand were reflected in the development pipeline as well. Roughly 1 million sf of office product delivered during 2020, compared with a 1.8 million-sf average over the prior five years, while just over 1.4 million sf of office product remained under construction across the metro area. Just over 101,000 sf of retail product, as tracked by Cushman, delivered during 2020, compared with a five-year annual average of 430,000 sf, while just 119,000 sf remained under construction at the end of the year. Industrial product delivered over 4.4 million sf over the course of 2020, nearly matching the 4.6 million-sf average of the prior five years, while a massive 7.7 million sf remains under construction across the metro today. The development pipeline should continue to skew toward industrial product for the foreseeable future as demand has held steady while there remains substantial uncertainty surrounding retail and office product.

"We are seeing a lot of industrial requirements in other major cities across the country that haven't shown up in Denver yet and are confident that similar requirements from these companies will be coming to Denver in the next six to 18 months," said Cushman's Tyler Smith.

So what does all this mean for investors? Investment activity in industrial product recorded a strong year in 2020 as over $1.7 billion in product changed hands, compared with a $1.3 billion annual average over the prior five years. Office investment activity recorded a more robust $1.9 billion in sales volume during 2020, but this figure represented a decrease from the $2.7 billion annual average for the prior five years. Retail investment similarly dropped off, recording $909.6 million in sales, compared with a $1.2 billion average over the prior five years.

"We expect a continued acceleration of investment sales activity for industrial product," said Cushman's Will Strong. "As the market continues to perform and leasing activity remains strong, more and more investors will start to sell their assets, many of which will hit new records on a cap rate and price-per-square-foot basis. The secondary markets have recovered faster and stronger than the primaries/gateways and records seem to be set every time we look up." ▲

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INDUSTRIAL — TRENDS

Multiuse logistics assets become investor darling

Peter Kroner
Manager, national industrial capital markets research, JLL

Industrial real estate had the second-best year on record in 2020 with transaction volume nearing $96 billion in the United States, and 2021 is off to a positive start. As competition among investors for industrial product stays strong, our capital markets research isolated one subclass that is gaining investor interest: multiuse logistics.

The profile for multiuse logistics assets includes those older 20,000- to 100,000-square-foot multitenant buildings that have a solid footprint within infill urban logistics markets across the U.S. These assets can contain a mix of distribution, flex showroom, industrial showroom, research-and-development, warehouse and/or manufacturing space and often have a diversified, local tenant base.

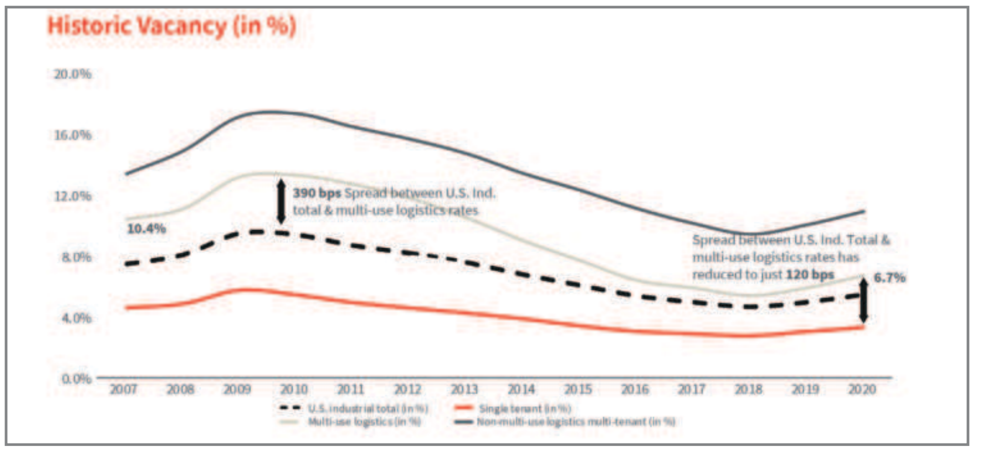
Multiuse logistics assets boast compelling rent growth profiles and a strong long-term outlook. With new yield-focused investors jumping into the industrial space, multiuse logistics product is desirable as an alternative to the bulk industrial market, which is getting tighter.

Given multiuse logistics assets often are older properties, they witnessed population centers growing around them, making them not only almost impossible to replace but also highly sought after as last-mile logistics locations close to end users. Compounded by industry fundamentals driven by macroeconomic factors such as reshoring and acceleration of e-commerce adoption, the increased demand for these smaller, multitenant industrial assets has dropped vacancy rates nationwide significantly, now holding at under 9%.

An example of this property type recently trading in Colorado was the $16 million sale of Commerce Square, a 44,464-sf light-industrial facility leased to 13 diverse tenants within suites ranging from 4,000 to 14,000 sf in Aurora. From a logistics perspective, the property allows tenants to occupy space in Denver's primary logistics submarket typically known for bulk distribution, and its proximity to the entire Front Range and the region's major highways – Interstates 225 and 70 and E-470 – makes it a short drive to major population centers in and around Denver.

We believe this subclass has an enormous potential upside on rent growth, which is driven by low vacancy and limited new supply. Multiuse logistics rent has grown more than 54% since 2010 and nearly 21% since 2017, outpacing the national average for the broader industrial market.

Based on the historical five-year compounded annual growth rate, our firm anticipates a nationwide 4.6% rent growth for triple-net-leased multiuse logistics between 2021 and 2024, compared with 3.8% for all U.S. multitenant industrial and 3.7% for the entire property sector. Yet, this subclass accounts for only 15% of overall industrial product inventory. For trades in 2020 of over $5 million, these properties accounted for only 1,973 transactions at $128 per sf with an average cap rate of 6.62% (down from the five-year average of 6.72%), demonstrating their value.



JLL

The need for proximity to population hubs around the country has contributed to tenant activity in the multiuse logistics space, driving vacancy for these assets to their lowest recorded levels.

For the Denver industrial market, the subclass accounts for 22% of the 223 million sf of industrial inventory. This current multiuse logistics inventory of 49.25 million sf has a low vacancy of 6.6%, which is down significantly from the 12% it was in 2010, demonstrating the growth in tenant demand for this space.

Adding to the advantages are a limited supply and lack of new construction. Construction activity for multiuse logistics properties is hovering between 0.1% and 0.3% of existing inventory this cycle, which is significantly below the national average of 1.6%. The Denver market, for example, has only 207,250 sf under construction, which is 2.5% of the total industrial square footage under construction in the market.

With little new product entering the market and increasing pressure from rising land values to redevelop for other uses, tenants have very limited options outside their current space – helping constrain vacancy not just in Denver but nationwide.

This is also an asset subclass that, at 55%, is primarily owned by local or regional noninstitutional investors, providing a unique opportunity to build a footprint from a large, decentralized set of owners. Given the highly fragmented ownership within the subclass, it's challenging for investors to amass scale.

Partnership with proven and trustworthy owner-operator platforms that have consistently executed on transactions within the multiuse logistics asset class is vital for investors looking to gain exposure within this subclass; however, these partnerships are increasingly being offered at premiums, as consolidation of ownership within the multiuse logistics space is trending upward within high-growth markets. ▲

INDUSTRIAL — MARKET OUTLOOK

What's next in the industrial development dance?

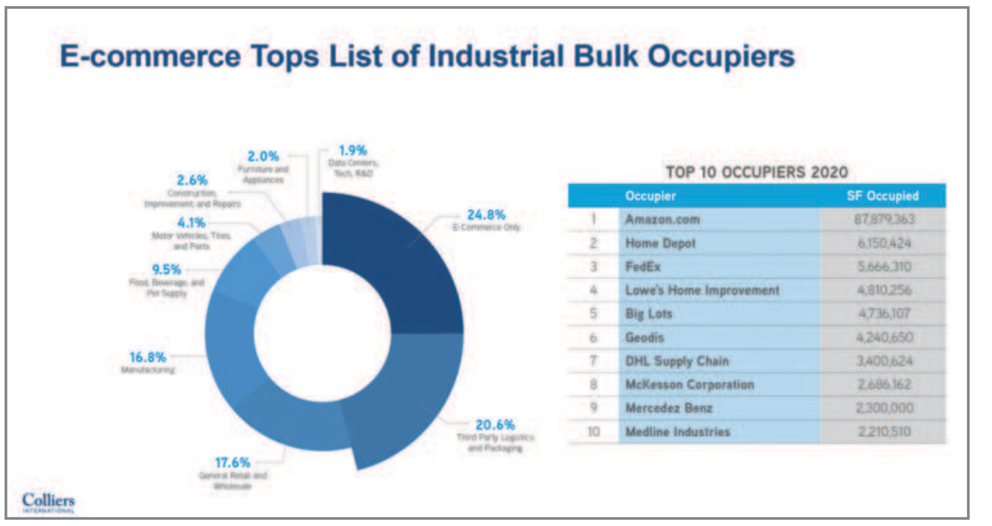
If you have had the opportunity to attend a Denver industrial panel by video or in person the past few years, I would be surprised if you haven't heard an industry veteran mention, "Industrial is now the preferred asset class" or "Industrial is now the prettiest girl at prom." But for those of us who started our careers post-2008 and are shocked when a package can't arrive in two days, industrial's attractiveness always has been our normal. What is shifting are the key industrial players. A quick glance at the top industrial users in the country by leased space in 2020 reads Amazon (87.9 million square feet), Home Depot (6.2 million sf), FedEx (5.7 million sf), Lowe's Home Improvement (4.8 million sf) and Big Lots! (4.7 million sf). Yes, you read that correctly: Amazon absorbed over 14 times more space than the second-most aggressive tenant last year. Due to that rapid pace, "e-commerce-only" users now represent 24.8% of the national industrial market.

With this intense demand led by Amazon and an apparent rumor it will not seek as much space in 2021, it is fair to ask, "Will this dance continue or is Denver approaching a precarious amount of oversupply?" It is no secret that Denver currently is eclipsing over 8.4 million sf of product under construction, which is an all-time high. As a user, you are spoiled for choice with high-quality speculative industrial developments in every major submarket and typically several projects to evaluate in each of these locations.

Nick Rice
Broker associate, Colliers International

The central market, considered by many to be the most active, has four institutional-quality projects with buildings under construction and several more in the pipeline. Despite the Interstate 70 construction project presenting logistical concerns, the airport submarket has no shortage of "big bombers" (buildings over 500,000 sf) planned and in the construction phase. In contrast, west Denver is experiencing new spec development in a land-constrained market, with two well-planned projects that already have experienced leasing success. A once secondary submarket, the southeast has seen an influx of institutional investment resulting in more product currently under construction than ever before. The northwest is buoyed by the Colorado Technology Center, achieving some of the highest rents in Colorado, with many Broomfield sites looking to capitalize on this momentum as well.

Each submarket is experiencing a full pipeline of activity; however, many comparable metro areas have more construction as a percentage of existing supply. Memphis, Tennessee, is a 260 million-sf market with 14.8 million sf under construction (5.69%); Columbus, Ohio, has 256 million sf total and an additional 9.2 million sf under construction



	Occupier	SF Occupied
1	Amazon.com	87,879,363
2	Home Depot	6,150,424
3	FedEx	5,666,310
4	Lowe's Home Improvement	4,810,256
5	Big Lots	4,736,107
6	Geodis	4,240,650
7	DHL Supply Chain	3,400,624
8	McKesson Corporation	2,686,162
9	Mercedez Benz	2,300,000
10	Medline Industries	2,210,510

The top industrial users in the country by leased space in 2020

(3.62%); Phoenix represents 312 million sf total with another 9.2 million sf under construction (3%); and Salt Lake City has a staggering 9 million sf under construction to add to its 144 million total sf (5.6%). With these other metro areas in mind, it is hard to say the addition of Denver's 8.4 million sf to the 255 million-sf market (3.3%) is considered oversupplied.

In our analysis, Denver is taking a measured and more disciplined approach when it comes to development projects. Also, it must be taken into consideration that of the aforementioned 8.4 million sf under construction, 3.4 million sf of that is represented by build-to-suit projects for large users such as Lowe's, Shamrock Foods and Amazon that will absorb the buildings upon delivery. With each new project taking place, it is one less developable industrial site on the map and the underwriting becomes more scrutinized. Many developers have taken on extremely daunting challenges by remediating former smelter plants, filling in lakes and boring under rail lines to bring their visions to fruition. With tenants having the power of choice, the building design, site plan and offering modern features become extremely important. Speed to market can make or break a potential lease and construction costs are increasing rapidly.

In light of the many risks described above, there is insatiable capital demand seeking a position here, which has proven to make Denver an extremely hard market to plant a flag. When considering the

Please see Rice, Page 30

Industrial Properties Quarterly - Financing Sources Matrix

TYPE OF CAPITAL	SOURCE OF CAPITAL	EXPLANATION	RATES/SPREADS	LTV/COVERAGE	TERM	AMORTIZATION	FOCUS	TRENDS
LIFE INSURANCE COMPANY	• Insurance premiums • Annuity and GIC sales	• Non-Recourse • Longer-term fixed rate loan	2.25%-3.25%	• Up to 65% LTV • 1.35x Minimum DCR	5-30 Years	20-30 Years	• Established industrial corridors or properties with superior access, last-mile product very popular • Vintage and new product, will compete aggressively for new construction • Single-tenant with long-term lease (credit preferred) or multi-tenant with staggered rollover • Major metro areas & secondary markets (being more selective on secondary markets)	• Industrial is seen as one of the most attractive asset classes for insurance companies given the current risk environment associated with office, retail, and hospitality assets • Competing on value-light lease up deals with floating rate programs and hybrid bridge programs • Newly constructed or well-maintained product is in high demand with additional interest for construction financing from select life companies • Full-term interest only to be considered for 50% - 55% with strong sponsors • Sensitivity around loan basis on older product, especially at higher leverage • Lender sensitivity to deals with a large cash-out component, especially for newly constructed assets • Properties with CBD or marijuana tenants are still challenging, despite the continued changes in legislation
CONDUIT (CMBS)	• Sales of mortgage-backed securities through public markets	• Non-Recourse • Longer-term fixed rate loan	2.75%-4.00%	• Up to 70% LTV • 1.25x Minimum DCR • 8.0% Minimum Debt Yield	5, 7, & 10 Years	25-30 Years	• Secondary/Tertiary Markets • Large transactions or portfolios that are tough for other lenders to pursue alone	• Strong B-piece buyer demand for stabilized industrial • Leasing capital reserves or cash management incorporated for large rollover events • Will consider full-term I/O on select deals at LTVs less than 60% • Can be more competitive on larger one-off deals or portfolios that may be too large for other lending sources
BANK	• Corporate Debt • Deposits	• Recourse (non-recourse becoming more available on case-by-case basis) • Shorter-term fixed and floating rate loans	3.00% - 4.00%	• Up to 65% LTV • 1.30x Minimum DCR	Up to 10 Years Fixed, Typical Max Term is 5-7 Years	25-30 Years	• All industrial assets • Value-add with guaranties • Secondary/Tertiary Markets	• Very strong appetite for construction or re-position on assets with strong sponsor and good location • Most competitive for sponsors with established banking relationships and strong borrower history that are willing to accept recourse • Establishing a deposit relationship is becoming a requirement • Primarily recourse loans, with non-recourse becoming more available to strong sponsors at lower leverage • More flexible (open) prepayment terms
DEBT FUND / BRIDGE LOAN	• Private Capital • Institutional Capital	• Non-Recourse • Shorter term bridge loans for acquisition and/or repositioning	L+275-450 bps spreads	• Up to 75% LTC • Going-in 1.0x DCR	1-5 Years (3+1+1)	Interest Only	• Value-Add Transactions • Recapitalizations • New construction	• Most lenders have a LIBOR floor of 25 or 50 bps • Competing on ground up construction at higher leverage than banks are considering • Pricing depends on leverage level, property quality, and Sponsor strength • Needs to have strong business plan and attractive location
MEZZANINE/ PREFERRED EQUITY	• Private Capital • Institutional Capital	• Junior financing secured by a pledge of, or participation in ownership interest	Mezzanine 8%-12%	• Up to 85% LTC • 1.10x DCR	2-10 Years	Interest Only (in most cases)	• All industrial assets • Value-Add Transactions • Recapitalizations	• Preferred equity offers higher funding than mezzanine, but at a higher cost • Minimum investment is typically $5MM but can start as low as $1MM when paired with senior position

DCR - Debt Coverage Ratio
DUS - Delegated Underwriter Servicer

LTV - Loan to Value Ratio
LTC - Loan to Cost Ratio

LIBOR - London Interbank Offered Rate
REIT - Real Estate Investment Trust

This information is intended to illustrate some of the lending options currently available. Other options may exist. While Essex Financial Group strives to present this information as accurately as possible, no guarantee is made as to the accuracy of the data presented, or the availability of the terms at time of application. Rates and terms are subject to change. Please contact one of our mortgage bankers for up to date rate and term information.

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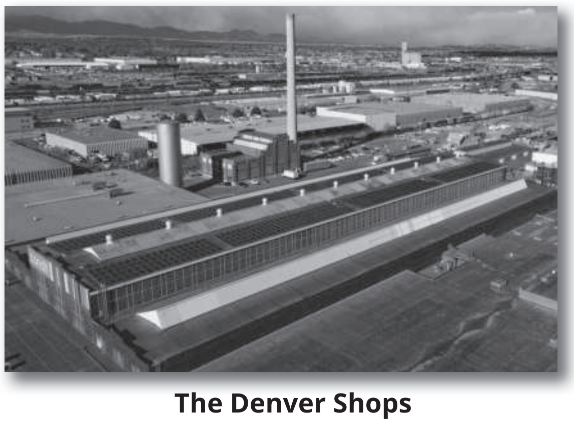
Essex Financial Group - Recent Industrial Transactions



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Life Insurance Company

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INDUSTRIAL — LEASING

Streamline leasing to keep up with market realities

Kyle Waldrep
Founder and CEO, Dottid

The pandemic has had dramatically opposite effects on the office and industrial markets in Colorado and throughout the U.S. Office markets such as Denver are seeing vacancy rates rise to the highest levels in a decade as office-occupying industries suffered significant employment losses due to COVID-19 throughout 2020.

Industrial markets, on the other hand, which prepandemic already were seeing an upsurge due to steady growth in online sales, have seen that growth accelerated as the work-from-home model has been fully embraced. Denver saw over a million square feet of new industrial properties introduced in the last quarter of 2020, with another 8.2 million sf in the pipeline set to meet growing demand.

The Denver office vacancy rate hit 15.6% at the end of the year, the highest level since the end of 2011, according to CBRE research. An estimated 2.2 million sf of sublease space hit the market since the pandemic began, an 86.1% increase.

Meanwhile, the industrial market saw more than 3.4 million sf of warehouse, manufacturing and other industrial space absorbed by new tenants in 2020, a 14.9% increase over 2019, according to CBRE.

In the office market, companies are embracing a distributed real estate model, pushing against the rising cost of real estate leasing and ownership by combining work from home with smaller, satellite offices in suburban locations and downsizing to token offices in major metropolitan centers to reduce costs. Others are taking advantage of rising vacancies to upgrade their offices in a strategic flight to quality.

On the industrial side, new space is being snapped up faster than it can be built, and online retailers are constantly on the lookout for last-mile warehouse and distribution facilities in urban locations to meet demand, both on a long- and short-term basis.

While telecommuting may not be a viable option for all industries or even all employees within a company, many organizations have utilized remote work models with great success, reducing the amount of office space needed and changing what constitutes an ideal location. However, location will remain a key factor for sectors that rely on talent, transportation and ease of access to other companies.

What this means across both the office and industrial sectors is that deals are happening faster than ever, and owners, asset managers and brokers have had to find new ways to adapt the property search, evaluation and lease consummation processes to accommodate this new way of doing business.

Technology continues to be a catalyst for change in all areas of business and industry, and the real estate market – which has long been resistant to incorporating new tech – is no exception. It has become clear during the past 12 months that it is time for the commercial real estate industry to catch up with the innovation office and industrial property tenants use.

While there has been some development of technologies out there aimed at operational aspects of real estate, very little has changed in the industry when it comes to the deal-making aspect of the business. Owners, asset managers and brokers often are challenged by the antiquated and inefficient processes used in modern leasing transactions that are mired in administrative tasks that could be easily solved with the right technology. With the velocity of deals in commercial real estate today, there is no time to waste.

New commercial real estate technology platforms created in partnership with industry experts focus on providing a single location for brokers, landlords and tenants to share information, work seamlessly throughout the leasing process and, ultimately, close deals faster and with greater efficiency.

The U.S. and the world are experiencing a new and rapidly evolving model of how business is done, and office, industrial and retail markets are adjusting to this new business environment. The pandemic and resulting historic economic shutdowns have had a dramatic impact on the commercial real estate world.

The enduring industrial boom is a stark contrast to the sudden office market crash. CRBE's research shows that 1.1 million sf of new or existing office space hit the Denver market last year that was not taken on by tenants. This is the first time in a decade that the city's office market experienced negative absorption. Office-using employers shed more than 8,400 jobs in Denver compared with the same period in 2019, according to CBRE. That doesn't account for people working from home and not using their office space. In contrast, the industrial side added 1,800 jobs in Denver through the same period.

We expect these trends to continue. On the office side, with additional sublease inventory hitting the market and a plethora of new, unused space, we expect companies that have paused renewal and relocation plans over the past year to start making decisions quickly in either a flight to quality or move to a more hub-and-spoke approach to leasing. The industrial sector is expected to continue to grow unabated as work from home and reducing higher-priced downtown office space become a bigger part of employer strategies. ▲

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INDUSTRIAL — MARKET UPDATE

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opment company.

The RMCIT property, a four-building complex consisting of a total of 811,757 sf, sold for $15.5 million, or $19.09 per sf. The Woodward building consists of 209,000 sf and sold for $4.2 million, or $20.22 per sf.

By removing these three transactions from the calculations, the average sale price of industrial sales in 2020 becomes $137.28 per sf, which is much more reflective of the actual market. This average price reflects core-and-shell delivery with minimal finish.

The industrial market in Weld County slowed a bit but still is strong and growing again. The vacancy rate of 4.65% grew from 2.5% but is still very good. Lease rates are at an all-time high of $10.54 per sf. Almost 526,000 sf of new construction was delivered to the market in 2020. By contrast over 734,000 sf was delivered in 2019. Most of the starts were in the second quarter. Construction activity slowed dramatically in the third and fourth quarters. That slowing trend has turned around as 559,000 sf are now under construction. Weld had only 52,600 sf of negative absorption in 2020. Industrial sales volume was $102 million at an average price of $115 per sf.

Weld County may see an increase in demand for industrial space as oil prices rebound after the disruption to the supply due to the disaster in Texas caused by the cold snap in February. According to CoStar, over one-third of Colorado's oil and gas wells are in Weld County. As of this writing, West Texas Intermediate Crude was at $61.03 per barrel. A year ago, pre-pandemic, it traded at $53.88 before dropping to a low of -$37.63 (yes, negative) on April 20, 2020.

To summarize, Larimer and Weld industrial markets are very similar in activity. The pace of new construction in Weld County decreased in mid-2020 but has picked back up. Lease rates are historically high and vacancy rates are low in both markets. Larimer County prices tend to be 10% to 15% higher than those in Weld County.

The office markets began to see struggles as the effects of the COVID-19 pandemic took hold. Most businesses that are able to do so have minimized office staff. Companies have transitioned to a work-from-home environment using Zoom or other online products to hold meetings. That trend is expected to continue for a while, but employers and employees are beginning to miss the social aspect of seeing and collaborating with colleagues.

Trade @ 2534 is a three-building, 280,000-square-foot project in the 2534 development in Johnstown.

The office market in Larimer County was hit hard by the pandemic. Vacancy rates have increased to 7.9%, almost double from a year ago. Lease rates are down less than 1% to $23.09, but I expect more downward pressure as the year progresses. Only 89,000 sf of new construction was delivered to the market in 2020. CoStar is reporting 381,000 sf of negative net absorption.

The office market in Weld County mirrors Larimer County. Vacancy rates increased to 5.6%, double from a year ago. Lease rates are down less than 1% to $19.63 per sf. Only 25,000 sf of new construction was delivered to the market in 2020 and none is under construction. CoStar is reporting 131,000 sf of negative net absorption over the last 12 months.

So, office bad, industrial good. Analytics are moving in the wrong direction for office. While things are bad now, we have not completely fallen off a cliff as we did in 2009. If the vaccine is effective and life returns to a semblance of normal, we should recover nicely. Northern Colorado still is one of the most desirable places to live in the country. ▲

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Rice

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pro forma, this capital is attracted to the intense cap rate compression in recent sales that can make any deal look a little more attainable. With the newest Class A sales approaching 4% cap rates, the yield on cost spread for these deals is too attractive to ignore and even a less expertly executed project can be a home run on the disposition.

For those considering this market, population growth has driven the conversation, as over 50,000 people have moved to Colorado between July 1, 2019, and July 1, 2020. U.S. News ranked Colorado as the No.1 economy in the country and SmartAsset has designated Colorado as the state with the second-most "boomtowns." With a lifestyle that sells itself and an extremely educated workforce, investors continue to be enamored with Denver.

As a result, there was over $1.2 billion in industrial transaction volume in 2020 alone, up 16% year over year. The market fundamentals remain strong and Denver has considerable runway. While many of my contemporaries debate the prudence of going all in on GameStop stock, I'll stick with industrial real estate; the "prettiest girl at prom" also happens to have a great grade-point average.

All research not cited was provided by Colliers Denver and Colliers USA. ▲

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