

Denver Office Market

Concerns Turned from the Pandemic to the Economy in 2022

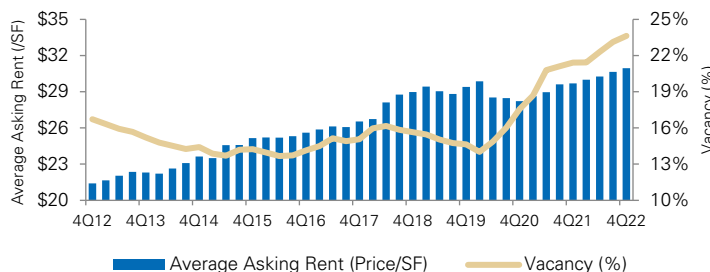
Although 2021 marked a slow climb back towards normality and ended with optimism going into 2022, hopes for a more robust restart of market activity only lasted the first quarter of 2022, as concerns about the pandemic were replaced with looming questions about the economy and its persistent inflation. The new uncertainty spurred bifurcation in multiple aspects of the market, with smaller suites, high-quality space and small tenants seeing the bulk of activity in the market throughout the year. Many large companies began to plan for a possible recession, either by placing their search for new space on hold or embracing a work-from-home model and putting space on the sublease market. This trend created a historic amount of available sublease space. Smaller, more nimble companies were able to be less cautious, snatching up premium, short-term, plug-and-play space, which provides the highest level of flexibility. Tenant sectors that highly value collaboration and have only embraced hybrid work-from-home models on a limited basis, such as law and engineering firms, were the most consistently active, favoring new construction with high-quality amenities in a bid to attract workers back to the office and attract new talent. New construction and certain submarkets are still attracting high interest, especially in the Cherry Creek and LoDo/CPV micromarkets.

Current Conditions

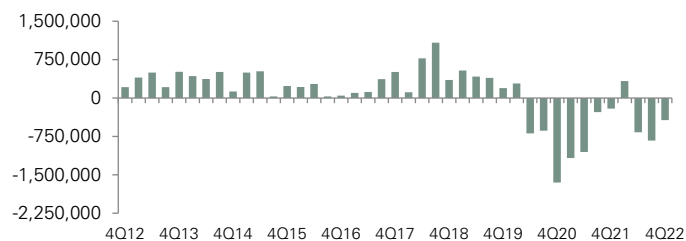
- Market split between the “have”s and “have not”s.
- Activity remains focused on small, high quality space with shorter lease terms.
- Negative quarterly absorption was concentrated in older Class A buildings.
- There is 5.9 MSF of available sublease space in the Denver market with 3.9 MSF of it vacant. This is the highest amount for both in over twenty years.

Market Analysis

ASKING RENT AND VACANCY RATE



NET ABSORPTION



Market Summary

	Current Quarter	Prior Quarter	Year Ago Period	12-Month Forecast
Total Inventory (SF)	101.7 MSF	101.6 MSF	100.8 MSF	↑
Vacancy Rate	23.64%	23.13%	21.51%	↑
Quarterly Net Absorption (SF)	-430,477	-832,676	-207,635	↑
Median Asking Rent/SF	\$30.96	\$30.65	\$29.70	↑
Under Construction (SF)	1.7 MSF	1.7 MSF	813,903 SF	↓
Deliveries	238,811 SF	0 SF	0 SF	↑

RESEARCH Q4 2022

Submarket Activity

Only two of Denver's nine submarkets posted positive net absorption for the fourth quarter of 2022: the Southeast submarket with 69,873 square feet, followed by the Northeast submarket with 26,292 square feet. The Downtown submarket continued to see several tenants downsize and logged a quarterly absorption of negative 160,350 square feet. Three submarkets did not contract year over year, with the Northeast posting the highest annual absorption of 93,420 square feet. Landlords who are getting aggressive continue to offer concessions in tenant allowance and free rent but asking start rates are largely holding firm for space that is not new construction and high finish. Landlords with such space or space in select areas, like Cherry Creek, are continuing to tentatively push rates, largely due to the ever-increasing cost of construction and tenant improvements. Negotiating power remains on the tenant side, with many asking for multiple concessions from landlords for increases in tenant improvements and free rent, as well as maximum flexibility, such as shorter terms or the right to terminate.

Investors Still Active for the Right Product

Although investor activity remained limited for office product through 2022, select buildings still pulled in near-record-breaking numbers. After MetLife Investment Management set the new high-water mark for price-per-square-foot in 2021 when it purchased Civica Cherry Creek for a total of \$108.0 million, or \$921/SF, Gart Properties acquired 240 Saint Paul Street in the same Cherry Creek micromarket for \$69.0 million, or \$920/SF, in the third quarter of 2022. The largest sale of 2022 was Beacon

Capital's purchase of 1800 Larimer Street in Downtown for \$291.0 million, or \$533/SF, in the first quarter of 2022.

Looking Forward

The market will continue tentatively improving, even as the economic uncertainty persists through the first half of 2023. Local job growth is projected to continue to grow and a persistently low unemployment rate will keep the demand high for quality space in select markets. This flight to quality will continue for older Class A and select Class B tenants as many companies compete for talent in a job market that will only ease in increments. Tenant activity for space under 10,000 square feet will remain the strongest. Small, high-finish, plug-and-play options will remain attractive to companies looking for quick occupancy, but large blocks of space are likely to linger on the market longer. Vacancy will only incrementally increase, largely due to companies moving to Class AA space and downsizing, rather than tenants entirely leaving the market. Sublease space will begin to level off at the current high point as companies become more confident in their short-term future and some begin to walk back remote-work policies. Stubbornly high inflation and labor scarcity will continue to push the costs of construction, tenant improvements and operating expenses that will in turn be at least partially passed onto tenants as increases to full service asking start rates, especially for landlords of top-quality space or highly desired micromarkets that will be more able to push rates. Effective rates will decrease as landlord concessions will be made in term flexibility, free rents and tenant improvement allowance.

Lease Transactions

Tenant	Building	Submarket	Type	Square Feet
Burns McDonald	9191 South Jamaica Street	SES	Sublease	155,000
Antero Resources	201 Fillmore Street	Midtown	New	132,000
Gibson Dunn	1900 Lawrence Street	Downtown	New	31,000
Matillion Inc.	675 15th Street	Downtown	New	29,000
Pivot Energy	1601 Wewatta Street	Downtown	New	23,000

Select Sale Transactions

Building	Market	Sale Price	Price/SF	Square Feet
Easterly Government Properties, Inc. Portfolio	Aurora & West	\$60,742,067	\$262	232,060
5500 Greenwood	SES	\$15,700,000	\$225	69,855
The DC Building	Downtown	\$14,790,000	\$54	274,598
American Family Insurance Building	SES	\$14,357,500	\$91	157,639
333 Inverness Drive South	SES	\$11,000,000	\$76	144,438

RESEARCH Q4 2022

Submarket Statistics						
	Total Inventory (SF)	Under Construction (SF)	Total Vacancy Rate	4Q Absorption (SF)	YTD Absorption (SF)	Direct FSG Asking Rent (Price/SF)
Overall (Classes A, B & C)						
Aurora	4,589,190	0	22.49%	-154,152	-142,993	\$18.00
Downtown	31,995,529	1,357,264	29.25%	-160,350	-1,045,245	\$45.23
Midtown	5,866,099	270,453	16.71%	-37,346	-122,749	\$33.50
Northeast	2,080,997	106,527	9.38%	26,292	93,420	\$23.95
Northwest	8,429,889	0	19.51%	-95,982	-79,051	\$27.00
Southeast	6,469,671	0	21.58%	69,873	7,191	\$24.50
Southeast Suburban	31,058,065	0	23.72%	-21,845	-355,186	\$25.00
Southwest	3,006,470	0	17.10%	-5,693	47,647	\$21.00
West	8,180,075	0	18.90%	-51,274	-3,729	\$23.75
Total Market	101,675,985	1,734,244	23.64%	-430,477	-1,600,695	\$30.96
Class A						
Aurora	445,960	0	52.31%	-26,336	60,855	\$23.00
Downtown	21,501,183	1,357,264	26.86%	-129,305	-629,308	\$53.69
Midtown	2,898,314	246,453	14.65%	-43,395	-17,300	\$45.75
Northeast	783,902	106,527	0.92%	4,826	4,826	\$28.71
Northwest	5,108,200	0	19.06%	-88,460	-136,507	\$30.30
Southeast	2,658,600	0	22.00%	-839	10,820	\$29.25
Southeast Suburban	18,248,399	0	24.69%	-96,333	-250,686	\$28.50
Southwest	1,250,376	0	26.54%	-1,062	40,997	\$31.06
West	1,086,754	0	23.59%	-15,977	-75,152	\$27.00
Total Class A	53,981,688	1,710,244	24.25%	-396,881	-991,455	\$38.15
Class B						
Aurora	3,297,326	0	22.35%	-133,913	-193,909	\$20.24
Downtown	8,574,940	0	35.44%	-24,181	-400,401	\$39.75
Midtown	2,082,635	24,000	18.86%	3,042	-5,965	\$28.00
Northeast	873,070	0	12.03%	21,466	96,872	\$26.82
Northwest	2,848,241	0	22.00%	-9,486	59,052	\$25.09
Southeast	2,414,293	0	26.77%	69,988	-48,856	\$25.42
Southeast Suburban	10,921,165	0	24.25%	100,641	-141,012	\$24.00
Southwest	1,204,414	0	11.55%	-7,686	-2,134	\$20.00
West	6,043,077	0	19.14%	-21,667	49,429	\$22.00
Total Class B	38,259,161	24,000	24.81%	-1,796	-586,924	\$26.15

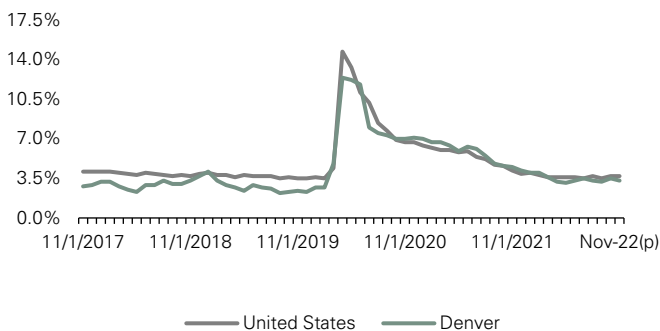
Economic Conditions

Denver and the State of Colorado had a stronger than expected year in 2022, with both outperforming the nation. Denver and Colorado posted job growth of 4.5% and 4.6%, respectively, compared to the nation's 4.2%. After spiking to 8.5% in December 2020, the unemployment rate has, by and large, continued a downward trajectory. It reached 3.3% in November 2022 based on preliminary numbers, below both the state unemployment at 3.5% and the nation at 3.7%.

The professional and business sector posted the largest job growth based off preliminary numbers in November, with year-over-year growth at 8.8%. The important professional and business services sector is Denver's largest employment sector, accounting for 20.2% of total nonfarm employment. Only one of the 10 employment sectors posted job losses; financial activities, traditionally adverse to volatility, saw a decrease of 2.1%.

Unemployment Rate

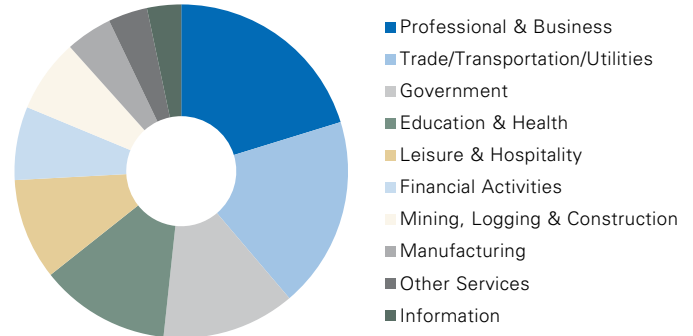
SEASONALLY ADJUSTED



Source: U.S. Bureau of Labor Statistics

Employment by Industry

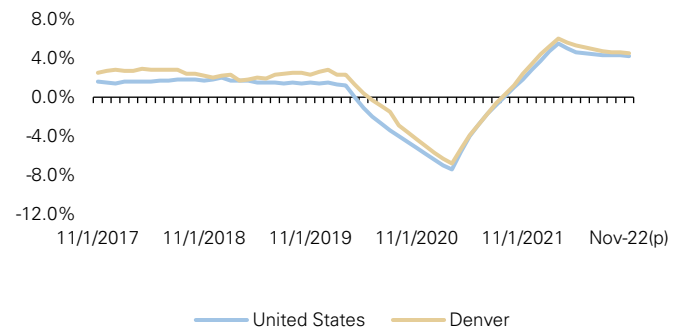
DENVER, November 2022



Source: US Bureau of Labor Statistics

Payroll Employment

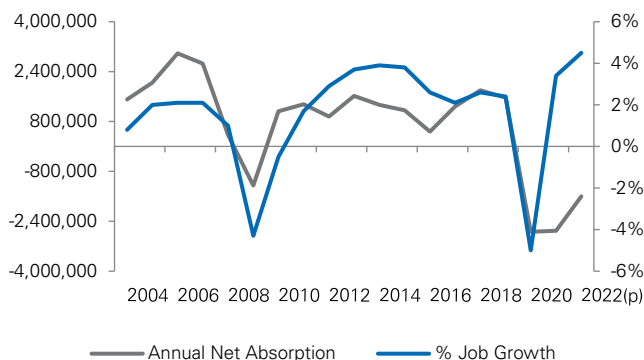
TOTAL NONFARM, NOT SEASONALLY ADJUSTED, 12-MONTH % CHANGE



Source: U.S. Bureau of Labor Statistics

Employment Growth and Absorption

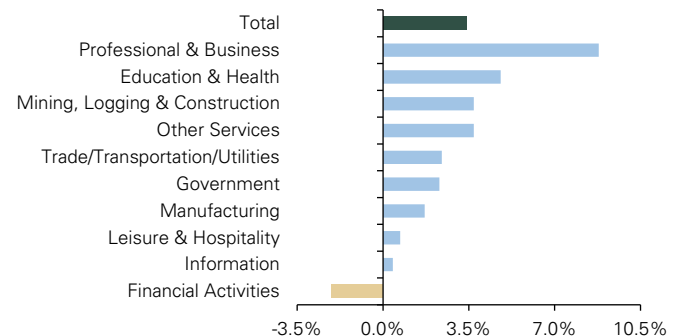
DENVER YOY EMPLOYMENT GROWTH AND OFFICE ANNUAL ABSORPTION



Source: U.S. Bureau of Labor Statistics

Employment Growth by Industry

DENVER, NOVEMBER 2022 (P), 12-MONTH % CHANGE, NOT SEASONALLY ADJUSTED



Source: U.S. Bureau of Labor Statistics

For more information:

New York Headquarters

125 Park Ave.

New York, NY 10017

t 212-372-2000

Denver

1800 Larimer Street, Suite 1700

Denver, CO 80202

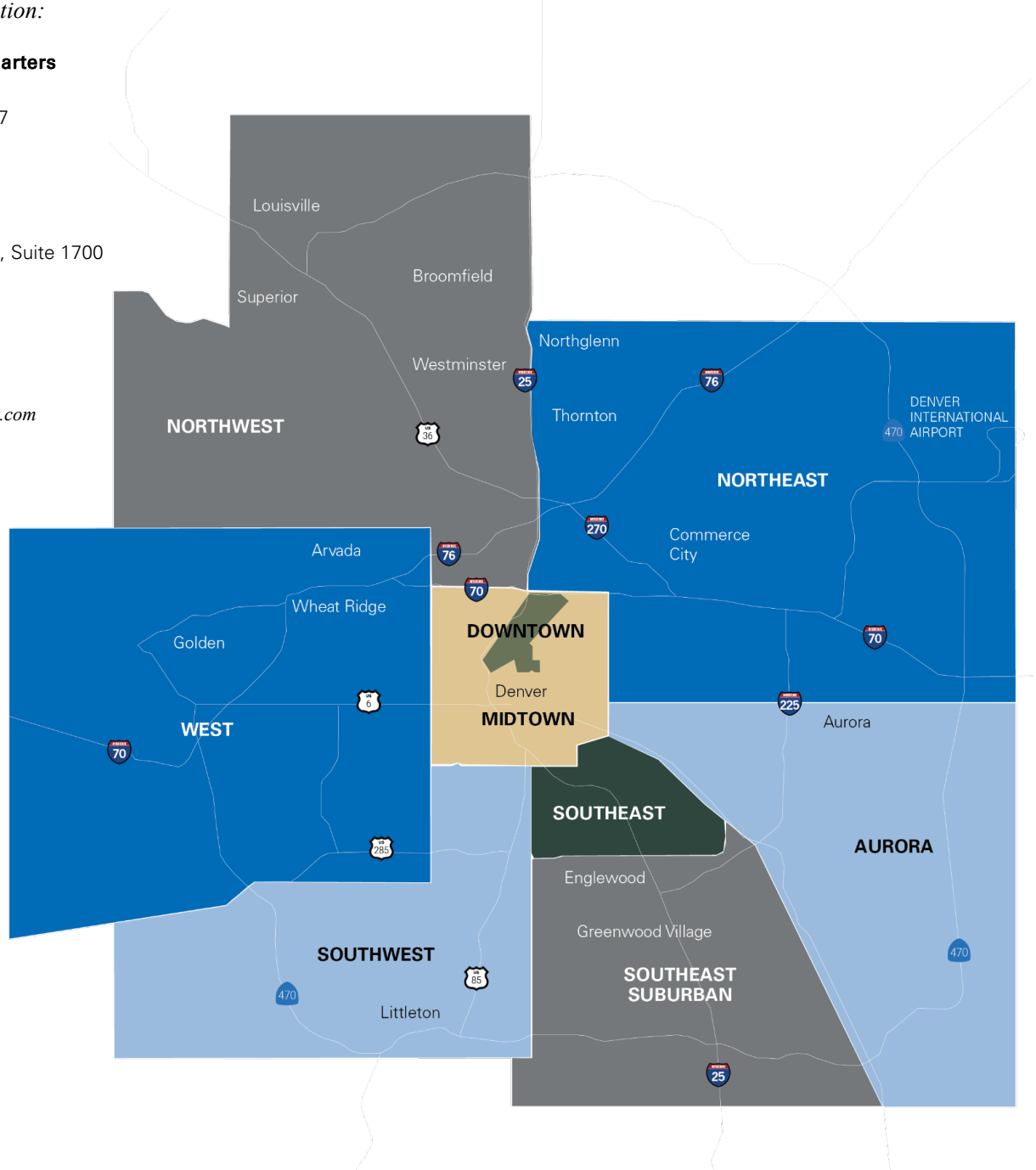
t 303-892-1111

Mandi Johnson

Research Manager

mandi.johnson@nmrk.com

nmrk.com



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