CONCRETE THOUGHTS

Lies, Damn Lies & Statistics

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The numbers actually paint a clearer picture than many of the adjectives being spouted.

The investment sales market in New York City can currently be described by market participants as: moderately improving, booming or frustrating. It all depends on who you are, what you do and your perspective. Remarkably, each of these adjectives appropriately describes current conditions.

At the end of the third quarter of 2012, the dollar volume of sales is moderately improving, but the number of buildings sold is booming, approaching totals seen at the peak of the market. Buyers are faced with rising prices and short supply, creating much frustration for all who want to deploy capital; at the same time, with values for most property types in most geographical submarkets at or above peak 2007 levels, sellers couldn't be happier with these great market dynamics.

As is always the case, I will illustrate these conditions with statistics rather than adjectives to let you draw your own conclusions about how the investment sales market is performing. Mark Twain once said there are three types of lies: lies, damn lies and statistics. In this case, I have to strongly disagree with this legendary author, as the statistics paint a very clear picture of our market.

Robert Knakal

In the first three quarters of 2012, there have been $21.75 billion in investment sale transactions closed. If annualized, we are on pace for about $29 billion for the year, which would be up a modest 6 percent from the $27.4 billion seen in 2011. Based on the increased activity expected in 4Q12, we forecast the annual total to reach $31 to $32 billion for the year. To give some perspective, this total would be about five times the $6.1 billion seen at the market's low point in 2009, but would remain about half of the peak level of $62.5 billion in 2007.

The dollar volume of sales has mirrored fluctuations within the broader economy. In the first half of 2011, it appeared that the economy was gaining good traction, with several economic indicators showing an upward trajectory. Since then, they have moderated, and several key indicators, such as GDP growth, net private sector job creation and wage growth, have limped along. Similarly, after some quarters with just $2 billion to $3 billion of activity, we saw approximately $8 billion in 2Q11 and 3Q11. These totals were cyclical highs, and we appeared to be heading back to the $10 billion-plus quarters that were common during the 2005 to 2007 boom years. Since 3Q11, dollar volume has not broken $7.3 billion, and therefore could be considered "moderately improving."

The number of properties sold tells a very different story. I believe this number is much more indicative of market activity, as a few very large transactions can skew dollar volume statistics greatly.

In the first three quarters of 2012, there were 2,336 properties sold in the city, already exceeding the 2,222 that sold last year. If annualized, we are on pace for 3,115, which would be a whopping 40 percent increase on a year-over-year basis. More impressively, in 3Q12, there were 948 properties sold, representing the best quarterly total since 1Q08, in which there were 951 trades. Importantly, we are rapidly approaching the magic 1,000 mark, which the market observed in all but one quarter (1Q05) in the boom years of 2005 to 2007. We expect to reach this level in 4Q12 as sellers scramble to get transactions closed prior to the year's end, when many market participants anticipate capital gains taxes going up significantly. This externality has already tangibly impacted the market and is, to a large degree, responsible for 3Q12 totals.

Property values, for most property types and in most geographic submarkets, are at, or above, peak levels seen in 2007 on a price-per-square-foot basis. A notable exception is the office building market in Midtown Manhattan, which is being impacted by soft conditions in the leasing market as uncertainty within the broader economy has created inertia within corporate decision-making circles. Cap rates are about where they were during the peak, but the bargain is much better today as our extraordinarily low interest-rate environment is providing investors with positive leverage. Negative leverage was the condition most commonly seen during the peak years.

The big question is whether these artificially low rates (courtesy of a Fed that is doing all it can to stimulate the economy but, without policy help, appears to be spitting in the wind) are creating an asset bubble in commercial real estate, the way they did in the housing market when then-chairman Greenspan kept rates too low for too long. Time will tell. For now, enjoy the wild ride that 4Q12 promises to be.

rknakal@masseyknakal.com

Robert Knakal is the chairman and founding partner of Massey Knakal Realty Services; he has brokered the sale of more than 1,250 properties in his career, with a market value in excess of $8.5 billion.