A Colorado Real Estate Journal Publication

November 2017

MULTIFAMILY PROPERTIES *Quarterly*

Blake Hayunga, Virtu Investments

Virtu Investment's Archer Tower property in Denver teamed up with Pillow Residential to enable tenants to rent their units on Airbnb, facilitating a revenue-sharing agreement between the owner, Pillow Residential and the tenant. Pillow coordinates advertisement, key swap and professional cleaning. Virtu is offering residents discounted monthly lease rates in exchange for participation.

Airbnb: The $31 billion gorilla in the room

Revenue generated by the sharing economy totaled $15 billion in 2014, a figure expected to grow to $335 billion by 2025, propelled by exponential growth of Uber and that $31 billion gorilla in the room – Airbnb. A 2016 National Multifamily Housing Council survey found that just 1 percent of apartment owners currently allow home sharing, while 42 percent conceded their residents list units on Airbnb despite leases explicitly prohibiting short-term rentals. Preliminary numbers from the 2017 NMHC survey found that the majority of renters under 54 years old would be open to allowing short-term rentals in their apartment communities, with 81 percent of those under 25 responding favorably to the idea.

Brian Mooney
Senior associate, Moran & Co., Denver

Nearly half of all renters spend more than 30 percent of their income in rent, while one in four renters spend more than half of their income, the 2017 State of the Nation's Housing report published by Harvard University found. As the percent of rent-burdened households remains near historic highs, the growing share of renters looking to Airbnb to make ends meet should come as little surprise to landlords. While the nation's largest landlords have waged fierce battles against the short-term rental giant, it is apparent that home sharing is not simply a trend, but rather a lasting staple in the multifamily industry.

A 2015 Pew Research survey found that 11 percent of Americans have used a home-sharing service like Airbnb, which is projected to grow to 27 percent by 2021. Revenues generated by Airbnb hosts in the U.S. increased 140 percent in 2016 from the prior year to $5.7 billion, while the number of active listings increased 70 percent to 650,000.

Given the growing acceptance of the

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INSIDE

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Letter from the Editor

Evolving apt. demand

During the Colorado Real Estate Journal's multifamily fall conference, an interesting pattern emerged from speakers on the development and investment panels – the multifamily market in Denver is too competitive. Several said they are choosing to sit and be patient, rather than try to commit to something new right now. There was even discussion among panelist on whether value-add properties were worth the cost – with some saying they could justify new builds over value-add projects in the current climate.

This reaction seems reasonable when you consider that some value-add properties are getting as many as 17 bids, making these older vintage sales prices escalate quickly. According to Cary Bruteig, 1970s product is now four times more expensive per square foot than it was in 2010, and it's still going up – 1970s and 1980s buildings now average about $200 per sf.

The good news about all this competition is we continue to see record-breaking sales in the Denver metro, and 2017 may be one of the best years yet. While there always will be demand for the downtown area, especially among out-of-town investors, many conference panelists and authors within this issue say the real opportunities now are outside of the downtown core.

For example, Castle Rock has seen vacancy dip below 2 percent in five quarters since 2013, including this year's second quarter. Likewise, Aurora North saw the largest increase in occupancy from 2006 to 2016 – it increased from 87.5 percent to 98 percent, according to ARA's Jeff Hawks' conference presentation. Meanwhile, Colorado Springs' slower recovery from the Great Recession may have insulated the area from overcompetition and overbuilding fears that we're seeing in Denver, the article on Page 8 argues.

Some investment panelists anticipate seeing increased demand in the suburbs of Denver. These properties ideally would feature larger units located within strong school districts. This prediction seems logical when you consider the facts about millennials in Denver: There are more than 850,000 millennials living in the metro area, they comprise more than 50 percent of our in-migration and the older millennials are coming into their mid-30s. Homeownership remains elusive for many – with the average price for a single-family home being close to $500,000. While some of these young families can support the mortgage, the original down payment leaves many in the lurch. All told, this prediction about a new kind of multifamily demand seems like safe bet in our hyperactive market.

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Market Update

CO will need 100K more apartments by 2030

Renting is at historically high levels, and despite all the cranes in major metro areas across the country, including Denver, supply is simply not keeping up with demand.

Nationally, the U.S. will need 4.6 million new apartments by 2030, according to a new study produced by Hoyt Advisory Services and commissioned by the National Multifamily Housing Council and the National Apartment Association.

Hitting that number will require an average of at least 325,000 new apartment homes every year; yet, on average, just 244,000 apartments were delivered from 2012 through 2016. The last time the industry built more than 325,000 in a single year was 1989. To add to the challenge of accommodating 4.6 million apartment households, as many as 11.7 million existing apartments could need to be renovated or risk being lost from the stock.

The research, which examines rental demand in all 50 states and in 50 major metro areas, finds that Colorado will need 100,000 more apartments by 2030, and 56,000 of those will be needed in Denver.

• **Surge in demand.** We're experiencing fundamental shifts in our housing dynamics, as more people are moving away from buying houses and choosing apartments instead. Every year for the past five years, the U.S. has averaged 1 million new renter households, a record amount.

There are several factors behind this surge. Much has been written about the millennials, and it's

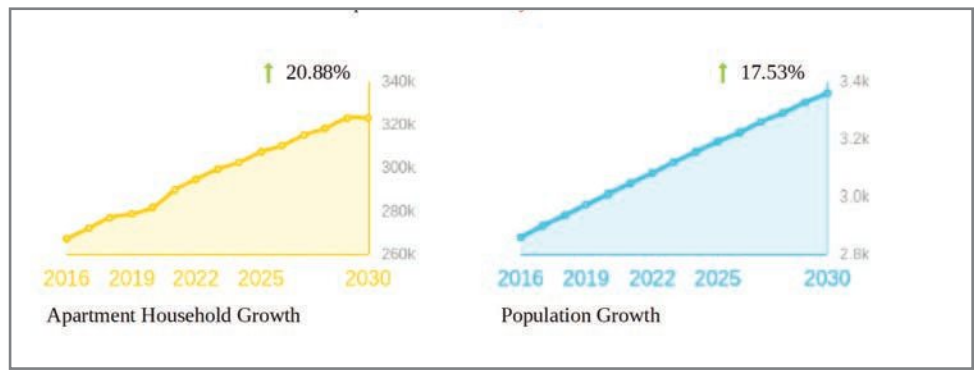
Kim Duty
Senior vice president, public affairs, National Multifamily Housing Council, Denver

true that more than 75 million people between 18 and 34 years old are entering the housing market, primarily as renters. But renting is not just for the younger generations anymore. Increasingly, baby boomers and other empty nesters are trading single-family houses for the convenience of rental apartments. In fact, more than half of the net increase in renter households over the past decade came from those aged 45 or older.

Demographics are driving meaningful lifestyle changes that are being expressed through our housing choices. In 1960, 44 percent of all households in the U.S. were married couples with children – the prime drivers of homeownership. Today, it's less than one in five (19 percent), and this decline is expected to continue.

Immigration also is an important factor. Approximately half (51 percent) of all new population growth will come from immigration, and research has shown that immigrants have a higher propensity to rent and typically rent for longer periods of time.

• **The supply gap.** In a perfect market, the private sector would step up and fill the growing demand. But anyone who has ever developed an



National Multifamily Housing Council, National Apartment Association

New research shows that demand for apartments is on the rise. Whether it's young professionals, couples, families or empty nesters, Denver will need to add 56,000 new apartment households by 2030.

apartment property knows there is no such thing as a perfect market.

Land shortages, local regulations, complicated permitting processes and more conspire to make it difficult for developers to deliver the necessary supply. They also drive up prices that make delivering apartments at a wide range of prices nearly impossible.

The NMHC/NAA-commissioned research also ranked the top 50 metros to identify cities where it's hardest to build new apartments with a Barriers to Apartment Construction Index. Denver ranked in the top 10, coming in at No. 9.

If Denver is serious about addressing its housing shortage, it will need to take a hard look at the obstacles that are delaying or increasing the cost of new apartments.

• **Policies to bridge the gap.** While the number of new apartments built each year has been rising, it hasn't been enough to meet current demand and make up for any possible shortfall at certain price points in the years following the recession. This imbalance between high demand and limited supply options has driven down affordability and reduced housing options for renters. We've seen that firsthand in Denver, where average metro rents are up $700 per month since 2004.

For many reasons, building apartments has become costlier and more time-consuming than it needs to be. Over the past three decades, not only have hard costs like land and materials risen sharply, but regulatory barriers to apartment construction also have increased significantly, most notably at the local level.

These obstacles to development, such as outdated zoning laws, unnecessary land use restrictions, arbitrary permitting requirements, inflated parking requirements,

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Market Update

Prolonged expansion supports calls for optimism

A mathematician, an accountant and an economist apply for the same job. The interviewer asks each of them, "What does one plus one equal?" The mathematician replies, "Two. Exactly two." The accountant replies, "Two … give or take three percent but, on average, two." When the economist's turn comes, he gets up, locks the door, closes the blinds, sits down next to the interviewer and says, "What do you want it to equal?"

Economics is funny. While a snapshot of economic indicators are what they are, there are a number of levers to pull and buttons to push in order to move those indicators in the desired direction. Ideally, making the right moves allows us to reverse a recession or continue economic growth. But, we all know that what goes up must come down. We might disagree as to when the next recession will hit, but we can all agree that it's coming … sooner or later.

Travis Hodge
Vice president, multifamily, capital markets, JLL, Denver

In general, brokers are optimistic. Whether that's by nature or nurture, we feel it's our obligation to inform you that good times are still ahead. There's no doubt many of you are concerned about overbuilding the apartment market. Indeed, there are nearly 30,000 units under construction in metro Denver with another 25,000 in planning. This certainly seems like a lot, especially when considering metro Denver has permitted approximately 4,000 multifamily units per year on average over the last 30 years.

Craig Kalman
Vice president, multifamily, capital markets, JLL, Denver

Enter optimism.

Per Apartment Insights, annual absorption was 6,069 in the third quarter, which marked the 14th consecutive quarter of annual absorption above 5,000. Annual in-migration for the Denver metropolitan statistical area has averaged nearly 33,000 people per year since 2010. Metro Denver has experienced annual job growth of 2 percent or above in 67 of the past 69 months. Denver's economy is more diversified than it's ever been. As long as our economy keeps churning, strong absorption and in-migration should continue. It may not be enough to immediately fill all of the units under construction and currently in lease-up, but that just means rent growth in some spots will level off for a bit.

The Class A luxury market will see the most moderation, and there might be a few value-add plays that end up extending their hold period, but given current levels of leverage and underwriting standards, the vast majority should have no problem weathering any slight dip in the market. All of that could change if our economy enters into another recession in the next two years, but we don't think that's likely to happen.

Instead, we're busting out the cake and cookies in celebration of the current economic expansion's birthday! Happy 101st consecutive month! It's the third-longest economic expansion in U.S. history – dating back to 1854, a time when you could die from a splinter because doctors didn't understand infection.

Not until July 2019 will it surpass the 120 months during 1991-2001 to become the oldest U.S. economic expansion. If you're already doubting that possibility, then you're only looking at the typical length of a cycle and not the whole picture. First of all, you're pulling from a small sample size of 34 cycles. If you're going to use past cycles as a barometer, you have to analyze all of their circumstances and indicators. The Bulls only won 30 games in 1985-1986, but that's not because they assembled a bad team; it's because Michael Jordan was injured for 64 games.

There's some truth to Janet Yellen's argument that cycles don't die of old age. Like living beings, they die of symptoms. Just as modern medicine has allowed us to overcome splinters and extend life expectancy, modern economics has allowed for extended periods of economic prosperity. The chart shows the growing trend of prolonged expansion.

This chart doesn't show pre-World War II times, when expansionary peri-

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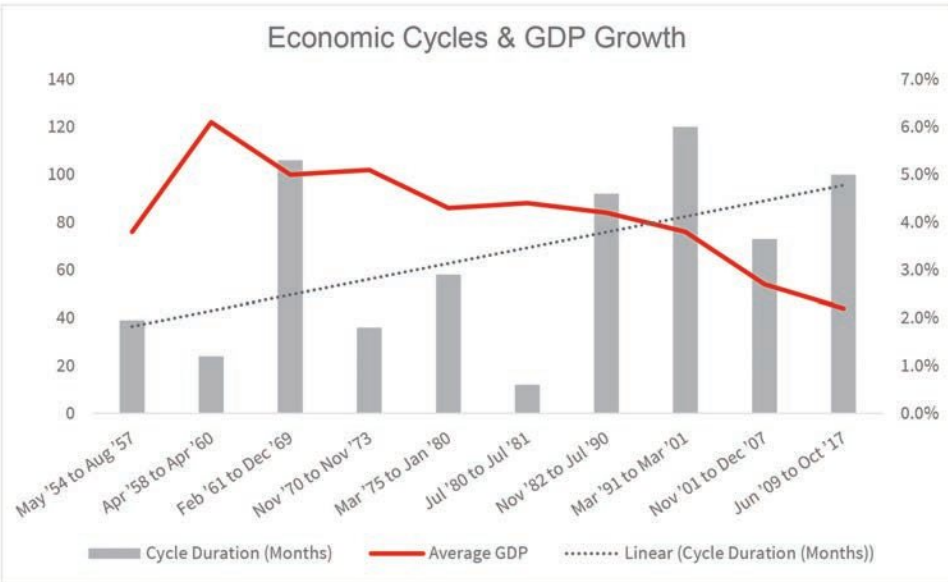

JLL

The growing trend of prolonged expansion in the U.S. since World War II.

Market Update

Springs enjoys highest-rent growth in area

These are rare circumstances we're experiencing in Colorado Springs – accelerating job growth, 7 percent apartment rent growth, 4 percent market vacancy and restrained apartment development. Colorado Springs apartments continue to attract acquisitions from large market investors. West Coast and Denver apartment investors see Colorado Springs as an "upswing" market, with still much potential. This market also is a safe haven from the risks in overbuilt apartment markets and overheated stock markets. Further, Colorado Spring's strong job growth across various sectors is driving strong population growth. These dynamics bode well for local multifamily investment.

Tatiana Bailey, PhD
Director, University of Colorado Colorado Springs, Economic Forum

• **Forecast.** With increasing job growth, our apartments will respond with high occupancy rates and significant growth in rental rates in the short term, at the very least. Investor interest will focus more on Colorado Springs due to weakening rental markets in Denver, Fort Collins, Loveland and Greeley. Rent growth has slowed in Denver, yet Colorado Spring's rental rates remain affordable by comparison and still have room to move higher. Additionally, average rent compared to median income is still reasonable in Colorado Springs compared to Denver. This has lured many people to reside in northern Colorado Springs, while commuting to Denver where salaries are significantly higher.

Doug Carter
Managing director, Sperry Van Ness | Apartment Insights, Colorado Springs

• **Population and job growth.** El Paso County, which holds the clear majority of the population for the Colorado Springs metropolitan statistical area, has had population growth of almost 2 percent every year since the early 2000s. This is roughly double the population growth rate of the U.S. The past growth will be eclipsed by future growth. El Paso County is one of four counties in the state projected to have a population increase of at least 300,000 people between 2010 and 2040, according to the State Demographer's Office. At the current pace of growth and with the given age composition, El Paso County needs approximately 5,400 new jobs to be created per year. Since 2013, the region met and exceeded this threshold. This positive trend continues with 7,083 new jobs from first-quarter 2016 to first-quarter 2017.

Cary Bruteig, MAI
Principal, Apartment Appraisers & Consultants | Apartment Insights, Denver

These new jobs are primarily concentrated in higher-paying sectors, including health and education services, and professional and technical services, specifically information technology. Registered nurse and software engineer have been the two occupations with the highest number of job postings for the last two years. This trend should continue, as the Colorado Department of Labor projects the high rates of employment growth to be in the health care and professional/technical sectors from 2015 to 2025. Furthermore, the median salary in Colorado Springs for job postings from September is higher than the Colorado median – $72,050 vs. $65,575. The current regional median is an impressive 30 percent higher than it was in April 2015, according to Talent Neuron. The healthy job growth and salary increases have large implications for all residential real estate, especially multifamily.

• **Fort Carson.** This region has five military installations with a combined employment contribution in 2017 of approximately 55,000 workers (including active duty and contractual workers), and this still only represents 17

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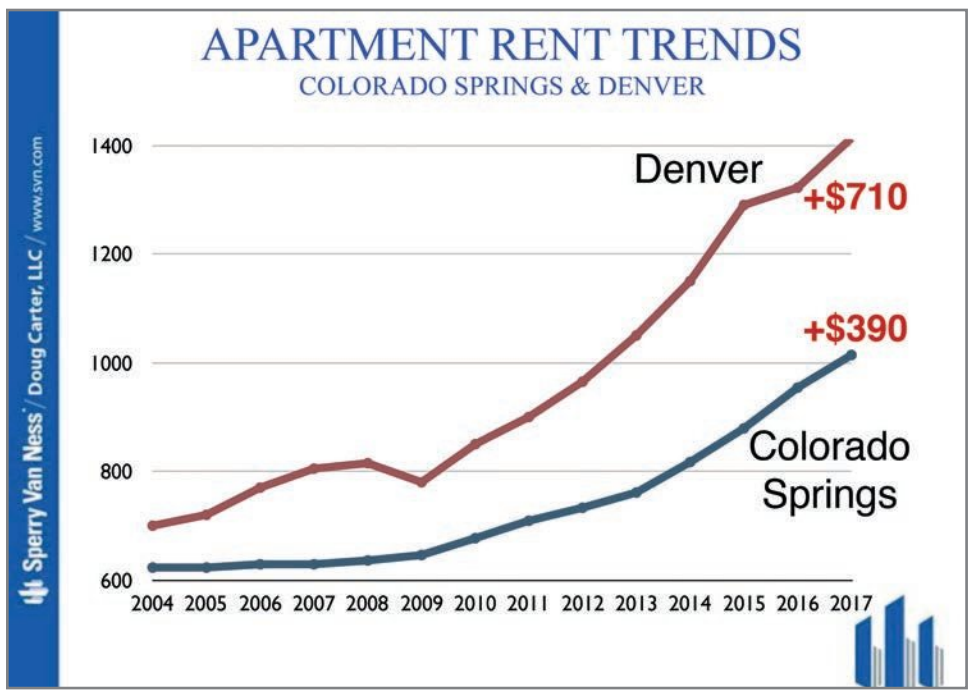

SVN, Apartment Insights

The average apartment rents in Denver have increased $700 per month – or doubled – since 2004. Colorado Springs average rents are up only $400 per month during the same period and still have room to rise.

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Market Update

Northern Colorado investment activity normalizes

Multifamily commercial real estate has been a sweet spot in Northern Colorado, benefitting from the attractive housing prices of the last few years. Last year, Northern Colorado experienced record sales volumes that netted $644 million on about 60 transactions – nearly three times the region's previous high. Through the first three quarters of last year, nine properties of more than 100 units traded hands, totaling $360 million in sales volume. During the comparable span this year, four properties have sold, representing $167 million in sales – less than half the amount transacted in 2016. We now have the last quarter of 2017 to meet the typical regional level of six annual transactions involving 100 units or more.

Our region continues to attract large investors from around the country who recognize the value of Northern Colorado's stable employment market, strong post-recession performance and appealing inventory levels. All of this is buoyed by the growing interest of people wanting to live in this region to attend school, work and retire.

That said, last year was an anomaly. The inventory in the Northern Colorado market is not large enough to accommodate that sheer number of transactions year in and year out. In 2017, the acceleration in rent and property value growth we saw in 2016 started to stabilize.

Although overall sales have normalized, opportunities continue to exist. We are seeing increased inventory in the market, including

Brian Mannlein
Director, Cushman & Wakefield, Fort Collins

from older properties that haven't changed hands for many years as owners decide to cash out while prices are so attractive.

Multifamily investment remains desirable for several reasons. The ability to hedge risk by having many tenants in smaller priced investments is appealing to investors – if owners lose a tenant, there's generally somebody out there trying to find a place to live. On the other hand, if an office tenant leaves, it does not necessarily mean that there is another company searching for a place to put its employees.

Most of the investment in the region is from local and regional investors who fully understand the region's dynamics and can be near their investments. However, we have seen an increase of institutional investors from around the country who are realizing the strength and desirability of Northern Colorado. And the institutional investors are very satisfied with their positions in this market.

One significant indicator is the substantial number of national developers with multifamily construction projects either out of the ground or in the pipeline, which conversely is a reason for the slowdown in rent and value growth along with increased vacancy, all contributing to some apprehension in the marketplace.

The current construction pipeline of the Northern Colorado market, which includes Larimer and Weld counties, has 6,000 units under construction or planned, significantly above the typical-year numbers of 500 to 1,000 units. This considerable number of properties being added to our market include approximately 4,000 market-rate units, 1,200 student-housing units, and another 1,000 units of affordable and senior housing.

The aggressive construction over the last few years has been decently absorbed. But in the last quarter we saw absorption soften. Incentives are edging their way back into the market, and vacancy is starting to climb with these new units coming on line.

Immigration into the region remains strong, between 2 and 3 percent per year. There appears to still be strong demand from students, companies and retirees choosing to locate here. Just as robust are the numbers of people relocating here for good jobs and quality of life, particularly from the Midwest, Texas and California.

We are at that interesting moment in the market when we will see if the intense activity will pay off for investors who were enticed by our low vacancy rates and steady demand. Will the sheer number of units being added match the population influx?▲

Cushman & Wakefield

Multifamily activity in Northern Colorado normalizes after a record year in 2016.

Market Update

4 projects signal relief in tight Northern CO market

Northern Colorado continues to experience strong demand from market-rate apartment developers, with the majority of the interest being in Fort Collins, Loveland and the outlying communities, including Johnstown, Windsor and Timnath – although there also is some demand in the Greeley/Evans area. This demand is due to the ongoing favorable drivers in Northern Colorado – employment and population growth. Employment in Larimer and Weld counties, combined, grew at a tremendous rate of 4.4 percent from July 2016 to July 2017, according to the Colorado Department of Labor & Employment. This equates to approximately 11,300 new jobs in a single year.

Jake Hallauer, CCIM
Vice president, Chrisland Real Estate Cos., Fort Collins

With respect to population, the Fort Collins/Loveland metropolitan statistical area grew by 6,125 people, or 1.8 percent, from July 2015 to June 2016, ranking the MSA's growth 51st in the nation. I believe this population growth was held back somewhat by the extremely tight housing market during that time period, which made it difficult for both buyers and tenants to secure housing. The beneficiary of that extremely tight housing market was the Greeley MSA, which experienced population growth of 9,879 people, or 3.5 percent, during the same time period, ranking as the fourth-fastest growing MSA in the U.S., according to the U.S. Census Bureau. Another factor that likely contributed to the Greeley MSA growing faster than the Fort Collins/Loveland MSA is the relative advantage the Greeley MSA has in terms of housing affordability.

These strong demand drivers have resulted in a stable apartment market despite a significant number of new units being delivered. Asking rents for Class A, institutional-quality/scale communities increased approximately 4.35 and 5.03 percent in Fort Collins/Loveland and Greeley/Evans, respectively, from October 2016 to October 2017. During that same time period, occupancy remained virtually the same, declining by just 0.6 percent in Fort Collins/Loveland area, to an average of 95 percent. The communities in the Greeley/Evans area experienced impressive occupancy growth of 4.63 percent to an average of just over 97 percent, according to our October market report.

With the strong demand drivers and the stable apartment market, I expect that several projects that just began leasing units or will begin to lease units within the next six months, will experience strong lease-up phases (subject to seasonality). These Class A, institutional-quality/scale projects include:

- **Cycle Apartments**. Loveland-based McWhinney is developing this 405-unit apartment community, located adjacent to the newly redeveloped Foothills Mall in midtown Fort Collins. The project will consist of 18 three- and four-story buildings. The unit mix will consist of approximately 20 percent studio units, 60 percent one-bedroom units and 20 percent two-bedroom units. The first units became available for occupancy earlier this month. McWhinney is targeting the urban professional and baby boomer demographics.
- **Bucking Horse Apartments.** There are 322 units under construction, consisting of condo-style apartment units and townhome-style apartment units within the development, just northeast of Timberline and Drake roads in Fort Collins. The project will include one-, two- and three-bedroom units within two- and three-story buildings situated on an 18.26-acre parcel and will include 572 parking spaces. The project broke ground in January, with plans to deliver units in December. This project is being developed by Fort Collins-based Bellisimo Inc.
- **Vibe Apartments.** This project is under construction and is located north of the Terra Vida apartment community, southeast of Harmony Road and Lady Moon, in southeast Fort Collins. The community will include 276 units within 10 three-story apartment buildings, plus a 6,000-square-foot clubhouse, pool and picnic area, constructed on a 10.2-acre site. Additionally, nine live-work units will be included. Delivery of units is estimated for this winter. The project is being developed by a joint venture between Fort Collins-based Imago Inc. and Denver-based Milestone Development Group.
- **Pinyon Point.** McWhinney also is under construction on a 166-unit lifestyle apartment community in south Loveland, near the north-east corner of U.S. 287 and 14th Street SE. The community is being constructed on approximately 10 acres. The project will include studio, one-bedroom, two-bedroom and three-bedroom units ranging in size from 549 sf to 1,300 sf. The community is expected to deliver units in December, with construction scheduled for completion by April.

With the continued population and employment growth Northern Colorado is experiencing, additional apartment development should continue and the apartment developers should enjoy strong performance of their projects for the next several years.▲

Market Insights

Key factors driving our market performance

It is readily apparent that Denver's multifamily market has surged in recent years, reaching new levels of strength, stability and growth. Vacancy rates remain below the market's historical average, sitting at 6.6 percent, despite a large number of deliveries over the preceding three-year period. Net absorption year to date is on pace to break the 10-year high achieved in 2014 (9,189 units of net absorption). Rent growth has cooled slightly in the past 12 to 18 months, but it has been on a strong, positive run since coming out of the 2009 Great Recession.

Most believe that the recent slowdown is more of a correction rather than a warning sign. However, it's important to note how and where this success originated in order to recognize what warning signs might substantially affect them. Upstream of this market growth is a strong foundation of fundamental economic drivers that are laying the framework and positioning Denver for continued, sustainable growth.

Ryan Floyd
Senior director, Greysteel, Denver

Scott Whitfield
Director, Greysteel, Denver

• **Population and demographic shifts.** Population growth has been one of the key drivers for Colorado multifamily with the true value coming from the "who" as opposed to "how many." The answer: millennials and well-educated adults. Denver ranks among top cities like Austin, Texas, Seattle, Dallas and Richmond, Virginia, in terms of millennial in-migration to the area.

Colorado also is the nation's second-most highly educated state for residents with a bachelor's degree or higher, according to the U.S. Census Bureau. In October, Bloomberg released its annual Brain Concentration Index report, which ranked Boulder, Fort Collins and Denver as No. 1, 4 and 10, respectively, in the nation measuring business formation as well as employment and education in the sciences, technology, engineering and mathematics fields.

• **Job growth and higher wages.** The second key driver for apartment market demand is Colorado's ability to continually add a consistent number of new jobs while maintaining one of the nation's lowest unemployment rates. Employment gains for the Denver area peaked in 2015 around 4 percent and has moderated slightly since then. Colorado employment increased 2 percent between August 2016 and August 2017, adding 48,800 new jobs. A report by the Brookings Institute listed Denver as a high-performing metro area with large increases in employment for research- and technology-intensive advanced industries like information, energy and professional services. Colorado also ranks second, behind North Dakota, in the nation for lowest seasonally adjusted unemployment rate in September. A recent Manpower Employment Outlook Survey indicated that over 30 percent of metro Denver employers would be looking to hire throughout the third quarter (one of the highest rates in years).

Large corporations are taking note of Denver's potential and are investing in its future. In June, Amazon.com announced plans for a second Colorado fulfillment center in Thornton, which will create more than 1,500 full-time, associate-level jobs. Trimble Inc., a GPS-technology company, plans to add hundreds of jobs once its Westminster office is expanded next year.

Another important factor spurring multifamily rent growth is the accompanying growth in wages throughout the Denver area. According to PayScale Inc., a Seattle-based compensation data company, Denver tied for second place, with San Diego and Austin, in terms of year-over-year wage growth across 31 major U.S. metros. Area wages grew an incredible 3.5 percent in the second quarter.

• **Threat of overbuilding in core submarkets.** Confidence in future market performance appears high throughout Denver and Northern Colorado, evidenced by the historic number of units either under construction or recently delivered. More units are under construction right now (21,399 units) than in any year since 2000 and is 158 percent above the all-time average. Nearly 12,000 new units are forecasted to come on line in 2018, which is second only to 1973 when 12,300 units were delivered. As of the third quarter, there were more than 10 properties simultaneously in lease-up, with properties targeting the high end of the market seeing slowed traffic and increased upfront concessions.

So, at what point is the construction pipeline outpacing the actual demand for new residential units in the area and what warning signs should we start looking for? One key metric to follow is the occupancy of these new projects at delivery. New construction delivering in 2017 has, on average, been occupied at 35.8 percent at the time of delivery, which is below the all-time average of 47.4 percent and a far cry from the nearly 70 percent occupancy at delivery seen in 2014. One encouraging counterpoint to this recent shift is that properties delivering in 2017 are achieving stabilized occupancy much quicker (nine months, on average) than the prior four years. ▲

Denver Highlight

Denver remains a leader for market strength

Two years ago, the Denver apartment market was one of the nation's strongest. The market was fuller than it had been in 15 years, and rents were growing at a dizzying pace. A lot of that momentum traced back to phenomenal growth in the metro's young, talent-rich labor force. Today, educated millennials will move toward the metro for well-paid employment opportunities and a quality of life rivaled by few other places in the country. While Denver is still a hot spot for relocations, the apartment market has cooled off significantly.

If the market's fundamentals remain strong, then why isn't the Denver apartment market performing at the same level as in 2015? Simply put, developers are bringing new apartments to the market faster than renters can fill them.

Developers delivered 5,835 new apartment units to the metro during the first three quarters of 2017, according to our pipeline figures. Some 4,990 more are identified for completion in the fourth quarter, bringing the year-end total to 10,825 new units – the most this cycle. Some 9,720 units have been identified for delivery for all of 2018. That's a total of 20,545 new units in two years.

At the same time, annual job growth levels in Denver have declined from 3.5 percent in September 2015 to 1.4 percent in September 2017. That's an average pace in the national picture, but a slowdown is expected in a market where unemployment is very low. Even

Jay Denton
Senior vice president, Axiometrics, a RealPage Co., Richardson, Texas

with the slowdown, apartment demand remains high because of a variety of factors, including:

- Denver is a growing tech hub with a vibrant arts culture that is attracting highly educated millennials to the area.
- Population of the prime renter group (ages 20-34) has increased by 13.3 percent from 2010-2015, according to Census Bureau statistics. This rise has been buoyed by the relocation of several companies, particularly in the financial services sector, from higher-cost California locations to Denver.
- Single-family inventory is tight, especially in the $100,000-$300,000 price range, which keeps more people in apartments.

No matter how strong the apartment demand is, it still is not enough to keep up with supply, which is why rent growth has remained comparatively low compared to earlier in this cycle. The Denver average effective rent has increased $91 since the beginning of this year to $1,451 in September, according to our data. Annual effective rent growth was 3.1 percent, compared to the cycle low of 1.5 percent last September. Still, that's down more than 7 percentage points since mid-2015.

A large percentage of these new

units are amenity-rich, Class A spaces that are marketed to higher-end renters. And although luxury apartment rent growth spiked in September, it remained the lowest of the three primary classes in September.

Meanwhile, as rents are rising from the cyclical low, concessions fell at existing properties, but increased in new properties, which are not included in the rent-growth calculation. Existing properties that cut an average of 0.7 percent off asking rent for concessions in January were only taking off 0.3 percent in September, signifying property owners' confidence in filling their properties.

Concessions offered in lease-up properties, however, have increased this year, from 5.1 percent off asking rent in January to 5.9 percent off in September. This increase shows how owners of new properties are realizing the competition they face for residents, especially when effective rent growth for these newer properties was -0.7 percent in September.

Digging down into Denver submarkets, the urban core, in this instance the downtown submarket, is taking the lion's share of new supply. Some 3,141 new units have been identified for delivery in the next two quarters, 34.8 percent of the metro total, on top of the 2,128 units completed in the first three quarters of 2017. Given those supply figures, it's no surprise that downtown Denver has the lowest annual effective rent growth in the metro, -2.7 percent in September.

Please see Denton, Page 34

Valuation

Construction costs not diminishing profits, for now

A persistent gripe in developer circles is the constant upward movement of construction costs. This has been a substantial brake on the fast-moving train of new construction within the Denver market. Steadily rising payroll and materials costs have prevented new deals from penciling, which has resulted in tightened purse strings of construction lenders. More and more proposed projects are being left without financing, forcing developers to drop sites they have under contract for acquisition. Don't cry for the down-trodden developer, though, because there is more to this story ahead.

These rising costs have made cashing out of projects a lucrative prospect for builders who brought their projects to market. As costs have risen over the past eight years in the post-2009 doldrums, we have seen the per-unit cost metric change dramatically. The two tables reflect "all-in" costs of projects brought to market over the past 10 years. This all-in cost is inclusive of hard and soft costs, as well as land acquisition costs. This cost does not include a profit incentive. The data reflects the trends on over 50 completed or underway projects in the Denver metropolitan statistical area.

Mark Lodmill
Director, National Multifamily Valuation Group, CBRE, Denver

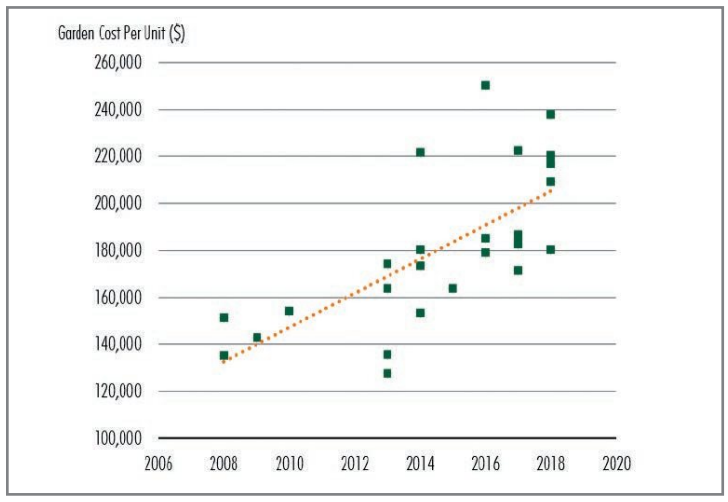
The dramatic shift shown in the charts has moved the typical all-in garden apartment construction costs from a level of $135,000 to $150,000 per unit at the start of the cycle to current projects in the $210,000 to $240,000 per unit range. More dramatically, we have seen elevator-style projects shift in cost from $180,000 to $210,000 per unit to current projects under way at costs north of $500,000 per unit. This leap in construction costs has changed the value per unit landscape of the market today.

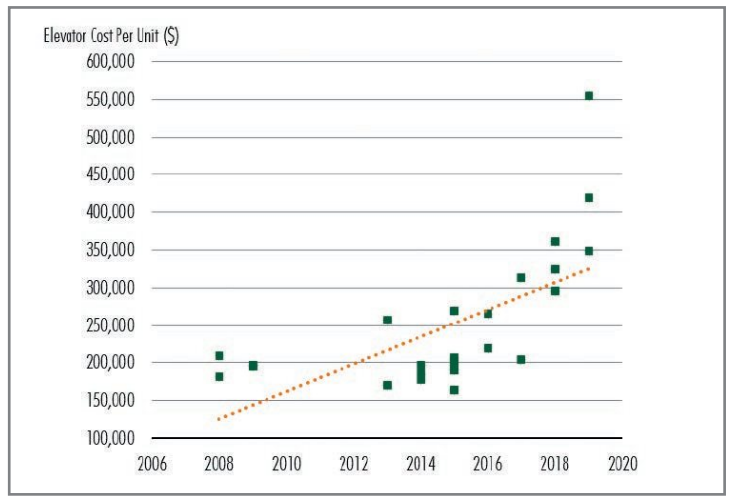
As appraisers, we are armed with the principle of substitution; we state that a prudent buyer would pay no more than construction cost new today plus a profit incentive. However, the concept of "cost new today" is a moving target, steadily advancing with the market. Next, we ponder the more elusive topic of how much profit? The answer to this question is hard to extract. In our discussions with market participants, we often hear a range of 15 to 25 percent. But this will only be borne out in an active marketing process, with buyers pitted against one another to provide the highest price to the seller.

This leads to a second area of research: What profit have developers actually been achieving? As costs have inflated on the order of 10 percent per year over the last several years, we have costs today that are 20 to 30 percent higher than the costs actually locked in by the developer at the project's origination. Adding this market movement to "cost new today" sweetens the pot for our developer friend mentioned earlier.

CBRE researched closed transactions of new properties in the last several years where construction costs were known. This data leads us into the pie-chart graphic. We aggregated the

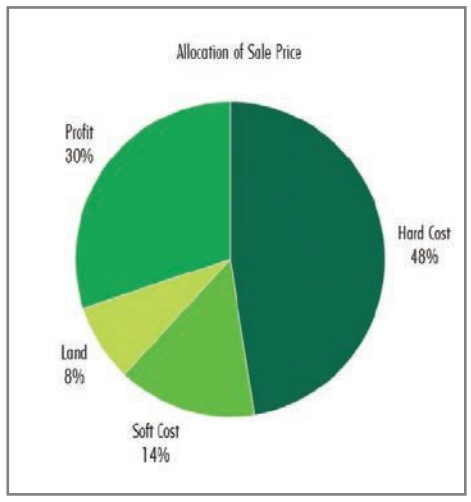
Please see Lodmill, Page 34





CBRE

All-in costs of projects brought to market over the past 10 years. This cost is inclusive of hard and soft costs, as well as land acquisition costs, but does not include a profit incentive. This data reflects the trends on over 50 completed projects and projects underway in Denver.



CBRE

The chart shows where the average sale price on a newly developed asset goes.

Multifamily Properties Quarterly - Financing Sources Matrix

TYPE OF CAPITAL	SOURCE OF CAPITAL	EXPLANATION	RATES/SPREADS	LTV/COVERAGE	TERM	AMORTIZATION	FOCUS	TRENDS
LIFE INSURANCE COMPANY	• Insurance premiums • Annuity and GIC sales	• Non-Recourse • Longer-term fixed rate loan	125-175 bps over the comparable US Treasuries	• Up to 70% LTV • 1.25x Minimum DCR	5-30 Years	25-30 Years	• Market rate properties in major metro areas • B quality properties and above	• Life companies have become increasingly competitive on low-leverage requests in primary and secondary markets • Most competitive at lower to moderate leverage with strong sponsor • Flexible prepayment penalties available for small pricing premium • At right leverage (~60%) lenders can do Interest Only • Best source for terms over 10 years • Looking to do early construction loan takeouts to win business early
AGENCY	• Sales of mortgage-backed securities with implied government guaranty	• Non-Recourse • Longer-term fixed rate loan	180-220 bps over the comparable US Treasuries	• Up to 80% LTV • 1.20x Minimum DCR	5-30 Years	30 Years	• Market Rate • Age-Restricted • Affordable/Workforce • Major metro areas • Secondary/Tertiary Markets • C quality properties and above	• Operating through specially designated underwriters • Comparable pricing for affordable/workforce housing • Minimum investment is typically 750k with no maximum loan size • Agencies are on pace to have another record setting year of origination volume
CONDUIT (CMBS)	• Sales of mortgage-backed securities through public markets	• Non-Recourse • Longer-term fixed rate loan	180-230 bps over the greater of Treasuries or Swaps	• Up to 75% LTV • 1.25x Minimum DCR • 8.0% Minimum Debt Yield	5, 7 & 10 Years	30 Years	• Market Rate • Second tier properties • Secondary/Tertiary Markets • C quality properties and above	• Spreads have narrowed 25-50 bps since early 2017 • Most competitive at higher leverage in secondary and tertiary markets • 10 years interest-only under 65% LTV • 5 years interest-only under 70% LTV • Focused on debt yield as an important metric
BANK	• Corporate Debt • Deposits	• Recourse (some non-recourse available) • Shorter-term fixed and floating rate loans	200-300 bps over bank cost of funds	• Up to 75% LTV for permanent loans • Up to 60% of cost for construction loans	Up to 7 Years Fixed	Interest Only to 25 Years	• Market Rate • Age-Restricted • Affordable/Workforce • Major metro areas • Secondary/Tertiary Markets • B quality properties and above	• Standards are tightening for Sponsors with no deposit relationship, and establishing a deposit relationship is becoming a requirement • Maximum LTC for construction loans has dropped to 55%-60% in last six months • Most competitive for Sponsors with established banking relationships and strong borrower history that are willing to accept recourse • Primarily recourse loans, with non-recourse available to strong sponsors at low leverage • More flexible (open) prepayment terms
DEBT FUND / BRIDGE LOAN	• Private Capital • Institutional Capital	• Non-Recourse • Shorter term bridge loans for acquisition and/or repositioning	LIBOR + 300-500 bps (some w/ floors)	• Up to 85% LTC • Going-in 1.0x DCR	1 - 5 (3+1+1)	Interest Only	• Market Rate • Secondary/Tertiary Markets • C quality properties and above	• Pricing depends on leverage level, property quality, and Sponsor strength

Essex Financial Group - Recent Multifamily Transactions

Belmont Buckingham Apartments
Denver, CO
$18,350,000 Permanent Loan
Life Insurance Company

The Nuvo Apartments
Denver, CO
$10,000,000 Permanent Loan
Life Insurance Company

Decatur Point Apartments
Denver, CO
$39,000,000 Permanent Loan
Life Insurance Company

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Ed Boxer
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Development

HOA exit strategies for condominium developers

As we begin to see the development of condominium units once again in Colorado, developers should be aware that the sale of units is not the only involvement in the project the developer will have. Specifically, a developer will need to form and run, for a period of time, a homeowner's association to enforce the covenants within the condominium community, collect assessments for the community's common elements, and maintain the community's common elements.

Initially, the HOA will be controlled by the developer as the owner of all the units. However, as the condominium units are conveyed to homeowners, the developer will gradually turn over the control and responsibility of the HOA to the homeowners. This turnover of control is subject to certain legal requirements and practical considerations.

Developer control of the HOA for new condominium construction is governed by the Colorado Common Interest Ownership Act, set forth in Article 33.3 of Title 38, Colorado Revised Statutes. When the milestone is reached under Section 303 of CCIOA that requires the developer to transition control to the homeowners (or at an earlier time if the developer so desires), an election must be held where homeowners elect at least a majority of the executive board. From that point, control of the financial operation of the HOA effectively transitions from the developer to the homeowners. Within 60 days after the transition

Catherine A. Hildreth
Associate, Brownstein Hyatt Farber Schreck, Denver

election, the developer must comply with the property delivery requirements of Section 303(9) of CCIOA, which require a developer to deliver to the HOA all property of the homeowners and the HOA held or controlled by the developer.

Below is a developer checklist to use for the HOA property delivery requirements:

1. All entity documents of the HOA, including the original or a certified copy of the recorded declaration as amended; the HOA's articles of incorporation, if the HOA is incorporated; bylaws; minute books; other books and records; and any rules and regulations that may have been promulgated.

2. Audited financial statements of the HOA. The accounting period for the audited financials must be from the date the HOA first received funds and ending on the date the developer completes transition of the control of the HOA to the homeowners. The financial statements must be audited by an independent certified public accountant and must be accompanied by the accountant's letter, containing a generally accepted accounting principles compliance statement. The expense of the audit cannot be paid for or charged to the HOA, and instead will be paid for by the

Bryce Beecher
Counsel, Brownstein Hyatt Farber Schreck, Denver

developer in most circumstances.

3. All HOA funds.

4. All HOA personal property, such as property maintenance equipment, computers, software, etc.

5. A copy of all plans and specifications used in the construction of the improvements in the community.

6. All insurance policies then in force, in which the homeowners, the HOA, or its directors and officers are named as insured persons.

7. Copies of any certificates of occupancy that may have been issued with respect to any common element improvements.

8. Any other permits issued by governmental bodies applicable to the common elements and which are currently in force or which were issued within one year prior to the date on which the homeowners other than the developer took control of the HOA.

9. Written warranties of the contractor, subcontractors, suppliers and manufacturers that are still effective.

10. A roster of homeowners and mortgagees, and their addresses and telephone numbers, if known, as shown on the developer's records.

11. All HOA employment contracts and service contracts.

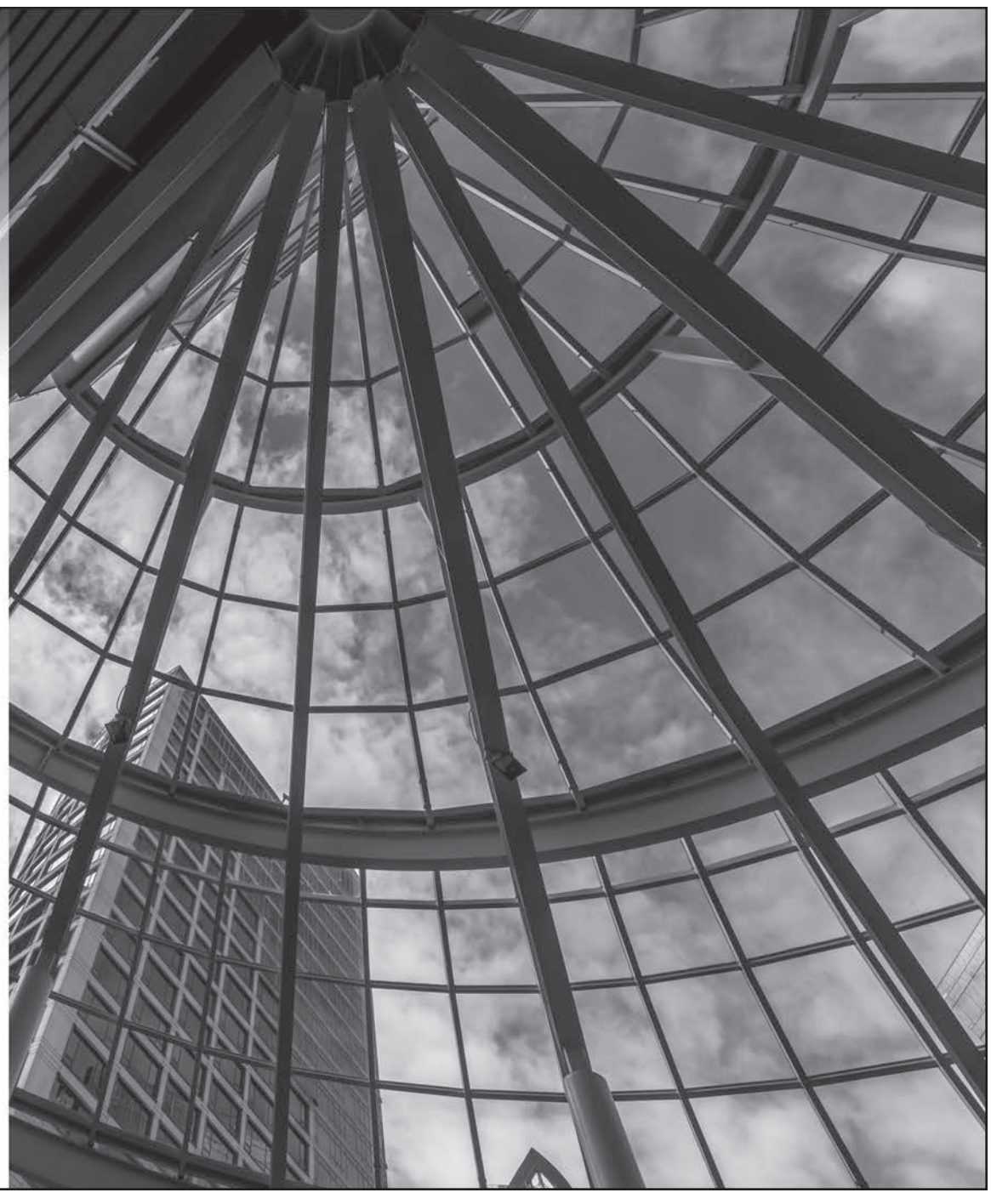
12. For large planned communi-

Jonathan Pray
Shareholder, Brownstein Hyatt Farber Schreck, Denver

ties, as defined within CCIOA, copies of all recorded deeds and all recorded and unrecorded leases evidencing ownership or leasehold rights of the large planned community HOA in all common elements within the large planned community, according to C.R.S. §38-33.3-303(9).

Due to the lead time associated with some of the above-referenced requirements, the developer should plan for, collect and prepare the required transition documents well before the transition election. Failure to do so could result in the developer scrambling to prepare the transition documents in a short time frame.

Developers also may consider some practical exit strategies to encourage a favorable relationship with homeowners on a go-forward basis. For example, developers may consider a homeowner warranty program that includes an on-site warranty representative that can quickly resolve warranty claims. Further, developers may consider a maintenance manual as part of the warranty program to educate homeowners on the maintenance obligations for their individual units and establish parameters for the HOA's maintenance of the community's common elements.▲



Development

3-D modeling can help 'find' precious space

For apartment developers, every square foot of space matters. Efficient building design practices provides them with more rentable square footage, taller ceilings, larger areas for lobbies and amenities and the opportunity to maximize the building's user experience and profitability. Internal mechanical, electrical and plumbing building systems – heating, ventilating and air-conditioning, electrical, plumbing and specialty low-voltage systems – play a large role with forming the final shape of a building. In this case, the expression "sharpen your pencil" has never been more true.

Fortunately for apartment developers, today's technology far exceeds a pencil and paper. One of these advanced technologies is building information modeling, an intelligent 3-D model-based process that gives architects, engineers and contractors the insight and tools to more efficiently plan, design and construct buildings and infrastructure. And BIM – and the professionals who know how to use it – is helping apartment developers discover precious space during the design and construction of their buildings.

The ability to design and build a building three dimensionally on a computer, before actual construction begins, helps architects and engineers tighten up gaps and maximize usable square footage. With the basic architectural and structural bones of a building in place, major components can be added and routed (such as pipes, conduits and duct work) to help fill in and form the building.

Travis Middlebrooks
Electrical project engineer, MEP Engineering Inc., Denver

At the outset of the design process, building system engineers work through calculations, which then lead to equipment specifications, ductwork sizes and piping/conduit sizes, and overall anticipated routings. This information is then provided to a BIM modeler, who has the information he needs to work on three-dimensional placement of the major equipment in the building. This is critical to verify the major equipment in the building can be installed in the space allocated. The BIM modeler continues this process by modeling ductwork, piping and conduit throughout the building to achieve fully connected and functional systems. The 3-D aspect enables the entire team to visualize a building's design in ways that a two-dimensional format could never provide, including orbiting the building and looking through the structure.

Via the BIM process, the design and construction team can identify opportunities for conserving space. Once the building systems MEP model has been populated with content, a collaborative process follows with the design team to shift, tuck and slide systems around to minimize space that does not directly generate revenue for a developer. Systems are routed in a virtual environment with the goal of efficiently arranging these components to minimize the space occupied in building walls, vertical shafts, ceiling plenums and soffits.

> With the basic architectural and structural bones of a building in place, major components can be added and routed (such as pipes, conduits and duct work) to help fill in and form the building.

Three-dimensional modeling of MEP components can play a role in determining the overall floor-to-floor height of a project as well as the overall height and footprint of the building – big-ticket items for the development of a project. On a recent project, our team successfully reduced the overall project building height by minimizing the floor-to-floor space for each level of the building through efficiently routing and coordinating building system components in the ceilings.

For apartments developers who want to work with a firm specializing in BIM, there are a few important things to consider:

- Does the firm specialize in mechanical, electrical and plumbing design, the three most relevant disciplines associated with BIM? If they do, it will lead to a more seamless coordination of the overall design and make the communication process easier.
- Is the firm using the most advanced software associated with BIM? (For example, AutoDesk, Revit and NavisWorks are three of the superior software systems for the design industry.)
- Is the firm experienced with BIM modeling procedures and aware of the challenges that exist?

For apartment developers, providing tenants with the maximum and most-efficient space allowances will make their buildings all the more desirable and leasable by enhancing the user experience. BIM can find added space, while also identifying potential design problems and challenges before construction begins. It not only provides a "sharper pencil," but also a competitive edge to apartment developers who decide to make it part of their design process. ▲

Sustainability

Green living is important part of apartment life

Colorado's booming housing market is creating uniquely greener lifestyle options for residents and newcomers. Much of Colorado's recent real estate growth has been focused on multifamily living, which offers many advantages for individuals and the greater community. This is especially true for those seeking a healthier and more responsible lifestyle. In an effort to capture that sentiment and further build upon it, we recently created the "Green Manifesto," which maps out the advantages of apartment living and could be a guide for Colorado developers to adopt green initiatives that will produce healthier and more environmentally responsible buildings. The manifesto guides AMLI in its construction and facility management efforts from the moment the ink first lands on the blueprints.

Studies have shown that apartment life is an unequivocally greener lifestyle choice compared to single-family housing. Continuing to expand Colorado's multifamily real estate developments based on the perspectives mapped out in the Green Manifesto could be a major step toward building a healthier environment for the community as a whole.

• **Thinking small.** Apartments are sensibly sized. They use fewer resources during construction and the lifecycle of the development. With more appropriately sized dwellings, apartment renters also use less energy and water, saving both the owner and resident money. Additionally, limited storage space discourages unnecessary consumption of goods and resources, which is a main component of living a greener lifestyle.

Erin Hatcher
Vice president of sustainability, AMLI Residential, Chicago

Studies also show that per capita, apartment dwellers drive fewer miles than those choosing single-family living, because the density of housing units supports greener transportation options, such as mass transit, carpooling, bicycling and walking. Shared outdoor space limits the amount of water needed for asthenic purposes such as lawn irrigation. Materially less energy and water usage can be attributed to more shared walls, roofs and community amenities. Collectively, this can easily help individuals lower their carbon footprint with little effort.

• **Healthy living.** Our recent Sustainability Index, which surveyed 380 residents in the Denver area, found that more than 85 percent of residents believed that living in communities with green amenities was beneficial to their health.

This is understandable given that many apartment homes are held to higher building and maintenance standards, making them more likely to utilize low- or no volatile-organic-compound emitting materials. Moreover, apartment communities often include healthy amenities like fitness centers and are located in dense, walkable communities that encourage a more active lifestyle.

Champa Street Productions

Sustainable landscaping at AMLI Interlocken promotes pollinator growth, currently a big topic in sustainability.

By following the initiative set forth in the Green Manifesto, Colorado developers have the opportunity to not only embrace these requirements and concepts, but also take them even further by adding additional healthy features that are highly impactful without compromising the bottom line. Some of these features include:

• Advanced ventilation and filtration to improve indoor air quality;

• Green transportation amenities like electric car-charging stations, bike storage and repair shops; and

• Green cleaning products that can lower the level of harsh chemicals within shared spaces.

These simple additions and changes can vastly improve the experience and health of Colorado residents, making apartment living not only a more sustainable option, but also more appealing.

• **A win-win for the Centennial State.** From a public-policy perspective, apartment living is not just better for residents, but also for entire communities and the state. Apartment buildings typically are located near existing infrastructure, which greatly decreases the taxpayer cost

Please see Hatcher, Page 35

Sustainability

How we secured utility's largest toilet rebate

Denver is an attractive city for multifamily purchasers. Just one year ago, Pensam Residential and BH Equities identified an opportunity for substantial value creation through the purchase of the Breakers Resort (today known as Tava Waters) for nearly $350 million, among the highest in the United States for multihousing in 2016.

Beyond plans to modernize and enhance the property's amenities, the investor team recognized the value of incorporating long-term, water-efficiency planning. Why? Not only to extend Colorado's water supply as demands increase from a growing population, but also because water conservations offers the greatest opportunity to affect the bottom line and exceed the 15 percent savings target most lenders require.

The Environmental Protection Agency estimates that 20 percent of all toilets in the United States are leaking and that U.S. homes waste more than 1 trillion gallons of water yearly. Apply these statistics to a property and imagine what kind of savings, in addition to increased efficiency, can be achieved. Hefty rebates are made available from utilities and financiers for implementing water-efficiency programs, and it appeals to today's modern residents who want to use water efficiently.

Here's a look at how our project was able to implement water conservation efforts, secure financing support from Freddie Mac and land the largest toilet rebate in Denver Water's history.

• **Partnering with Denver Water.** According to the Downtown Denver Partnership, the population in the downtown Denver core has tripled

Richard Lamondin
CEO, EcoSystems, Miami

since 2000, and with added population comes more demand for water. Denver Water, the city's oldest and largest water utility, offers conservation rebates to help property owners finance the implementation of water-efficiency programs. As a result, property owners land rebates that make the investment worthwhile for the ownership team as well as for renters.

The ownership team focused on Denver Water's toilet rebates, which is offered to homeowners and commercial property owners. The utility has given toilet rebates to more than 251,000 customers since 2009. The requirement – installing toilets that use 1.1 gallons of water per flush for $150 per toilet rebate. Denver Water reserves the right to inspect all installations. By partnering with a company like EcoSystems that specializes in securing water conservation rebates, applicants can experience a smooth process.

• **Additional financing support – Freddie Mac**. On top of utility rebates from Denver Water, property owners who are refinancing or purchasing new property can take advantage of Freddie Mac rebates. The process is similar for most programs, including eligibility requirements (conventional apartments, targeted affordable and senior housing) and the borrower commitment to install capital improvements that will achieve a minimum 15 percent reduction in the whole property's annual water and energy use.

Eddie Reiner, CFA
Director, asset management, Pensam Residential, Miami

Freddie Mac requires a minimum green improvement budget of $350 per unit, commencement of work within 180 days and installation within two years. Once our project was deemed eligible for a rebate, an energy audit report was conducted to qualify for the Freddie Mac Green Advantage program. Property owners can receive a $3,500 credit for an energy and water audit, which identifies opportunities for reducing utility costs. Typically, the more rigorous the energy audit, the better the financing terms.

• **Implementation.** Once approved for the rebates, Pensam Residential and BH Equities knew they needed an experienced partner to execute the retrofit – one who is experienced in green-financing projects with lenders like Freddie Mac, who understands Denver Water utility requirements and who could seamlessly make it all happen in a matter of weeks.

Having worked with EcoSystems, an established water conservation company, on previous multifamily projects in Texas, Florida and Illinois, the ownership team brought them on board. EcoSystems' WaterWise program is specifically designed to maximize the impact of federal apartment rebate incentives. It includes affordable solutions such as high-efficiency toilet, shower and sink replacements that achieve savings that often exceed the 15 percent target and require minimal implementation time. As a result, residents experience very little interruption.

The company helped the project conserve even more water than the Denver Water utility required. The definition of an EPA efficient toilet continues to change – the majority of the toilets they installed were 0.8 gallons (down from the 1.1 gallon requirement) and flapperless, eliminating the No. 1 cause of toilet leaks and saving both up front and long term.

Highlights of the retrofit include:

•Between January and April, EcoSystems replaced 2,507 toilets with ultra-high efficiency models in partnership with Denver Water. They replaced 2,507 showerheads and 2,507 bathroom sink faucet aerators with more water-efficient models.

•The EcoSystems team installed water-efficient kitchen faucet aerators and fixed leaks they found in pipes across the apartment community.

•Replaced roughly 7,500 fixtures in about three months.

• **Tava Waters today.** The water-efficiency renovations are projected to help the apartment community save an estimated 35 percent on its annual water bill and, even better, Denver Water estimates the project will save around 33 million gallons of water each year. New showerheads use 1.5 gallons per minute, a full gallon less per minute than the old models. Sink aerators reduced water flow from 2 gallons per minute to 1.

Before the changes, the residents

Please see Lamondin, Page 34

Design

Multifamily design adapts to mirror renter changes

Multifamily design in Denver has evolved from a minor part of most architectural practices to a booming business endeavoring to deliver a rental experience defined by lifestyle-based amenities and the increased demand for service and convenience. And that convenience comes in many forms – everything from a community's location, to its amenity spaces to its service offerings.

As consumer preferences have shifted and the supply of apartments has skyrocketed, developers and the architects who design their buildings have looked for new, creative ways to differentiate each community and stand out from the competition.

• **Zeroing in on renter profiles**. In order to effectively program a building, developers and architects must first understand who will live in it. Today, there are two types of renters: "renters by need," or those who cannot qualify to purchase a home, and "renters by choice," who may qualify but choose to rent for increased flexibility.

These two renter cohorts may have the same demands – for example, a preferred number of bedrooms – but often they are on opposite ends of the price spectrum. Therefore, the market has adapted to capture each of the two respective markets, fine-tuning variables like unit mix, size, finishes and amenities.

With renter profiles spanning the demographic spectrum, new multifamily buildings are increasingly designed to have multigenerational appeal. Amenities such as a playroom cater to both young couples with children and empty nesters with grandchildren. Health-oriented offerings such as fitness centers, pools and yoga studios also have stood the test of time during this most recent cycle.

Terry Willis
Principal, KTGY Architecture + Planning, Denver

• **Reimagining for maximum return**. In metro Denver, condominium construction was booming prior to the Great Recession, while apartment construction lagged. Once the economy shifted, it became clear that three-story walk-up apartments – the most common and economical subset of the multifamily housing genre – would be the first housing type to reemerge.

During the recession, we set out to redefine the common three-story walk-up from a typical garden apartment – historically surrounded by a ring of parking – to a uniquely urban condition. We turned the traditional model inside out, hiding the parking in tuck-under garages and courtyards between and behind buildings, while addressing the streets in an urban rowhouse fashion, often with porch stoops leading to the public sidewalk. Doing so gave these classic apartment homes a new and widely appealing aesthetic.

As large, undeveloped sites became harder to find, and land costs escalated, developers needed to increase density to achieve desired returns.

Today, in addition to designing high-rises, we are designing more apartment projects of five, six and seven stories in height – often with wood-frame construction over a concrete parking podium. TriVista on Speer, a 322-unit rental community in Denver's Golden Triangle, which we designed and is being developed by Legacy Partners, features a five-story wood frame atop a two-story concrete podium. Scheduled to open in 2019, it is the first project of this construction type approved by the city and county of Denver, even prior to Denver's adoption of the 2015 International Building Code, which first allowed such construction.

KTGY Architecture + Planning

TriVista on Speer, designed by KTGY Architecture + Planning and developed by Legacy Partners, is a 322-unit apartment building under construction in Denver's Golden Triangle neighborhood.

• **Expanding beyond the traditional.** As Denver's multifamily market continues to evolve, there is a growing concern, particularly in center city neighborhoods, that supply is catching up with, or surpassing, demand. As a result, some developers are choosing not to compete head-to-head with the new product coming on line. Instead, they're diversifying, either geographically outside the downtown core or by targeting alternative – yet similar – product types, such as age-qualified (55+) apartments or condominium projects.

It may seem that the recent influx of people moving to Colorado are mainly millennials, who account for 52 percent of in-migration. But the growing number of people retiring in the state is staggering. From 2010 to 2025, the number of people retiring is expected to increase by 74 percent

Please see Willis, Page 35

Design

Multifamily housing: The future is looking fresh

Maybe it is the 300-plus days of sunshine, the booming cityscapes boasting multiple cranes or the call of adventure in the mountains, but whatever the reason, people are drawn to our beautiful state. Due to this attraction, Colorado is experiencing a housing boom like never before. This increase has obligated our housing market to adapt and explore new concepts and conveniences wanted by the current renter.

For multifamily housing, one thing has remained true: People of all walks of life are looking for the conveniences and unique amenities it offers. Multifamily housing continues to answer the call of millennials looking for their own spaces, young couples looking to be first-time homeowners facing a challenging market, baby boomers looking to downsize, and families of all shapes and sizes looking for a sense of community and home. Keeping these diverse demographics in mind, the design trends and appeal of multifamily housing is more crucial now than ever.

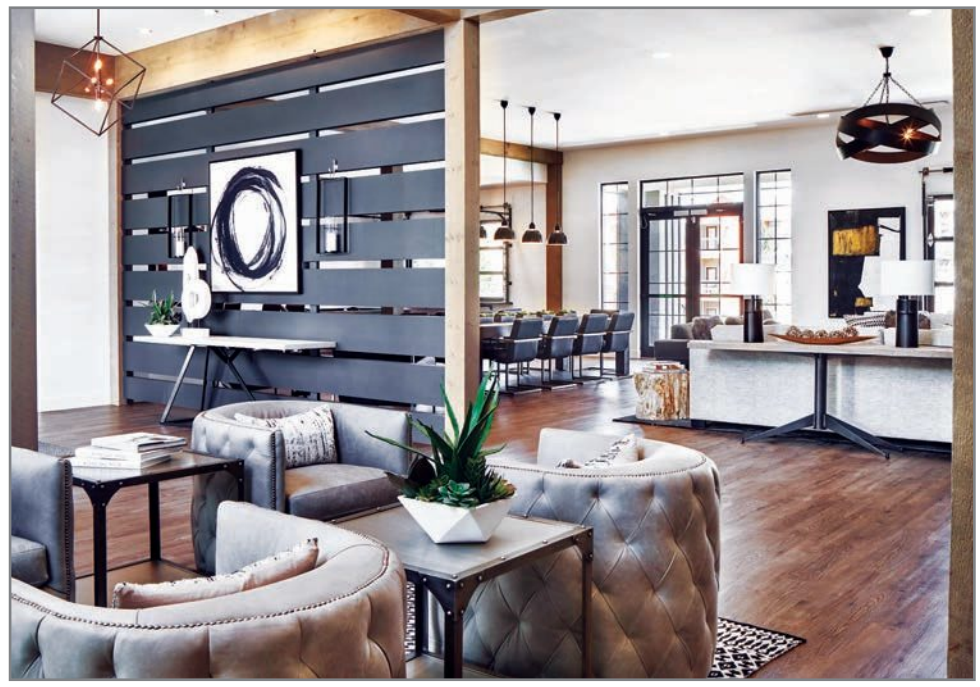
The multifamily housing scene is flourishing across Colorado, and competition for renter's attention is not scarce. Ensuring your property stands out can be vital for success. Below we've shared some ideas and trends to help set your property apart.

• **Amenity spaces.** Amenity spaces are continuing to make a shift in their offerings to stay competitive in the ever-growing market. Past trends have included things such as big theater rooms with popcorn machines and entertainment offerings. Today's multifamily housing is looking to support their tenants through a more practical approach. Sleek community spaces with café-like vibes offering beverage stations with coffee and keg taps, high-speed Wi-Fi and community computers and printers look to accommodate residents who telecommute but may not want to stay in their home all day. Offering a private co-working space or individual offices that can be rented out is another amenity gaining in popularity.

Kristen Terjesen, NCIDQ
Principal designer, Studio 10 Interior Design, Denver

In the past, we saw amenity spaces that were broken up or secluded from one another in a more compartmentalized floorplan. Now it is about creating an open space where the different areas can merge. This vision is achieved through large community tables where folks can host group gatherings, and comfortable lounge areas where all sectors of the family are entertained and relaxed. Further complementing this trend is the recent interest in indoor-outdoor compatible zones; such as an indoor-outdoor bar or game room with the use of a garage door. Accommodating resident's lifestyles remains an active focus as well. Dog washes and dog parks, repair shops for bikes/skis/snowboards, and electric car charging stations are all popular offerings of current day multifamily housing.

• **Design trends.** While in the past we have seen a design focus on bright colors and pop-art effects, we're grateful to report a shift back to natural tones and textures is in the works. Fresh spaces with subtle tones, contrasting light and dark, and textures that work to add a touch of depth are creating the multifamily spaces of the future. Playing with light and keeping it bright works to create this desired natural effect. We are happy to see this shift back into creating a timeless space for a sleek and clean living experience. Additionally, this style lends itself to not needing replacement in three to four years, extending the property's longevity.



David Patterson

Apartment design is shifting back to natural tones and textures, as featured at Urban Farmhouse.

The design focus for shared areas in multifamily housing is all about using textiles to activate the space. For urban settings, we are loving the use of graffiti graphics and bold wall murals. These go great in fitness facilities, hallways and busy areas of the community. Art pieces are bigger and tend to feature a mix of mediums with daring design and bold details. By activating these zones with eye-catching items, a unique and fun atmosphere is created.

• **Finishes.** We all know the design is truly in the details. Creating these fresh, clean living spaces is brought to completion in the finishing touches. What used to be a focus on darker

Please see Terjesen, Page 34

Final Thoughts

Low-budget designs still can have a big impact

After 17 years as an interior designer in Denver and as a Colorado native, I have been witness to all the changes the large influx of people to our state has brought. Clearly, somewhere along the line, we were discovered for our fantastic weather, our beautiful mountains and the seemingly never-ending array of things to do out of doors – or indoors, for that matter. With that, the need for housing, especially affordable housing, has never been so great. Over the years, I have been involved in countless multifamily projects, most in Denver metro and mostly mid- to high-end price points – projects in which the target audience has been savvy and makes buying or renting decisions based on aesthetics along with other factors, demanding high design and a growing list of amenities.

The demands of these projects have taught me what people really want out of their homes and communities; those things are largely the same across the economic spectrum.

"It takes a certain amount of darkness to see the light" is a phrase I was reminded of while wrapping up my most recent project, The Meadows at Montbello, a new four-story affordable senior rental building for the Volunteers of America, supported by public finance partner Colorado Housing and Finance Authority. While installing the common areas, I encountered residents moving in whose overwhelming gratitude was humbling. While I regularly receive

Jennifer Pruett
Senior interior designer, Mandil Inc., Denver

some thanks and general appreciation for the work I do, this was different. These folks expressed something deeper, and I felt that this place was going to mean more to them than simply home.

Low-income people and seniors are among our most vulnerable residents; many have been homeless, near homeless or institutionalized in the past. For them, this building is a new start and an opportunity at normalcy. These are the people whose lives can be changed meaningfully, in some part, by design.

While touring other low-income properties around town as research for this project, it became clear that many of these types of buildings were fulfilling only the basic function of shelter and little or no thought had been given to aesthetics or amenity. I wondered if it was a result of a low budget that drove the outcome, or if it was simply lack of insight into the needs of the population.

In my mind, great design is not a function of a big budget, but rather a result of creative thinking and careful consideration of the end user. While 10 years ago it would've been much harder to design something beautiful on a dime, these days the market is flooded with low-cost/on-trend materials, and

Scott Dressel-Martin/CHFA

The lobby at The Meadows at Montbello, a new four-story affordable senior rental building

many are sustainable to boot. Some low-budget design elements that are part of any building can have significant impact – paint, for instance. Color can instantly transform a space from basic housing to a welcoming home.

Many amenities available to the average apartment dweller are invaluable to this more vulnerable population. And, some of the amenities that have the biggest impact on these communities are the ones we all care about.

- **Connection to nature.** We all crave it, especially in our gorgeous state. The architects responsible for the Montbello project thoughtfully placed the building on the site opposite the already existing building, creating a green space in between – a minipark for residents to gather and soak up the sun. It connects the two buildings as well as creates a verdant space for events and recreation. A little outdoor space goes a long way.
- **Access to technology.** For those seeking jobs, keeping track of family and trying to regain financial stability, this can be critical. Simply utilizing a small space with a few computers to create a business center can easily service those who

Please see Pruett, Page 35

Airbnb

Continued from Page 1

sharing economy and rapid disruption to traditional business models, the resistance of the multifamily industry to Airbnb's inevitable entry into long-term rentals is somewhat alarming. Obvious concerns lie within the archaic liability and regulatory framework that have guided our industry for decades. However, ingenuity is rewarded in the new economy, and proactive landlords able to get ahead of this transformation could reap a tremendous competitive advantage.

The first hurdle to Airbnb's acceptance among landlords is local regulatory policy. Cities across the country have battled Airbnb in the admirable interest of affordable housing preservation. Critics argue Airbnb reduces the rental supply thus driving up rents, an undeniably accurate assessment in small vacation markets like Vail and Aspen. Yet, the correlation falls dramatically in large metro areas where Airbnb accounts for only a fraction of the total housing stock; studies have found virtually no impact on rents in markets with a small percentage of commercial Airbnb rentals (e.g., units rented less than 180 days annually).

No matter the verdict, Denver has taken one of the most progressive and socially sustainable approaches to regulating short-term rentals. As of January, Denver requires hosts to obtain a license to offer short-term rentals with the requirement that the property be the hosts' primary residence. This effectively mitigates many of the negative externalities created by Airbnb by, in theory, eliminating absentee landlords. Airbnb bookings reached an all-time high in Denver in September with a 67 percent (and growing) licensing compliance rate. Looking at the last six months of revenue, Denver stands to collect nearly $11 million in taxes from Airbnb hosts in 2018 – a figure that could balloon if apartments are added to the short-term rental pool.

The primary concerns cited by apartment landlords in regard to short-term rentals are safety (80 percent), liability (74 percent) and quality of life (74 percent), according to a NMHC survey. However, platforms exist to help alleviate some of these concerns. Airbnb conducts background checks on its members and provides host protection insurance through its Friendly Buildings Program. Pillow Residential, a short-term rental compliance start-up, takes this a step further by integrating five layers of liability protection.

While several apartment real estate investment trusts have declined partnering with Airbnb in recent months, Equity Residential is piloting the Friendly Buildings Program on its 554-unit Vista 99 development in San Jose, California, while Ironton has partnered with Airbnb on its 69-story Jersey City Urby deal in New Jersey. In October, Airbnb announced the logical next step in this program with a 324-unit apartment development through a JV with Florida-based Newgard Development Group.

Virtu Investment's Archer Tower property in Denver is an equally compelling case study. Virtu teamed up with Pillow Residential to enable tenants to rent their units on Airbnb, facilitating a revenue-sharing agreement between the owner (10 percent), Pillow (10 to 20 percent) and the tenant (70 to 80 percent). For their share, Pillow coordinates advertisement, key swap and professional cleaning. Virtu is offering residents discounted monthly lease rates in exchange for participation.

The program has received a warm reception from residents at Archer Tower, according to Virtu COO Blake Hayunga. He noted a 20 percent increase in applications since inception with a 50 percent penetration rate on new leases. Hayunga views the program as an amenity that empowers residents to "monetize slack in the economy" where tenants can profit from their empty apartments. While revenues are reinvested in the property, Hayunga also anticipates significant bottom-line improvement through strong occupancy, low turnover and the ability to increase rents while maintaining affordability.

Blake Hayunga, Virtu Investments

Airbnb bookings reached an all-time high in Denver in September with a 67 percent (and growing) licensing compliance rate. Looking at the last six months of revenue, Denver stands to collect nearly $11 million in taxes from Airbnb hosts in 2018.

On any given day, there are numerous Airbnb listings for Class A apartment units in Denver disguised as "downtown condos" with host instructions to avoid interaction with neighbors and management. The nightly Airbnb rate for one of these listings in a popular Lower Downtown high-rise apartment is $399, resulting in host revenues of roughly $299 (after factoring in the 10 percent landlord fee and the 15 percent fee to Pillow). Assuming the tenant rents the unit 15 nights per year, her effective monthly rent declines 16 percent, from $2,291 to $1,917, resulting in annual savings of $4,485. With savings of this magnitude, the competitive advantage gained by an Airbnb-friendly building is truly staggering.

It wasn't long ago where pet-friendly buildings were an industry anomaly. Today, 98 percent of Denver apartments allow pets to some degree as bottom line rewards far offset the inherent risks to landlords. As home sharing becomes an increasingly coveted amenity – synonymous with pet spas and yoga studios – landlords may no longer be able to resist financial incentives created by Airbnb. As the saying goes, if you can't beat them, join them. ▲

Note: After this article was submitted, a Nov. 5 Wall Street Journal article reported that Veritas Investments, San Francisco's largest landlord, is partnering with Pillow Residential and Airbnb to pilot the Friendly Buildings Program.

Duty

Continued from Page 4

environmental site assessments and more, discourage housing construction and raise the cost of those apartment communities that do get built.

In addition to the research, NMHC and NAA also released a report called Our Vision 2030, a set of recommendations for policymakers at all levels of government on how to increase housing production and lower its cost.

The report notes the toolbox of approaches states and localities can take to address the apartment shortage and help reduce the cost of housing. First and foremost, they can adopt local public policies and programs that harness the power of the private sector to make housing affordability more feasible. Some of the options explored in the report are:

- Establish "by-right" housing development;
- Expedite approval for affordably priced apartments;
- Reduce parking requirements;
- Establish density bonuses to encourage affordable housing development;
- Adopt separate rehabilitation codes;
- Counteract not-in-my-backyard movements, commonly referred to as NIMBYism, with an efficient public-engagement process;
- Leverage underutilized land; and
- Waive fees for properties with affordable units.

• **Unleashing economic potential.** What's good for renters is good for everyone. A shortage of affordable housing is a drag on local economies. Moreover, the new apartment construction Denver needs will boost the economy in the coming years.

The combined direct and indirect contribution of 100 existing apartments in Denver, including the local spending of those renters, is $3.8 million and 38 jobs supported. This is not just a problem for today. By 2030, the affordable housing crisis will become even more severe unless public and private sector leaders take bold, innovative action.

The future apartment demand research and Our Vision 2030 are available at www.WeAreApartments.org. Visitors also can use the Apartment Community Estimator – or ACE – a tool that allows users to determine the economic impact of a given number of apartment units in 50 metro areas.▲

Hodge

Continued from Page 6

ods averaged less than 39 months. Post-WWII expansions, including the current one, have averaged almost 62 months. Starting with the creation of the Federal Reserve in 1913, and continuing in 1933 when it went off the gold standard to completely cutting ties to gold in 1971, we've been able to hone our economic skills and sharpen our tools, constantly breaking new ground and learning from our mistakes.

Another thing to point out in the chart is the average gross domestic product growth during these periods. Most economists agree that ideal GDP growth rate is between 2 and 3 percent. Have we finally landed in that sweet spot where we can expect continued steady growth? Look carefully at the last four periods of expansion. If we hadn't acted so foolishly leading up to the financial crisis, could that expansion have lasted longer than the one prior? Who knows, but it sure taught us some valuable lessons, and that's the point. We'll continue to improve in managing the booms and busts that have plagued the past.

During this cycle, Japan and the Euro-zone have flip-flopped between contraction and expansion. With these two major economies now finally in simultaneous expansion along with the U.S., we're just beginning to enter a period of synchronized global growth. The economy at home and abroad appear to be in decent shape, suggesting business as usual. Of course, there are always curveballs, but there's no cure for those. In the movie "Major League", Pedro Cerrano tried to get Jobu to help him hit curve balls by offering cigars and rum … that just doesn't make any sense. There's no reason for us to start doing the same.

Each part of the current cycle has been prolonged, starting with the slow recovery of credit after the crisis. From there, we've gradually expanded leverage, and now the Fed is gradually hiking rates. We've yet to enter the next phases of rising default rates or an overheated economy; in assessing the current situation and nature of this cycle, there's reason to believe those next phases will be prolonged as well, allowing everyone to continue sitting on fastballs in the strike zone. What we're really saying is this cycle still has a lot of room to run.▲

Bailey

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percent of all workers in the region. The current positive trajectory with new jobs in high-skill sectors alongside the statewide in-migration of highly educated people implies that the past reliance on the military is dwindling.

• **Average apartment vacancy: 4 percent**. The bottom-line message from the Q3 Apartment Insights vacancy survey is local rental market stability. The citywide average vacancy rate for Colorado Springs has been consistently within 1 percent above or below the current vacancy rate for over two years.

• **Average apartment rents: $1,020 per month.** Colorado Springs apartments are achieving the highest-rent growth of any Front Range metro area. Rents are growing at a highly consistent rate of between 6 and 9 percent annually since 2014. The current rent reflects a $1.25 per square foot average. Note, the average apartment rents in Denver have increased $700 per month – or doubled – since 2004. Colorado Springs average rents are up only $400 per month during the same period and still have room to rise.

• **New development: 2,500 units.** Colorado Springs has 2,500 apartment units under construction with 2,600 units planned. This compares to Denver's 30,000 apartment units under construction with another 25,000 units planned.

Colorado Springs was late to the party with economic recovery and rent growth. This may prove to insulate Colorado Springs from the over construction that some first-tier cities are experiencing that can result in the painful burst of a bubble. ▲

Denton

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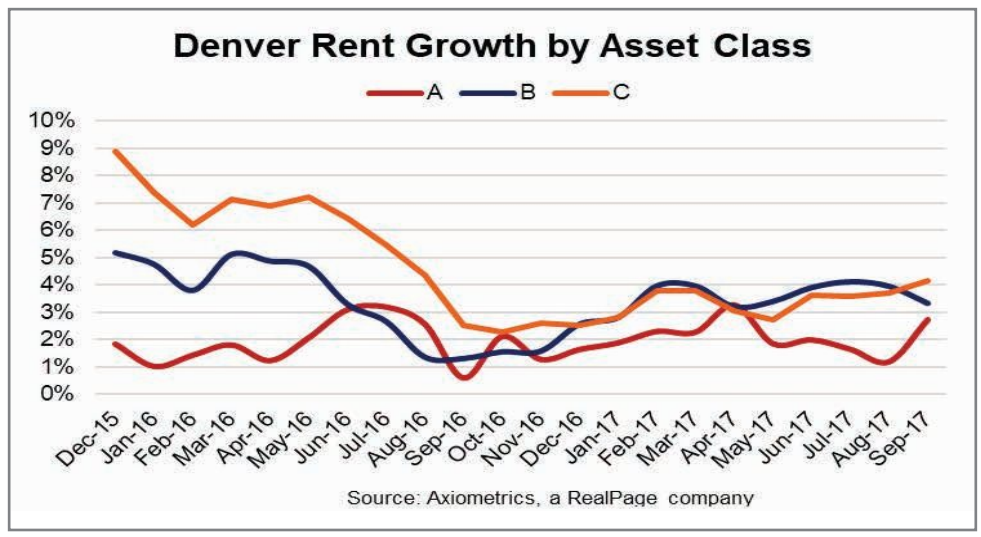
Two other Aurora submarkets recorded the highest rent growth in the area. The 7.3 percent in the Aurora-central-southeast submarket and the 6.6 percent in Aurora-north make the suburb the strongest for apartments in the Denver area. Those two submarkets have just 100 new apartments opening in 2017 – all this quarter in Aurora north.

The total influx of new supply in the Denver metro would mean that in order for rent growth to remain steady in the near future, job growth must step up. We forecast that job growth will increase over the next year, just not to the level of 2015.

In the meantime, annual effective rent growth is expected to average 3.6 percent in 2018, a slight increase from the current 3.1 percent, while occupancy should continue to hover around 95 percent.

Denver has been one of the nation's leading apartment markets since the end of the Great Recession. It just happens to be in somewhat of a lull now. But the attractiveness of the metro to potential residents and growing business opportunities should return Denver to full strength in the next few years.▲



Lodmill

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cost and sales data on several projects in the Denver market to report the level of profit actually achieved. The chart shows where the average sale price on a newly developed asset goes. The average sale price reflects 8 percent paid for the land, 48 percent of hard costs, 14 percent of soft costs and a healthy 30 percent slice of the sale price headed to the developer as profit. When viewed as a return on the lower "all-in" developer costs figure, this indicates a 43 percent rate of profit to the developer, well above the 15 to 25 percent return seen as typical in the market.

This substantial profit slice of the pie is reflective of a short-term market imbalance and not a "normal profit." This atypical profit level has been the carrot to lead developers to our planning departments to discuss their project, with their eyes focused on the pot of gold at the end of the rainbow. However, additional cash flow pressures will further impact pricing due to increased rental concessions, higher vacancy, additional competition on rental rates, greater expense loads, higher tax assessments, etc. As more projects are brought to market under higher cost burdens, this pot of gold will shrink.

The moral to the overall story is that our developer friend has been quite well compensated for past work. The question as to the return to current projects will be answered with time.▲

Lamondin

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were using about 51 gallons per person, per day; after the renovations, each person is using around 33 gallons per day. Beyond the environmental impact of lowering water usage, the multifamily community will continue to save on its mortgage, achieve a rapid return on investment, and increase property profitability and property value through the resulting increase in net operating income.

As utilities and lenders continue to expand green-financing benefits, there is no better time to take advantage of green property investments for your own financial benefit and the environmental benefit of the Colorado community.▲

Terjesen

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accents and dark-stained wood now is moving to a much more natural state. Raw woods used for flooring and trim bring a touch of nature to these bright living spaces, and mixing mediums such as wood and steel creates a modern approach to classic finishes. This balance of dichotomy between materials is a trend we are seeing across properties and styles – playing off the balance of light and dark mentioned earlier. If a mix of wood and steel doesn't do it for you, consider mixing differing metals and tones. One of our favorite finishing details is antique brass, which is a fantastic complementary look for unfinished wood. Pair these together for a crisp finish.

The trends of multifamily housing will continue to change and we will continue to adapt to current residents and their demands. However, answering the call of creating beautiful living spaces for families to call home will always stay fresh and at the forefront of development. Having that "wow" factor for a multifamily housing property ultimately will distinguish it from competitors and set the property apart. We love the direction these trends are moving in and cannot wait to continue working with inspired, fresh ideas.▲

Hatcher

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of building and maintaining roads, sewers, utilities and schools to service new homes. The added population provided by apartments can help support local merchants and restaurants, which make neighborhoods and cities so unique. Apartment living is an environmental and economic win-win.

The state of Colorado is accelerating the green aspects of apartment living by implementing advanced energy and sustainability intensive building codes and action plans, which are applied to apartment communities. Denver, along with many other cities, is setting aggressive targets for sustainability. The city and county of Denver created the 2020 Sustainability and Climate Action Plan, which aims to reduce greenhouse gas emissions below 1990 levels and sets a long-term greenhouse gas reduction goal of reducing emissions 80 percent below 2005 levels by 2050. Denver Water also is pushing for more water-efficiency measures by offering developers incentives and rebate programs focused on landscaping and plumbing fixtures – many of which are most impactful in dense apartment communities.

Colorado developers are adjusting to more stringent energy codes and enforcement. They are aided by a benchmarking ordinance that is in place to assist the improvement and engage building owners. Other priorities of Denver government groups include land use, transportation, and water and its consumption. Through smart, green design, apartment communities, more easily than single-family homes, can assist Colorado in achieving its goals. And this is what our Green Manifesto is all about. Its principles have helped our company invest in these beneficial changes to the Colorado landscape.▲

Willis

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compared with only a 27 percent increase in labor force. While some may question why a developer would choose to limit the rental pool to only those over 55 – actually, the average tenant is closer to 72 years old – these renters tend to stay for longer periods of time, typically about seven years, reducing turnover costs associated with younger, more transient renters. The KTGY-designed Vita for Zocalo Community Development, a 55+ community in Littleton, addresses the empty nester, down-sizer and retiring baby boomer generation.

Luxury condominiums are becoming more attractive and we've seen projects shift from apartments to condos because developers simply couldn't achieve the desired returns by building a rental community on the site. Such was the case for Metropolitan Homes at Boulevard One in the Lowry neighborhood.

• **Transit-oriented development for living and working.** The public investment in the continued expansion of Denver's FasTracks rail system has resulted in a building boom of sorts around many stations. The common wisdom is that if you can't afford to live downtown, you can at least be connected to it – and the rest of the Denver metro – for work or entertainment purposes. In addition to lower housing costs than comparable units downtown, this type of location can reduce or eliminate expenses associated with owning a vehicle, adding to the value proposition.

The rising number of work-from-home professionals has driven the creation of next-level live/work spaces that go beyond the traditional business center found in many residential communities. TriVista on Speer, for example, includes four ground-floor, storefront-style live/work units. Each 1,490-square-foot space is split into two levels: a fully open first floor with a half bath – ideal for a home-based business – and a second-level living quarters with one bedroom and one bath. While these renters may not need access to transit for a daily commute, they still want to be connected to nightlife, entertainment, culture and recreation.

Going into 2018, trends likely to impact the state of multifamily housing in Denver include demographic shifts, land availability and a movement toward outlying neighborhoods. More than ever, architects and developers will need to continue to deliver stand-out communities that incorporate timeless design aesthetics and built-in service and convenience, but at an ever-increasing density … even in the suburbs.▲

Pruett

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may not be able to afford their own.

• **Community rooms.** These are dynamic spaces that can be used for many functions, like movie nights, sports events and parties. They also can create minicommunities within a larger space. Lounges placed on each floor of a multistory building can provide a social space for those sharing the floor and feel like an extension of their own homes, fostering socialization and building relationships.

• **Aesthetics.** While it may not be an amenity per se, the aesthetic of a space can transform the well-being of those within. We experience a space with all our senses, so by using materials that not only look inviting, but also feel soft to the touch and welcome us in are crucial. Lighting also plays a critical role in this category, and while security is likely an important factor and some fluorescent lighting may be necessary, other layers of light can be added to tone down an institutional vibe. Chandeliers, lamp lighting and keeping the ambient lighting at 2700K (warm white) can effectively warm up a space.

• **Curb appeal.** The exterior of the building can play a role in the happiness of its residents as well. Who doesn't want a little curb appeal? Many of these buildings often are positioned within communities that are becoming increasingly higher end and a sense of fitting in is imperative.

In the end, when we lift those who are at the bottom, we all benefit. I am grateful to have participated in a project that had a meaningful impact on those most in need. Take this project as a step toward good design earning a permanent home in low-income housing and a way to share a little love for all.▲