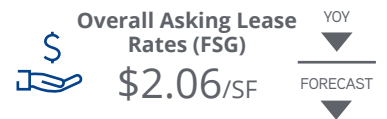


## Key Takeaways

- The market vacancy rate has increased for seven consecutive quarters and finished 2021 at 16.7%, its highest point since Q3 2015.
- Annual net absorption was -1.47 MSF. Since the end of Q1 2020, nearly 2.15 MSF (3.7% of inventory) of vacant space has been added back to the market.
- Market average asking rents have been unchanged for three straight quarters. Downtown Class A rents have begun to stabilize while Suburban Class A rents dropped 2.4% year-over-year.
- Quarterly sales volume of \$218.7 million was well above the post-pandemic quarterly average. Second half 2021 sales volume of nearly \$589 million signals a return to pre-pandemic investor appetite for office assets.



# Sacramento Office 21Q4



## A Challenging Year with Hope on the Horizon in 2022

2021 was a tough year for Sacramento's office market. Annual net absorption recorded its lowest total in 23 years as companies and public sector agencies continue to downsize, consolidate, or give back space altogether. While the national office market posted its first quarter of positive net absorption since the start of the pandemic in the third quarter, Sacramento has seen seven straight quarters of negative demand and rising vacancy rates. The State of California accounted for a majority of occupancy losses in the fourth quarter as it continues to consolidate and move out of leased space into owned new construction. Though the market's fundamentals softened throughout the year, some large leases are due to commence in the first half of 2022 and buyer interest in Sacramento has led to increased investment activity in the second half of the year. While the overall occupancy trend remains negative, there are signs of stabilization starting to materialize as many companies prepare for a return to the office in early 2022.

## Market Indicators



## Historic Comparison

	20Q4	21Q3	21Q4
Total Inventory SF	57,962,097	58,095,178	57,934,337
New Supply SF	519,800	0	0
Net Absorption SF	-466,405	-244,397	-252,525
Overall Vacancy	14.9%	16.5%	16.7%
Under Construction SF	0	0	0
Overall Asking Lease Rates (FSG)	\$2.07	\$2.06	\$2.06

## Market Fundamentals



Sacramento's office market vacancy rate rose to 16.7 percent in Q4 2021, which is up 360 basis points from Q1 2020. Net absorption stayed significantly negative at -252,525 square feet in Q4 2021, however, the average net absorption from the last two quarters was about half the amount of occupancy losses recorded from Q4 2020 through Q1 2021. The road to recovery is beginning even as tenants continue to downsize and consolidate, but the lack of new supply, swelling labor pool, and spiking capital funding of local companies should aid in the market's return to form by the second half of 2022.

## Recent Transactions

 <b>Renewal</b> 101 Creekside Ridge Court Roseville   29K SF	 <b>Renewal</b> 555 Capitol Mall Downtown   27K SF	 <b>Renewal</b> 2998 Douglas Boulevard Roseville   17K SF	 <b>Lease</b> Elks Tower Downtown   15K SF	 <b>Sale</b> Parkshore Plaza Folsom   \$266/SF	 <b>Sale</b> 620 Roseville Parkway Roseville   \$165/SF
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## Absorption & Demand

Annual net absorption in 2021 of -1,471,819 square feet was nearly three times as low as 2020 and the lowest amount of demand recorded since 1998. It is likely that the worst of the market's downturn is behind us as many major vacancies have already been added to the market. Still, private sector companies and public sector tenants continue to implement hybrid work strategies which will likely hamper demand for office space in 2022 and beyond. The Department of Conservation vacated approximately 147,000 square feet from 801 K Street in Downtown Sacramento this quarter as it moved into the new Natural Resources Building. The State of California accounted for 84 percent of occupancy losses during the fourth quarter. Highway 50 East posted -528,806 square feet of net absorption for the year with many back office functions going fully remote while Downtown recorded -313,707 square feet of occupancy losses. Submarkets with positive annual net absorption include Howe/Fulton/Watt Ave, Campus Commons, Elk Grove, Midtown, and Davis/Woodland.

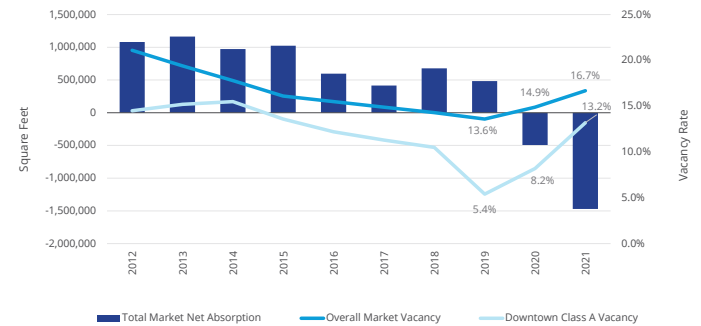
## Rents

Market average direct asking rents have stayed flat at \$2.06 per square foot for three consecutive quarters but are down 0.5 percent year-over-year. Tenants are gaining an edge in lease negotiations and effective rents are on the decline due to rising availability across the market. After dropping slightly in 2020, Downtown Class A asking rents are up 0.8 percent year-over-year though overall Downtown asking rents are down 0.2 percent since Q4 2020. Elk Grove's vacancy rate has fallen to 3.5 percent while its rents increased to \$2.66 per square foot by Q4 2021, up 6.3 percent year-over-year and now the second highest in the region. Asking rents are down 2 percent to 9 percent year-over-year in the South Natomas, Highway 50 East, North Natomas, Point West, Highway 50 West, Rocklin, and South Sacramento submarkets, which have all seen notable increases in vacancy in 2021. Meanwhile, stable suburban submarkets like Davis/Woodland, El Dorado, Howe/Fulton/Watt Ave, Folsom, and Campus Commons recorded positive annual asking rent growth in 2021.

## Sales

Buyer interest is returning to the Sacramento region. Annual sales volume was down 4.6 percent year-over-year in 2021, however, second half 2021 sales volume increased 78 percent compared to the second half of 2020. Though value-add acquisitions continue to lag pre-pandemic levels, investor appetite for stable assets in durable submarkets is increasing. Kingsbarn Realty Capital's \$72.15 million purchase of the four-property Parkshore Plaza in Folsom is the latest example of buyer demand in the Sacramento office market. In addition, NexCore Group and Nuveen's \$33.2 million purchase of 620 Roseville Pkwy, where Penumbra recently expanded, signals new buyers entering the market due to the region's diversifying employment base and relatively stable market fundamentals compared to high-cost West Coast markets like San Francisco, Los Angeles, and Seattle. The amount of high-quality assets trading in the fourth quarter equated to a \$228 per square foot average sale price, which is up 19 percent year-over-year and the highest average sale price recorded since Q4 2019.

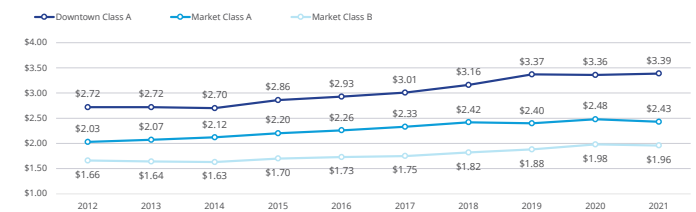
Sacramento Office Market Annual Net Absorption & Vacancy Rate



Source: Colliers Sacramento Research

Sacramento Office Average Asking Rates

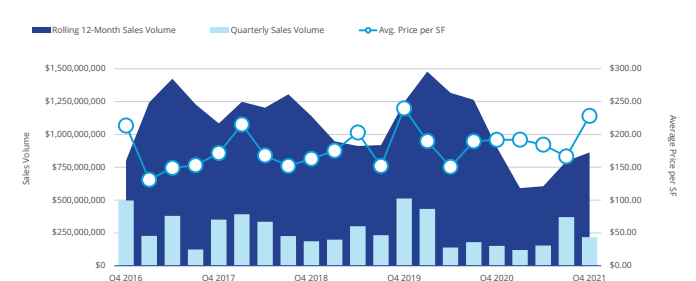
Average Asking Rates (\$/SF FSG) - 2012 to 2021 | Downtown Class A vs. Market Class A/B



Source: Colliers Sacramento Research

Sacramento Office Sales Activity

Quarterly Sales Volume, Rolling 12-Month Sales Volume, Average Quarterly Price per SF - Last 5 Years



Source: Colliers Sacramento Research

## Commentary & Forecast

The need for office space will not disappear but the way we use the office is certainly shifting. The pandemic has forced employers to rethink their office space and the overall trend continues to be a decline in overall demand. The cyclical trend of rising COVID-19 cases and emerging variants has resulted in companies continuing to push back their official return to office dates. In addition to difficulties managing a remote workforce, companies are also now grappling with the Great Resignation with record amounts of employees quitting their jobs. Though the way we work is changing, we will likely start to see the return to the office in some form in 2022. The major question locally remains what the State of California will do with its leased office space as thousands of public sector employees continue to work from home at year-end 2021.

The Sacramento office market might have reached peak disruption in Q4 2021. The sublease market declined for the first time since Q2 2020, falling to 1.12 million square feet or 1.9 percent sublease availability. Some subleases were signed,



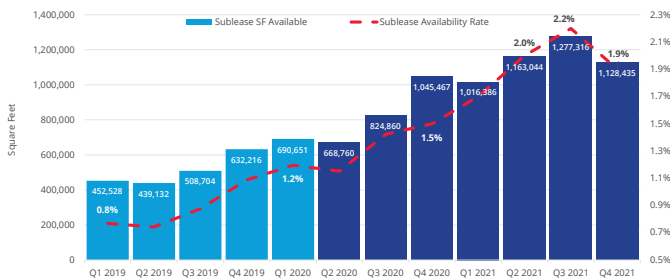
*The new Sacramento County Courthouse under construction in mid-November 2021. The 17-story, 53-courtroom courthouse is located in Downtown Sacramento on the block bordering H and G streets and 5th and 6th streets behind the federal Robert Matsui United States Courthouse. The new courthouse will replace the existing courthouse at 720 9th Street and will cost nearly \$500 million to build. Located on the southeast corner of The Railyards, the Sacramento County Courthouse is scheduled to open by year-end 2023.*

earlier in the year and the renewal of Murphy Austin's 26,697 square foot space. Two new State of California tenants are moving into new spaces at 400 & 500 Capitol Mall as the Jesse Unruh Building is slated to be renovated in 2022. The newly renovated 660 J Street will test a still uncertain market with roughly 100,000 square feet of office space available for occupancy by Q2 2022. Centr'l Office will see what coworking demand is like in early 2022 when it opens its new location at 1201 J Street. Nashville-based Southern Land Co. made a big bet on Downtown Sacramento with its purchase of the 2.5-acre Lot X site in October for \$16.75 million where it will build a 30-story apartment tower and a five-story, 83,000 square foot office building.

While the overall office market deteriorated in 2021, the outlook is brighter for 2022. The region's diversifying employment base and escalating migration should provide welcome tailwinds for the office market as employees return to the office. Sacramento companies also posted a record amount of venture capital and private equity funding through the first nine months of 2021, up to \$1.6 billion, a 173 percent increase above the previous four years combined. UC Davis Health and Amazon Web Services announced the launch of a Cloud Innovation Center at Aggie Square to address challenges and real-world problems related to healthcare, smart cities, sustainability, and cybersecurity. This development will break ground in early 2022 and launch Sacramento into the emerging life science markets category. Bay Area-based biotech firms like JOINN Biologics and Orca Bio entering the market in 2022 will continue to grow the vibrant life science sector. Though challenges remain, Sacramento's office market is well positioned to see positive momentum build throughout 2022 as it strives to return to stability.

### Sacramento Sublease Market

Total Sublease Space Available - Q1 2019 to Q4 2021



Source: Colliers Sacramento Research

and others were taken off the market. While this is a positive development, overall leasing activity decreased quarter-over-quarter in Q4 2021 after three straight quarters of increases. While the market is likely to take another six months to return to positive demand, there is a chance net absorption could return to the black in 2022 due to previously signed leases totaling 327,000 square feet of vacant space that will be occupied. UC Davis Health is slated to open its new Rancho Cordova location totaling 194,150 square feet in Q2 2022. Five other spaces of more than 15,000 square feet will be occupied next year by General Dynamics, CapRadio, Talon Solar, SHRA, and MHSOAC. The new year should provide more clarity for executives as they look to lease new office space. Furthermore, companies from the Bay Area and institutional and private equity investors continue to set their sights on Sacramento due to its surging labor pool.

Downtown Sacramento is still seeing rising vacancy but there are some signs it is beginning to turn the corner. 555 Capitol Mall is now 99 percent leased after several new leases signed

# Sacramento | Q4 2021 | Office | Market Statistics

Submarket/ Class	Total Inventory SF	Direct Availability Rate	Sublease Availability Rate	Availability Rate	Vacancy Rate	Vacancy Rate Previous	Net Absorption Current	Net Absorption YTD	Under Construction	Deliveries YTD	Avg Direct Asking Rate (FSG)
<b>Downtown</b>											
A	5,304,251	15.3%	0.9%	16.2%	13.2%	10.4%	-149,203	-252,526	0	0	\$3.39
B	3,519,455	26.3%	0.6%	27.0%	24.7%	24.6%	-10,025	-59,102	0	0	\$2.85
C	1,380,967	19.6%	0.7%	20.3%	18.2%	18.6%	5,466	-2,079	0	0	\$2.04
<b>TOTAL</b>	<b>10,204,673</b>	<b>19.7%</b>	<b>0.8%</b>	<b>20.5%</b>	<b>17.8%</b>	<b>16.4%</b>	<b>-153,762</b>	<b>-313,707</b>	<b>0</b>	<b>0</b>	<b>\$2.90</b>
<b>Suburban</b>											
A	14,013,626	20.4%	2.3%	22.7%	16.6%	16.4%	-138,359	-574,376	0	0	\$2.19
B	24,050,062	18.7%	2.6%	21.3%	17.0%	17.2%	27,353	-396,572	0	0	\$1.85
C	9,631,034	15.8%	0.4%	16.2%	14.6%	14.9%	12,243	-187,164	0	0	\$1.56
<b>TOTAL</b>	<b>47,694,722</b>	<b>18.6%</b>	<b>2.1%</b>	<b>20.7%</b>	<b>16.4%</b>	<b>16.5%</b>	<b>-98,763</b>	<b>-1,158,112</b>	<b>0</b>	<b>0</b>	<b>\$1.91</b>
<b>Total</b>											
A	19,317,877	19.0%	1.9%	20.9%	15.7%	14.8%	-287,562	-826,902	0	0	\$2.43
B	27,569,517	19.7%	2.3%	22.0%	18.0%	18.2%	17,328	-455,674	0	0	\$1.96
C	11,012,001	16.3%	0.4%	16.7%	15.0%	15.4%	17,709	-189,243	0	0	\$1.65
<b>TOTAL</b>	<b>57,899,395</b>	<b>18.8%</b>	<b>1.8%</b>	<b>20.6%</b>	<b>16.7%</b>	<b>16.5%</b>	<b>-252,525</b>	<b>-1,471,819</b>	<b>0</b>	<b>0</b>	<b>\$2.06</b>

## Submarkets

Downtown	10,204,673	19.7%	0.8%	20.5%	17.8%	16.4%	-153,762	-313,707	0	0	\$2.90
Highway 50 East	9,596,538	28.4%	4.4%	32.8%	24.9%	24.6%	-102,454	-528,806	0	0	\$1.82
Roseville	6,520,602	17.3%	5.3%	22.5%	16.2%	15.5%	-21,032	-217,301	0	0	\$2.02
South Natomas	3,248,020	21.9%	1.1%	23.0%	17.4%	17.3%	-2,524	-106,068	0	0	\$2.21
Folsom	2,468,277	10.4%	0.4%	10.9%	8.5%	10.0%	12,908	-11,800	0	0	\$2.22
Midtown	2,365,679	17.3%	0.1%	17.4%	12.8%	12.1%	-18,468	16,829	0	0	\$2.41
North Natomas	2,853,703	11.5%	1.9%	13.4%	12.1%	12.4%	7,031	-28,996	0	0	\$1.68
Rocklin	1,470,556	20.2%	0.7%	20.9%	19.2%	18.8%	-5,954	-79,864	0	0	\$1.98
Highway 50 West	2,308,853	16.9%	1.3%	18.1%	16.9%	17.8%	7,544	-45,853	0	0	\$1.64
Point West	2,361,592	22.4%	0.5%	22.9%	17.9%	18.2%	7,374	-131,525	0	0	\$2.00
South Sacramento	1,231,188	14.9%	0.2%	15.1%	8.2%	7.4%	-9,710	-15,563	0	0	\$1.53
Davis/Woodland	1,238,249	5.6%	6.6%	12.2%	7.3%	9.3%	6,715	12,207	0	0	\$2.12
El Dorado	1,298,780	19.8%	6.0%	25.8%	12.0%	11.6%	-10,316	-34,658	0	0	\$2.01
Elk Grove	1,151,795	4.0%	0.0%	4.0%	3.5%	5.1%	5,725	20,010	0	0	\$2.66
West Sacramento	1,349,487	10.4%	0.0%	10.4%	9.7%	10.2%	5,936	-19,253	0	0	\$2.02
Campus Commons	994,035	13.7%	0.3%	14.0%	13.0%	15.8%	27,815	29,116	0	0	\$2.24
Howe/Fulton/Watt Ave	3,450,895	22.3%	0.2%	22.5%	21.2%	21.1%	-1,297	40,782	0	0	\$1.63
Citrus Heights	856,108	13.9%	0.0%	13.9%	13.7%	13.7%	-232	-11,022	0	0	\$1.40
East Sacramento	748,736	5.7%	1.3%	7.0%	4.1%	4.3%	1,956	-25,217	0	0	\$2.42
Rio Linda/N Highlands	815,180	17.0%	0.0%	17.0%	14.8%	14.8%	0	0	0	0	\$1.23
Auburn/Lincoln	717,557	7.9%	1.1%	9.0%	8.9%	8.9%	111	-20,949	0	0	\$1.47
Carmichael/Fair Oaks	648,892	22.9%	0.0%	22.9%	23.2%	21.2%	-9,891	-181	0	0	\$1.30
<b>Total</b>	<b>57,899,395</b>	<b>18.8%</b>	<b>1.9%</b>	<b>20.7%</b>	<b>16.7%</b>	<b>16.5%</b>	<b>-252,525</b>	<b>-1,471,819</b>	<b>0</b>	<b>0</b>	<b>\$2.06</b>

### Sacramento Quarterly Comparisons and Totals

Q4 2021	57,899,395	18.8%	1.9%	20.7%	16.7%	16.5%	-252,525	-1,471,819	0	0	\$2.06
Q3 2021	58,095,178	18.5%	2.2%	20.7%	16.5%	16.3%	-244,397	-1,219,294	0	0	\$2.06
Q2 2021	58,165,186	17.8%	2.0%	19.8%	16.3%	15.6%	-463,555	-974,897	0	0	\$2.06
Q1 2021	58,488,125	17.3%	1.7%	19.0%	15.6%	14.9%	-511,342	-511,342	0	0	\$2.12
Q4 2020	57,962,097	16.4%	1.5%	17.9%	14.9%	13.5%	-466,405	-493,759	0	552,200	\$2.07

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