



Retail Report

Q2 2016
GALLELLI REAL ESTATE MARKET REPORT

Overview

The Sacramento retail market saw a slight uptick in vacancy during Q2 2016, as a number of corporate retailer closures hit the market. Regional shopping center vacancy stood at 10.6% at the end of Q2, reflecting a small increase over the 10.5% rate recorded in Q1. Vacancy has wavered within the 10.0% range for the last four consecutive quarters - one year ago, this metric stood at 10.8%. The vacancies of Kmart in Citrus Heights, Save Mart in Orangevale and all three local Sport Chalets (in Roseville, Arden and Elk Grove) were the primary culprits behind the vacancy increase. These vacancies helped to push quarterly net absorption into the red to the tune of 27,000 square feet. When added to the over 150,000 square feet Macy's vacated in Q1, these vacancies also helped to push year-to-date net absorption figures into the negative, with the market losing a total of 94,000 square feet.

The good news, however, is that these vacancies are the result of corporate failures rather than a failing regional market. Regional leasing activity is strong and the market also saw a number of larger occupancies during Q2 which prevented a larger vacancy increase. Fitness Evolution moved into nearly 40,000 square feet in South Sacramento, while 99 Ranch Market took occupancy of 31,000 square feet in Folsom. Leasing momentum increased during Q2, with the market recording nearly 784,000 square feet of deals. Year-to-date, 1.4 million square feet of retail leases have been signed, which is increased over the same time period last year, which recorded 1.1 million square feet of leases signed.



Market Trends

- Positive and negative absorption was spread evenly across the local submarkets. The largest occupancy gains were seen in the South Sacramento, Highway 50 and Folsom submarkets, which all recorded positive net absorption in excess of 40,000 square feet. The largest losses were seen in the Carmichael/Citrus Heights/Fair Oaks, Rio Linda/North Highlands and Arden/Watt Howe submarkets, respectively.
- Fitness centers, discount retailers and fast casual restaurants continue to be very active in the local marketplace.
- The average asking rate for retail space saw a slight uptick during Q2, increasing from \$17.06 to \$17.19 per square foot, on an annual, NNN basis.
- The average asking rate for Class A specialty centers remained at \$26.16 per square foot. Asking rates for strip centers currently stand at \$15.42 per square foot; neighborhood and community centers are commanding \$16.73; and regional/power centers are asking \$15.49 per square foot, on an annual, NNN basis.*

*Average asking rates are based upon publically quoted rents; withheld rents are not included in survey.

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Retail Q2 2016

A number of retail closures hit the market in Q1 and Q2, which has helped to push vacancy upwards.

<p>Vacancy</p> <p>10.6%</p> <p>▲</p>	<p>Net Absorption</p> <p>-27,301</p> <p>▲</p>	<p>Avg. Asking Rate</p> <p>\$17.19 PSF</p> <p>▲</p>
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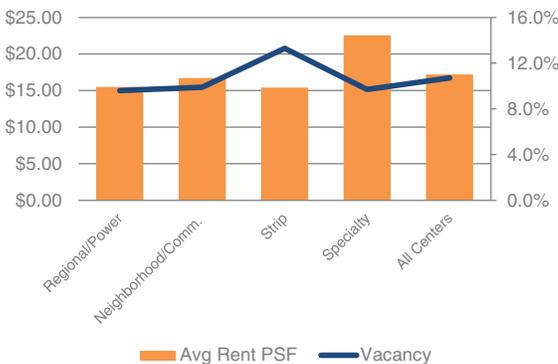
Investment Highlights

- Retail investment activity slowed during Q2, as the market recorded \$113 million in transactional volume, which is down from the \$144 million that was recorded during Q1.
- The average price per square foot declined from \$199 in Q1 to \$173 in Q2.
- The average asking cap rate for retail investments went from 6.9% during Q1 to 6.2% during Q2.
- Year-to-date, the Sacramento retail market has recorded \$257 million in transactional volume.
- The largest retail investment sale of the quarter was the sale of Sierra Oaks Plaza at Douglas Blvd and Sierra College Blvd in Roseville for \$28.1 million at a 5.72% CAP rate.

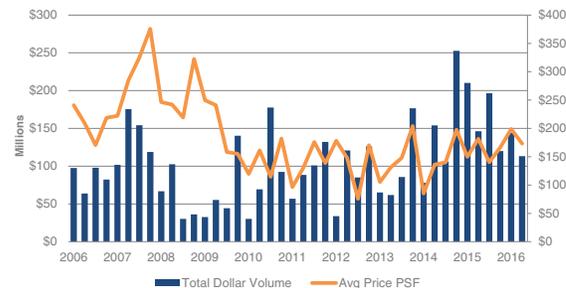
Retail Vacancy vs. Net Absorption



Vacancy & Avg Price PSF by Retail Center Type



Retail Investment Sales Volume





Construction
976,691 ^{SF}
 ▲

Sacramento Unemployment
5.6%
 ▲

US Unemployment
4.9%
 ▼

Class A Market Trends

- Vacancy in Sacramento's Class A centers currently stands at 7.2% which is below the overall regional vacancy rate of 10.6%.
- Net absorption for Class A space was positive for the quarter, recording over 55,000 square feet of occupancy growth.
- The overall average asking rate for Class A centers in Sacramento is \$26.16 per square foot, on an annual, NNN basis. However, shop rents at Class A centers in high-demand submarkets such as Roseville/Rocklin and Folsom have been much higher, with asking rates at \$36.00 per square foot, per year. The Folsom submarket currently has the highest average asking rate at \$33.60 per square foot, per year.
- High-quality, Class A availabilities are beginning to decline, as Class A remains a hot commodity for national tenants. As competition for these spaces increases and vacancy continues to decline, we will begin to see incremental increases in Class A rental rates, particularly in higher-profile markets like Roseville/Rocklin and Folsom.

Outlook

Until recently, local retail shopping center vacancy had been on the decline, but a number of retail closures hit the market in Q1 and Q2, which has helped to push vacancy upwards. Unfortunately, there are still more closures to come, as it was confirmed in Q2 that Sports Authority would be closing all of their stores. Sports Authority has six locations in the Sacramento region that total over 241,000 square feet. Dick's Sporting Goods bid for and won the leases for two of these locations, in Roseville and Elk Grove, but subtracting these locations still leaves over 150,000 square feet going back to the market. The good news is that regional retail leasing activity remains strong – the market has seen over 1.4 million square feet of leasing activity during the first half of the year, which should help to absorb some of the impact of the large vacancies, once these tenants occupy.

Research

Our team focuses on providing high quality, data driven, accurate market information to our clients. We provide in-depth commercial real estate market analysis and insight into market trends in order to help optimize our clients' real estate decisions.

Market Statistics

Submarket	Inventory	Direct	Available Space Sublease	Total	Vacancy Q2-16	Net Absorption		SF Under Construction	Avg. Asking Rate (NNN)
						Q2-16	Q2-15		
Arden/Watt/Howe	5,838,095	1,107,430	29,802	1,137,232	19.5%	(35,078)	(101,593)	116,955	\$16.56
Auburn/Lincoln/Loomis	2,626,105	177,907	6,900	184,807	7.0%	13,006	13,068	12,000	\$18.49
Carmichael/Citrus Heights/Orangevale	6,622,886	791,090	75,100	866,190	13.1%	(99,329)	3,707	28,362	\$15.42
Davis	1,046,302	58,424	0	58,424	5.6%	7,201	(16,984)	0	\$20.34
Downtown/Midtown	1,349,079	49,857	0	49,857	3.7%	3,589	(1,070)	279,860	\$16.93
El Dorado	2,500,291	212,291	4,050	216,341	8.7%	17,337	(1,992)	0	\$19.74
Elk Grove	4,493,859	251,059	8,543	259,602	5.8%	(27,105)	46,193	519,414	\$18.95
Folsom	4,648,672	333,919	1,544	335,463	7.2%	49,510	16,260	8,200	\$21.50
Highway 50	3,246,034	505,437	10,021	515,458	15.9%	56,369	17,867	0	\$13.68
Natomas	3,130,823	272,620	6,874	279,494	8.9%	(9,535)	5,451	0	\$20.21
Rio Linda/North Highlands	2,912,762	464,138	10,276	474,414	16.3%	(43,999)	15,801	2,200	\$13.03
Roseville/Rocklin	10,567,598	928,896	4,674	933,570	8.8%	(21,364)	46,034	9,700	\$17.21
South Sacramento	7,555,190	862,065	0	862,065	11.4%	64,433	93,145	0	\$15.27
West Sacramento	1,789,882	54,273	0	54,273	3.0%	5,772	(2,325)	0	\$18.53
Woodland	2,258,644	206,255	0	206,255	9.1%	(8,108)	(8,756)	0	\$12.01
Totals	60,586,222	6,275,661	157,784	6,433,445	10.6%	(27,301)	124,806	976,691	\$17.19

About Gallelli Real Estate

Gallelli Real Estate is a boutique firm that specializes in commercial estate services and property management. We believe that as a boutique firm whose understanding of the business runs as deep as our core values, our advantage is large. We take pride in our unique approach to offer more individual solutions that address the ever changing needs of our clients and the industry. After all, our success is measured by the success of our clients and the strength and longevity of our relationships. For the latest news from Gallelli Real Estate, visit GallelliRE.com, or follow us on Twitter @Gallelli_RE and LinkedIn.

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