Market Update

Investors continue to eye Denver favorably

Healthy demographic and economic metrics continue to improve Denver's apartment market. Increasing rental demand and robust rent growth entice investors, including an abundance of local buyers, as well as those from out of state. With a vibrant economy, Denver remains a popular destination for both residents and investors.

As Denver's reputation as a global city continues to strengthen, population growth remains heightened. Roughly one-third of new residents welcomed to the metro in the past five years are 20- to 34-year-olds, the prime renter cohort. Many of the new inhabitants are lured to the Mile High City by the increasing number of tech positions. Tech companies migrating from Silicon Beach and Silicon Valley have become a common theme in recent years, as these businesses seek lower costs of doing business compared with their local markets. Decisions to move inland are supported by the metro's talented labor pool, as about 40 percent of the Denver's residents obtain at least a bachelor's degree, which is notably higher than the national average of 29 percent. The recent surge of high-wage jobs propelled the median household income near $80,000. Although this figure sits far above the national median, the metro's rapidly rising single-family home prices put homeownership out of reach for many residents, boosting the need for apartments.

Amid intensified demand, builders completed roughly 8,600 units in the past four quarters, slightly higher than the previous 12-month total of 7,500 rentals. Downtown Denver and adjacent neighborhoods received almost half of the new supply, specifically areas near Union Station. Due to a lack of available space on the south side of the light-rail tracks in downtown, developers remain interested in the adjoining Highland neighborhood. Here, the Highlands 32 and Infinity LoHi complexes were both completed in the past year, adding to the area's growing rental inventory. The Capitol Hill and Cherry Creek neighborhoods, located just south of the city center, also recorded considerable development with the addition of more than 1,000 units.

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Outside of the urban core, the Denver Tech Center witnessed heightened apartment construction. Demand in this area is aided by a number of corporate campuses, generating the desire for a live-work-play community. Heightened development also occurred in North Lakewood, which can be largely attributed to the light-rail expansion to the west side of the metro. Expect increased commercial development in this area in the coming years, as convenient access to public transit attracts new residents.

Even with the wave of construction experienced in the past year, rental demand still managed to drive vacancy down to 5.5 percent, a 30 basis-point decrease compared with March 2017. Vacancy in the downtown submarket slid 130 basis points despite increased development, reiterating the strength of Denver's apartment market. North Lakewood/Wheat Ridge also documented a surge in demand as vacancy descended 160 basis points to 3.8 percent, the lowest rate among metro submarkets.

Although a number of submarkets recognized bolstered demand in the past four quarters, the metro's construction boom affected some areas negatively, particularly South Denver/Englewood. Here, tenants were lured away by new developments with upgraded amenities in neighboring submarkets, such as those in Cherry Creek and the DTC. Similar circumstances exist in Glendale, an area sitting adjacent to Cherry Creek. Despite the average effective rent being much more affordable in Glendale, monthly rents for Class B and C units are similar in both neighborhoods, supporting tenants' decisions to sign new leases in Cherry Creek, where upscale dining and shopping is more accessible.

Denver registered modest rent growth in the past 12-month period thanks to the healthy rental demand. Metrowide, average effective rents increased 3 percent, pushing the monthly rate to $1,394. This follows a 4 percent hike in the prior year-long time frame. Considerable rent gains in Broomfield aided the metro's 3 percent boost as new luxury units supported the heightened average. South Lakewood also noted strong rent growth at 5.4 percent, aligning the monthly figure with the market average. Complexes in south Lakewood near major transit routes such as Highway 285 tend to carry more potential for rent growth, incentivizing investors.

A healthy economy and positive demographic trends draw investors from across the country. While the majority of properties still are trading among Colorado investors, the number of sales to West Coast buyers ticked up last year. Investors from Illinois and Texas also increased activity. Tight vacancy in Class B and C properties throughout the market has attracted strong investor interest as the majority of new units coming on line are Class A properties. Rents for Class B and C units have climbed well above $1,000 per month, rising at an annual average of 7.5 percent over the past eight years. Low vacancy and strong rent growth will continue to draw investment in these properties, with cap rates averaging in the mid-5 percent area.

Healthy demand for apartment assets has facilitated strong price appreciation over the past few years, with the average rising more than $100,000 per door above the prerecession peak at $187,900 per unit. Because of this, initial yields continue to compress in Denver, with the average tightening 10 basis points to 5.7 percent during 2017. Looking ahead, rising interest rates could widen buyer and seller expectations this year as yield spreads narrow, but apartment properties priced competitively will garner intense buyer interest. ▲