



Industrial Report

Q1 2016
GALLELLI REAL ESTATE MARKET REPORT

Overview

Though the Sacramento industrial market has continued to improve over the last few years, momentum slowed during Q1 2016, with the market experiencing only modest occupancy growth and a slight decline in vacancy. Industrial vacancy declined from 13.7% to 13.6% during Q1 and though the rate has wavered within the 13% range for the last four consecutive quarters, overall regional industrial vacancy has declined nearly 4% over the last five years. Net absorption was positive for the quarter, recording just over 102,000 square feet of growth. While this figure is improved over the previous quarter, which saw just 22,000 square feet of positive net absorption, it is below the 376,000 square feet of absorption the market has averaged per quarter for the last five quarters.

Though market momentum has slowed slightly, leasing activity is still strong. We tracked just over 1 million square feet of industrial deals inked during Q1, which is a significant increase from the 798,000 square feet seen in the previous quarter. Four out of the last five consecutive quarters have all seen gross leasing figures in excess of 1 million square feet.

Market Trends

- Industrial leasing activity and demand is strong though there have been a few larger requirements (50K+ SF) in the market, demand is primarily focused on industrial space under 20,000 square feet.



- Net absorption was mostly positive across the local submarkets, with Northeast Sacramento, Northgate/Natomas and Roseville/Rocklin seeing the largest occupancy gains. The two largest losses happened in the West Sacramento and Power Inn submarkets.
- The average asking rate for industrial space was unchanged, standing at \$0.41 per square foot at the end of Q1. Industrial rental rates have been flat for quite some time, wavering between the \$0.30 and \$0.40 range for the last three years.

Industrial Vacancy vs. Net Absorption



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Industrial Q12016

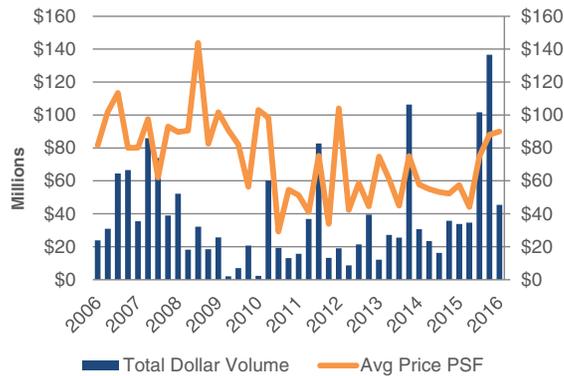
Industrial investment activity slowed during the first quarter of 2016.

<p>Vacancy</p> <p>13.6%</p> <p>▼</p>	<p>Net Absorption</p> <p>102,162</p> <p>▲</p>	<p>Avg. Rent PSF</p> <p>\$0.41 PSF</p> <p>—</p>
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Investment Highlights

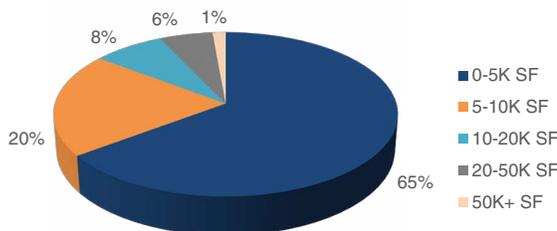
- Industrial investment activity slowed during Q1 2016, with the market recording \$45.4 million in transactional volume over 18 transactions. This is down from Q4 2015, which saw 30 transactions totaling \$136.6 million.
- The average price per square foot increased slightly, rising from \$88 per square foot in Q4 2015, to \$90 per square foot during Q1 2016.*
- The average asking CAP rate ended the quarter at 6.89%.
- The largest investment sale of the quarter was the sale of three buildings totaling 366,000 SF in the Coastal/KMS Commerce Center in Roseville, which sold for \$18.8 million.

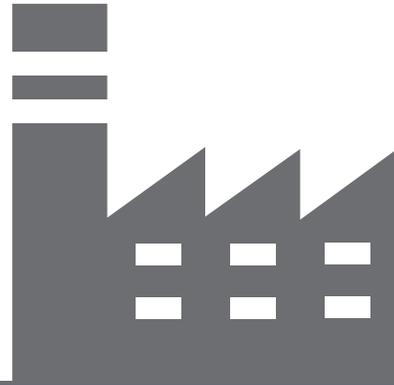
Industrial Investment Sales Volume



* Footnote: Q4 2015 average price PSF has been adjusted, as the original number was higher due to a company sale that was erroneously marked as a building sale. The number has been adjusted to reflect only building sales.

Q1 Industrial Leasing Volume by SF





Units Under Construction

0_{SF}
-

Sacramento Unemployment

5.4%
▼

US Unemployment

5.0%
▲

Spotlight: Construction/Development

As market fundamentals continue to improve in all property types, the Sacramento region has seen a rise in construction projects over the last two years. Construction has been primarily focused on multifamily and retail projects, but the industrial market has seen activity as well. 2015 even saw some of the first post-recession speculative industrial projects come to completion.

While there are no industrial projects currently under construction, the future development pipeline contains 4 million square feet of potential projects. However, whether or not these projects get built depends on a few factors – first, market fundamentals need to further improve. Rental rates have remained flat for the most part and though vacancy rates are nearing their pre-recession lows, they are still relatively high compared to surrounding markets like the Bay Area and Central Valley. Some local developers have even turned to these surrounding markets to build due to their tight vacancy and high demand levels. While Sacramento is seeing a healthy amount of industrial demand, current vacancy and rental rates are not yet where they need to be to justify new construction, except in select submarkets. Secondly, local developers are waiting to see what happens with the most recently completed spec projects before they proceed with new projects.

For now, ‘cautious optimism’ is the name of the game as far as new industrial development. It is likely industrial construction will remain minimal until rental rates increase and vacancy falls into the 10% range.

Outlook

Though market momentum slowed during Q1 2016, vacancy continued to decline and leasing activity remained steady. Industrial demand in the region is still very strong and we anticipate this will continue going into the rest of the year. The 1 million square feet of deals inked during the quarter will help push vacancy down further, once these tenants take occupancy. Investor interest in the region is still strong, as the area continues to be a cheaper alternative to the skyrocketing prices of the Bay Area. The outlook for the Sacramento industrial market is good; however, it is likely that rents will remain flat until vacancy declines further.

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 Q1-16	Net Absorption		SF Under Construction	Avg. Asking Rate (NNN)
						Q1-16	Q1-15		
Auburn	1,188,993	51,888	0	51,888	4.4%	(6,805)	(5,000)	0	\$0.52
Davis/Woodland	7,834,311	1,590,124	0	1,590,124	20.3%	(8,980)	74,620	0	\$0.29
Downtown	862,838	112,000	0	112,000	13.0%	0	(112,000)	0	-
East Sacramento	175,668	0	0	0	0.0%	0	0	0	-
Elk Grove/Laguna	3,018,198	215,775	0	215,775	7.1%	4,388	37,362	0	\$0.39
Folsom/El Dorado Hills	1,446,657	28,465	0	28,465	2.0%	(4,800)	(4,800)	0	\$0.65
Mather	2,593,339	336,986	6,400	343,386	13.2%	(4,136)	42,109	0	\$0.36
McClellan	10,113,763	1,997,909	142,978	2,140,887	21.2%	4,023	40,753	0	\$0.38
Northgate/Natomas	9,169,394	910,928	75,100	986,028	10.8%	46,107	(5,487)	0	\$0.38
Northeast Sacramento	2,749,181	179,358	20,000	199,358	7.3%	50,393	(7,668)	0	\$0.34
Power Inn	16,147,287	1,278,979	0	1,278,979	7.9%	(18,873)	752,910	0	\$0.31
Richards	2,799,610	254,091	0	254,091	9.1%	0	30,618	0	\$0.33
Roseville/Rocklin	8,926,441	1,879,856	0	1,879,856	21.1%	44,572	(14,503)	0	\$0.35
South Sacramento	2,489,269	1,021,248	0	1,021,248	41.0%	3,115	(2,799)	0	\$0.53
Sunrise	5,931,654	337,656	0	337,656	5.7%	13,780	67,736	0	\$0.51
West Sacramento	14,358,224	1,763,079	6,240	1,769,319	12.3%	(20,622)	80,993	0	\$0.38
Totals	89,804,827	11,958,342	250,718	12,209,060	13.6%	102,162	974,844	0	\$0.41

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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