Aging CBD office stock pushing landlords toward capital reinvestment

CBD office inventory by time period constructed

Examining year-built data for Downtown office product shows that buildings came online in 72 different years. A full 70.0 percent of total rentable building area was constructed in just 13 of those years, from the early 1970s until the mid 1980s.

With seven of 10 square feet at least 30 years old, owners of dated properties are beginning to invest heavily back into properties, hoping to remain competitive with projects coming out of the ground today and seeking increased prospects for existing-tenant retention.

Capital improvement plans have been recently completed, commenced or planned for at least 14 CBD assets that total 10.6 m.s.f. From brand new amenity floors to reskinned exteriors to new elevators and HVAC, these owners have invested (or will invest) a weighted average of $9.86 p.s.f. in upgrades.
CBD capital improvements

Not including 1801 California, $46.3 million has been spent (or is in planning) on re-investment.

CBD new construction

<table>
<thead>
<tr>
<th>Address</th>
<th>16M</th>
<th>1601 Wewatta</th>
<th>Triangle Building</th>
<th>The Lab</th>
<th>1801 Wewatta</th>
<th>1401 Lawrence</th>
<th>Z Block</th>
<th>1144 Fifteenth</th>
</tr>
</thead>
<tbody>
<tr>
<td>Developer</td>
<td>Elevation Development Group</td>
<td>Hines</td>
<td>East West Partners</td>
<td>Opus Development Company</td>
<td>Portman Holdings / Hines Phelps</td>
<td>First Gulf</td>
<td>Grand American / McWhinney</td>
<td>Hines</td>
</tr>
<tr>
<td>RSF</td>
<td>146,000 s.f.</td>
<td>300,000 s.f.</td>
<td>230,000 s.f.</td>
<td>73,108 s.f.</td>
<td>100,000 s.f.</td>
<td>311,015 s.f.</td>
<td>260,000 s.f.</td>
<td>660,000 SF</td>
</tr>
<tr>
<td>Completion Date</td>
<td>2014</td>
<td>2016</td>
<td>2016</td>
<td>2016</td>
<td>2016</td>
<td>2017</td>
<td>2017</td>
<td>2018</td>
</tr>
<tr>
<td>% Leased</td>
<td>58%</td>
<td>37%</td>
<td>35%</td>
<td>65%</td>
<td>0%</td>
<td>30%</td>
<td>36%</td>
<td>0%</td>
</tr>
</tbody>
</table>
CBD average asking rents

- New record-high achieved in each of last 4 quarters
- Up 23.6% since recession-era trough
- Up 10.1% over pre-recession peak

CLASS A
- Up 25.8% since recession-era trough
- Up 4.1% over pre-recession peak

Industry breakdown

Over the past three years, leases signed by new-to-CBD tenants have increasingly represented a larger share of the market's total annual net absorption.

- 2012: 1 in 5 SF absorbed
- 2013: 1 in 3 SF absorbed
- 2014: 7 in 10 SF absorbed

Such moves have increasingly represented a larger share of the CBD's total annual net absorption. Below is a look at the industry composition of these transactions.
CBD headwinds – top four trends

1. **Oil & Gas Subleases**
   More sublease space has been put on the market last quarter than was leased by Oil & Gas tenants all of last year in top tier buildings.

   - 506,200 SF sublease on the market
   - 56 months average remaining term
   - $25 / SF average asking rent

2. **Employee Density**
   At present, roughly 1,000 oil and gas layoffs. Using below density ratio, you need 1.8 non-Oil & Gas jobs to backfill the space lost by a single Oil & Gas layoff.

   - Average non-industry user: 234 SF per employee
   - Average Oil & Gas user: 421 SF per employee
CBD headwinds – top four trends

**Assessed Values / Tax Increase**

Owners will receive new property tax bills in January, and, in many cases, the additional costs—likely to be rather substantial—will be passed on to tenants in the form of higher tax expenses.

![Graph showing commercial property values: movement from July '12 to June '14.]

Source: JLL Research, county assessors’ offices

**Cost of Living**

Denver ranked fourth in drawing residents from other states last year. Denver County has recorded the highest number of gains. Housing construction hasn’t kept pace with the growing population. The result—few metros in the nation have seen home prices and apartment rents climb faster than here.

![Graph showing net-migration by county from 2001 to 2015.]

Source: JLL Research, county assessors’ offices