



A VIEW FROM THE TOP OF PIKES PEAK

DAVID R. DELICH
PRESIDENT



In spite of the difficult economic environment that our industry has been working in, when looking down from the "Peak", I can still see one of the most desirable places to live and work in the United States. Decision makers from Intel, Federal Express, Boeing, Lockheed Martin, Quantum, Hewlett Packard and countless more corporate representatives all seem to feel the same way. I suppose that's why they're here.

Education, competitive labor, technology, and quality of life form the cornerstone on which our marketplace is constructed. The growth of the metro area to nearly 550,000 people has provided a diverse economic base unlike any other time in our history. Jobs in finance, insurance, manufacturing, service, engineering, and the military continue to drive our local economy into the future. Colorado Springs has not been immune to the difficult economic conditions that have prevailed nationwide since mid 2000. The good news is Colorado Springs has reached its "statistical bottom" in every commercial sector and the market's rebound is only delayed by the "psychological bottom" that must accompany it before a vibrant recovery can occur. We expect this to happen in 2004. Some bright spots on the horizon are the Northern Command (Homeland Security) expecting to create approximately 1,000 new primary jobs; ICT group (an information processing company) announcing plans to bring over 1,000 jobs to the market, and Progressive Insurance currently under construction with a 300,000 S.F. campus capable of housing up to 1,500 employees. Colorado is a great state, Colorado Springs is a terrific city, and with our "big brother" Denver to the north, we have a great deal to offer. Take a trip to the top of Pikes Peak and enjoy the view sometime soon. You will be amazed at what you can see.

In closing, I want to state on behalf of every member of the Sierra Commercial Real Estate and Sierra Properties team, that we are proud and excited to become a part of the CB Richard Ellis family. Our clients and customers will receive the tremendous benefits this affiliation will provide and together we can look forward to an exciting future.

OFFICE PROPERTIES

KENTON R. MAU
SENIOR MANAGING DIRECTOR



2003 market conditions reflect a current vacancy rate of 9.1% for the entire Colorado Springs office market which is consistent with vacancy levels for the previous three years. Since 2001 the vacancy number has remained between 8.5% and 9.5%. The inclusion of sublease space increases the vacancy rate to 11.1% city wide. The general trends in the market place are a decline in leasing activity, absorption and average rents; all of which mirrored the national, regional and local economies. The amount of sublease space has declined dramatically from 882,000 SF established in 2002, to 472,000 SF in late 2003. This decrease is a result of leases burning off, becoming "direct" space, and isn't attributed to absorption. Overall vacancy rates within specific sectors are high compared to historical levels (29% in the Class "A", multi-story, North I-25 market including sublease space) however, the market is more resilient than in the late 1980s for a number of reasons:

- The vacancies aren't a result of over-building, but a contraction of the economy. The result has been an abundance of second generation space (versus speculative shell space) requiring a lower cash contribution for conversion.
- A significant amount of the vacancy has been carried by corporate America since 2000, and although the space is vacant, corporations have assisted in financing projects for landlords (almost 50% of the vacancy in Colorado Springs for 2001 and 2002 was sublease vacancy).
- Historically low interest rates have allowed landlords to extend lease-up schedules while maintaining proformas.

OUTLOOK FOR 2004

- All submarkets should hit their vacancy highs and begin to reverse the downward trend during 2004.
- Demand should begin to recover in the local economy, due to the forecast of improving economic conditions and the continued implementation of the Northern Command in Colorado Springs (Homeland Security).
- Class "B" buildings in certain submarkets, will experience higher vacancies, while lower rents in Class "A" product will allow tenants currently occupying lesser quality space to upgrade.
- The market should experience some investment opportunities with Class "A" projects during the second half of the year.
- The medical office market will continue to demonstrate strength with new announcements for development and expansion in 2004.

OFFICE	CHANGE FROM YEAR END 2002 TO YEAR END 2003	PROJECTED CHANGE BY YEAR END 2004
VACANCY	↗	↔
NET ABSORPTION	↓	↗
LEASE RATES	↓	↘
CONSTRUCTION ACTIVITY	↔	↔



INDUSTRIAL PROPERTIES

In 2003, the 31 million SF industrial market continued to reflect corporate downsizing and lack of user demand by exhibiting a near record high vacancy rate of 10.1%, as well as negative absorption, and a 2.2% decline in asking lease rates from 2002. The greatest impact has been in light manufacturing and flex-tech product located in the Garden of the Gods Industrial Park, the airport area and the North I-25 corridor.

The eastern submarket near the Airport continues to add inventory in existing and new industrial and distribution space. Absorption of this product was slow in 2003, with most of the activity occurring in owner/user buildings between 2,000 SF and 10,000 SF in size on 1 to 3-acre lots. This was the strongest segment in the industrial market during 2003.

INDUSTRIAL	CHANGE FROM YEAR END 2002 TO YEAR END 2003	PROJECTED CHANGE BY YEAR END 2004
VACANCY	↑	↘
NET ABSORPTION	↓	↗
LEASE RATES	↓	↘
CONSTRUCTION ACTIVITY	↓	↔

OUTLOOK FOR 2004

- New construction will be limited to smaller owner/user buildings until vacancy declines in the flex-tech, light manufacturing and distribution product city wide.
- Some large “vacant” single-use flex and light manufacturing product will be converted into multi-tenant space as landlords see the need to cater to a different tenant mix.
- The demand for new 1 to 3-acre platted lots will continue to increase as the existing supply is depleted.
- The price for small “finished” industrial land sites will continue to rise into the \$2.75/SF to \$3.50/SF range as the existing inventory is absorbed.
- Asking lease rates will continue to decline (in all large facilities north of 10,000 SF) until this product type begins to show positive absorption in late 2004.

DAVID L. BACON
MANAGING DIRECTOR



MIKE L. MCDOWELL
MANAGING DIRECTOR



RETAIL PROPERTIES

Although most segments of the 2003 commercial real estate market remained challenging, the retail sector was the one bright star. Near-record housing starts in El Paso County once again fueled consumer spending, resulting in the need to provide well-located retail for these fast growing areas. The North and Northeast corridors benefited most, due to brisk residential growth in these submarkets. Support also came from the fact that the highest average household income in the region is located along the North I-25 corridor. Upscale retailers entering into the maturing marketplace in 2003 included such names as Whole Foods, Pottery Barn, Williams Sonoma, P.F. Chang’s and Biaggi’s. Lease rates in well anchored centers along the Powers Boulevard corridor and the North Academy Boulevard submarket have reached all-time highs, with annual rates for prime space ranging from \$28-\$35/SF, NNN. The new Lifestyle Center at Briargate is anchored by some of the country’s most successful operators, establishing new highs for market rents. The past year saw new grocery and discount-anchored centers gain the majority of new leasing and absorption, with older centers experiencing increased vacancy.

OUTLOOK FOR 2004

Expect the development of two new “power centers” to take place in the northern sector; one located in Monument, North El Paso County, and another in Interquest at the northern edge of Colorado Springs. New grocer-anchored centers will be limited to 3 or 4 projects with at least one being an infill development in an older established section of Colorado Springs. Secondary and non-anchored centers will continue to see declining rents and increased vacancy until new construction and opportunity has a chance to cool off a bit. Land for future development is readily available in the region’s fastest growing corridors, so expect large retailers - particularly Wal-Mart, Target, Costco and Kohl’s to continue hunting sites and expanding their already strong presence in the region.

MARK M. USEMAN
SENIOR MANAGING DIRECTOR



GREG KAUFMAN
DIRECTOR



RETAIL	CHANGE FROM YEAR END 2002 TO YEAR END 2003	PROJECTED CHANGE BY YEAR END 2004
VACANCY	↔	↗
NET ABSORPTION	↗	↔
LEASE RATES	↗	↔
CONSTRUCTION ACTIVITY	↔	↗



LAND: INVESTMENT/DEVELOPMENT

**DALE D. WHEELER
MANAGING DIRECTOR**



At times our industry can become so involved with the improved facility requirements of our clients, that a simple truth can be obscured; "beneath it all lies the land." In Colorado Springs, affordable and available land opportunities continue to supply our ability to grow. In 2003, residential land once again took the market lead. Retail land sales also remained strong in select markets. The reason for residential activity - despite static or negative job growth - is threefold: 1) Colorado Springs remains a very desirable place to live, work and play; 2) the ever increasing time required for entitlements forces builders/developers to keep their "pipelines" consistently full to avoid being caught without finished product; 3) Colorado Springs is still a very inexpensive place to do business compared to most of its out of state competition. Unentitled land prices begin under \$10,000 per acre on the low-end, approaching \$30,000 per acre at the high-end. Finished lots begin at \$25,000 per lot and go up from there. The demand for residential land is strong in submarkets from the communities surrounding Ft. Carson in the south, along the Powers Boulevard/Marksheffel corridor in the east, through Briargate, Northgate and Tri-Lakes to the north. Large annexations of land into the Colorado Springs city limits continue to occur with the 1,600-acre Flying Horse Ranch being the most notable in 2003.

Land for retail use continues to demand record pricing, for either developer opportunities in anchored centers or for end users acquiring pad sites. This is especially evident in the Powers Boulevard corridor on the east side, and Academy Boulevard to the north. Land zoned for office or industrial development has had little activity with pricing flat due to the oversupply of existing improved product in these two classifications.

THE OUTLOOK FOR 2004

Looking forward to 2004, it is expected that strong demand for residential land, both raw and entitled, will continue unless stalled by significantly rising interest rates. An improving demand for multi-family land in select geographical submarkets should occur in response to an improving local job market, particularly in the high-tech sectors. Land for the development of office, R & D and industrial product will continue to receive little interest until the existing inventory is absorbed. There should be, however, good activity for medical and office/medical sites in the coming year. Speculative opportunities do exist for the patient and prudent investor as evidenced by approximately 3,000 acres of the Banning-Lewis Ranch now being opened up for development in the northeast Woodmen corridor. This is only the beginning of development on this 21,400-acre project.

ASSET SERVICES

**TAMARA BEGLEY
DIRECTOR · ASSET SERVICES**



Colorado Springs commercial property owners will once again be put to the test in 2004 as the local economic conditions begin to turn from a 3.5-year slide to a market-place with more promise for the future. Sublease and shadow space (occupied but under utilized) will give way to direct landlord vacancies with "no one home" to pay the bills. Reinvesting capital in dated properties, tenant retention (at whatever the cost) and attention to every single detail in building operations will be paramount during this extended period of recovery. Never before has it been more important to understand the simple fact that tenants are the owners' true partners in this industry. Responding to their requirements effectively, and keeping their full interests in mind will allow owners to take a big step in capturing or retaining tenants. Key factors to which your Asset Management Team should pay attention are outlined below, and can greatly improve the opportunity for success in 2004.

- Pay attention to vendors; regular meetings and close inspection of work being performed will allow owners' expectations to be met.
- Bid all service contracts and capital work. The lowest bid will not always be the "best deal", but the process will force service providers to perform at their highest level. Remember, you usually get what you pay for.
- Tenant contact **MUST** occur daily through either management, maintenance, architectural or leasing staff. This critical task should not be considered a responsibility, but a working philosophy.
- Never miss a chance to question your taxing authority. Use the best consultants to appeal assessments and review the process every year.
- Know the tenants' primary needs and recognize when they are not being fully met. From security issues for Department of Defense companies, to flexible building hours for high-tech users, to sanitary/cleanliness requirements for medical users - always be proactive in understanding the things that drive their success.
- Use capital dollars prudently. If proper and routine maintenance is performed rather than deferred, these capital resources can be used to enhance the property's image and go a long way towards tenant retention.

SIERRA PROPERTIES, INC. manages approximately 2 million SF of commercial property in Colorado Springs and is the region's leading company for managing institutionally owned real estate. Sierra's entire organization is committed to providing the highest level of service to all of its clients, customers and vendors.



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