MARKET OUTLOOK 2019 ROCHESTER

ROCHESTER OVERVIEW

Located on the southern shore of Lake Ontario in the western region of Upstate New York, the Greater Rochester Area is the State’s third largest metropolitan area, home to a population of 1.1 million. Situated on the I-90 (New York State Thruway) corridor, the community is centrally located in the Northeastern United States, within 500 miles of one-third of the U.S. and Canadian populations. Rochester enjoys close proximity to the global business centers of Toronto, New York City and Boston, while offering a lower cost of doing business and quality of life advantages not found in its larger neighbors.

ECONOMIC PROFILE

The presence of Eastman Kodak, Bausch & Lomb and Xerox has traditionally led to Rochester being viewed as a big company town. Today these companies employ less than 2% of the area’s total workforce, as Rochester has become home to a much more diversified and balanced economy. Some of the industry clusters for which Rochester is best known include healthcare, photonics, optics, digital & health imaging, precision manufacturing, telecommunications, information technology, higher education, and the biosciences. The established strength of the area’s high-tech industries and the continued investments that are being made in these industry sectors suggest a bright outlook for Rochester’s future economy. A few of the most recent accolades for the Rochester business environment include:

- The New Republic named Rochester “One of the most innovation-intensive metro areas in the country” and Atlantic magazine lists Rochester as one of its “35 innovations hubs in the country” based on the number of start-up companies, patents, and entrepreneurs.
- The Brookings Institute ranked Rochester 13th in the U.S. for patents issued per million residents.
- Scientific Reports ranked Rochester among the

ABOUT US

CBRE|Rochester is an affiliate office of CBRE Group, Inc. and offers a full suite of commercial real estate services to clients in the Greater Rochester Area. Please visit our website at www.cbre.com/rochester to learn more.

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Top 20 in its list of “The World’s Leading Science Cities”.

EDUCATION AND INDUSTRY
Education is a cornerstone of Rochester’s economy. The region is home to 18 colleges and universities and Rochester is one of only six cities in the U.S. to have multiple research centers, including the University of Rochester and the Rochester Institute of Technology. Area universities have a total enrollment of 80,000 students with 15,000 degrees conferred annually. Rochester ranks among the top locations nationally for degrees conferred in mathematics, physical sciences, biology, and engineering. These educational resources and the strong partnerships that exist between the academic and business communities are a critical component in sustaining Rochester’s growth in the high-tech sector. Recent highlights include:
• Seven area schools were ranked in U.S. News and World Report’s list of “top regional and national universities”.
• The University of Rochester Medical Center’s (URMC) Strong Memorial Hospital is consistently recognized in U.S. News and World Reports as one of “America’s Best Hospitals” with multiple specialties ranking among the top programs in the country.
• U.S. News and World Report ranked 8 area high schools in the top 5% in the U.S. and Newsweek ranked 5 area high schools in the top 500 in America.

QUALITY OF LIFE
Rochester enjoys a distinct four-season climate that is moderated by the City’s proximity to Lake Ontario. Due to the unique geography of the region, there are a wide variety of activities and cultural amenities available to appreciate. Warmer months find people flocking to some of the area’s 140 annual festivals as well as the numerous local waterways including Lake Ontario and the Finger Lakes (7% of the world’s fresh water supply is located in the Rochester region). Rochester is also home to numerous championship golf courses and Golf Magazine ranked Rochester as one of the 10 Best Golf Cities in America. Rochester takes pride in its quality of life, with a few recent highlights including:
• Bloomberg Businessweek ranked Rochester among “America’s 50 Best Cities” based on factors including leisure attributes, educational attributes, economic factors, crime, and air quality.
• Rochester was ranked the most affordable housing market in the U.S. (among 53 markets with a population over 1 million), according to a study by Demographia International
• Rochester ranked #2 on CNN Money’s list of “Least Stressed Out Cities”, Kiplinger named Rochester the “best city in the U.S. for commuters” and Forbes magazine ranked the Rochester area the “3rd best metropolitan region in the country for raising a family”.
• The Finger Lakes Region is home to the country's second largest wine region, and was listed among “Top 10 Lakeside Vacations that Have it All” by Yahoo! Travel.

And while Rochester’s weather is often discussed...
• The Weather Channel named Rochester one of “The Safest Weather Cities in the U.S.”
Rochester Retail, Outlook 2019

Significant changes at big-box properties continuing to reshape the retail market

- Metro Vacancy Rate: 11.3%
- Metro Inventory: 22.3 MSF
- Metro Vacancy: 2.5 MSF
- Metro Occupied: 19.8 MSF

*Arrows indicate change from previous year

Source: CBRE Research, Q4 2018.

- The closing of multiple big-box store and mall anchor locations over the past 24 month will continue into 2019. While creating a significant statistical impact on the retail market, these closings are also paving the way for some of these properties to transition to alternative (non-retail) uses.
- A limited amount of new construction is currently underway and minimal deliveries are forecast for the upcoming year.

**RETAIL MARKET OVERVIEW**

The Metropolitan Rochester retail market consists of 22.3± million square feet of space with approximately 89% of the total inventory distributed evenly across four submarkets: the Northwest, Southcentral, Southeast and Northeast. The key towns in the Greater Rochester retail market are Greece, Henrietta, and Victor, due to the influence of their superregional malls: The Mall at Greece Ridge Center, Marketplace Mall, and
Eastview Mall, respectively. These malls have served as catalysts for significant growth well beyond the boundaries of the properties and new retailers entering the Greater Rochester Area typically select one of these three trade areas as the location for their initial store. Recent deliveries in the City of Rochester have also reestablished this as a location retailers are considering for an initial store.

2018 saw a notable increase in vacancy as several big-box retailers announced closings including Sears, Kmart, Sam’s Club, Toys R Us and Tops Markets. While some of these properties will be backfilled by new retail tenants, others are likely to be adapted for alternative uses including office, industrial and residential. The conversion of these former retail properties is a trend which has already begun to reshape several large properties in the Rochester Area and is expected to continue.

As was the case in 2018, a limited number of new retail deliveries are forecast for 2019. Significant changes and activity within the market will largely focus on existing product, with the absorption or conversion of the aforementioned big-box and mall anchor space having the greatest potential impact.

**RETAIL MARKET DEVELOPMENTS**

* The latest addition to Rainaldi Real Estate’s Highpoint development is scheduled to open in early 2019. The 25,000 square foot retail building, which draws its’ architectural inspiration from the historic mill structures found across Upstate New York, will be anchored by The New York Beer Project.
* 2018 saw big-box home décor retailer, At Home, open their second location in the market. The new store is occupying 86,000 square feet vacated by Kmart in the Northwest Submarket.
* LA Fitness continues to expand in the local market with the start of construction on a new facility in the City of Rochester. The 34,000 square foot facility is scheduled to open in 2019.
* The adaptive reuse of former retail properties for non-retail uses is beginning to change the way we view vacant retail space in the Rochester market. Notably in 2018, Rochester Regional Health celebrated the ribbon cutting on a new 74,000 square foot medical care facility within a portion of what was formerly a grocery anchored shopping center. Similarly the former Irondequoit Mall continues to progress on its transformation into a mixed-use development with the announcement that PathStone plans to convert the former Sears department store into 73 apartments. A new five-story building is proposed as part of the project, adding space for an additional 100 apartments.
Rochester Office, Outlook 2019

Transitions in office market deliver significant changes to downtown

• Metro Rochester’s vacancy rate experienced an uptick in 2018 primarily due to a sizable move at one Downtown property. Looking outside this one property, leasing performance in most parts of the office sector was positive over the year.
• Interest in Downtown office space continues to increase as Downtown properties are once again considered alongside Suburban alternatives.
• Additions to suburban inventory are generally user driven, rather than speculative, allowing for continued stability in this sector.

OFFICE MARKET OVERVIEW

The Metropolitan Rochester office market is comprised of approximately 15.3± million square feet of competitive, Class A and B office space. (An additional 4.5± million square feet of single-tenant, owner occupied space is classified as part of the non-competitive inventory and is not included in office statistics.) Of the competitive inventory, 43.0% is located in the City and 57.0% is located in the suburban submarkets.
THE CITY SUBMARKET
The City of Rochester is home to approximately 6.6± million square feet of office space. Downtown's office market has gained significant momentum in recent years with new owners, expanding tenants, and mixed-use conversions all contributing to an increasingly vibrant market. Downtown's Class A market saw vacancy decrease to 17.7% at year-end. The Class B market experienced a sharp increase in vacancy, primarily due to Xerox's move from their iconic Downtown office tower to owned space within their campus in the Town of Webster. As recent years have seen a significant amount of older Class B office space converted to alternative uses, how this property will be utilized in the future remains an open question.

THE SUBURBAN SUBMARKETS
Rochester’s suburban office inventory is comprised of approximately 8.7± million square feet of space and is primarily focused in the Southcentral and Southeast Submarkets. 2018 saw suburban vacancy decrease to 9.9%, fueled by a combination of strong leasing in the Class B sector and steady performance from Class A properties. Additions to suburban inventory were limited in 2018 as new construction continues to be user driven.

OFFICE MARKET DEVELOPMENTS
* Buckingham Properties began construction on the first two buildings within Alex Park North, a mixed-use campus in the City of Rochester. Mindex Technologies, an I.T. and software development firm, will occupy the ground floor of a four-story, 78,000 square foot building which will have 48 apartments on the upper three floors. Elsewhere on the site, construction was started on a 19,200 square foot building for Central Rock Gym, a climbing and fitness facility with operations in four states. Both buildings are scheduled for delivery in 2019. Current plans for Alex Park call for the addition of five more buildings and a parking garage.
* 2018 saw Datto, a Connecticut based cybersecurity firm, celebrate the ribbon cutting on their new space within The Metropolitan. The firm is occupying 84,000 square feet on six-floors in Gallina Development’s mixed-use project.
* Office growth along the Southeast Submarket’s Route 96 corridor continued in 2018 with the construction of 1162 Pittsford-Victor Road. Developed by RYCO Management, the new 40,000 square foot building will be occupied by Macerich and Northwestern Mutual in 2019. RYCO also made two significant additions to their office portfolio in 2018 with the purchase of 330,000 square feet of office space at Corporate Crossings Office Park and Canal View Office Park.
Rochester Flex, Outlook 2019

Flex market demand remains strong as vacancy rate decreases in 2018

**Metro Vacancy Rate**
- metro vacancy rate: 10.3%

**Competitive Inventory**
- 5.1 MSF

**Construction Starts**
- 44,776 SF

**New Deliveries**
- 172,250 SF

*Arrows indicate change from previous year

**Figure 8: Flex Vacancy Rate**

Source: CBRE Research, Q4 2018.

• Rochester’s flex market closed out a strong year in 2018 with significant positive absorption and a slight decrease in the vacancy rate in spite of several new additions to inventory.

• 2019 should see further tightening in the flex market as deliveries are expected to decrease from 2018 and demand for flex product is expected to remain consistent.

• The geography of flex development continues to expand as both infill locations as well as the “edge” of the market continue to attract new development.

**FLEX MARKET OVERVIEW**

Metropolitan Rochester’s flex market is comprised of approximately 5.1± million square feet of competitive space. The primary submarkets for this property type are the South West, South Central, and South East which account for nearly 90% of the flex market. The Towns of Gates, Henrietta, and Victor possess the largest concentrations of space within the three primary submarkets.
Relative to Rochester’s industrial and office inventories, the area’s flex market is comparatively new with a significant percentage of the market’s total inventory having been constructed since the year 2000. This product type has performed well over time, consistently exhibiting positive annual net absorption. Much of the flex market’s success is attributable to its unique ability to respond to the changing needs of business and quite literally its “flexibility” in satisfying the demands of a broad spectrum of uses, most notably light industrial and open plan office uses. Consequently, the flex market has had a notable impact on the traditional office and industrial markets.

2018 saw an increase in the competitive inventory due to the delivery of new ground-up construction in the Southcentral Submarket, notably at Erie Station Business Park and on John Street in Henrietta. The Metro vacancy rate finished the year at 10.3%, down slightly from the prior year, and well below the 10 year average for the product type. Vacancy should continue to decline through 2019 as demand is expected to remain steady while a decrease in construction starts in 2018 will result in fewer new deliveries in the year ahead.

**FLEX MARKET DEVELOPMENTS**

* LeFrois Builders & Developers completed construction of a new 100,000 square foot flex building for IDEX Health & Science in the Southcentral Submarket. The facility, which was completed in the third quarter of 2018, will serve as an “Optical Center of Excellence” by consolidating multiple business units from three Rochester Area buildings as well as one operation previously based in California.

* 2018 saw Konar Properties complete construction of a 61,000 square foot flex building within Erie Station Business Park, a mixed-use development in the Southcentral Submarket. Pharmacy Alternatives is the first tenant in the new facility.

* Following a multi-year renovation effort by Rainaldi Real Estate, the Riverwood Tech Campus has begun to welcome its first new tenants. Innovative Solutions, eLogic, Pharos and Alstom Signaling will all call the four building campus home in 2019.

* Growth continues at MCA Development’s OmniTech Business Park in the Southeast Submarket. A new 21,776 square foot building is under construction and scheduled for delivery in 2019. Upon completion of this latest building, the park’s total size will be approximately 300,000 square feet.

* Gallina Development continued to expand the geography of their portfolio with the development of a 27,000 square foot flex building in Genesee County’s Gateway II Business Park.
Rochester Industrial, Outlook 2019

Industrial vacancy continues to decrease as occupier driven construction increases

Metro Vacancy Rate 6.7%
City Vacancy Rate 8.2%
Suburban Vacancy Rate 5.7%
Metro Inventory 77.1 MSF

*Arrows indicate change from previous year

Figure 11: Industrial Vacancy Rate By Geography

The Metro Rochester industrial market continued to tighten in 2018 as the vacancy rate decreased to 6.7%.
Industrial occupiers, particularly larger space users, are finding it difficult to find space within the existing inventory. For this reason, expansions and new construction continue to increase.
Despite numerous deliveries projected for 2019, new industrial development remains largely user driven rather than speculative.

Source: CBRE Research, Q4 2018.

INDUSTRIAL MARKET OVERVIEW

The Metropolitan Rochester industrial market is comprised of approximately 77.1± million square feet of owner and tenant-occupied space. Approximately 40.7% of the market’s inventory is located in the City of Rochester with the remaining 59.3% located in the suburban submarkets. Overall, 2018 saw the metro vacancy rate decrease to 6.7% led by the suburban submarkets which ended the year at 5.7%.
NEW CONSTRUCTION

Over the past 20 years, a significant amount of the industrial product introduced into Rochester’s competitive market has come from the repurposing of large, corporately owned facilities for use by third party tenants. (This contrasts with additions to competitive inventory by way of new construction.) While these formerly owner occupied facilities tend to be quite large, they are now multi-tenanted and have experienced extremely strong absorption. The remaining number of buildings which are good candidates for this type of conversion is rapidly dwindling.

Compounding this trend, much of the region’s older industrial product has reached a point of functional obsolescence, and is no longer viable for supporting modern manufacturing and logistics requirements. As a result, the Rochester Area has seen a noticeable up-tick in new, ground-up construction of industrial (and flex/industrial) space in recent years, notably for larger requirements. Expansions of existing facilities are also on the rise as companies are finding it more challenging to satisfy space requirements through existing inventory. With multiple user-driven projects currently under construction, this trend will continue through 2019.

INDUSTRIAL MARKET DEVELOPMENTS

• 2018 saw New York City based WBS Capital Inc purchase the former Eastman Kodak Hawkeye facility, a property with a secretive history due to the classified work done there for the US Government during the Cold War. The seven building, 785,000 square foot facility, will undergo a $55 million redevelopment effort which will be broken into three phases. Phase 1 will involve the creation of a 406,000 square foot Foreign Trade Zone (FTZ) warehouse which will be operational in 2019.

• Less than a year after breaking ground, American Packaging Corp celebrated the opening of a 215,000 square foot expansion to its facility in the Southwest Submarket. The $50 million project is the first phase of a three phase expansion effort projected to total 350,000 square feet.

• Online retailer Amazon selected the Rochester market for one requirement in 2018. Slightly smaller in scale than their HQ2 requirement, Amazon opened a 70,000 square foot distribution center in the Southcentral Submarket.

• Ground was broken on a new 300,000 square foot facility in the Southwest Submarket for C&M Forwarding. The freight transportation and commercial warehouse company is projected to occupy the space in the second half of 2019.

• 2019 will also see the completion of a new 50,000 square foot facility in the Southcentral Submarket for OFD Foods, a leader in freeze dried technologies.
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