

MARKETBEAT

DENVER OFFICE REPORT

A CUSHMAN & WAKEFIELD RESEARCH PUBLICATION



2Q09

ECONOMY

The pace of economic deterioration quickened through the end of second quarter as job losses mounted and growth in nonfarm-industry sales screeched to a halt. Through June 2009, year-over-year employment in metro Denver fell by 55,200 jobs (down 4.3%) and more than half of these were in office-occupying industries. Most notably, the professional & business services sector shed 11,600 employees in this time frame (a decrease of 5.3%), firms engaged in financial activities – including insurance, credit and real estate – cut 4,700 positions (a 4.8% contraction), and information downsized by 2,500 jobs (a 5.1% loss). Meanwhile, total nonfarm sales in the area were 2.0% lower (by \$1.6 billion) through the twelve months ending April compared to the same period one year ago. Hardest-hit were retail- and industrial-oriented businesses, with aggregate sales down 5.9% and 3.3% respectively. And, while office-occupying sectors did report a 9.2% year-over-year increase in sales, receipts through the first four months of this year were down 0.6% from the same period in 2008.

OVERVIEW

Results from Cushman & Wakefield's mid-year office market survey reflect economic strains. Vacancy rates are up, absorption has turned negative, and leasing activity is sluggish. Shocked by the sudden drop-off in sales, and confounded by extreme tightening of credit, area businesses which had been thriving are now hunkering down to ride out this storm. With prospects for recovery uncertain, many tenants have opted to downsize or seek short-term renewals. Landlords have been remarkably accommodating, dropping rents and offering generous concessions to stabilize income streams and protect asset values.

Overall vacancy increased 210 basis points (bps) to 16.7% between December and June. Class A vacancies were up 170 bps since the start of this year to 14.8% overall, class B vacancies jumped 220 bps to 18.9% overall, and class C vacancies surged 300 bps to 17.3% overall. Negative year-to-date absorption of over 1.3 million square feet (msf) is the worst recorded in over a decade, while new leasing activity of 3.2 msf year-to-date is off by almost a third from this market's historical average.

Significant lease transactions closed involved established firms still needing to expand or cut costs, and new entrants that recognized longer-term opportunities to be tapped in the Denver market. For instance, this year ZOLL Data Systems (which specializes in information management for fire and emergency medical responders) almost doubled its footprint in the Northwest by subleasing 67,250 square feet (sf) formerly occupied by McData at the Views II. Pendum (which provides ATM and cash transaction equipment services) committed to grow its operations by roughly 30,000 sf with its 51,418-sf direct lease of space previously tenanted by BEA Systems at Metropoint II in the Southeast suburbs. And, MarkWest Hydrocarbon (which invests in the volumetric throughput and processing capacity of the oil and gas industry) signed-off on an 18,040-sf expansion at Park Central in the Central Business District (CBD). Other existing companies like the law firm Holland & Hart leased 24,143 sf at Village Center Station and Jacobs Engineering leased 21,823 sf at Stanford Place III to open new offices in the Southeast suburbs, while new entrant Hostmysite.com of Louisville, Kentucky, leased 41,373 sf to relocate its headquarters to Broadway Station I in Midtown and Supervised Legal Services out of California subleased 18,000 for a new office in the Southwest. Transactions like these prove market momentum has not completely disappeared; yet caution abounds and will likely persist.

Sensing dangers on the horizon, landlords have slashed asking rents over the past several months, pushing effective rents even lower. Overall rental rates fell 2.3% since year-end 2008 to \$21.28 per square foot (psf). Declines were greatest in the CBD (where overall rents dropped 5.0% year-to-date to \$27.59 psf), the Southwest (down 4.9% to \$18.70 psf), and in the Southeast Suburban region (now 4.6% lower at \$20.31 psf).

FORECAST

Recessionary forces will keep spending down, sales volumes weak, and job cutting efforts ongoing through 2010. Vacancies are likely to rise another 300 to 400 bps through the end of next year, while rents continue to fall. Tenants can find good opportunities to lock in low rates in the near-term, yet inflationary pressures could emerge once recovery takes hold and limit the window for savings.

BEAT ON THE STREET

"Denver is entering this recession later than most other markets in the country, but is likely to emerge earlier and recover stronger. Its diversified economy, high-quality workforce and relative strengths in key sectors like energy, technology, and research and development, will help it turn around with a bang once this cycle matures."

– Sherman R. Miller, Executive Managing Director / West Regional Manager

ECONOMIC INDICATORS

National	2008	2009F	2010F
GDP Growth	1.1%	-3.0%	1.2%
CPI Growth	3.8%	-0.6%	1.7%
Regional			
Unemployment	5.0%	8.7%	9.5%
Employment Growth	0.8%	-4.3%	-0.8%

Source: Moody's | Economy.com, US Bureau of Labor Statistics

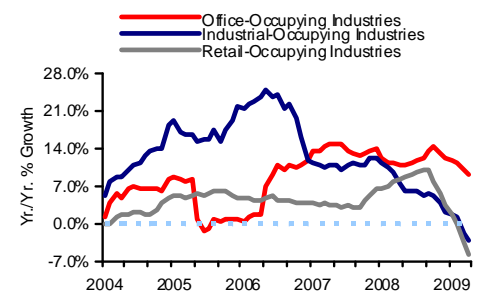
MARKET FORECAST

LEASING ACTIVITY is likely to remain weak, averaging 1.0 msf to 2.0 msf per quarter over the next four to six quarters. ↓

OVERALL ABSORPTION has been negative for the past three quarters and should remain so through 2010. ↓

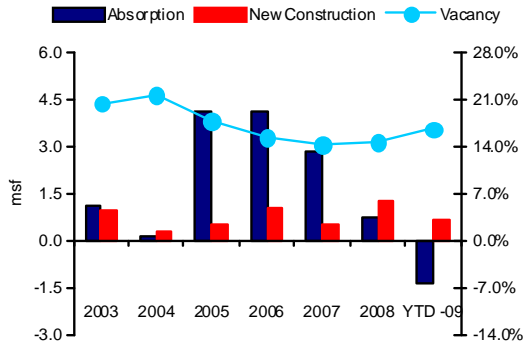
CONSTRUCTION deliveries are likely to be limited to the 1.6 msf already in the pipeline through 2011 as credit remains tight and declining rental rates fail to support cost of new development. ↓

NONFARM INDUSTRY SALES



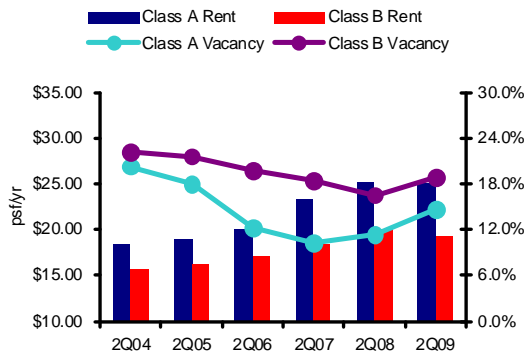
TOTAL MARKET

OVERALL SUPPLY AND DEMAND TRENDS



- Overall demand has weakened at an unprecedented rate, leading to negative 1.3 msf of absorption year-to-date and a 210 bps jump in overall vacancy rates since December 2008.
- With just 698,573 sf of new construction delivered this year and only 1.6 msf under construction, Denver's supply pipeline would be considered well-balanced under normal circumstances. New projects should still see good demand, albeit at a discount from original pro forma expectations and to the dismay of existing landlords having to backfill vacancies left by tenants trading spaces.

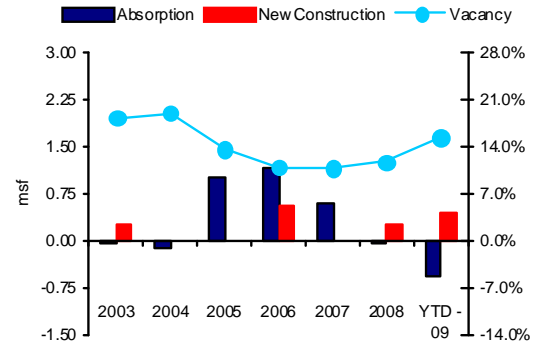
OVERALL RENTAL RATES VS. VACANCY



- Overall asking rents for class A properties appreciated by 42.0% from trough to peak between third quarter 2004 and third quarter 2008. They have since fallen 3.3% in the last three quarters, ending at \$25.09 psf in June of this year. Class B rents grew 30.6% during the same 2004 to 2008 time frame, but have since fallen 4.0% to end second quarter at \$19.27 psf overall.
- Class A vacancies rose 560 bps from a low of 9.1% overall at the end of 2007 to 14.8% overall at mid-year 2009 as 1.7 msf of new product came online and demand weakened. Rising class B vacancies mirror the onset of economic contraction, now up 220 bps to 18.9% from year-end 2008.

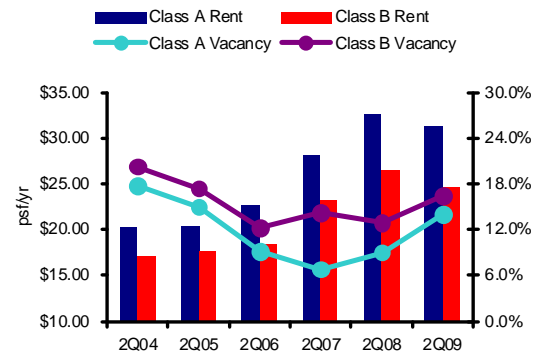
CBD

OVERALL SUPPLY AND DEMAND TRENDS



- Vacancy rates rose 370 bps from year-end 2008 levels, ending in June at 15.5% overall. Much of this was due to the delivery of 474,884 sf of new construction in LoDo over the past six months as well as Qwest Wireless' vacation of 241,677 sf in Uptown. Sublease availabilities also increased 51.9% during this time frame and now amount to 2.1% of total CBD vacancy, or 553,279 sf.
- Year-to-date absorption of -542,938 sf reflects weak demand for class B and C properties (respectively accounting for 44.2% and 53.8% of negative absorption recorded).

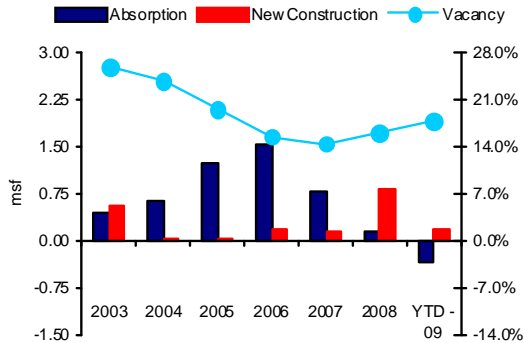
OVERALL RENTAL RATES VS. VACANCY



- The CBD witnessed a 62.1% spike in rental rates during its latest trough-to-peak cycle between second quarter 2004 and third quarter 2008. Yet, as economic troubles set in and vacancies started to rise, landlords were quick to give back some of prior-year pricing gains to remain competitive. Overall rents for all classes have fallen 5.0% in the past six months to \$27.59 psf, with class A rents down 2.5% in this period to \$31.22 psf and class B rents off 6.2% at \$24.56 psf.
- Class A vacancy jumped 710 bps from 8.4% in September 2007 to 15.5% overall in June of this year while adding 1.4 msf of inventory during this time frame. Class B vacancy moved up 260 bps over the same period to 16.4% overall.

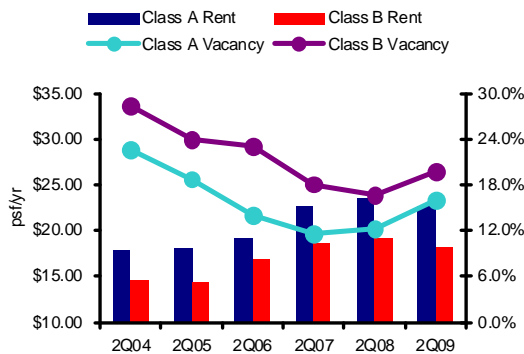
SOUTHEAST SUBURBS

OVERALL SUPPLY AND DEMAND TRENDS



- Southeast Suburban vacancies increased 450 bps in the past two and one-half years, from a low of 13.3% overall at year-end 2007 to 17.8% at the close of second quarter 2009. This region was impacted earlier than others by imploding housing and financial sector markets due to a higher concentration of these types of firms within its boundaries.
- To date, only one, 200,174-sf building has been delivered (Village Center Station) and only one, 140,000-sf project is under construction (The Streets at Southglenn).

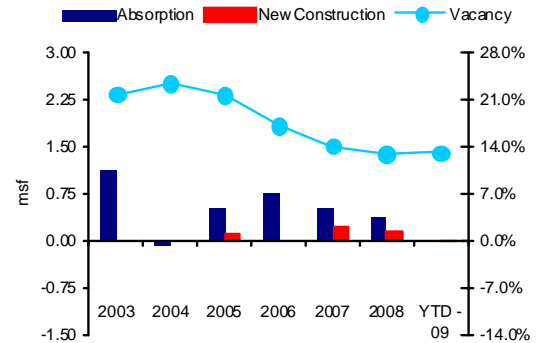
OVERALL RENTAL RATES VS. VACANCY



- Overall class A rents in the Southeast Suburban region increased 37.7% in this area's most recent trough-to-peak cycle between year-end 2003 and third quarter 2008. They have since fallen 5.7% from a high of \$24.01 psf to \$22.64 psf today while overall vacancy for this property class rose 330 bps in this time frame.
- Class B rents experienced a 27.9% rental rate rise from a low of \$14.20 psf overall in third quarter 2004 to its last peak in third quarter 2008 at \$19.24 psf overall. Since then, overall class B rents have fallen 5.6% to \$18.16 psf and overall vacancy rates have risen from 15.5% to 19.8% at the close of second quarter 2009.

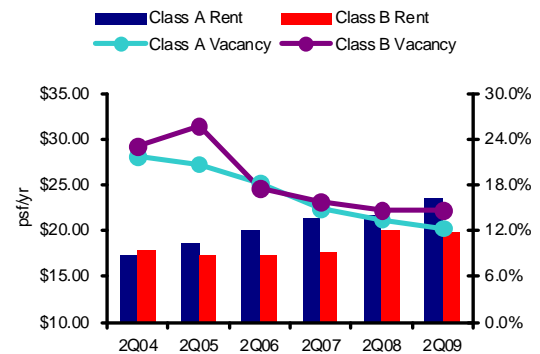
NORTHWEST

OVERALL SUPPLY AND DEMAND TRENDS



- Overall market conditions in the Northwest region held fairly steady over the past six months, with overall vacancy edging only 10 bps higher to 13.2% and negative overall absorption of just 6,975 sf year-to-date.
- Two projects are slated for completion by year's end which will add 87,794 sf of new product – Building 2 at Arista Place and Building 1 at Jefferson Office Park near the Jefferson County government center. Next year Franklin Street's 285,612-sf Central Park Tower will also be completed.

OVERALL RENTAL RATES VS. VACANCY



- The Northwest was one of two regions in the metro area to report increasing class A rental rates (rising 4.5% in the past 6 months to \$23.50 psf overall), and it was the only one to see class A vacancies decline in this time frame (down 50 bps to 12.4% in June).
- Class B rents, however, have fallen 2.4% since December 2008 to \$19.93 psf overall, while class B vacancies edged 30 bps higher to 14.7% overall.
- Given modest new supply levels and relatively stable demand, the Northwest is expected to perform better than other regions during this cycle due to above-average concentrations of high-tech, manufacturing and energy-related industries.

MARKET/SUBMARKET STATISTICS

MARKET/ SUBMARKET	INVENTORY	NO. OF BLDGS.	OVERALL VACANCY RATE	DIRECT VACANCY RATE	YTD LEASING ACTIVITY	UNDER CONSTRUCTION	YTD CONSTRUCTION COMPLETIONS	YTD OVERALL ABSORPTION	DIRECT WTD. CLASS A GROSS RENTAL RATE*
Central Business District	25,789,200	127	15.5%	13.4%	286,200	848,822	474,884	(542,938)	\$31.72
Midtown	3,547,007	60	7.4%	7.4%	63,922	0	62,350	(5,751)	N/A
Urban Core	29,336,207	187	14.6%	12.7%	350,122	848,822	537,234	(548,689)	\$31.72
Southeast Denver	2,796,822	57	21.8%	21.4%	49,608	0	10,971	(59,252)	\$20.16
Cherry Creek	7,455,772	83	16.8%	16.0%	115,494	0	0	(32,066)	\$23.57
Southeast	10,252,594	140	18.2%	17.5%	165,102	0	10,971	(91,318)	\$21.91
Aurora	4,794,558	72	23.5%	23.3%	65,435	0	0	(32,197)	\$16.67
Northeast	2,498,522	38	31.2%	31.2%	19,816	175,155	0	(144,890)	\$24.97
Aurora / Northeast	7,293,080	110	26.1%	26.0%	85,251	175,155	0	(177,087)	\$20.73
Southwest	7,032,430	136	16.5%	15.5%	133,546	30,000	0	(126,256)	\$24.46
Union Square	2,141,044	31	13.2%	12.4%	75,630	0	0	(51,818)	\$19.83
Southwest	9,173,474	167	15.7%	14.8%	209,176	30,000	0	(178,074)	\$22.38
Denver Tech Center	9,109,253	67	18.2%	16.5%	302,705	0	0	(155,582)	\$22.81
Greenwood Plaza	7,932,434	64	15.4%	13.7%	166,737	0	200,174	(15,955)	\$25.27
Inverness / Panorama	6,389,797	72	21.2%	20.0%	111,889	0	0	931	\$22.78
Arapahoe Road	3,237,754	79	19.5%	19.2%	51,806	140,000	0	(99,095)	\$21.25
Meridian	2,589,178	25	13.3%	12.6%	26,669	0	0	(52,147)	\$22.62
Southeast Suburban	29,258,416	307	17.8%	16.5%	659,806	140,000	200,174	(321,848)	\$23.08
Denver-Boulder Corridor	8,009,641	118	15.1%	11.9%	100,171	350,948	0	47,983	\$25.40
West Denver	4,690,004	113	9.9%	8.9%	67,769	22,458	12,544	(54,958)	\$19.88
Northwest	12,699,645	231	13.2%	10.8%	167,940	373,406	12,544	(6,975)	\$24.76
CBD	25,789,200	127	15.5%	13.4%	286,200	848,822	474,884	(542,938)	\$31.72
NON-CBD	72,224,216	1,015	17.1%	15.9%	1,351,197	718,561	286,039	(781,053)	\$22.85
DENVER TOTAL	98,013,416	1,142	16.7%	15.3%	1,637,397	1,567,383	760,923	(1,323,991)	\$25.44

* Rental rates reflect \$psf/year

MARKET HIGHLIGHTS

SIGNIFICANT 2Q09 NEW LEASE TRANSACTIONS				
BUILDING	SUBMARKET	TENANT	SQUARE FEET	BLDG CLASS
4610 South Ulster	Denver Tech Center	Pendum, LLC	51,418	A
101 West Colfax	Central Business District	State of Colorado Judicial Dept.	47,441	A
900 South Broadway	Midtown	Hostmysite.com	41,373	B
SIGNIFICANT 2Q09 SALE TRANSACTIONS				
BUILDING	SUBMARKET	Buyer	SQUARE FEET	PURCHASE PRICE
1225 17th Street	Central Business District	HRPT Properties Trust	666,653	\$134,250,000
333 West Colfax	Central Business District	American Real Estate Holdings I	51,795	\$5,950,000
6143 South Willow Drive	Denver Tech Center	Warner Pacific Insurance	48,938	\$4,500,000
SIGNIFICANT 2Q09 CONSTRUCTION COMPLETIONS				
BUILDING	SUBMARKET	MAJOR TENANT	SQUARE FEET	COMPLETION DATE
6380 South Fiddlers Green Circle	Greenwood Plaza	Cricket Communications	200,174	6/09
1127 Sherman Street	Midtown	Colorado State Board of Land Commissioners	62,350	4/09
SIGNIFICANT PROJECTS UNDER CONSTRUCTION/RENOVATION				
BUILDING	SUBMARKET	MAJOR TENANT	SQUARE FEET	COMPLETION DATE
1800 Larimer Street	Central Business District	Xcel Energy	490,822	6/10
1900 16th Street	Central Business District	N/A	358,000	10/09
385 Interlocken Crescent	Denver-Boulder Turnpike	N/A	285,612	6/10



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