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Billions on sidelines as problem deals pile up

By Daniel Geiger

There were $6.3 billion in real estate sales in 2009, according to the brokerage firm Massey Knakal Realty Services, a precipitous decline from the market's peaks in recent years.

In 2008, $25.3 billion of deals were done citywide and in 2007, at the height of the real estate bubble, a record $62.2 billion of deals were done.

Prices have retreated dramatically from record highs, but the decline also reflected a sharp downturn in the number of sales transactions.

Last year, just 0.87% of the city's stock of buildings changed hands, a paucity of deals below previous record lows set during past economic downturns and real estate collapses in the early 1990s and 2000s. In 1992 and 2003 for instance, Bob Knakal, chairman of Massey Knakal, explained during a breakfast yesterday (Tuesday) in midtown to discuss the year's results, there was a 1.6% turnover rate, what he had previously believed to be a baseline driven by unavoidable circumstances like "death, divorce, taxes and partnership disputes."

"Last year shattered that theory," he said, noting that the 25-year average turnover rate was 2.6% and in 2007, when

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sales reached a furious peak, the rate was 3.04%.

Though 2009 presented the gloomiest collection of data since Massey Knakal began carefully tracking the market in the early 1990s, Knakal indicated that it was at least partially skewed by the fact that the first half of the year was so bleak.

Amid the dearth of mortgage financing, few deals could get done and pricing "overshot" the bottom.

Although nine-figure property deals remain jammed because of an ongoing pullback in lending, Knakal said that regional and community banks have begun to provide financing for smaller property deals, a category he classified as sales below $50 million.

The capital has allowed portions of the market to "bounce back" although Massey Knakal executives were cautious to note that it's not clear if this pattern will be sustained in 2010.

In Manhattan for instance, Massey Knakal stated in its market report that prices began to rise in the third and fourth quarters of 2009 from earlier in the year.

Cap rates, a measure of profitability that can increase either when rental rates push up or property prices fall, rose overall because of a year-over-year decline in values.

Yet median sales prices did tick up during the second half. Massey Knakal reported that the median sales price for walk up apartment buildings ended the year at $488 per square foot, 20.1% below a peak in 2008 but up 2.5% from the first half.

The median price for elevator residential rental buildings meanwhile finished the year at $452 per square foot, 13.4% below peak 2007 levels for that property type, but up 11.9% from the first half of 2009.

Knakal noted the discrepancy between walk up buildings and elevator properties and said that although logic would indicate that buildings with an elevator should be more valuable, walk up properties usually had a higher turnover of tenants, including rent stabilized residents, who tired of trudging up and down stairs. That meant that walk up apartment buildings provided owners with more opportunity to swap out lower paying renters for better deals and were actually considered more valuable.

It appears the property sales market in 2010 in the city will be a tug of war between two opposing factors.

Knakal said that there are billions of dollars worth of idle capital eager to invest in deals that have been frustrated by the lack of available product.

On the other hand, interest rates are bound to rise, raising the price and perhaps also limiting the availability of capital in an already cash-constricted market that could discourage deals and push down prices further.

One way or another, Knakal seemed to indicate that the market can't remain jammed. He estimated that there were between $30 and $40 billion of problem deals that will have to be flushed onto the distressed sales market, a process he anticipated would begin this year and last though 2012. He said that he felt the turnover rate will rise in the boroughs to at least 1.2 to 1.3% and between 1.5 to 1.6% in Manhattan.