

SACRAMENTO | RETAIL

Q2 2019

DESPITE SOME BIG BOX CLOSURES THIS YEAR, SACRAMENTO'S VACANCY KEEPS FALLING

REGIONAL SUMMARY

Sacramento's retail market experienced a slight uptick in the vacancy rate in the second quarter of 2019 as some big box store closures begin to put upward pressure on vacancy. Nevertheless, net absorption is still positive so far this year. The market also posted an 11-year low vacancy rate last quarter and is still down year-over-year. With stable market fundamentals and a growing population, three new shopping centers broke ground this quarter in three separate suburban submarkets (South Sac, Elk Grove, and El Dorado Hills) while new concepts continue to open in new mixed-use projects in an expanding urban core. Though big box store closures are beginning to impact the Sacramento market, many of these spaces are being backfilled by a number of growing tenants looking for new space. Empty boxes provide landlords an opportunity to bring in new restaurant, food hall, medical, coworking, fitness, or entertainment uses in order to create an attractive destination with a diverse and experiential selection of concepts for consumers. Fitness, food and drink, and discount stores have been driving demand in Sacramento lately as asking lease rates and sale prices begin to soften with more space coming available. There are challenges ahead, but the outlook is far from dire.

Net Absorption

- > The negative absorption this quarter was the first in the red since 2016, driven primarily by Burlington Coat Factory's 84K SF store closure in Woodland.
- > Entertainment and experiential concepts were the top two openings this quarter with restaurants, fitness centers, and discount stores also driving demand.

Vacancy

- > The vacancy rate increased 20 basis points from the first quarter but is still down 70 basis points from Q2 2018.
- > There are seven available 40,000+ SF anchor spaces in the region that have hit the market in 2019 so far, putting upward pressure on vacancy moving forward.

Rents

- > After a year of steady rent growth, market average asking rates fell slightly, down both quarter-over-quarter and year-over-year.
- > Vacant big box anchor spaces will be quite flexible in terms of rent, while new mixed-use retail space in the urban core commands significantly above-market rents. Sacramento's retail market continues to be bifurcated in this way.

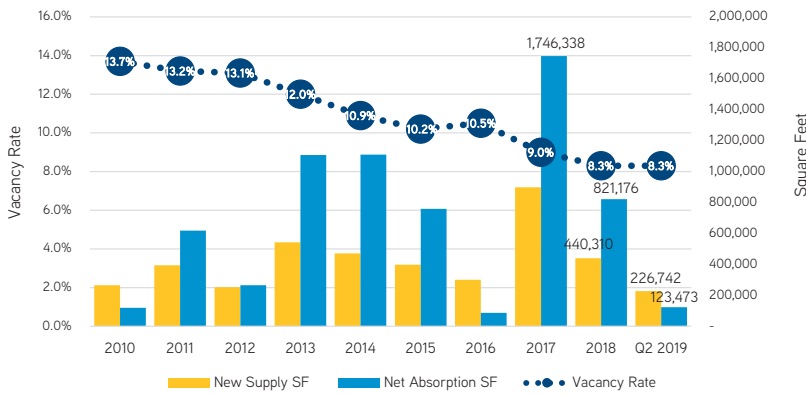
Sales Activity

- > After a slow start to the year, Sacramento saw 78 sales transactions in Q2 2019 (16 more than Q1) totaling \$146.4 million.
- > Average cap rates were 6.6% in Q2, up slightly from 6.4% one year ago and down from 7.0% last quarter. The average sale price recorded in Q2 was the lowest since Q3 2015 as there were a number of high vacancy, value-add assets acquired this quarter.



RETAIL MARKET FUNDAMENTALS

10-Year Annual New Supply, Vacancy, Net Absorption



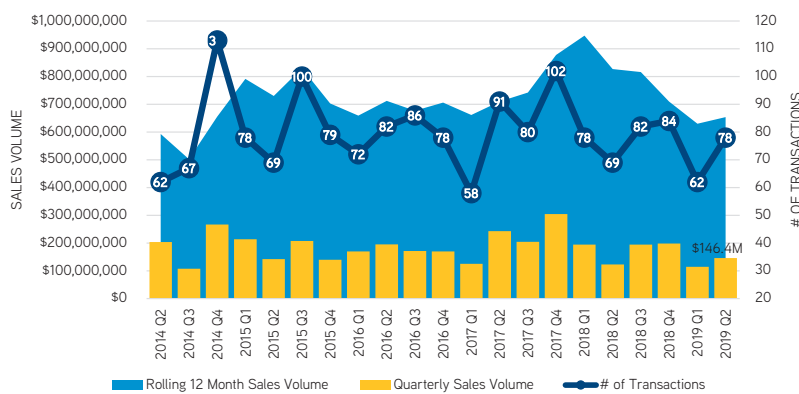
Q2 2019 New Constructions Starts



The Ridge Shopping Center / Elk Grove

233K SF center across 15 buildings underway at the SEC of Bass Lake Rd and Sienna Ridge Rd. The adjacent 150K SF Costco opened last September. 73% leased as of April 2019 for Pappas-owned project. Olive Garden, Pieology, and Stantpn Optical could open as soon as later this summer.

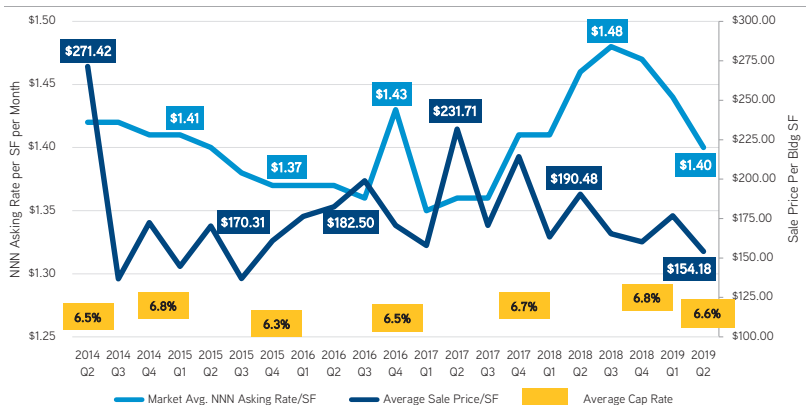
5-Year Sales Activity - Quarterly & Rolling 12 Month Sales Volumes



Sienna Ridge / El Dorado Hills

100K SF Safeway-anchored center being developed by Donahue Schriber, Safeway could open by December with 9 signed retailers opening next year (Pet Supplies, Chase Bank, Fresh Cleaners, Great Clips, Nail Retreat, Pacific Dental, Sourdough & Co., Jon & Bon's Yogurt and Mexico Lindo.

5-Year Quarterly Average Asking Rates, Sale Prices, Cap Rates



The Park / South Sac (South Land Park)

A 44K SF Raley's is anchoring a new 108K SF shopping center underway at the former Capital Nursery site, developed by Preserve West Capital. After an early May groundbreaking, the project is planned for an early 2020 opening. Signed tenants include Starbucks, Orange Theory Fitness, Pet Food Express, Chase Bank, Supercuts.

Q2 2019 Food & Drink Tracker

- 34 openings vs. 16 closings
- +18 net new food/drink offerings across Sacramento from April through June (and a 10K SF Cracker Barrel opening in Rocklin in Q4)
- Source: Sacramento Business Journal
- 46 new Sacramento restaurants in first half/2019
- Source: The Sacramento Bee

Q2 2019 Significant Leases Signed

SIGN DATE	ADDRESS	SF	TYPE	SUBMARKET	LANDLORD	TENANT
May 2019	4249 Elverta Rd	54,502	Community Center	Rio Linda / North Highlands	Ethan Conrad	California Family Fitness
June 2019	6071 Florin Rd	13,000	Power Center	South Sacramento	Starboard Realty Advisors	Falling Prices
May 2019	Rocklin Station (Sierra College Blvd @ I-80)	10,000	Restaurant	Roseville / Rocklin	Les Schwab Tire Center	Cracker Barrel
April 2019	5171 Auburn Blvd	7,400	Freestanding Retail	Rio Linda / North Highlands	John & Grace Hudek	Ace Metal Products
May 2019	140 Elm Ave	7,080	Auto Repair	Auburn / Loomis	Norma Harris	Dave's Family Automotive

Q2 2019 Significant Sales

SALE DATE	PROPERTY, CITY	SF	SALE PRICE	PRICE/SF	CAP RATE	SELLER	BUYER
6/13/2019	Prospector's Plaza - 3966 Missouri Flat Rd, Placerville *	243,907	\$24,130,000	\$98.93	Undisclosed	Weingarten Realty Investors	Rich Development & Gryphon Capital
5/1/2019	Norwood Center - 4201-4221 Norwood Ave, Sacramento	72,882	\$13,500,000	\$185.23	Undisclosed	Retail Opportunity Investments Corp.	Viva Supermarket HQ
4/29/2019	Woodcreek Village - 4001-4021 Woodcreek Oaks Blvd, Roseville	29,335	\$12,950,000	\$441.45	7.17%	ACF Property Management	Douglas M. Davis
5/24/2019	Green Acres Nursery - 2015 Serpa Way, Folsom **	30,220	\$8,600,000	\$284.58	N/A	Elliott Homes	Green Acres Nursery & Supply
4/2/2019	8505-8525 Madison Ave, Fair Oaks ***	62,994	\$7,556,000	\$119.95	6.60%	Bob Spence	Ethan Conrad

* Center was 87% leased at time of sale, Target planning on opening a new 84K SF location at the former Kmart space next summer, buyer plans on investing in extensive renovations for the property

** Buyer occupied 100% of the property and exercised its lease option to purchase from Elliott Homes, the owner and developer of the site

*** Property was 54% vacant at the time of sale, Ethan Conrad has 35K SF available for lease at the center

Q2 2019 Largest Openings, Closings, Move-Ins, And Move-Outs

ADDRESS	TENANT	SF	SUBMARKET	TENANT INDUSTRY
2405 Butano Dr	Cinema West	48,000	Arden / Howe / Watt	Motion Picture Theaters
1700 Arden Way	Urban Air Trampoline Park	40,407	Arden / Howe / Watt	Recreation
8525 Auburn Blvd	Big Lots	34,300	Citrus Heights / Orangevale	Variety Stores
6328 Fair Oaks Blvd	Goodwill	21,440	Carmichael	Used Merchandise
1917 Douglas Blvd	W Salon Suites	13,114	Roseville / Rocklin	Beauty Shops
9500 Greenback Ln	Falling Prices	10,976	Folsom	Discount Stores
9580 Oak Ave	Vic's Supermarket	-13,863	Folsom	Grocery
1815-1825 Prairie City Rd	The Phoenix Schools	-14,900	Folsom	Education
2430 Mission Ave	Mike's Supermarket	-27,000	Carmichael / Fair Oaks	Grocery
1280 E Gibson Rd	Burlington Coat Factory	-84,351	Woodland	Department Stores

MARKET ANALYSIS

SACRAMENTO RETAIL SUBMARKET STATISTICS - Q2 2019

Submarket	Rentable		Vacancy Rate	Availability Rate	Net		YTD Net		Under Construction
	Buildable Area	Vacant SF			Absorption SF	Construction SF			
Roseville / Rocklin	10,077,790	639,975	6.4%	7.8%	(1,868)	9,016	22,329		
South Sacramento	7,550,295	504,194	6.7%	9.8%	91,697	262,932	0		
Arden / Howe / Watt	6,017,964	757,096	12.6%	15.0%	(30,743)	(8,066)	4,811		
Citrus Heights / Orangevale	4,685,694	639,906	13.7%	15.1%	(11,929)	(67,846)	11,000		
Elk Grove	4,539,651	215,288	4.7%	6.2%	13,162	56,273	0		
Folsom	4,386,703	318,985	7.3%	7.5%	(39,263)	(2,081)	15,872		
Highway 50	3,495,012	469,149	13.4%	15.3%	(18,064)	(76,766)	0		
Natomas / Northgate	3,099,862	193,181	6.2%	7.9%	8,428	31,044	0		
Rio Linda / N Highlands	2,894,503	324,852	11.2%	11.5%	(4,497)	(22,269)	0		
El Dorado	2,508,959	189,352	7.5%	8.2%	8,253	11,479	82,496		
Woodland	2,246,947	258,273	11.5%	16.2%	(82,433)	(90,785)	6,500		
Auburn / Loomis	1,814,547	93,818	5.2%	7.3%	3,310	(267)	0		
Carmichael / Fair Oaks	1,856,490	165,408	8.9%	11.8%	(52,951)	(23,990)	0		
West Sacramento	1,807,127	100,080	5.5%	7.1%	0	1,394	0		
Downtown/Midtown/East Sac	1,591,598	103,543	6.5%	8.8%	5,642	65,634	0		
Lincoln	1,263,631	54,213	4.3%	4.8%	(2,508)	(21,139)	0		
Davis	1,065,400	47,186	4.4%	5.1%	(542)	4,960	0		
SACRAMENTO MARKET TOTALS	60,902,173	5,074,499	8.3%	10.0%	(114,306)	123,473	143,008		

Retail submarket statistics include the combined totals of all four property types (community neighborhood, power regional, specialty, and strip)

MARKET ANALYSIS

Q2 2019 RETAIL MARKET TOTAL

	Total Vacancy Rate	Net Absorption SF	YTD Net Absorption SF	Under Construction SF
Community Neighborhood	7.9%	(8,089)	203,803	21,611
Power Regional	7.8%	(75,092)	-45,543	6,500
Specialty	13.2%	7,544	37,312	82,496
Strip	9.5%	(38,669)	-72,099	32,401
Overall Market	8.3%	(114,306)	123,473	143,008

The information contained in this report was provided by sources deemed to be reliable, however, no guarantee is made as to the accuracy or reliability. As new, corrected or updated information is obtained, it is incorporated into both current and historical data, which may invalidate comparison to previously issued reports. Results include all retail space located in any type of shopping center or regional mall in all core areas of Sacramento, Placer, El Dorado and Yolo Counties. Community Neighborhood market includes both community centers and neighborhood centers. Power Regional includes both power centers and regional malls. Specialty market includes lifestyle centers, outlet centers, and theme/festival centers. Strip market includes all strip centers.

*Average rents used reflect the most recent asking rents available.

TRENDS, NEW CONSTRUCTION, AND FORECAST

The fact that three new shopping centers started construction this quarter speaks to the resilience of Sacramento's retail market. Pre-leasing has been encouraging at Crocker Village in Curtis Park (where a new 55K SF Safeway opened last quarter), The Ridge in Elk Grove, Sienna Ridge in El Dorado Hills, and The Park in South Land Park. Sacramento's expanding population will continue to support new retail development in vibrant areas, but there will still be vacant big box anchor spaces to lease. There will also be availability in obsolete strip malls in less affluent areas and struggling regional malls, both of which will keep upward pressure on vacancy moving forward. The next center to break ground should be Armstrong Properties' 240K SF Campus Oaks in West Roseville. The Nugget Markets and 24 Hour Fitness-anchored development is expected

to be 85 percent leased by the start of construction this summer or fall and could be completed by mid-2020. Also in Roseville, the 130K SF VillaSport Athletic Club and Spa near the Westfield Galleria is opening this summer. Even with all this new retail development, Sacramento will be far from over-supplied with new retail product as new development has been minimal. 2017 was Sacramento's high point for new supply in the last decade with 900K SF completed. However, new construction is nowhere near the pace set from 2006 to 2008 when an average of 2.6 MSF of new retail supply hit the market each year. Developers have been wise to pre-lease much of their projects before breaking ground in recent years. Grocery-anchored and e-commerce resistant assets will continue to be sought after by investors looking to place capital, but there are only so many opportunities available in the marketplace.



Flatstick Pub's sign at 630K St in DOCO went up this quarter. Dave Herrera and Mark Engemann of Colliers International's Sacramento office brokered this 15,000 SF lease late last year on behalf of the landlord, Swift Real Estate Partners. Tenant improvements are currently underway for the new pub with mini-golf next to the Golden 1 Center set to open this fall, just in time for the start basketball season.

TREND OF THE QUARTER

Now that we are halfway through 2019, it's time to revisit the overhyped retail apocalypse narrative. So far, more than 7,000 store closures have been announced by U.S. retailers in 2019 versus 3,017 new store announcements, according to Coresight Research. Last year, Coresight tracked 5,524 closures, down 30% from an all-time high of 8,139 in 2017. In addition to struggling department stores like Sears, Macy's, and JC Penney, companies like Fred's, Bed Bath & Beyond, Dressbarn, Party City, Pier 1 Imports, Gap, Victoria's Secret, and Abercrombie & Fitch are all closing a significant number of stores nationwide. Based on the current trend of accelerating store closures this year, Coresight calculates that the total number of closures nationwide could surpass 12,000 this year.

In the Sacramento market, significant store closures have not been as disruptive. While Sacramento has certainly seen a number of closures this year, many of these spaces are being backfilled by other tenants due to healthy demand. Through the first six months of 2019, a growing number of anchor spaces came available across Sacramento after a store was closed. Burlington Coat Factory closed its 84K SF Woodland County Fair location in April. OSH shuttered a 58K SF Antelope location (leased by Cal Fit this quarter), along with another 46K SF in Woodland. Toys R Us closed a 49K SF Elk Grove store, Rite Aid shut down a 46K SF store on Florin Road, Sports Chalet closed down a 42K SF store in Elk Grove, and a Walmart Neighborhood Market closed a 42K SF location on Florin Road.

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