

MARKETBEAT SACRAMENTO

Office Q1 2021



YOY
Chg

12-Mo.
Forecast

12.6%

Vacancy Rate



51K

Net Absorption, SF



\$2.15

Asking Rent, PSF



(Overall, All Property Classes)

ECONOMIC INDICATORS Q1 2021

YOY
Chg

12-Mo.
Forecast

968.5K

Sacramento MSA
Employment



7.3%

Sacramento MSA
Unemployment Rate



6.0%

U.S.
Unemployment Rate



Source: BLS

ECONOMY OVERVIEW: Local Economy Outlook is Cautiously Optimistic

Sacramento is recovering from the impact of the COVID-19 pandemic with the region seeing improving signs of economic life as restrictions begin to lift. With that said, the market's unemployment rate remains elevated reaching 7.3% during the first quarter of 2021, up 360 basis points (bps) year-over-year (YOY). But, the total impact of the pandemic to date has been less than was initially feared.

DEMAND: Demand slows with economic shutdown

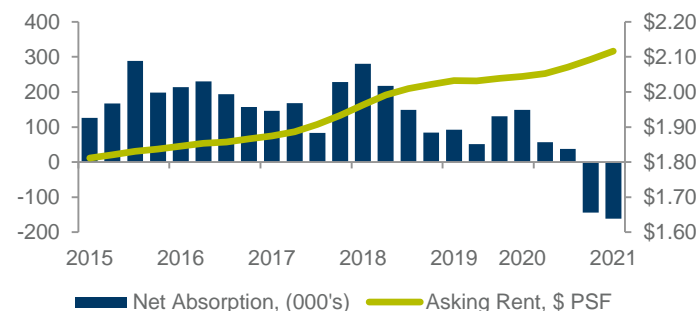
The first quarter of 2021 ended with positive net absorption, totaling 51,000 square feet (sf). The first positive total in the last three periods. However, this was almost entirely due to the completion of Centene's 513,000 sf building for their new headquarters in North Natomas. The balance of market activity totaled -462,000 sf, with Downtown reporting -125,000 sf to start the new year.

The long-term impact of COVID-19 on the office market is becoming clearer. While most tenants recognize the continued need for office space, they are reducing their footprint and shifting towards a hybrid real estate strategy by either allowing a portion of their workforce to go remote permanently or adopting a rotating workforce that comes in a reduced number of days. The result is an increased number of tenants in the market but with smaller requirements in terms of square footage. For example, the market currently has 87 tenant requirements for an average size of 17,000 sf compared to the market's peak in the fourth quarter of 2019 which had 68 requirements with an average size of 31,000 sf.

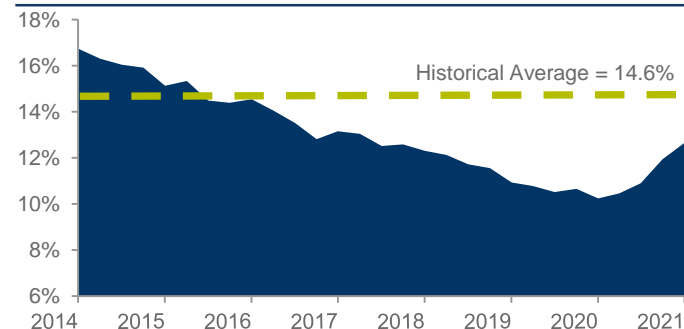
PRICING: Asking rents show signs of stabilization

Lease rates remained stable increasing by only \$0.02 during the quarter to \$2.15 per square foot per month on a full-service gross basis. Year-over-year rates are up \$0.10 (4.7%). Asking rates are largely inflated as landlords are hesitant to lower a building's rate to compete on price. This trend is not expected to continue for much longer as competition for quality tenants of size grows. While a pricing correction is likely, lease rates are not expected to fall as much as they did during the Great Financial Crisis as market vacancy is consistent with recent historical averages and most tenants demonstrate a continued need for office space.

Overall Net Absorption/Overall Asking Rent / 4 Qtr Trailing Average



Overall Vacancy



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Office Q1 2021



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SUPPLY

The vacancy rate increased by 90 bps quarter-over-quarter (QOQ) and 240 bps YOY ending the first quarter of 2021 at 12.6%. Despite the rapid rise in supply, market vacancy sits at mid 2017 levels and is well below the worst point of the Great Financial Crisis of 20.7% in the fourth quarter of 2011.

Prior to the first quarter, sublease activity had relatively little impact on the market. While no large companies have left the region as a result of the pandemic, many are taking the opportunity to reevaluate their real estate needs and reducing their office footprint. However, Sacramento remains in a much better situation than neighboring markets as the increase in sublease space is not expected to continue beyond the near term.

CAPITAL MARKETS

Sales volume totaled just \$76 million during the first quarter of 2021, down from \$124 million in the prior period. But once again, property values have not eroded and remain in line with pre-pandemic levels on a per square foot basis, averaging \$188 psf.

Sales volume is expected to increase significantly in the coming periods, as large projects like the 373,725 sf Ziggurat building at 707 3rd St in West Sacramento are back on the market.

MARKET OVERVIEW

Market activity is starting to increase as the economy reopens and tenants recognize the need for office space although often in a different footprint than they previously occupied. Overall, the impact of the pandemic on the Sacramento office market has been less than initially feared.

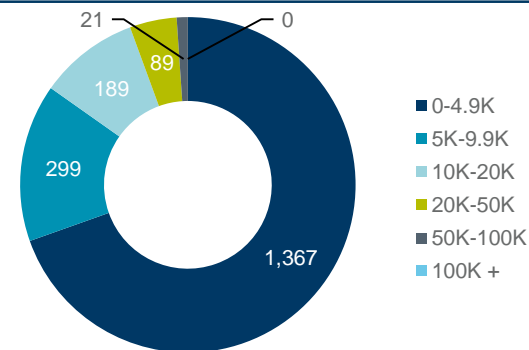
While it will likely take some time for market fundamentals to reflect growth once again, there are continued reasons for optimism. For example, new developments like Aggie Square continue to draw interest with the promise of new tenants and employment growth and vacancy remains largely in line with historical averages.

OUTLOOK

- Tenants active in the market but on a smaller footprint, likely leading to increasing vacancy in the near term
- With increasing vacancy landlords will be more willing to compete on price leading to decreases in the overall asking rate.
- Beyond the short-term, recovery will be tied to occupier and employee willingness to return to the office. If companies find synergy and innovation is lacking in a remote environment, they will be incentivized to return sooner.

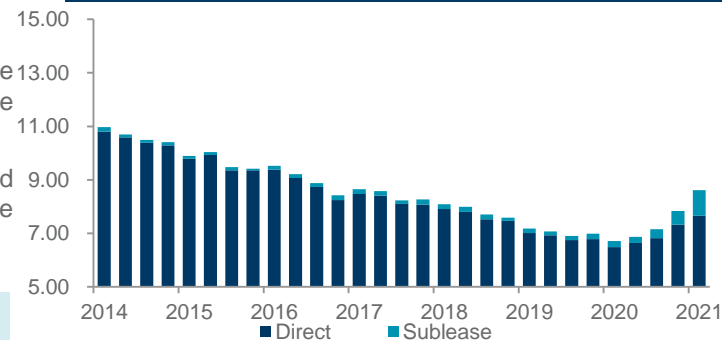
Availabilities by Size Segment

OVERALL AVAILABILITIES IN ONE SUITE



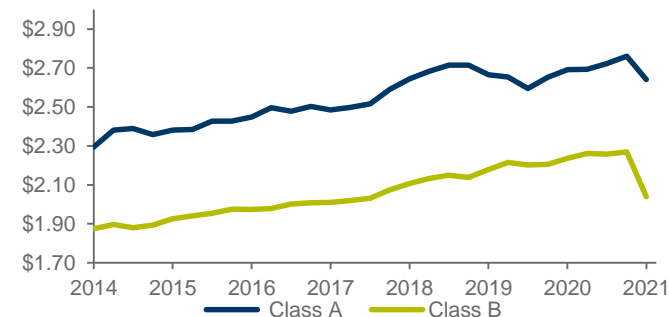
Direct vs. Sublease Space Available Comparison

SUBLEASE SPACE STARTING TO INCREASE



Average Asking Rate by Class (Full Service)

CLASS A & CLASS B RENTS BEGIN CORRECTION



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MARKET STATISTICS

| SUBMARKET | INVENTORY (SF) | SUBLET VACANT (SF) | DIRECT VACANT (SF) | OVERALL VACANCY RATE | CURRENT QTR OVERALL NET ABSORPTION | YTD OVERALL NET ABSORPTION (SF) | YTD LEASING ACTIVITY (SF)** | UNDER CNSTR (SF) | OVERALL AVG ASKING RENT (ALL CLASSES)* | OVERALL AVG ASKING RENT (CLASS A)* |
|------------------------------|-------------------|--------------------|--------------------|----------------------|------------------------------------|---------------------------------|-----------------------------|------------------|--|------------------------------------|
| Downtown Sacramento | 11,752,711 | 39,908 | 1,383,292 | 12.1% | -124,648 | -124,648 | 24,879 | 0 | \$3.30 | \$3.53 |
| Campus Commons | 1,555,623 | 15,575 | 218,896 | 15.1% | 3,062 | 3,062 | 11,021 | 0 | \$2.36 | \$2.65 |
| Carmichael / Fair Oaks | 837,893 | 0 | 146,493 | 17.5% | 26,192 | 26,192 | 3,637 | 0 | N/A | N/A |
| Citrus Heights / Orangeville | 1,415,040 | 9,030 | 132,730 | 10.0% | 7,064 | 7,064 | 9,022 | 0 | \$1.51 | N/A |
| Auburn / Lincoln | 1,253,531 | 0 | 67,657 | 5.4% | -3,658 | -3,658 | 5,779 | 0 | \$1.72 | N/A |
| Davis/Woodland | 1,952,410 | 13,640 | 100,250 | 5.8% | 28,085 | 28,085 | 10,458 | 0 | \$1.99 | N/A |
| East Sacramento | 1,214,549 | 0 | 3,889 | 0.3% | 1,396 | 1,396 | 0 | 0 | \$3.00 | N/A |
| El Dorado Hills | 1,542,655 | 0 | 187,220 | 12.1% | -14,259 | -14,259 | 18,416 | 0 | \$2.05 | N/A |
| Elk Grove | 1,298,6003 | 3,025 | 49,889 | 4.1% | 15,382 | 15,382 | 5,682 | 0 | \$2.25 | \$1.89 |
| Folsom | 3,362,240 | 91,117 | 267,627 | 10.7% | 47,578 | 47,578 | 9,190 | 0 | \$2.33 | \$2.18 |
| Highway 50 / Rancho Cordova | 12,758,997 | 448,829 | 1,742,863 | 17.2% | -146,091 | -146,091 | 116,556 | 0 | \$1.82 | \$2.07 |
| Howe Ave / Fulton Ave | 3,364,149 | 7,675 | 612,650 | 18.4% | -4,407 | -4,407 | 26,345 | 0 | \$1.64 | \$2.22 |
| Midtown | 2,790,550 | 6,363 | 294,307 | 10.8% | -37,101 | -37,101 | 34,584 | 0 | \$2.18 | N/A |
| North Natomas | 3,090,272 | 40,397 | 325,393 | 11.8% | 496,724 | 496,724 | 27,123 | 0 | \$1.64 | \$2.21 |
| Point West | 2,538,320 | 5,511 | 278,610 | 11.2% | -6,874 | -6,874 | 17,891 | 0 | \$2.03 | \$2.15 |
| Roseville / Rocklin | 10,082,963 | 259,119 | 1,164,692 | 14.1% | -171,272 | -171,272 | 76,891 | 0 | \$1.79 | \$2.23 |
| South Natomas | 3,305,861 | 15,536 | 497,544 | 15.5% | -105,944 | -105,944 | 11,201 | 0 | \$2.32 | \$2.34 |
| South Sacramento | 2,136,710 | 2,795 | 148,589 | 7.1% | 34,441 | 34,441 | 5,519 | 0 | \$1.69 | N/A |
| West Sacramento | 2,006,062 | 0 | 32,372 | 1.6% | 4,870 | 4,870 | 0 | 0 | N/A | N/A |
| Market Totals | 68,259,145 | 985,520 | 7,654,963 | 12.6% | 50,540 | 50,540 | 414,191 | 0 | \$2.15 | \$2.64 |

KEY LEASE TRANSACTIONS Q1 2021

| PROPERTY | SUBMARKET | TENANT | RSF | TYPE |
|-------------------------------------|---------------|-----------------------------|--------|-----------|
| 2880 Gateway Oaks Dr, Sacramento | South Natomas | State of CA – Dept of Aging | 48,808 | New Lease |
| 1610 Arden Way, Sacramento | Point West | SSA Office of Disabilities | 26,958 | Renewal |
| 428 J St, Sacramento | Downtown | Trifecta | 20,584 | Renewal |
| 10540 White Rock Rd, Rancho Cordova | Highway 50 | Child Action USA, Inc | 22,521 | New Lease |

KEY SALES TRANSACTIONS Q1 2021

| PROPERTY | SUBMARKET | SELLER / BUYER | SF | PRICE/\$ PSF |
|---------------------------------------|-------------------|---|---------|---------------|
| Olympus Corporate Center, Roseville | Roseville/Rocklin | Barker Pacific Group / KB Property Advisors | 196,467 | \$45.5M/\$232 |
| 1300 U St, Sacramento | Downtown | Fernbacher-Herzog-Ziegler, LLC / Clippinger Investment Properties | 47,541 | \$9.87M/\$208 |
| 1401 21 st St., Sacramento | Midtown | Tarigo Family Holding Co. / Friendly Grizzly, Co | 26,440 | \$4.95M/\$187 |

*Rental rates reflect full service asking **Renewals included in leasing statistics

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