

August 3, 2009

A Denver Based Commercial Real Estate Investment and Management Company  
Contact Ken Gillis at 303-407-8715

### Denver Office Market Suffers from Negative Absorption

Negative net absorption of nearly 431,000 square feet has put a damper on this city's office market, which has turned in favor of tenants as others have throughout the country after remaining stronger than some until the effects of the economy caught up with it. "Denver's commercial real estate market is clearly feeling the consequences of persistent turmoil in the financial markets, a credit market implosion and the national recession," says a second-quarter office market report from CB Richard Ellis. An outlook from Grubb & Ellis points out that, "Perhaps the greatest long-term threat moving forward is the impact of increased regulation at the state and federal level, which has crimped oil and gas industry growth" that formerly was keeping the office market going because of the region's active oil and gas industries. The loss in occupied space resulting from the negative net absorption in the first quarter increased the direct vacancy rate 40 basis points to 15.4%, according to the CBRE report, which lists the total availability rate, including sublease space, at 21.3% at the end of the quarter. Grubb & Ellis points out that the growing volume of sublease space means that tenants "will find increased opportunities with landlords willing to design creative lease terms and structures by blending existing sublease space with a longer-term direct lease." The Grubb report notes that these leases are typically beneficial to both parties, helping the tenants with low rates early in the term during the current economic downturn, and providing the landlord with an in-place tenant. "Landlords are also able to offer non-monetary concessions that can be important to a tenant, but are often unavailable from a sublessor company such as parking, tenant improvements, etc.," it says. Tenants will also find lower rates because of the worsening market conditions and reduced activity, according to CBRE, which pegs metro-wide average asking lease rates in the second quarter at \$20.69 per square foot on a full service basis, down from the first quarter, as landlords continue their effort to maintain occupancy and cash flows by offering aggressive rates and rent concessions. Despite the lure of these lower rates, "Tenants' attitudes remain conservative with a focus on short-term savings and an effort to delay real estate decisions until the market improves," CBRE points out. As a result, it says tenants are more frequently pursuing renewal and extension options over the cost associated with moving to new space. Despite the still-stagnant credit markets and the general malaise in the investment sales arena, CBRE notes, Denver did register a significant sale in the closing days of the second quarter. A trophy Downtown asset, Seventeenth Street Plaza sold for an estimated \$135 million or \$202 per square foot to HRPT, a Massachusetts-based REIT. Nationwide, the deal was the fifth-largest office transaction to close year-to-date, according to CBRE. (Globest.com)

...

### Study: Colorado Ranks No. 2 for Economic Recovery

Colorado's economic outlook ranks No. 2 out of 50 states, according to a new study from the American Legislative Council. The second edition of Rich States, Poor States: ALEC-Laffer State Economic Competitiveness Index offers a roadmap for economic recovery based on state policies that have a proven impact on growth. Poor labor laws, along with a high level of state debt from years of borrowing hurt Colorado's economic outlook. On the positive side, the study gives good marks to

Colorado for low tax rates, the absence of a "death tax" and competitive workers' compensation costs. The study applauds Colorado's Taxpayers' Bill of Rights and encourages states to follow Colorado's model for constitutional tax and expenditure limitation. Among neighboring states, Utah's economic outlook ranks No. 1, Arizona ranks third, Wyoming ranks sixth, Oklahoma ranks 15th, Kansas ranks 24th, New Mexico ranks 25th and Nebraska ranks 29th. The report shows how federal stimulus dollars may simply encourage out-of-control state spending, which is up 124 percent over the last 10 years, without requiring states to make the tough decisions needed to bring about financial stability. "States were quick to increase spending and add programs during the good times," said Sen. Bill Cadman, ALEC's Colorado state chairman. "Now we need to make tough choices to live within our means. The best solution to our budget woes is to reduce state spending to reflect the reductions in revenues. We must also promote policies that foster economic growth and job creation by reducing the regulatory burden that government places on the marketplace." The bottom five states were New Jersey, 46; Maine, 47; Rhode Island, 48; Vermont, 49; New York, 50. **(Boulder County Business Reports)**

...

### **Stores Squeeze Landlords When Big-Box Retailers Close, Other Tenants Look to shift or End Leases**

Vacant big-box retail space in shopping centers throughout metro Denver has left many neighboring retailers combing through their leases and looking for a way out. Many retail leases contain provisions known as "co-tenancy" clauses. The clauses take many forms, with some requiring a certain percentage of a shopping center to be leased and others naming specific retailers or categories that must remain open. If the conditions aren't met, the remaining tenants in a center can demand rent reductions or leave altogether. In other cases, tenants who are preparing to open can back out of a center if their promised neighbors fail to materialize. "The relationship among retailers is synergistic - they depend on each other to generate sales," said Rick Calhoun, senior managing director of CB Richard Ellis' Denver office. The advent of "power" shopping centers in the 1980s led to the inclusion of co-tenancy clauses in leases, when national retailers realized that there was strength in locating near one another. Now, the bankruptcies of national big-box chains such as Circuit City and Linens 'N Things have led to a spike in retail vacancies, causing the co-tenancy clauses to kick in. In Denver, the retail vacancy rate reached a record 9.3 percent in the second quarter, according to a report by CB Richard Ellis. The average asking lease rate for retail space in the metro area decreased for the first time in two years to \$17.42 per square foot in the second quarter. Most developers aren't willing to discuss co-tenancy clauses except in general terms because they don't want tenants to demand concessions. Gart Properties, which owns 10 shopping centers in Colorado, only has co-tenancy clauses at the Denver Pavilions downtown, said Mark Sidell, the company's president. The clauses, he said, are harmful to shopping centers and their owners. "When your leg gets chopped off, the tenant wants the right to chop the other leg off," he said. "It's a bad deal." At the Pavilions, however, Gart has made concessions to tenants who are staying through the redevelopment of the shopping center. The company also has granted concessions to struggling tenants at other centers to keep them from shutting their doors. "We've deferred rent and allowed them to pay it back over 18 months," Sidell said. "Some we'll lose because we're not willing to invest in them." He said it's better for tenants and landlords alike to keep shopping centers full. "We take very seriously

our responsibility to merchandise the shopping center, just the way we expect a retailer to merchandise their store." When Gart purchased City Center Marketplace in Aurora, the 233,000-square-foot shopping center was 70 percent vacant. Today, the shopping center is 70 percent leased, but only 60 percent of the space is open because a 35,000-square-foot Office Depot closed its doors after seven months at the directive of its corporate office, Sidell said. The company is still paying rent. "We turned down the mega churches, bingo halls and craft centers," Sidell said. "You don't really create value with tenants like that." Miller Weingarten Realty LLC, which owns about 3.5 million square feet in 11 shopping centers throughout Colorado, is having co-tenancy issues in several of its properties, said Bill Mackiernan, vice president of leasing and asset management for the company. He declined to discuss the details of the lease clauses. "In today's market, with as many boxes that are empty or having trouble, tenants are exercising those rights now," he said. While it's unclear who's asking for rent reduction or lease termination - several retailers and their brokers declined to comment - centers that could be facing issues include Flatiron Marketplace in Broomfield, where Office Depot and Linens 'N Things both went dark and tenants like Pier One, Borders and the Great Indoors are on the "endangered" retailers list. Among the tenants in a sea of vacant space in the Flatiron Marketplace is Nordstrom Rack. While the retailer doesn't discuss the details of its leases, it tends to stay in shopping centers for a long time, said Brooke White, a spokeswoman for the company. "We want to be in centers that are fully leased," White said. "We would be working with a developer to encourage leasing and filling up the center. It's better for the customer in the long run, and we're most successful when we're surrounded by good competition." (Denver Post)

...

### **Office Vacancy Rates in Colorado Springs Expected to Grow Through 2009**

Colorado's Grubb & Ellis commercial real estate and investment brokers predict a gradual quarter-by-quarter office vacancy rate increase through the rest of the year. Senior economist Bob Bach said lease rates will continue their downward slide, increasing 17.6 percent for second quarter. As a result, some tenants who are able to do so will take advantage of concessions and declining rents, signaling the market's underlying health. "What is different about the effect of this recession compared with others is that the negative trends are moving fairly gradually," said Mark Ballenger, executive vice president and managing director of Grubb & Ellis' Denver office. "We are experiencing gradual increases in vacancies and a steady downward slide in rental rates rather than significant shocks to the market." Citing a possible "flight to quality," if Class A buildings begin to empty out and rent rates decrease dramatically, Bach stopped short of predicting tenants would be confident enough in the economy to move in large numbers. Unlike Colorado Springs, Denver saw "significant" job growth in May - the first net job gain for the Mile High City since August 2008, fueled by companies like DaVita, Kirkpatrick Oil and ICF International. As a result, both Ballenger and Bach foresee some corporate expansion, requiring additional office space. In the Pikes Peak region, through second quarter, office space net absorption stood at a negative 282,370 square feet, but on the positive side, 336,835 square feet office space was leased during the first half of the year, based on the Turner Commercial Research "Commercial Availability Report." Average rents have remained slightly more than \$14 since late 2007, and average vacancy rates for the quarter jumped 2.1 percent since January to 14.4 percent. (Colorado Springs Business Journal)

## The Beginning of the End

Figures released by America's Commerce Department on Friday July 31st confirmed what most had expected: America's economy suffered yet another quarter of falling output in the three months to the end of June. The world's largest economy shrank at an annual rate of 1% in the second quarter. At least as of June 30th, America's economy was still contracting, thus the country's deepest post-war recession was not over. But the news has been greeted with something approaching relief. For one thing, the decline was smaller than many economists had predicted, and a lot less than the dramatic 6.4% annual rate of contraction of the previous three-month period. For another, there are reasons to hope that conditions improved in July. And some newly released data about earlier months give reasons to cheer too. These suggest that the decline in economic activity may have bottomed out at last. The S&P/Case-Shiller index of house prices in America's 20 largest cities rose for the first time since July 2006 in May, by 0.5%. Americans also bought more houses in June than they did in May: sales of new single-family homes rose by 11%. All of this suggests things are getting brighter in the troubled housing market. A sense of an end to the decline is also apparent from the Federal Reserve's most recent "Beige Book", a twice-quarterly publication in which the Fed sums up its assessment of the economy based on reports from its 12 constituent regional reserve banks. The latest, released on July 29th, indicates that activity has begun to stabilise, albeit at a low level. All this may explain Barack Obama's comment on Wednesday that America "may be seeing the beginning of the end of the recession". Reaching a bottom does not mean a quick rebound in economic activity, however. The recovery is expected to be shallow and prolonged because American consumers, worried about unemployment and the collapse in the value of their homes, are seeking to reduce their debts, and thus will not spend as freely as once they did. House prices still have a long way to go before they return to the level of a year ago (let alone to their peak). The Case-Shiller index may have risen in May but it remained 17.1% lower than a year earlier, when prices had already been falling for almost a year. Another concern is that the flexibility and mobility of America's workforce, long a strength of the economy, is limited as long as Americans find themselves unable to move home because of negative equity (when the value of a house is less than the mortgage on it). The situation is likely to persist until prices recover more. A greater worry is the bleeding in America's labour market. Unemployment typically continues to rise even after GDP starts to increase, so pain for workers is far from over. Already 9.5% of the workforce is unemployed, and 144 of America's 372 metropolitan areas reported unemployment rates of at least 10% in June. More jobless will probably mean less shopping and a slower recovery. The latest consumer-confidence numbers show that Americans are jittery: an index from the Conference Board, a research group, fell to 46.6 in July from 49.3 in June. The quarterly GDP report also makes it clear that consumer spending, which rose slightly in the first quarter, dropped again in the second, by 1.2%. The good news, therefore, was more a result of government stimulus than evidence of a real, sustainable recovery in private demand. The Commerce Department has also revised its estimates of just how bad 2008 really was, saying on Friday that American GDP expanded at a mere 0.4% last year, much less than its earlier suggestion of 1.1%. This means that the economy will have to grow even more than earlier thought to recover to the level before the crisis. The beginning of the end may be in sight, but recovery is some way off. **(The Economist)**

	<b>CURRENT</b>	<b>1 MONTH PRIOR</b>	<b>1 YEAR PRIOR</b>
<b>FED FUNDS RATE</b>	.25	.25	2.00
<b>3 MONTH LIBOR</b>	.48	.60	2.79
<b>PRIME RATE</b>	3.25	3.25	5.00
<b>10 YEAR TREASURY</b>	3.52	3.54	4.05
<b>30 YEAR TREASURY</b>	4.31	4.33	4.64

