



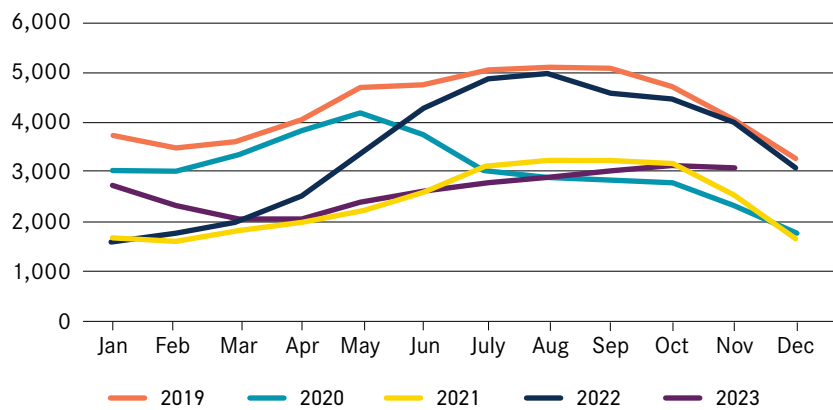
Residential

Seasonality has finally returned to Sacramento. However, the new home market continues to outperform the resale market as limited inventory and elevated mortgage rates persist in the second half of 2023.

Resale listings have gradually climbed since March 2023, but as of November 2023, they are still about 24% below listing levels of October 2019, a more normal year for housing. Trailing-twelve-month resale closings are at the lowest level since 2008. The recently cooling mortgage rates (peaked at 7.6% in October in Sacramento) may unlock more resale supply before the spring selling season.

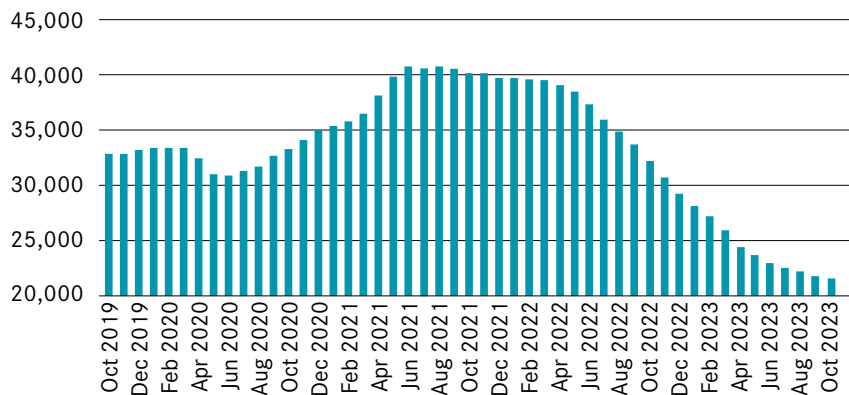
Public home builders continue to leverage mortgage rate buydowns to draw buyers in and help with affordability challenges. Many new home communities with quick move-in inventory offer rate buydown programs. These communities typically perform better than communities without quick move-in inventory, as quicker closes allow buyers to feel more confident about their closing mortgage rate.

Figure 1
Sacramento Total Resale Listings by Month



Source: JBRREC estimates; John Burns Research and Consulting LLC (Data: Nov-23, Pub: Dec-23)

Figure 2
Sacramento Trailing-12-month Existing Home Sale Closings



Source: John Burns Research and Consulting Analysis of Public Records; John Burns Research and Consulting LLC (Data: Oct-23, Pub: Dec-23)

The apartment market continues to normalize but remains stable. The Burns Apartment Rent Index™ shows rents as of October 2023 are down one percent year-over-year, but still up one percent since January 2023. Apartment occupancy also remains healthy at 94%.

Office

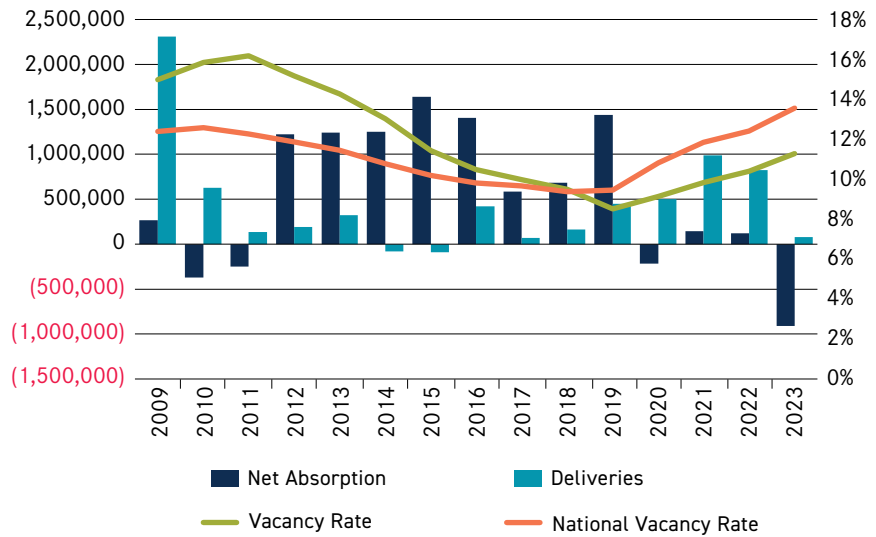
The Sacramento office market continues to struggle as tenants seek to downsize their space and increase operational efficiency. Prospective tenants are seeking high quality buildings in prime locations with as many amenities as possible at a cheaper rate, putting pressure on property level cash flows and values. Net absorption fell to the worst figure this century, but the lack of office construction over the past decade has kept vacancy rates lower than either San Francisco or Oakland.

Poor demand and decreasing effective rents are putting significant downward pressure on property values. On average, office properties traded for less than industrial buildings in 2023, and there are examples of deals closing at one-eighth the cost to build the project today. Falling prices have given users an opportunity to own their real estate. User sales tripled in 2023 as a percentage of total sales volume, with companies looking to take direct control of their costs. More pain is expected in the new year with some estimates pointing to a 30% or more decrease in value.

Industrial

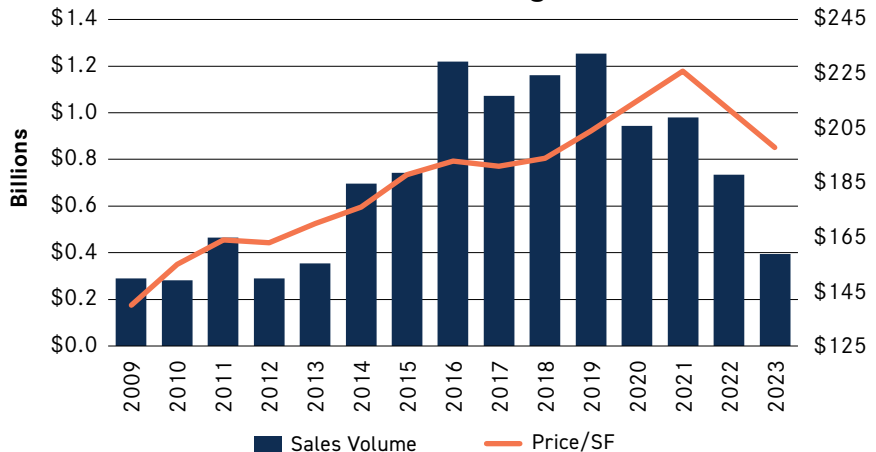
The industrial sector remains the best performing commercial asset class, but it has not been immune to a slowing economy. Demand for large distribution buildings has evaporated as the ecommerce boom that accompanied the pandemic has waned. At the same time, development totaling 2.4 million square

Figure 3
Office Market Activity: 2009-2023



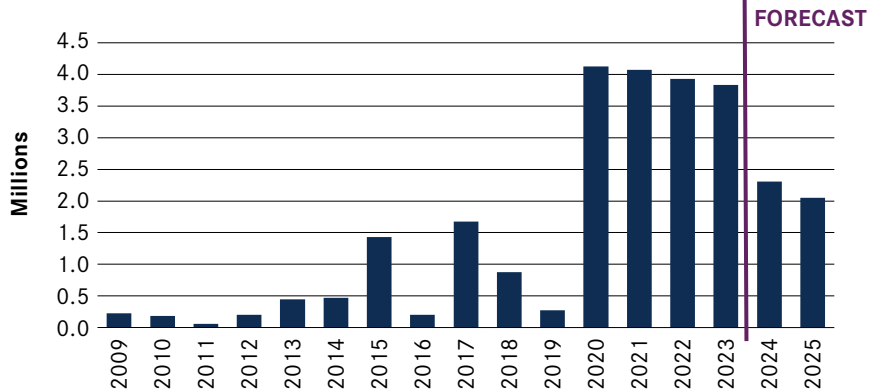
Source: CoStar

Figure 4
Office Sales Volume & Pricing: 2009-2023



Source: CoStar

Figure 5
Industrial Deliveries: 2009 - 2025



Source: CoStar

feet remains. However, construction starts have slowed to their lowest level since 2018, a sign that the risk of oversupply that existed earlier in the year is diminishing.

Demand remains for the market's smaller spaces, and space is still difficult to source. There have been no new industrial parks built for more than a decade, leaving small users with very few options in the market. That is unlikely to change in the near term, as replacement costs still far exceed sale prices for these properties.

Low vacancy has allowed for rent growth in the market, which is up by 5% year over year. The industrial market has not softened like the office sector, and tenants do not have the leverage to command similar concessions. However, there is some indication that property owners are more willing to offer something to attract tenants, especially compared to 12 to 18 months ago.

The industrial market also saw a slowdown in sales transactions during the year, but it is not expected to have the pricing erosion seen in other asset classes. It is one of the few aspects of the market where public and institutional capital was active throughout the year. These sophisticated investors have largely chosen to remain on the sidelines and wait for prices to fall, with industrial being the only exception. Sales volume is likely to increase in the new year as cap rates are expected to increase slightly. However industrial property values should remain relatively stable, comparatively.

Figure 6
Industrial Market • Vacancy & Avg Asking Lease Rate: 2009 - 2025

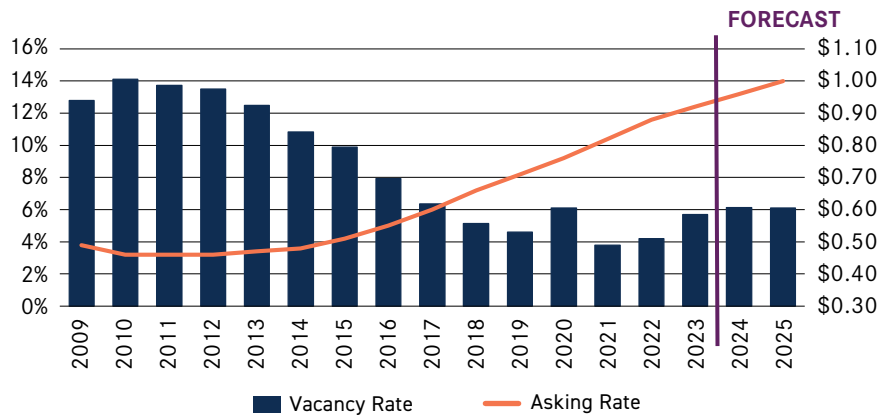
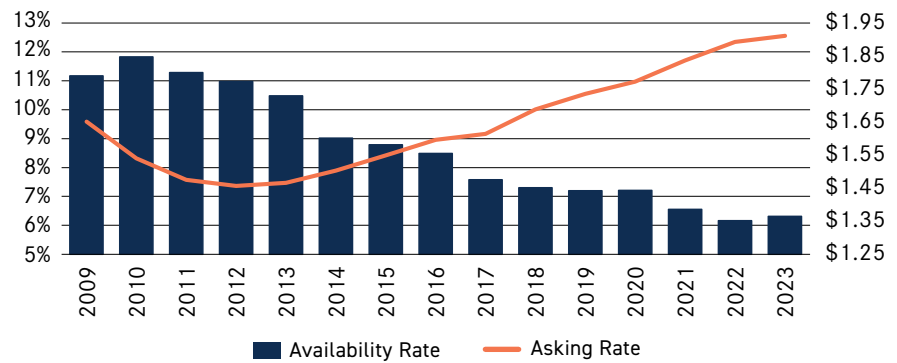


Figure 7
Retail Market • Vacancy & Avg Asking Lease Rate: 2009 - 2025



Source (Figures 6 & 7): CoStar

Grocery-anchored retail in particular has been resilient and continues to achieve a premium over the rest of the market.

Retail

The retail sector remains on good footing and leasing activity is solid. The market has benefited from the lack of construction in recent years, which has helped to keep the availability rate low. Current levels are some of the lowest since the Great Financial Crisis and are not expected to increase greatly in the new year. Net absorption was modest but positive in 2023, totaling 169,000 square feet. The figure would be higher, if not for moveouts in the Sunrise Mall as that property prepares for redevelopment.

Like the rest of the market, sales activity slowed significantly during the year. Fortunately, the underlying market fundamentals are strong and are helping some deals to close. Grocery-anchored retail in particular has been resilient and continues to achieve a premium over the rest of the market. The effect of higher interest rates is not expected to show in transactions data until 2024 as the bid-ask gap between buyers and sellers begins to diminish and properties trade at higher frequencies.