CONCRETE THOUGHTS

Land Slide

02/14/12

As price per buildable square foot drops, development sales market climbs

Perhaps the market segment most difficult to understand, particularly if we examine recent market data, is the development land market in Manhattan. For the purposes of this discussion, we will consider the Manhattan submarket to include sites south of 96th Street on the East Side and south of 110th Street on the West Side. In 2009, the average price paid per buildable square foot was $374. In 2010, this average dropped to $326, a 13 percent decline. In 2011, the average dropped again to $311, a 5 percent slide and a number which is 17 percent below the 2009 average, which was the peak during the past cycle.

Robert Knakal

Most participants in the market would think there must be some mistake with these numbers as it has been clear that a tangible increase in the health of the development market has been present since the disillusioned days of 2009. Actually, if we examine the data closely, this trend becomes easy to understand. And the conclusion is that the development land market has been improving and, today, is one of the better performing market segments.

The main factor impacting the land market has been volume. The year 2009 was probably the most challenging in which to obtain construction financing. For sure, better sites with strong sponsorship could obtain construction loans and several good-sized financings were made at that time. Due to the challenges of obtaining construction loans at the time, and the heavy equity requirements appurtenant to the loans that were available, the perception was that the value of land had fallen dramatically. Sites that may have been worth $400, or more, per buildable square foot during the boom years of 2006 and 2007 were receiving offers of just $100 or $150 per buildable square foot. The result was that sellers simply did not capitulate. (It must be noted that there were still very prime sites that still commanded lofty offers and transactions occurred.)

This dynamic left the land market in a position where we saw only a few trades. For some relative perspective, in 2006, which was the year in which we observed the most activity in the land market, there were 186 development sites traded. Everyone during these years, it seemed, was a "real estate developer" including many first timers who had been architects, plumbers, doctors, brokers and just about anyone else who could spell real estate. Remarkably, construction financing was available to these novices. Not surprisingly, the overwhelming majority of stalled sites and foreclosures seen in subsequent years were on the backs of these inexperienced developers.

In 2009, the number of sites sold evaporated to just 11, a 94 percent drop. Of these 11 sites sold, eight were purchased by users who purchased the land for the construction of facilities for their own occupancy. The result was that just 416,000 buildable square feet were sold for a total of approximately $180 million. The result, notwithstanding the miniscule volume, was a healthy average price paid per buildable square foot of $374 (not a weighted average). Essentially, sellers pulled the trigger only if they got their price.

In 2010, activity picked up significantly with 41 sites sold. These sites contained a total of about two million buildable square feet, which sold for an aggregate price of about $715 million. These sales resulted in an average price paid per buildable square foot of $326.

Last year, the land sales market gained tremendous traction with 95 sites selling. These sites contained a total of about 4.5 million buildable square feet with an aggregate price tag of about $1.4 billion. The average selling price of this land was $311.

It is important to note that the averages presented here are for all land sales, including those for retail, office, hotel, residential and institutional uses. The value of each of these subsets is different; therefore, applying the average to any particular site may derive a misleading result.

From a macro perspective, we have seen what appears to be a drop in the average price paid for land in Manhattan. However, when we look at volume trends closely and really understand the market dynamics, we see that the land market is healthier than it has been in several years, and we expect this positive trend to continue.

rknakal@masseyknakal.com

Robert Knakal is the chairman and founding partner of Massey Knakal Realty Services and in his career has brokered the sale of more than 1,175 properties, having a market value in excess of $7.8 billion.