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COLORADO REAL ESTATE JOURNAL

THE COMMUNICATION CHANNEL OF THE COMMERCIAL REAL ESTATE COMMUNITY

JUNE 17, 2015 – JUNE 30, 2015

Oil crash then vs. now: The diversification of Denver's economy

What do the oil crash of the 1980s and "big hair" have in common?

They both represent an era the Denver commercial real estate community would like to forget. My dad liked to tell me that the '80s were both awesome and horrible at the same time. The Cold War ended and the Berlin Wall fell. Movies like "The Blues Brothers," "ET," "Dirty Dancing" and "Full Metal Jacket" graced the big screen. And Bird vs. Magic, well LeBron vs. Curry just isn't the same. Now, the horrible part had to have been the fashion: big hair, acid washed jeans and all the neon. And back to my dad: He definitely wasn't a fan of '80s music, which was a far cry from the music of his youth.

If you talk to commercial real estate professionals who worked in Denver in the '80s, the stories are much more that of the latter, as the crash of oil prices sent the Denver economy tumbling. The late Sherman Miller, an industry icon and a friend and mentor of mine, told woeful tales of "see-through buildings," newly constructed buildings sitting empty for years. Why, almost 29 years after the 1985 oil bust, hasn't the recent crash in oil prices affected Denver's central business district office market the same way it did in the '80s? It likely can be explained by two major differences between the Denver of the 1980s and the Denver of today.

In the late '70s and early '80s, thanks to a booming oil industry, Denver's economy surged. The downtown Denver office market generated record metrics. Overall office vacancy reached an all-time low of 1.5 percent, and to meet the surge in demand, developers built and delivered over 13 million square feet of CBD office space between the years of 1980 and 1985. This more than doubled the square footage of leasable office space in downtown Denver. At that time, the oil and gas industry occupied more than 30 percent of Denver's CBD office space and over 50 percent of CBD high-rise office space. Then, from November 1985 to March 1986, the price of oil plummeted 67 percent.

Dan Konecny
Vice president of loan production, Essex Financial Group, Denver

Between the months of June 2014 and January 2015, oil prices plummeted 57 percent. There was initial concern about how Denver would weather the oil crash. Yet five months later, Denver's CBD office market is continuing to be healthy and vibrant. So what has changed over the past three decades?

To start with, Denver's economy is no longer solely reliant on the energy industry. In the '80s, it was the only show in town. Today, the energy industry is the Denver metro's third-largest industry cluster, behind health care and financial services, which boast 189,000 and 95,000 jobs, respectively. And if you break out the clean-tech jobs from the energy cluster, only 30,340 energy sector jobs are related to O&G. O&G is actually the fifth-largest industry cluster, dropping below both IT and software, and broadcasting and telecommunications.

A significant proportion of O&G jobs are still located in Denver's CBD. According to an economic impact study commissioned by the Downtown Denver Partnership, roughly 10,500 of Colorado's industry jobs are located downtown (34.5 percent). Research compiled by CBRE at the end of 2014 showed 25.7 million sf of leasable office space, of which 22.67 million sf was occupied. DDP's study found 4.4 million sf of downtown Denver office space, or 19.4 percent of the leasable square footage, directly occupied by O&G users. It also shows an additional 731,000 sf indirectly occupied by O&G, the indirect occupancy often being a question that arises when discussing O&G's share of downtown office space. So at most one could argue that 22.6 percent of the leased downtown office space can be tied to O&G.

In addition to a more diversified base of office users in Denver and downtown, the development landscape is much different than it was in the '80s. With the nation coming out of the Great Recession, there is much less new construction in the pipeline. CoStar indicates seven office properties currently under construction in downtown Denver, totaling 1.3 million sf of net rentable space, only a 3 percent increase to downtown's office supply as opposed to a 126 percent increase in the early '80s.

For more than 30 years, we have helped Denver real estate investors and developers finance projects. The lenders we work with are located across the country – from New York to Des Moines, Iowa, to Los Angeles. Not being in our market day in and day out, it is important that they understand the Denver of today. Fortunately, the majority of these lenders can quickly rattle off the stats previously mentioned – only 20 percent of downtown office space is occupied by O&G and only 13 percent by oil. During a recent visit from the West Coast, one of Essex's life company lenders, who is actively trying to increase his debt allocation placed in the Denver market by 30 percent, told me that he believes that Denver is firing on all cylinders and cited the diversification of companies relocating to Denver as the reason. In his mind, the infrastructure put in place over the past two decades has created a quality of life that encouraged companies to relocate to Denver, allowed for healthy growth and will provide for continued upside to Denver's economy. The overarching message we hear from lenders is not only are they unconcerned with Denver's exposure to O&G but also they believe Denver is still one of the best office markets in the nation. Nearly all of our life company lenders are continuing to allocate more money to the Denver market. And commercial mortgage-backed securities lenders are aggressively trying to get Denver properties into their securitizations.

Denver is a much different city than it was in the '80s. So far we haven't overbuilt new downtown office space; it boasts a broader and diversified economy than that of the past. It is no secret that real estate is cyclical and as a real estate professional who will still face numerous cycles, I am grateful for the city Denver has become. That leaves me only to worry about whether or not acid-washed jeans will make a comeback and whether LeBron vs. Curry will ever become a rivalry that – well – rivals Bird vs. Magic. ▲