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Sierra Commercial Real Estate, Inc.

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- *Commitment to our clients*
- *Commitment to our industry*
- *Commitment to integrity in everything we do*

## WHERE THE BUCK STOPS

**COMMITMENT:** *to pledge or promise; engagement and involvement; to devote (oneself).*

Definitions can occasionally be tricky things, but for the individuals at SCRE the word “commitment” is as easy to define as anything that we do. The single most critical duty we perform each day is to honor and pursue the following: *commitment to our clients, commitment to our industry and commitment to integrity in everything we do.* These basic principles are the foundation on which Sierra Properties, Inc. has built its business and reputation for the past 16 years and they are the very principles that guide all of our actions at SCRE. Our clients, industry peers and many vendors, should accept no less from us and more importantly we accept no less from ourselves. As we continue to face the ever changing and extremely challenging demands of the Pikes Peak region commercial real estate market, it is important to maintain a balanced perspective. Opportunities are created and profits are best secured when markets appear difficult and at their worst. This is the time when creative and dedicated professionals can make the most positive difference. We would like to sincerely thank all of our clients and the many vendors and business associates who have supported and trusted us through our recent transition. You have our ongoing “commitment” to leave no stone unturned in the pursuit of helping you accomplish each and every one of your goals.

David R. Delich, President - Sierra Commercial Real Estate, Inc.

## OFFICE REPORT - CLASS “A” SUBMARKETS

General office market statistics are easy, however the truth about the Colorado Springs office market is challenging to understand. The total size of our market continues to stand in excess of 22 million square feet with an overall vacancy rate of 9.1%, which is the highest level in the past 30 months. Characteristics of this condition have been low lease activity and low absorption reflecting poor overall economic conditions. Any positive gains have been more than offset by the contraction of our economy and steadily increasing supply. To understand the truth, one must look into the primary Class “A” submarkets to “feel” the marketplace.

The focus in this report will be the North End, for several reasons, but some discussion on the submarkets is necessary. There are three primary submarkets in Colorado Springs: The Central Business District, the Airport and the North End. The Airport and Central Business District submarkets are both in excess of 3 million square feet. As of 9/30/03 the Central Business District is experiencing a vacancy rate of 8.9% and the Airport is 10.5%. The North End, in excess of 11 million square feet, is experiencing vacancy of 8.9%. The trend in all submarkets is the same: Supply ↑, lease activity ↓, rents ↓. These conditions have persisted since the end of 2000.

Today’s story lies in the North End for the following reasons: (1) it is the largest and most vital submarket, and (2) SCRE is in-

roducing it’s outline for reclassified submarkets in Colorado Springs for Class “A” Buildings. The Class “A” submarket in the North End is segmented into approximately 40 multi-story and approximately 20 single story buildings. The vacancy rate in the North End Class “A” multi-story is 29% (including sublease space) and the Class “A” single story is 23%. The statistical bottom has not yet been hit, but it is very close. The statistical bottom is important because the psychological bottom is right behind it and without both of these events occurring, the market cannot recover. The actual timing of both events can only be seen in the “rearview” mirror.

A 29% vacancy rate is not good, but analysis of the condition can produce an understanding for potential opportunity. Contiguous blocks of space are very important to Tenants/Landlords and it breaks down like this:

Contiguous Blocks of Available SF	# of Competitive Buildings
100,000 SF	1
50,000 SF	2
25,000 SF	6
15,000 SF	10
10,000 SF	18
5,000 SF	Many

The result is if a user requires a multi-story image and a large block of space, there are few choices available. The number of com-

petitive buildings with blocks of space is not significant until you hit 15,000 square feet and below. Within this market segment there are very few opportunities for partitioned office space and this type of configuration will experience more demand.

The single story product complicates the available large block situation due to the fact that there are four buildings on the market today with over 100,000 square feet and a fifth building will be vacant in the 2<sup>nd</sup> quarter of 2004. Not all of these buildings are classified as office buildings. Out of the five large blocks of space, three are readaptive uses leaving only two for more traditional office uses. None of the five can be easily subdivided. Analysis further shows the existence of shadow space, i.e. space occupied, but under utilized, and not on the lease market, of about 5% in the North End.

The fact is that high vacancy remains a challenge on the North End, but with some economic help recovery will come quickly. A good year in the Colorado Springs office market will yield one to two 100,000 square foot deals, three to five 50,000 square foot deals and so on. Therefore, certain market areas will tighten more quickly than others and as mentioned above, certain configurations of space will experience greater demand.



# COLORADO SPRINGS EVOLVING INDUSTRIAL MARKETPLACE

Historically industrial buildings have been easily identified and classified by their intended uses of manufacturing, storage and distribution. These buildings were typically located near major transportation corridors, i.e. highways, railroads and airports. The onset of rapid advancement in the fields of electronics, telecommunications, defense contracting and medical technology created a need for a combination of industrial features having varying amounts of office space. This has resulted in the evolution of a "hybrid" building referred to as "research and development" or "flex tech" space. This type of space, which is abundant in Colorado Springs, had appeal for high tech employers during the boom of the 1990's. Subsequently, this product has suffered the greatest turnover and vacancy growth during Colorado Springs' loss of nearly 10,000 "high tech" jobs since the second quarter of 2000.

The abundance of vacant industrial space, created by this reduction in market demand for high tech products and subsequent job losses, is highly visible along the north I-25 corridor, Garden of the

Gods Industrial Park and industrial zones east of the city. While generally thought to be a negative factor, this vacant space also provides creative opportunities for those businesses needing to renew leases, expand or relocate into these competitive properties to fulfill their current and future requirements.

Currently in the market there are creative "changes of use" occurring in traditional industrial buildings. Recent examples that illustrate this can be seen in the Wiggand Wood Products/Steelcase manufacturing plant in the Garden of the Gods Industrial Park, which has been converted to a ministry headquarters location. Additionally, Western Forge sold a traditional manufacturing plant which produced Sears Craftsman hand tools to a high-end home furnishings retail store for showroom, warehouse and distribution.

A positive movement in the industrial market is the ongoing need to buy or lease 2,000 to 10,000 square foot buildings located on small lots. Some of the greatest demand in this market segment has occurred in 2002 and 2003. It is

evident that the vacant "research and development" "flex tech" type buildings in certain submarkets are candidates for conversion to multi-tenancy to address the demand for smaller space as the economy improves. Industries and users that will benefit from these conversions are defense contractors, call centers, destination retail, small to medium size value-added engineering and assembly firms, software developers and service/distribution/storage centers. As this conversion occurs, overall vacancy rates will decline with positive absorption taking place and lease rates stabilizing in existing inventory.

INDUSTRIAL BUILDINGS

SIZE/SF	TOTAL SF	VACANCY SF	VACANCY %	AVERAGE RATE/SF
100,000 - 750,859	9,873,906	990,160	10.0%	\$8.17
50,000 - 99,999	4,995,965	886,944	17.8%	\$7.54
25,000 - 49,999	5,847,169	733,763	12.5%	\$6.25
10,000 - 24,999	7,101,640	455,231	6.4%	\$6.36
1,000 - 9,999	3,947,507	140,148	3.6%	\$6.96
Totals:	31,766,187	3,206,246	10.1%	\$7.06

Source: TCR - Turner Commercial Research

## RETAIL SNAPSHOT

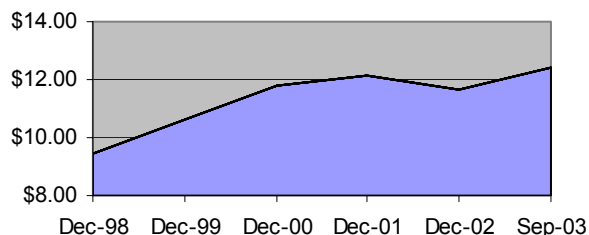
Although the overall commercial real estate market remains challenging, albeit slowly improving, the retail segment remains solid. Several pockets such as Briargate, the Powers Blvd. corridor and the Southgate/World Arena area are extremely strong. Fueled by healthy new home construction and the accompanying consumer spending, lease rates and retail land prices continue to climb and set historical highs. This environment has encouraged new retail development to flourish. One of the most important highlights of the third quarter was the opening of the Shops at Briargate promoting first time entry into the Colorado Springs market by a variety of high-end retailers signifying a new level of confidence in our market.

Leasing and the accompanying rates in these dynamic areas of Colorado Springs are extremely strong and have set record highs with rates for some space at \$28.00 to \$35.00 per square foot, triple net. There is a significant amount of pre-leasing that has occurred in new grocery and discount anchor centers that are currently under construction. The majority of leasing and absorption activity in 2003 went into these new centers, leaving many of the older centers with higher vacancies. For example, vacancy rates in shopping centers are nearly 50% higher along the South Academy Blvd. corridor than in shopping centers

throughout the region in general. Vacancy in established and well anchored shopping centers along the Powers Blvd. and North Academy Blvd. corridors is almost non-existent. Not surprisingly, rents in these various submarkets reflect similar trends either up or down.

The overall vacancy in shopping centers has slightly increased over the past two years to eight percent (8%), which is partly attributable to new construction. Asking rates citywide have increased to an average of \$12.41 per square foot, triple net, while strong anchored centers are commanding rates in the \$18.00 to \$30.00 per square foot, triple net range.

Average Asking Rents - Shopping Centers



Source: TCR - Turner Commercial Research

