



## Regular Meeting

### Item Number 12 – Open Session

**Subject:** Leasing Strategy for 100 Waterfront Place

**Presenter(s):** Melissa Norcia, Jeff G Isham, and Alexis Garrett, JLL

**Item Type:** Information

**Date & Time:** January 10, 2024 – 15 minutes

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**Attachment(s):** None

**PowerPoint(s):** Leasing Strategy Update

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#### **Item Purpose**

The purpose of this item is to update the board on CalSTRS leasing strategy for leasing floors that will be available at 100 Waterfront Place, once the headquarters expansion is completed.

#### **Summary/Background**

In 2016, the board reviewed a financial analysis of three different options to support CalSTRS long-term facilities strategy. The option to expand the existing campus, which was ultimately approved by the board, included assumptions for CalSTRS tenant improvement costs, the revenue expected from leasing about 175K square feet of office space available at 100 Waterfront Place, and the timing of recapturing the space for its own projected growth. The market at that time supported the terms assumed and JLL and CalSTRS were both extremely confident in our ability to lease space to a state agency or a private tenant. In 2019, CalSTRS engaged JLL's real estate team to market our space to third party tenants. Through this effort, a website and marketing materials were developed dedicated to the CalSTRS building and broad outreach was conducted with city representatives and the state announcing the availability of the space. It was assumed at that time that a state tenant would be the most logical fit based on the existing layout and ratio of open office and private offices per floor, and the opportunity to reuse the existing furniture at no extra cost to the tenant.

But in 2019, the COVID pandemic hit and significantly changed the way we all work. Out of necessity, companies and state agencies sent their employees to work from home until the crisis was over and it was safe to return to the office. Unfortunately, the return to work has not been consistent across the state, and many companies and state agencies are still allowing 100%

telework while others are working in some hybrid fashion. Because of this, the demand for commercial office space has been reduced dramatically. Nearly three million square feet of occupancy loss has occurred since the onset of the pandemic and the downtown Sacramento market is seeing vacancy rates as high as 22%. The pandemic has had a significant impact on leasing activities as many state agencies and private companies continue to work in 100% telework or hybrid working environments. As leases expire, tenants are modifying office usage to reduce space and renegotiate lease terms. With a smaller pool of active tenants in the market, landlords have been compelled to reduce lease rates and offer increased leasing incentives such as free rent and turn-key tenant improvements.

This current climate has created more challenges than anticipated in a pre-COVID environment for CalSTRS to find tenants to lease the office space that will be available at 100 Waterfront Place, especially with the more favorable tenant terms expected with the original analysis. The number of tenants in the market for office space are limited, so the team is embracing ways to meet the requirements of the requests for proposals we have received to date, while mindful of the return on investment to the fund.

### **Discussion**

The main goal has always been to find a long-term stable public or private tenant, requiring full floors at a time. This continues to be the focus with a state or city agency being ideal due to their utilization of large open floor plates which complement the existing build out of the available floors and would require fewer tenant improvements.

We have continued interest from three prospects: a private tenant, a state agency and a school district office. We have responded to the proposals of the private tenant and the school district, but the state agency is still working with Department of General Services to determine their square footage needs and space programming requirements as well as timing for occupancy. We also continue to track a large state agency who is currently located in downtown Sacramento and the CalSTRS building remains an option for a large private company currently located in West Sacramento. In addition, we will begin marketing the building to support the state and local community for any training, conference or meeting needs for rental income for floors that aren't leased by long-term tenants.

Staff and JLL have engaged with the CalSTRS Real Estate investment team on our current leasing efforts and strategy and they are in agreement with our approach. The CalSTRS Real Estate team is experiencing similar leasing challenges on the nationwide office portfolio they manage. Demand in virtually every market is muted. Capital expenditures for tenant improvement allowances needed to secure new leases has increased significantly. Real Estate staff concur that continuing to seek state office users who can make use of CalSTRS existing premises with minor tenant improvement modifications makes the most sense at this time. The CalSTRS Real Estate team believes CalSTRS staff and JLL personnel who are working on trying to sublease CalSTRS premises have been employing the correct leasing strategy and have excellent marketing materials. The lack of results to date in their opinion is a reflection of the

extremely challenging leasing market. CalSTRS HQ has numerous features and amenities that should make it a candidate for consideration for tenants in the market when leasing activity picks up again.

In addition, we are continually tracking CalSTRS growth and additional spacing requirements as it aligns with CalSTRS strategic plan. The spacing needs of business areas such as Legal, Investments, and Technology Services programs requires a comprehensive strategy to efficiently accommodate the expansion needs of the organization. This may involve holding back a few floors from leasing if the timing for CalSTRS needs does not align with a potential lease agreement.

Alexis Garrett with JLL will walk the board through how they evaluate potential leasing opportunities as well as present an 18-month Sacramento region leasing activity history to discuss what types of tenants are moving where. Staff look forward to board feedback on CalSTRS strategy to leasing 100 Waterfront Place.

**Next Steps:**

Staff will continue to partner with JLL in preparing 100 Waterfront Place for leasing opportunities and will provide the board quarterly progress updates in the CEO report at the regular board meetings.

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Strategic Plan Linkage: Goal 1: Ensure a well-governed, financially sound trust fund.

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