

MANSFIELD COMMERCIAL REAL ESTATE

Overview of the Commercial Real Estate Market in Orange County, NY at Year-End 2016

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The Industrial Market in 2016

A significant amount of speculative industrial construction was commenced in 2016, for the first time in over ten years. And, not surprisingly, before those buildings were completed, 100% of the space was leased. But even with speculative development starting up again, the vacancy rate for prime industrial space in Orange County, NY continued to drop, setting a new record low at 3.2%. Tenants seeking to lease industrial space had limited choices, as did those seeking to own. Some of the older buildings have filled that void, with renovations and restorations able to accommodate the needs of smaller users. But for most, build-to suit construction continued to be the solution.

The total inventory of prime industrial space stood at 21.2 million square feet at year-end 2016, with eight new construction projects coming on-line totaling 214,000 square feet. Six of these were constructed to suit: Old Dominion Freight Lines constructed 40,000 square feet on Ballard Road in the Town of Wallkill; PharmaCann completed its 26,000 square foot medical marijuana research, development and processing facility alongside its grow houses in the Town of Hamptonburgh; Piller, a manufacturer of uninterruptible power systems, moved into its new 24,000 square foot U.S. Headquarters on Wes Warren Drive in the Town of Wallkill; Suresky, a local auto dealer, constructed a 12,500 square foot storage and prep facility in the Town of Chester; Highground Industrial, a demolition contractor, built a 7,500 square foot facility on Industrial Drive in the Town of Goshen; and Pavestone, a manufacturer and distributor of modular concrete landscape products, expanded its Town of Montgomery facility by 6,000 square feet.

The remaining two projects were constructed on spec: in the Town of Goshen, a 40,000 square foot flex building, designed to accommodate tenants as small as 10,000 square feet, was leased to three tenants, and is now fully occupied. This developer has plans to construct two more 60,000 square foot flex buildings on the site, and will reportedly start the next, on spec, as soon as the approvals are in place. In the Town of Chester, a 58,000 square foot building on Bellvale Road was completed by a local investor and sold to Allstate Manufacturing, a marble and granite countertop wholesaler that expanded into the area from Rockland County. Initially approved as a fitness center, the steel for this building was erected about 25 years ago, but the project stalled until this investor converted the approvals to industrial and finished it.

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Approximately 860,000 square feet of industrial space was absorbed in 2016, a level of activity that is below average for the last ten years. Over 550,000 square feet of this was activity in prime industrial buildings. Some of the notable transactions were the sublease by Alumil Fabrications of 50,000 square feet in Newburgh's Northeast Business Center; in the Town of Montgomery, the U.S. Department of Homeland Security leased 41,000 square feet on Bracken Road, and Valad Electric purchased a 41,000 square foot building on Leonards Drive (they will occupy 30,000 square feet, seeking a tenant for the remainder); Russin Lumber leased 26,000 square feet in Maybrook; and the 21,000 square foot former Grainger building in the Town of Newburgh was purchased by Big Shine Energy, a distributor of LED lights. Approximately two-thirds of these prime deals were lease transactions and the remainder were purchases.

The remaining 300,000 square feet absorbed in 2016 was in older, non-prime buildings. The two largest of these transactions were both in Port Jervis: the purchase by Kolmar, a cosmetics manufacturer, of a 92,000 square foot facility on Ralph Street; and the acquisition by US Crane & Rigging of a 140,000 square foot building on Skyline Drive (formerly occupied by Kolmar). The total industrial inventory, including non-prime space, was 27.8 million square feet, with a vacancy rate of 4.9%. This vacancy rate is about one-third of what it was at its peak in 2009. Both users and investors seeking to satisfy the need for additional product are turning to these facilities more frequently, given the savings compared to new construction, and the increasingly limited number of prime buildings and development sites.

Over 1.3 million square feet of industrial space was under construction as of year-end 2016, the most ongoing industrial development in the County in over 15 years. In early 2017, Matrix Development Group is expected to complete its 565,000 square foot Town of Newburgh building, 317,000 square feet of which was preleased to AmerisourceBergen, a pharmaceutical provider. The balance of the building - 248,000 square feet - was being constructed on spec, and quickly leased to Amscan, the world's largest designer, manufacturer and distributor of decorated party goods and accessories. Amscan is no stranger to Orange County, having had several of its distribution and manufacturing facilities located here for many decades. Amscan will be using the new facility in Newburgh to consolidate and expand its manufacturing operations.

Seven other build-to-suit industrial facilities were under construction at year-end. Pharmaceutical giant McKesson Corporation's 340,000 square foot regional distribution center at Hudson Valley Crossing in the Town of Hamptonburgh is expected to be ready in the spring of 2017. FedEx Ground will be taking occupancy in the second quarter of 2017 of its new 250,000 square foot distribution facility on Neelytown Road in Montgomery. In Chester Industrial Park, Steris AST, which provides contract sterilization services for medical, pharmaceutical, consumer, and industrial applications, will be finishing its second building in the Park, a 71,000 square foot facility also slated to be ready in the second quarter of 2017. Restaurant Depot, a food service supplier to restaurants, is building their 62,300 square foot wholesale cash and carry facility in the

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Town of Newburgh. Monroe Cable will be finishing its 40,000 square foot expansion in early 2017, and Revere Smelting & Refining Corp. is adding 16,700 square feet to its Ballard Road campus, both in the Town of Wallkill. And the Union of Operating Engineers Local 825 is constructing a 7,420 square foot training facility in the Town of Wawayanda.

As of year-end 2016, there was nearly another 1,000,000 square feet of planned and/or approved industrial development, some of which will commence construction in 2017. Most notable is Amy's Kitchen, which received conditional site plan approval in late 2016 for its manufacturing plant in the Town of Goshen. The 369,000 square foot facility is expected to produce 640,000 organic vegetarian meals per day when it is operational in 2018, assuming construction begins in early 2017. About 20%, or 200,000 square feet, of this planned and/or approved industrial development is speculative space which will be a welcome addition to this tight industrial market.

On the horizon, the County is now taking a more proactive approach to economic development in an effort to keep the momentum going. A proposed expansion of the IDA's Shovel Ready Program to include private owners and developers is currently under consideration. Initially enacted in mid-2014, the program was designed to assist only municipalities with the upfront cost to obtain generic approvals and to provide infrastructure for commercial development sites, but its application has been limited. Broadening the program will help to ensure the supply of shovel ready sites that has enabled the County to attract such companies as McKesson and PharmaCann; these two projects alone will make a combined investment in the County of over \$100 million. In New Windsor, 200 acres at Stewart Airport is now being offered for sale. Previously this land was available only via land lease - a structure not typical in industrial development - which had inhibited demand.

The County is also working with municipalities and developers to rezone large tracts for commercial development. Redevelopment plans for the former Camp LaGuardia homeless shelter, which the County purchased ten years ago from NY City, have changed from residential/mixed use to industrial. The property straddles the Towns of Chester and Blooming Grove; the former has already rezoned their portion of the property, and Blooming Grove has been considering a similar rezoning. Approximately half of the 258 acres are suitable for up to 11 development lots. Also, in the Town of Hamptonburgh, the developer of 250 acres adjacent to the successful Hudson Valley Crossing is seeking a rezoning from residential to commercial; the property reportedly could accommodate up to 2,000,000 square feet. All of this will help Orange County to better maintain a ready supply of industrial product to accommodate expected growth.

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The Office Market in 2016

Over the last 15 years, more than 56% of all Class A office space constructed in Orange County, NY was medical related. And in 2016, 100% of the space constructed was build-to-suit medical office space. Other than medical space, though, the demand for office product continued to be softer than most landlords would have liked. But investors seeking bargains were active in 2016, and several of the County's premier office buildings were acquired by new owners.

In 2016, the build-to-suit construction of three medical office buildings, totaling 250,000 square feet, were the only additions to the office inventory. Crystal Run Healthcare, the County's fastest growing multi-specialty physician practice, continued its expansion with construction of a 70,000 square foot facility in the Village of Monroe. Of all the medical space constructed in the County over the last 15 years, 40% of it has been for Crystal Run Healthcare. Orange Regional Medical Center (ORMC), which five years ago constructed the first new hospital in NY State in 20 years added two new buildings to its campus in the Town of Wallkill: a 153,000 square foot medical office building, and a 26,000 square foot cancer center. With these three new buildings, the inventory of Class A office space in Orange County, NY stood at 4.7 million square feet at year-end 2016.

The vacancy rate for Class A office space continued to trend downward slightly, ending the year at 9.1%. There has been no significant speculative office development in the County for over seven years, which has helped to chip away at the vacancy rate, but some of this is offset by the increasing supply of space in two buildings in particular. In the Town of Wallkill, when ORMC relocated to its new on-site medical office building, it vacated approximately 70,000 square feet of leased medical and surgical space at 75 Crystal Run Road. And next door, at 85 Crystal Run Road, a total of 75,000 square feet of back office space will be available when Empire BlueCross BlueShield downsizes again in early 2017. This is a significant amount of space for a market as small as Orange County, a market where the majority of users have historically been in the 1,500 to 3,500 square foot range. But with hospitals and medical practices merging and expanding territories, and with R&D companies seeking to reduce high occupancy costs at their current bases of Westchester or Northern NJ, such large blocks of space provide an opportunity for the County to compete for these users. Both the Town and the County are stepping up efforts to attract office tenants, and are exploring how they might amend their zoning or retool their marketing efforts to do so.

Only one office building was under construction as of year-end 2016: in the Village of Warwick, Dr. Mark Stamm, an ophthalmologist, is constructing 6,000 square feet, of which 3,000 square feet is spec space. It is expected to be ready for occupancy in April of 2017.

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Construction is expected to commence on one other office building in 2017. On Hatfield Lane in the Village of Goshen, an 8,000 square foot medical office building will break ground in the spring for American Renal Associates.

Over 300,000 square feet of office space was absorbed in 2016, over 85% of it in Class A buildings. Most was due to the new medical buildings for Crystal Run Healthcare and ORMC, but other notable deals include the purchase of a 10,000 square foot office building at Hudson Valley Professional Plaza in the Town of Newburgh by Creo Dental, a dental laboratory; Tri-State Bariatrics' purchase of a 9,000 square foot office building on East Main Street in the Town of Wallkill; the lease of 5,000 square feet at Eastgate Corporate Park in Goshen by 10-15 Associates, an investment advisory firm; and the purchase by Stand Back Construction of the 7,500 square foot building on Little Britain Road, formerly owned by Hudson Valley Builder's Association, which leased back a portion of the building. In the Town of Newburgh, the long vacant 15,000 square foot office building constructed on spec in 2009 was finally leased to Grace Church of God.

The renovation of the former O&W Railway Station into the new offices of the Middletown Community Health Center in the City of Middletown is no longer being considered; rehabilitation of this historic building proved to be too costly. The non-profit healthcare provider is now planning to consolidate its operations in the former Horton Hospital. This should be a good fit with Touro College of Osteopathic Medicine, the anchor tenant in the repurposed hospital facility.

Some developers who constructed office space during the 1980's and 90's put their office buildings up for sale for the first time. Four office buildings along the County's premier office corridor, Crystal Run Road, changed hands in 2016. Two of these were partly vacant and the sale prices reflected this. The appetite for Class A assets in the County remains strong.

At year-end 2016, the inventory of total office space in the County, including non-Class A space, was 6.2 million square feet, with a vacancy rate of 10.3%. The City of Middletown, with many of the region's older buildings, was recently awarded a \$10 million grant after competing in a state-wide competition for urban revitalization. Plans for spending the money are underway and will likely include façade improvements, public art, new bus loops, enhanced walkability, additional parking, broader telecommunications capacity and developing infrastructure for fitness and recreation. This transformation is designed to attract young professionals, students, and new businesses to the Downtown area. In 2017, the City will also become home to the County's next business accelerator; this IDA-funded program provides work space and support for start-up businesses.

So whether future office demand is for large blocks of high-tech, medical, or surgical space, or for a rehabbed historical building in a more urban setting, Orange County should be able to satisfy whatever comes its way.

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