



# Q4 OFFICE

*market report*

2022 | GALLELLI REAL ESTATE

Gallelli Real Estate  
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Q4  
22

  
**14.9%**

Vacancy  
Rate

  
**(±256,799) SF**

Net  
Absorption

  
**\$1.98**

Average Asking Rate  
(FSG)

  
**\$490,537**

Median Home Value in  
Sacramento MSA  
*(Source: Zillow, December 2022)*

  
**4.0%**

Sacramento  
Unemployment

  
**3.5%**

United States  
Unemployment

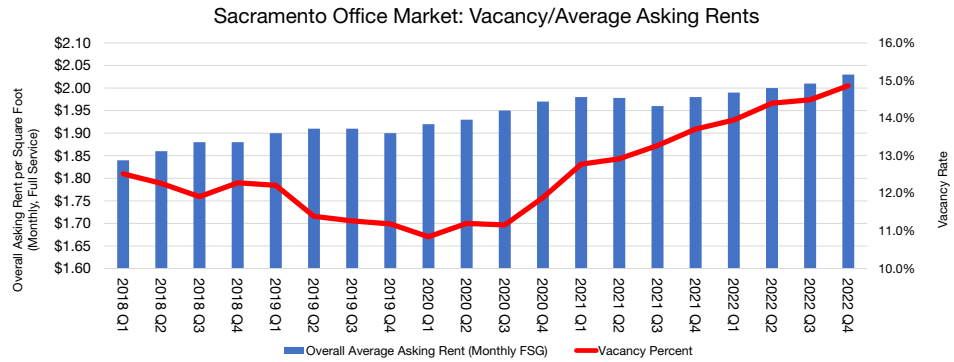
market overview

As of the close of Q4 2022, overall office vacancy in the Sacramento region stood at 14.9%. This reflects an increase from the 14.5% rate posted three months ago and the 13.9% level recorded one year ago. The market recorded 257,000 square feet (SF) of negative net absorption in Q4. All told, 785,000 SF of previously occupied space came back to market over the course of 2022. This past quarter also reflects the ninth consecutive quarter of negative occupancy growth in the region; vacancy had been on a downward trend until Q1 2020 when it fell as low as 10.8%. That was, of course, the quarter in which the pandemic arrived. Since that time, just over two million square feet of space has been returned to market. As daunting as those statistics may sound, we saw nearly twice that amount of space vacated in the aftermath of the Great Financial Crisis.

The initial work from home (WFH) period of the pandemic and the emergence since of hybrid work models has, and will continue to be, a major disruptor for the nation's office sector. However, compared to other major markets, Sacramento has largely been spared the worst impacts. For example, prior to the Covid crisis, office vacancy in San Francisco had fallen to just 4%, it now stands at roughly 26% and analysts there fear it could approach the 40% level by the end of 2023 due to numerous large tech leases that may not be renewed in the coming year.



Sacramento Office Market  
All Classes of Product, Q4 2022



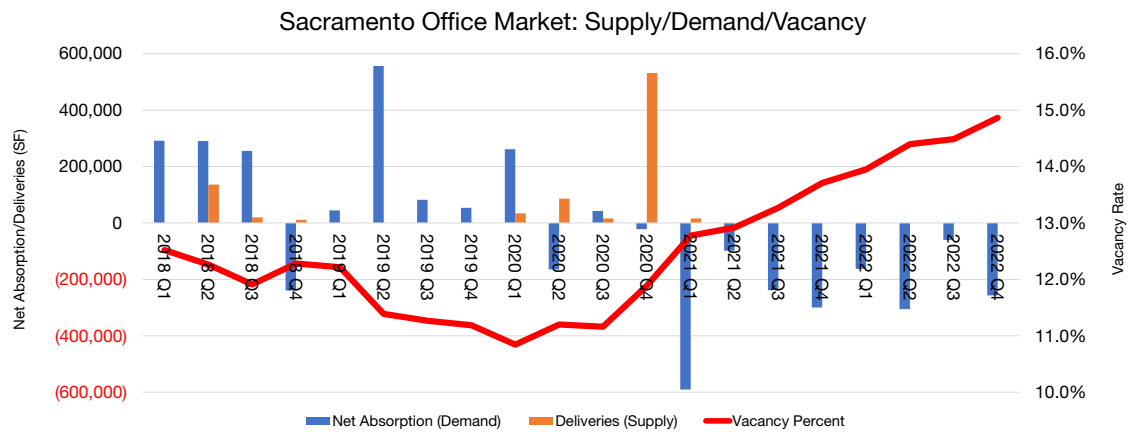
Source: Gallelli Real Estate; Costar Group

Overall office asking rent based on direct and sublease availabilities.





## Sacramento Office Market All Classes of Product, Q4 2022



### market overview continued

There are multiple reasons for Sacramento's comparative strength; nearly one third of the region's office space is occupied by governmental entities—which largely have not shifted their real estate strategies (a few smaller build-to-suit projects for the State of California were delivered and occupied in 2022, helping to reduce overall negative net absorption numbers by roughly 156,000 SF). While the region is home to multiple corporate campuses and corporate headquarters users, the bread and butter of the Sacramento office market is the smaller professional business tenant. In general, these users have both less space to consolidate and have been less likely to move to hybrid or WFH models. The largest space givebacks nationally have been from large block corporate users—particularly in the tech sector. While Sacramento is home to Intel and other tech players, the local presence here is dominated by small space startups.

According to Kastle Systems' Back to Work Barometer Index, keycard and building security data indicate that the percentage of workers in office nationally had reached a pandemic era high in January 2023 of just under 50%. While some Texas markets posted numbers as high as 65%, the lowest tallies came from the two largest tech-focused markets in the United States, San Francisco (35.8%) and San Jose (31.0%). The number of workers returning to their offices in those cities has simply not budged in over 18 months. A shortage of skilled tech workers has meant these workers have had the leverage to demand WFH or hybrid models. However, with tech sector experiencing a significant reset following its pandemic boom, some of that leverage is bound to evaporate as layoffs mount. "Out of sight, out of mind, out of a job," may become a painful reality for some remote workers. However, with building recessionary pressures and most

economists anticipating a likely mild downturn in 2023, there will undoubtedly be some tenants looking to economize space.

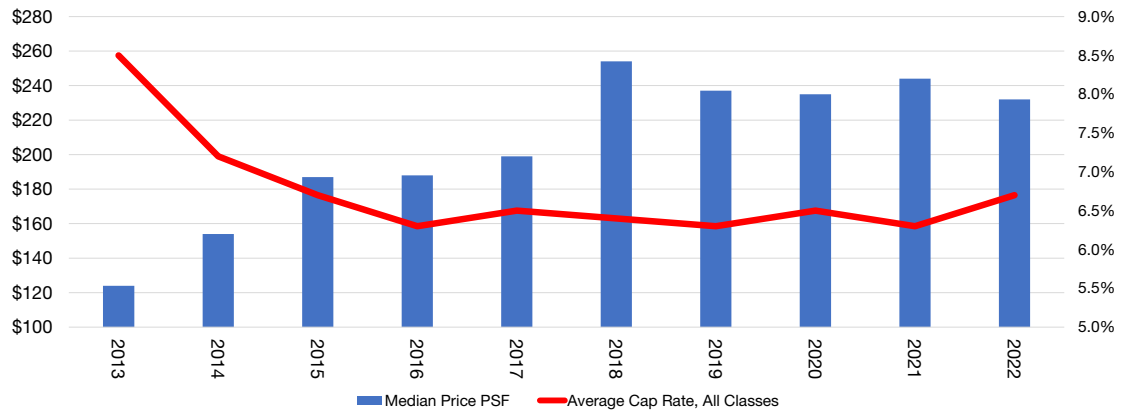
It is impossible to predict with absolute precision the impact of hybrid work models on office usage over the next couple of years. On the one hand, we think a trend of normalization will continue to occur as Covid slowly fades into the rear-view mirror. Many employees thrive with WFH or hybrid work models. But just as many do not. Younger workers who have not yet built experience or expertise in their chosen fields, miss out on training, mentoring and—perhaps most importantly—the social interaction with others that is even more important to those that have not started their own families yet. Meanwhile, the challenge of managing and training employees from afar is a serious one—particularly for larger organizations. And even with new tracking tools that can monitor employee productivity from afar, managers often find themselves struggling with the new hybrid reality when it comes to issues of trust, sometimes with good reason. At the end of the day, we see greater normalization occurring simply because of the gravity of human psychology.

But none of this means that we will be rolling the clock back to 2019. How much space a user can consolidate will depend on their individual hybrid models, the size of their current footprint and, critically, their industry. All told, we think it a safe assumption that the space needs of a user in 2019 will likely shrink an average of 10% to 20% going forward as part of the new hybrid reality. Those space givebacks obviously started in 2020, but still have a way to go, especially as leases inked prior to the pandemic come up for renewal. Meanwhile, the possibility of a downturn is also bound to result in space givebacks in 2023.



## Sacramento Office Market All Classes of Product, Q4 2022

Sacramento Office Market: Median Price PSF/Average Cap Rate



Source: Gallelli Real Estate; Costar Group

### market overview continued

Look for office vacancy in the Sacramento region to climb over the coming year, but for the local landlords and investors to experience far less pain than their counterparts in other major US markets. Submarkets with exposure to large block users are likely to experience the greatest challenges, though the likelihood of a recession—even if it proves to be brief and minor—is going to be another factor impacting demand. That said, flat rent growth in 2023 may be the best that landlords can hope for. It is highly likely that some submarkets may see rates dropping. Expect a growing trend of flight to quality ahead; active space users will increasingly see the opportunity to upgrade space (though many of these will be footprint consolidations) in the current rent environment.



6060 Sunrise Vista Drive



2420 Professional Drive

OFFICE MARKET STATISTICS: Criteria based on: 10,000 SF and above, does not include owner occupied, Existing, Under Construction, Proposed, Final Planning

Submarket	Total Number of Buildings	Inventory	Vacant Space			Vacancy Rate Q4-22	Availability Rate Q4-22	Net Absorption		Avg. Asking Rate (FSG) Weighted
			Direct	Sublease	Total			Q4-22	Q4-21	
Arden/Arcade										
Class A	8	872,773	182,868	2,850	185,718	21.3%	25.8%	(843)	(20,608)	\$2.13
Class B	87	3,871,251	860,023	31,505	891,528	23.0%	27.0%	(1,047)	7,429	\$1.83
Class C	96	2,676,194	384,987	8,837	393,824	14.7%	15.9%	(31,361)	(66,554)	\$1.83
<b>Total</b>	<b>191</b>	<b>7,420,218</b>	<b>1,427,878</b>	<b>43,192</b>	<b>1,471,070</b>	<b>19.8%</b>	<b>22.9%</b>	<b>(33,251)</b>	<b>(79,733)</b>	<b>\$1.87</b>
Auburn/Lincoln										
Class A	-	-	-	-	-	-	-	-	-	-
Class B	21	408,275	17,519	11,718	29,237	7.2%	7.6%	463	(647)	\$1.52
Class C	27	503,814	30,621	-	30,621	6.1%	6.5%	7,531	(67)	\$1.46
<b>Total</b>	<b>48</b>	<b>912,089</b>	<b>48,140</b>	<b>11,718</b>	<b>59,858</b>	<b>6.6%</b>	<b>6.9%</b>	<b>7,994</b>	<b>(714)</b>	<b>\$1.49</b>
Downtown Sacramento										
Class A	20	5,518,529	820,065	19,958	840,023	15.2%	18.9%	(71,492)	(150,414)	\$3.43
Class B	63	3,957,640	769,531	6,003	775,534	19.6%	21.4%	(48,668)	(69,972)	\$2.83
Class C	84	2,517,003	152,565	-	152,565	6.1%	10.1%	25,246	475	\$2.16
<b>Total</b>	<b>167</b>	<b>11,993,172</b>	<b>1,742,161</b>	<b>25,961</b>	<b>1,768,122</b>	<b>14.7%</b>	<b>17.9%</b>	<b>(94,914)</b>	<b>(219,911)</b>	<b>\$2.97</b>
El Dorado Hills/Folsom										
Class A	11	925,911	99,801	32,716	132,517	14.3%	24.5%	(8,863)	12,060	\$2.31
Class B	93	2,965,391	326,209	63,993	390,202	13.2%	27.3%	(7,594)	28,762	\$2.09
Class C	37	761,739	39,324	-	39,324	5.2%	5.4%	(2,707)	3,777	\$1.49
<b>Total</b>	<b>141</b>	<b>4,653,041</b>	<b>465,334</b>	<b>96,709</b>	<b>562,043</b>	<b>12.1%</b>	<b>23.2%</b>	<b>(19,164)</b>	<b>44,599</b>	<b>\$2.04</b>
Highway 50/Rancho Cordova										
Class A	32	3,050,682	591,301	142,338	733,639	24.0%	36.9%	(95,093)	(28,877)	\$1.90
Class B	144	7,822,897	1,583,112	65,053	1,648,165	21.1%	24.5%	(141,599)	(84,333)	\$1.75
Class C	69	1,863,295	192,677	-	192,677	10.3%	11.2%	10,500	12,694	\$1.39
<b>Total</b>	<b>245</b>	<b>12,736,874</b>	<b>2,367,090</b>	<b>207,391</b>	<b>2,574,481</b>	<b>20.2%</b>	<b>25.5%</b>	<b>(226,192)</b>	<b>(100,516)</b>	<b>\$1.73</b>
Midtown/East Sacramento										
Class A	4	465,701	-	5,811	5,811	1.2%	5.0%	2,119	957	\$2.89
Class B	55	3,393,116	191,087	9,398	200,485	3.7%	6.0%	145,710	(46,998)	\$2.34
Class C	42	837,735	101,442	-	101,442	12.1%	16.5%	(2,456)	1,554	\$1.86
<b>Total</b>	<b>101</b>	<b>4,696,552</b>	<b>292,529</b>	<b>15,209</b>	<b>307,738</b>	<b>6.6%</b>	<b>7.8%</b>	<b>145,373</b>	<b>(44,487)</b>	<b>\$2.31</b>
Natomas										
Class A	36	3,659,233	601,948	40,729	642,677	17.6%	19.8%	(21,391)	(3,507)	\$2.22
Class B	50	2,163,956	246,406	-	246,406	11.4%	21.0%	35,937	14,371	\$1.86
Class C	16	569,839	79,596	-	79,596	14.0%	27.4%	(31,358)	-	\$1.49
<b>Total</b>	<b>102</b>	<b>6,393,028</b>	<b>927,950</b>	<b>40,729</b>	<b>968,679</b>	<b>15.2%</b>	<b>20.9%</b>	<b>(16,812)</b>	<b>10,864</b>	<b>\$2.03</b>
Northeast Sacramento										
Class A	1	79,163	-	-	-	-	-	-	-	-
Class B	39	1,267,242	175,333	2,083	177,416	14.0%	15.2%	25,624	4,266	\$1.67
Class C	65	1,516,918	256,859	1,358	258,217	17.0%	23.3%	(9,348)	(2,458)	\$1.42
<b>Total</b>	<b>105</b>	<b>2,863,323</b>	<b>432,192</b>	<b>3,441</b>	<b>435,633</b>	<b>15.2%</b>	<b>19.1%</b>	<b>16,276</b>	<b>1,808</b>	<b>\$1.49</b>
Roseville/Rocklin										
Class A	39	3,236,467	512,798	1,616	514,414	15.9%	25.5%	23,201	(29,052)	\$2.29
Class B	145	5,105,384	524,998	224,749	749,747	14.7%	19.8%	(40,679)	(20,216)	\$1.70
Class C	50	1,064,414	168,244	10,203	178,447	16.8%	17.3%	(3,391)	22,929	\$1.42
<b>Total</b>	<b>234</b>	<b>9,406,265</b>	<b>1,206,040</b>	<b>236,568</b>	<b>1,442,608</b>	<b>15.3%</b>	<b>21.5%</b>	<b>(20,869)</b>	<b>(26,339)</b>	<b>\$1.87</b>
South Sacramento/Elk Grove										
Class A	6	481,431	4,153	-	4,153	0.9%	0.2%	(3,025)	(343)	\$2.49
Class B	68	2,109,084	126,755	24,278	151,033	7.2%	8.5%	6,892	(11,804)	\$2.29
Class C	51	1,177,068	65,589	-	65,589	6.1%	13.7%	(17,121)	2,024	\$1.42
<b>Total</b>	<b>125</b>	<b>3,767,583</b>	<b>196,497</b>	<b>24,278</b>	<b>220,775</b>	<b>5.9%</b>	<b>9.1%</b>	<b>(13,254)</b>	<b>(10,123)</b>	<b>\$2.04</b>
Yolo County										
Class A	7	706,467	84,601	3,464	88,065	15.2%	13.1%	-	(7,424)	\$2.30
Class B	46	1,695,882	174,099	10,663	184,762	19.6%	12.4%	(3,427)	111,882	\$2.09
Class C	38	793,455	27,714	1,573	29,287	6.1%	3.7%	1,441	20,690	\$1.64
<b>Total</b>	<b>931</b>	<b>3,195,804</b>	<b>286,414</b>	<b>15,700</b>	<b>302,114</b>	<b>9.5%</b>	<b>10.4%</b>	<b>(1,986)</b>	<b>125,148</b>	<b>\$2.02</b>
<b>Totals</b>	<b>1560</b>	<b>68,037,949</b>	<b>9,392,225</b>	<b>720,896</b>	<b>10,113,121</b>	<b>14.9%</b>	<b>19.4%</b>	<b>(256,799)</b>	<b>(299,404)</b>	<b>\$1.98</b>
<b>Class A</b>	<b>164</b>	<b>18,996,357</b>	<b>2,897,535</b>	<b>249,482</b>	<b>3,147,017</b>	<b>16.6%</b>	<b>22.6%</b>	<b>(175,387)</b>	<b>(227,208)</b>	<b>\$2.56</b>
<b>Class B</b>	<b>811</b>	<b>34,760,118</b>	<b>4,995,072</b>	<b>449,443</b>	<b>5,444,515</b>	<b>15.7%</b>	<b>19.9%</b>	<b>(28,388)</b>	<b>(67,260)</b>	<b>\$1.78</b>
<b>Class C</b>	<b>575</b>	<b>14,281,474</b>	<b>1,499,618</b>	<b>21,971</b>	<b>1,521,589</b>	<b>10.7%</b>	<b>13.9%</b>	<b>(53,024)</b>	<b>(4,936)</b>	<b>\$1.67</b>
<b>Downtown</b>	<b>167</b>	<b>11,993,172</b>	<b>1,742,161</b>	<b>25,961</b>	<b>1,768,122</b>	<b>14.7%</b>	<b>17.9%</b>	<b>(94,914)</b>	<b>(219,911)</b>	<b>\$2.97</b>
<b>Suburban</b>	<b>1,383</b>	<b>56,044,777</b>	<b>7,650,064</b>	<b>694,935</b>	<b>8,344,999</b>	<b>14.9%</b>	<b>19.7%</b>	<b>(161,885)</b>	<b>(79,493)</b>	<b>\$1.91</b>