



Q1

RETAIL MARKET REPORT

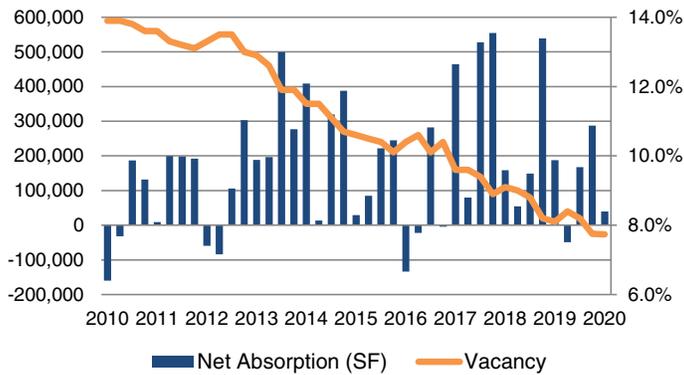
MARKET OVERVIEW

Sacramento's retail market entered 2020 with record-low vacancy and solid tailwinds, but unparalleled disruption has put much of the industry in dire straits. Covid-19 has hit retail tenants and landlords harder than any other commercial sector, and aside from grocers and other essential goods providers, it has turned what is a historically slow (yet momentum-building) start to the year into a harsh first glimpse of what may be a long and arduous road to recovery.

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MARKET TRENDS

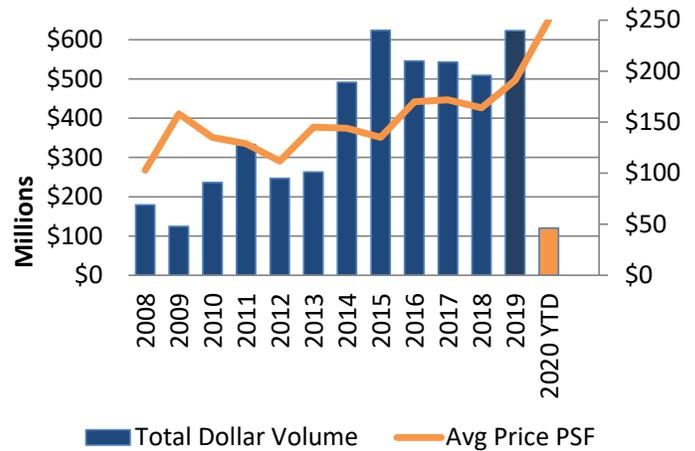
Retail Vacancy vs. Net Absorption



- Vacancy rates managed to creep down by a single basis point from Q4 to 7.7% and set another regional-low thanks to early activity, but demand will undoubtedly wane in coming quarters and a significant spike is expected.
- The region saw just ±40,030 square feet of positive net absorption in Q1, remaining positive as ten of the region’s fifteen submarkets recorded positively, but coming in as the third lowest quarterly total in the past four years.
 - Carmichael/Fair Oaks/Orangevale had the highest quarterly total with ±41,269 square feet of positive net absorption.
- Asking rates were flat to start the year, averaging \$17.88 NNN per square foot monthly in Q1 after a modest increase of \$0.06 per square foot year-over-year.
 - The Downtown/Midtown submarket continues to ride tailwinds from the wave of development which has rejuvenated the urban core, averaging \$31.52 per square foot asking, over 45% above second place Davis which had the next highest average asking rate of \$21.59 per square foot.
- The first quarter is a consistently slow time for new deals, but this year was particularly sluggish as the region saw just ±349,548 square feet of leasing activity, the lowest quarterly total since Q1 of 2009.
 - Roseville/Rocklin led all submarkets with just under 61,000 square feet of deals signed, but they were all for smaller spaces and none exceeded 3,500 square feet.
- Discount retailers continue to drive major leasing activity in the region and accounted for the five largest new leases executed in Q1.
 - That’s Cheap topped the list with their lease of ±24,985 square feet at Country Club Plaza in Arden/Watt/Howe, followed by Ross Dress for Less agreeing to lease ±23,557 square feet in Elk Grove at Laguna Crossroads with plans to open this Fall.

INVESTMENT HIGHLIGHTS

Retail Investment Sales Volume



- The Sacramento region had an understandably lackluster quarter for retail investment, seeing just shy of \$120.4 million in sales as current events led many parties to either sit back and wait or hit pause on current transactions.
 - Average sale price increased more than 10% year-over-year to \$249.98 per square foot, although overall sales volume saw more than a 27% from Q1 2019.
- This marked only the third quarter in nearly seven years where just a single retail transaction surpassed \$10 million, with Nissan of Sacramento at 2820 Auburn Blvd changing hands for \$11.1 million in the Arden/Watt/Howe submarket.
 - Three of the quarter’s five largest sales were car dealerships, including the top two, as the lack of traditional retail entering and changing hands in the marketplace speaks volumes to the level of uncertainty shared by parties on both sides.
- The average cap rate in Q1 was 6.4%, unchanged year-over-year, and will likely rise due to the effects on the economy caused by the pandemic. Cap rates should remain stable on single tenant retail uses that are both financially strong and prove to be resistant to this pandemic.

7.7%



Vacancy

±40,030 SF



Net Absorption

\$17.88



Avg. Asking Rate
(Annual NNN)

±252,654 SF



Construction

4.7%



Sacramento
Unemployment

4.4%



United States
Unemployment

SPOTLIGHT ON: COVID-19 FIRST TAKE

The retail market is in uncharted waters, both locally and globally, and although widespread economic shutdowns will lead to the unfortunate shuttering of countless retailers, the sector looks poised to bounce back in a productive fashion once shops can re-open. Large-scale closures have dominated headlines for many years, and this will surely push additional overstretched retailers past the breaking point, but quality tenants will survive. Those with the foresight to discuss proactive solutions with their landlords are likely to come out of this on solid ground via extended lease terms, amortizing deferred rent, and various other mutually agreeable solutions. Stimulus packages will hopefully keep most at-risk businesses afloat, but the first quarter was two thirds over before widespread stay-at-home orders came into play, so the coming months will be the true test for the overall retail industry.

OUTLOOK

The true extent of this crisis will begin to reveal itself in the coming quarter, so for now the retail industry must weather the storm and do everything it can to reopen quickly and responsibly once stay-at-home orders are lifted. That timeline will vary across different communities, but inevitable changes are likely going to affect retailers for some time. Restaurants will continue to hurt, as dramatically reduced occupancy limits and strict protocols will take its toll on profits, but they will adapt, and well-suited establishments will survive. Vacancy rates are predicted to jump as much as 10% over the coming year but are expected to make a quick recovery once the economy and consumer sentiment rebound. It may seem easy and understandable to forecast gloom in such uncertain times, but the retail industry is resilient and will certainly rally once this crisis is brought under control.

There will be many small business tenants that will not reopen or fail in the near future. This will drive a number of centers that are not well located and well leased into foreclosure. Due to the pandemic and how the government reacts, the timing of these foreclosures and subsequent value add opportunities are unknown. Well located centers especially those anchored by quality tenants will fair well as tenants will flee to quality as will investors.

Retail Market Statistics

Submarket	Inventory	Direct	Available Space Sublease	Total	Vacancy Q1-20	Net Absorption		SF Under Construction	Avg. Asking Rate (NNN)*
						Q1-20	Q1-19		
Arden/Watt/Howe	7,086,687	720,412	0	720,412	10.2%	12,021	(30,743)	0	\$15.13
Auburn/Lincoln/Loomis	3,061,636	121,579	8,278	129,857	4.2%	1,447	(19,423)	0	\$17.94
Carmichael/Citrus Heights/Orangevale	7,865,701	850,723	48,917	899,640	11.4%	41,269	(32,975)	0	\$15.98
Davis	1,055,612	72,902	21,609	94,511	9.0%	(37,218)	5,502	0	\$21.59
Downtown/Midtown/East Sacramento	1,588,913	89,707	0	89,707	5.6%	12,843	59,992	0	\$31.52
El Dorado Hills	2,479,065	156,692	0	156,692	6.3%	6,710	5,319	100,712	\$20.92
Elk Grove	4,466,444	250,685	0	250,685	5.6%	(35,180)	40,211	20,813	\$20.32
Folsom	4,406,779	246,501	2,020	248,521	5.6%	15,471	37,182	0	\$20.35
Highway 50	3,488,964	455,880	10,021	465,901	13.4%	(178)	(58,690)	0	\$15.58
Natomas	3,091,573	164,175	0	164,175	5.3%	19,991	22,616	0	\$20.86
Rio Linda/North Highlands	2,901,886	197,517	0	197,517	6.8%	18,186	(17,621)	0	\$13.39
Roseville/Rocklin	11,158,880	644,767	6,701	651,468	5.8%	(18,882)	94,990	9,629	\$19.20
South Sacramento	8,289,750	647,627	74,410	722,037	8.7%	(20,995)	88,102	115,000	\$15.89
West Sacramento	1,819,922	58,361	0	58,361	3.2%	20,738	1,394	0	\$18.11
Woodland	2,227,423	172,379	7,500	179,879	8.1%	3,807	(8,352)	6,500	\$14.50
Totals	64,989,235	4,849,907	179,456	5,029,363	7.7%	40,030	187,504	252,654	\$17.88

About Gallelli Real Estate

Gallelli Real Estate is a private firm that specializes in commercial real 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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