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Research & Strategic Analysis

EXECUTIVE SUMMARY

An Analysis of Residential Market Potential

The JOSANA Neighborhood

The City of Rochester, Monroe County, New York

October, 2010

This study was undertaken to examine the market potential for newly-introduced housing units—created through new construction, as well as the adaptive re-use of suitable existing buildings—that could be leased or sold within the JOSANA Neighborhood in the City of Rochester, New York. This study includes the determination of the market potential for workforce/affordable (affordable to households with annual incomes between 30 and 80 percent of the Rochester Area Median Family Income) as well as market-rate (above 80 percent of AMI) housing units.

The extent and characteristics of the potential market for new and existing housing units within the city and the JOSANA Neighborhood were identified using Zimmerman/Volk Associates' proprietary target market methodology. This methodology was developed in response to the challenges that are inherent in the application of conventional supply/demand analysis to urban development and redevelopment. Supply/demand analysis ignores the potential impact of newly-introduced housing supply on settlement patterns, which can be substantial when that supply is specifically targeted to match the housing preferences and economic capabilities of the draw area households.

In contrast to conventional supply/demand analysis, then—which is based on supply-side dynamics and baseline demographic projections—target market analysis determines the depth and breadth of the potential market derived from the housing preferences and socio-economic characteristics of households in the defined draw area. Because it considers not only basic demographic characteristics, such as income qualification and age, but also less-frequently

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analyzed attributes such as mobility rates, lifestyle patterns and household compatibility issues, the target market methodology is particularly effective in defining a realistic housing potential for urban development and redevelopment.

The current constrained market—characterized throughout most of the United States by significantly reduced housing values; high levels of unsold units, both builder inventory units as well as foreclosed and/or abandoned houses; and high levels of mortgage delinquencies by speculators and investors as well as homeowners—has resulted in very restrictive development financing and mortgage underwriting, taking a significant percentage of potential homebuyers out of the market and preventing numerous for-sale developments from going forward. Nationally, financing has also been challenging for rental developers, with the result that few new residential projects, regardless of tenure, are moving forward.

These market constraints do not reduce the size of the potential market; however, depending on the timing of market entry, they could reduce the initial percentage of the potential market able to overcome those constraints.

This study therefore determined:

- Where the potential renters and buyers of new and existing housing units in the City of Rochester in general, and the JOSANA Neighborhood in specific, would be moving from (the draw areas);
- Who currently lives in the draw areas and what they are like (the target markets);
- How many have the potential to move to the neighborhood if appropriate housing units were to be made available (depth and breadth of the market);
- What their housing preferences are in aggregate (rental or ownership, multi-family or single-family);
- What their alternatives are (relevant new construction or existing rental housing stock in the Rochester market area);
- What they will pay to rent or purchase new units within the neighborhood (rents and prices); and

- How many new dwelling units, both income-qualified and market-rate, could be leased or sold annually within the neighborhood (market capture).

CONCLUSIONS OF THE ANALYSIS

The depth and breadth of the potential market for market for new and existing housing units within the city and the JOSANA Neighborhood have been derived from the housing preferences and financial capacities of the draw area households, identified through Zimmerman/Volk Associates' proprietary target market methodology and extensive experience with urban development and redevelopment.

Where does the potential market for new and existing housing units in the City of Rochester currently live?

Analysis of Monroe County migration and mobility patterns from 2003 through 2007—the latest data available from the Internal Revenue Service—shows that three counties adjacent to Monroe County—Wayne, Ontario, and Livingston Counties—together account for approximately 20 percent of Monroe County's in-migration. Even though the county continued to experience net migration losses, in 2007, the county's net migration loss had dropped to less than 1,000 households, from the high of over 2,700 net households in 2004.

Based on the migration data, then, the draw areas for Monroe County, the City of Rochester and the JOSANA Neighborhood have been delineated as follows:

- The local (or internal) draw area, covering households currently living within the Rochester city limits, as well as those currently living in the balance of Monroe County.

- The regional draw area, covering households with the potential to move to the City of Rochester from three adjacent counties—Wayne, Ontario, and Livingston.

- The national draw area, covering households with the potential to move to the City of Rochester from all other U.S. counties.

How many households represent the market for new housing units in the JOSANA Neighborhood?

As determined by the target market methodology, up to 770 households currently living in the draw areas comprise the annual potential market for new and existing housing units within the JOSANA Neighborhood. The housing preferences of these 770 households—according to tenure (rental or for-sale) and general financial capacity—are detailed as follows: (*see also* Table 1):

Annual Potential Market
For New and Existing Housing Units
THE JOSANA NEIGHBORHOOD
City of Rochester, Monroe County, New York

HOUSING TYPE	NUMBER OF HOUSEHOLDS	PERCENT OF TOTAL
Multi-family for-rent*	330	42.8%
Multi-family for-rent† (lofts/apartments, leaseholder)	220	28.6%
Multi-family for-sale*	40	5.2%
Multi-family for-sale† (lofts/apartments, condo/co-op ownership)	40	5.2%
Single-family attached for-sale*	0	0.0%
Single-family attached for-sale† (townhouses/live-work, fee-simple/ condominium ownership)	20	2.6%
Single-family detached for-sale*	60	7.8%
Single-family detached for-sale† (houses, fee-simple ownership)	60	7.8%
Total	770	100.0%

* Affordable to households with incomes between 30 and 80 percent of AMI in 2010, calibrated by household size.
† Affordable to households with incomes above 80 percent of AMI in 2010, calibrated by household size.

SOURCE: Zimmerman/Volk Associates, Inc., 2010.

Who are the households that represent the potential markets for the neighborhood?

The significant transformation of American households (particularly shrinking household size and the predominance of one- and two-person households) over the past decade, combined with steadily increasing traffic congestion and fluctuating gasoline prices, has resulted in important changes in neighborhood and housing preferences, with major shifts from predominantly single-family detached houses in lower-density suburbs to higher-density apartments, townhouses, and detached houses in urban and mixed-use neighborhoods. This fundamental transformation of American households is likely to continue for at least the next decade.

This transformation has been spurred by the convergence of the two largest generations in the history of America: the 78 million Baby Boomers born between 1946 and 1964, and the 76 million Millennials, who were born from 1977 to 1996. The convergence of two generations of this size—simultaneously reaching a point when urban housing matches their life stage—is unprecedented.

Based on the target market analysis, the potential market for new housing units within the JOSANA Neighborhood consists of a diverse mix of households. The general market segments for the neighborhood, grouped according to lifestage and housing preferences, include (*see also* Tables 2 *through* 6):

- Traditional and non-traditional family households, of which a significant number are single parents with children (52 percent);
- Younger singles and childless couples—including young office, retail, and service workers (29 percent); and
- Empty nesters and retirees, some with incomes from social security alone, others who also have small pensions or savings, and the remainder who are still working (19 percent).

What are their current housing alternatives?

In the JOSANA neighborhood, more than 70 percent of the units, including detached houses, are rented, with rents typically below $650 per month. Some of the rental units are well-maintained, but significant numbers are owned by persons or firms located outside Rochester and are in poor condition, or are over-crowded.

Outside of the JOSANA neighborhood, in the High Falls District of Downtown Rochester, the Mills at High Falls is a 67-unit, mixed-income property located on State Street. The property opened in 2009 and was almost fully leased as of June 2010. Fifty-six of the units are income-restricted to households at or below 50 and 60 percent of the Rochester AMI; restricted rents range from $525 for a 752-square-foot one-bedroom, to $640 for a 1,316-square-foot two-bedroom unit. The remaining 11 units are market-rate, targeted to households at 90 percent of AMI, with rents ranging from $825 to $1,090 for the same units. (*See* Table 7.)

In Downtown Rochester, rents start at $575 per month for a 515-square-foot studio at the Michaels-Stern Lofts and are as high as $2,175 per month for a 1,600-square-foot two-bedroom unit at St. Paul's Lofts. In general, rents per square foot range between $0.49 to $0.70 for the tax credit units, and $0.83 to $1.36 for market-rate units. Vacancy rates are extremely low, with all but the St. Paul's Lofts—which opened in June 2009 and has 16 of its 48 units still under construction—and the Kirstein Building—in lease-up with reconfigured units—at no lower than 98 percent occupancy.

There are very few new multi-family (condominium) and single-family attached (townhouse) units for sale in and around Downtown Rochester. Seven of the 19 Carlton Lofts on Capron Street have sold since the property opened for sales in March 2008. Current prices for the two-bedroom, two-bath units range between $249,000 for 1,528 square feet of living space to $429,000 for a 2,272-square-foot apartment. (*See* Table 8.)

Outside the Loop, townhouses are being marketed at three properties: the six-unit Barrington Park on Barrington Street, the six-unit Rowhouses at 100 Union Street, and the three-unit Tudors on East Avenue. All of the units are priced above $535,000; only one of the 15 townhouses had sold at the time of the field investigation. Unit sizes range between just over 1,900 square feet to nearly 3,900 square feet, with prices per square foot falling between $171 and $285.

In May 2009, active listings of single-family houses on the market in the JOSANA Neighborhood and vicinity have asking prices between $12,000 and $35,000. All of these houses were built between 1866 and 1935, with unit sizes starting at just under 700 square feet (for two bedrooms and one bath) to nearly 2,000 square feet (for four bedrooms and two baths). Five have been on the market for more than 160 days. (See Table 9.)

Single-family houses in the neighborhood and vicinity and marketed between 2005 and 2009 through the Multiple Listing Service were sold for prices ranging between $2,000 and $41,900. All of the houses were built prior to 1935, with sizes ranging between just over 825 square feet to nearly 2,100 square feet. Most of the houses sold in less than 90 days, although a few took half a year or more. Habitat has built several houses over the same period, which are sold at approximately $65,000 for 1,400 to 1,500 square feet of living space.

What kind of units match target household preferences, and, from the perspective of the target markets, what are achievable rents and prices for new construction in the neighborhood?

At the present time, there are 115 vacant buildings in the JOSANA Neighborhood, and 171 vacant parcels which, combined, comprise more than 28 acres. Many of these parcels/buildings are located within the LYLAKS Brownfield Opportunity Area, which will require remediation. Many of the parcels are owned either by the City of Rochester or the Rochester Housing Authority. As a result, the number of new units that could ultimately be constructed within the neighborhood is uncertain; this analysis has therefore tested a total number of 250 units, distributed according to target household preferences, as follows:

Optimum Residential Mix
250 New Housing Units
THE JOSANA NEIGHBORHOOD
City of Rochester, Monroe County, New York

HOUSING TYPE	PERCENT OF TOTAL	NUMBER OF UNITS
Multi-family for-rent*	42.8%	107
Multi-family for-rent† (lofts/apartments, leaseholder)	28.6%	71
Multi-family for-sale*	5.2%	13
Multi-family for-sale† (lofts/apartments, condo/co-op ownership)	5.2%	13
Single-family attached for-sale*	0.0%	0
Single-family attached for-sale† (townhouses/live-work, fee-simple/ condominium ownership)	2.6%	6
Single-family detached for-sale*	7.8%	20
Single-family detached for-sale† (houses, fee-simple ownership)	7.8%	20
Total	100.0%	250

* Affordable to households with incomes between 30 and 80 percent of AMI in 2010, calibrated by household size.

† Affordable to households with incomes above 80 percent of AMI in 2010, calibrated by household size.

SOURCE: Zimmerman/Volk Associates, Inc., 2010.

—UNIT TYPES—

Based on target household preferences, the proposed unit types include soft lofts and apartment flats—in the 83-unit Gardner lofts, in smaller apartment buildings along Broad Street, and in six- to eight-unit mansion buildings on vacant corner locations—rowhouses, and small detached houses.

- Soft Loft: Unit interiors typically have open floorplans, high ceilings and large commercial-style windows, but are fully finished and, where appropriate, have sleeping areas partitioned from the main living area. A soft loft may also contain architectural elements reminiscent of "hard lofts," *e.g.*—exposed ductwork.

- Apartment Flat: Conventionally-finished apartment unit on a single level, with completely-partitioned rooms.

- Townhouse: Similar in form to a conventional suburban townhouse except that the parking pad is located to the rear of the unit and accessed from an alley or auto court. Unlike conventional townhouses, urban townhouses conform to the pattern of streets, typically with shallow front-yard setbacks.

- Detached House: A smaller detached house with a parking pad. The front-yard setback should conform to the context of the block on which it is located.

Based on the socio-economic and lifestyle characteristics of the target households, then, the market-entry base rents and prices for up to 250 newly-developed market-rate and affordable residential units that could currently be sustained by the market is shown as follows (*see also* Table 10):

Optimum Market Position: 250 Dwelling Units
THE JOSANA NEIGHBORHOOD
City of Rochester, Monroe County, New York

NUMBER	HOUSING TYPE	UNIT RENT/PRICE RANGE	UNIT SIZE RANGE	BASE RENT/PRICE PER SQ. FT.
MULTI-FAMILY FOR-RENT—71.4%				
57	Lofts/Apts. *(Income-restricted)*	$450 to $600/mo.	550 to 1,000 sf	$0.60 to $0.82
38	Lofts/Apts. *(Market-rate)*	$650 to $850/mo.	550 to 1,000 sf	$0.85 to $1.18
83	Gardner Lofts *(Mixed-Income)*			
MULTI-FAMILY FOR-SALE—10.4%				
13	Lofts/Apts. *(Income-restricted)*	$40,000 to $50,000	600 to 850 sf	$59 to $67
13	Lofts/Apts *(Market-rate)*	$75,000 to $90,000	650 to 950 sf	$95 to $115
SINGLE-FAMILY ATTACHED FOR-SALE—2.6%				
6	Rowhouses *(Market-rate)*	$95,000 to $110,000	900 to 1,150 sf	$96 to $106
SINGLE-FAMILY DETACHED FOR-SALE—15.6%				
20	Houses *(Income-restricted)*	$65,000	1,400 to 1,500 sf	$43 to $46
20	Houses *(Market-rate)*	$115,000 to $145,000	1,100 to 1,400 sf	$104 to $105
250 Total Units				

SOURCE: Zimmerman/Volk Associates, Inc., 2010.

The proposed rents and prices are in year 2010 dollars and are exclusive of consumer-added options or upgrades. The proposed rent/price points place the units within the current financial capabilities of the target households. However, without subsidies or financial incentives, it will be difficult to build these units at these rent and price points.

The proposed 83-unit Gardner Lofts on Lyell Avenue will accommodate over 60 percent of the 178 new rental units detailed in the optimum market position. The remaining 95 rental units should be developed in mixed-income, mixed-use buildings—with the potential for retail spaces on the ground floor—on the vacant parking lots along Broad Street across from the Marina Auto Stadium or in smaller mansion apartment buildings on vacant lots on Child Street.

The 26 multi-family for-sale units (condominiums) could be developed in small four- to six-unit mansion buildings on corner vacant lots within the neighborhood. The six townhouses could be developed, in three two-unit buildings or two three-unit buildings, on wider vacant parcels within the neighborhood.

Subsidized for-sale houses should continue to be developed on lots within close proximity to each other to create a critical mass of higher-value new construction. The values of the owner-occupied houses in the neighborhood are so low that, over the near term at least, subsidized houses represent a significant increase in value over the existing housing stock. Once both sides of a neighborhood block reach the point where all of the existing units have been upgraded to at least good condition, and most of the vacant lots are occupied by subsidized houses, it should be possible to build and sell two or three "market-rate" houses as long as they are located next to, or across from each other.

As the housing stock in the neighborhood continues to improve, and more new units occupy currently vacant lots, the rent and price points outlined in the optimum market position will begin to rise. The goal will be to reach rent and sales levels that no longer require subsidy.

How many new dwelling units, both income-qualified and market-rate, could be leased or sold annually within the JOSANA Neighborhood?

After more than 22 years' experience in numerous cities across the country, and in the context of the target market methodology, Zimmerman/Volk Associates has determined that those households that can afford, and would prefer new construction, rather than existing or renovated units, represent approximately five to 10 percent of the potential market, given the production of appropriately-positioned new housing. (Until the collapse of the housing market in the fall of 2008, newly-constructed dwelling units represented 15 percent of all units sold in the nation.)

Over the near term, absorption rates could be lower than the annual number of units forecast below due to the uncertain timing of a mortgage and housing market recovery. As noted in the INTRODUCTION, the current constrained market is characterized in many locations by reduced housing prices, high levels of unsold units, high levels of mortgage delinquencies and foreclosures, and restrictive mortgage underwriting and development finance. These market constraints do not reduce the size of the potential market; however, depending on the timing of market entry, they could reduce the initial percentage of the potential market able to overcome those constraints.

Annual absorption for new dwelling units within the JOSANA Neighborhood is forecast as follows:

Annual Average Absorption
THE JOSANA NEIGHBORHOOD
City of Rochester, Monroe County, New York

Multi-family for-rent Lofts/apartments	48 units net of turnover
Multi-family for-sale Lofts/apartments	6 units
Single-family attached for-sale Rowhouses	2 units
Single-family detached for-sale Houses	12 units
Total	68 units

SOURCE: Zimmerman/Volk Associates, Inc., 2010.

Based on this analysis, absorption of 250 new dwelling units within the site would likely be achieved within approximately five years, depending on phasing, construction and site constraints, and barring a long-term continuation of the downturn in the national, regional and local economies,.

These average absorption paces require specific capture rates of those households that, in the year 2011, represent the potential market for each housing type within the neighborhood, as follows:

REQUIRED CAPTURE RATES
Based on Annual Average Absorption
THE JOSANA NEIGHBORHOOD
City of Rochester, Monroe County, New York

HOUSING TYPE	ANNUAL MARKET POTENTIAL (HHS)	ANNUAL AVERAGE ABSORPTION (UNITS)	REQUIRED CAPTURE RATE
Multi-family for-rent Lofts/apartments	550	48	8.7%
Multi-family for-sale Lofts/apartments	80	6	7.5%
Single-family attached for-sale Rowhouses	20	2	10.0%
Single-family detached for-sale Houses	120	12	10.0%

SOURCE: Zimmerman/Volk Associates, Inc., 2010.

From the market perspective, these housing type-specific capture rates of the market for units at the indicated rents and sales prices are reasonable assumptions during recessionary conditions. As the economic environment improves over the next five years, it is likely new construction could begin to capture higher percentages of the annual market potential.

The target market capture rates of the potential purchaser or renter pool are a unique and highly-refined measure of feasibility. Target market capture rates are not equivalent to—and should not be confused with—penetration rates or traffic conversion rates.

> The **target market capture rate** is derived by dividing the annual forecast absorption by the number of households that have the potential to move to the site in a given year.
>
> The **penetration rate** is derived by dividing the total number of dwelling units planned for a property by the total number of draw area households, sometimes qualified by income.

> The **traffic conversion rate** is derived by dividing the total number of buyers or renters by the total number of prospects that have visited a site.

Because the prospective market for a property is more precisely defined using target market methodology, a substantially smaller number of households are qualified; as a result, target market capture rates are higher than the more grossly-derived penetration rates. The resulting higher capture rates remain within the range of market feasibility at the indicated rents and sales prices.