

Multifamily, Up From the Rocky Bottom

Manhattan leading way out of recessionary doldrums as metrics appear to be improving steadily in 2011; one uncertainty remains—rent regs

In 2010, New York City's multifamily housing market demonstrated trends that were indicative of the market as a whole. The dollar volume of sales was up significantly over 2009 levels, and the number of buildings sold was up but not nearly by the same rate as dollar volume.



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Values in the multifamily sector, however, appear to be bouncing along a rocky bottom as prices per square foot either rose slightly or decreased slightly versus 2009 levels, depending upon the specific geographic submarket and whether the category was walk-up or elevator.

Generally, we saw reductions in gross rent multiples and capitalization rate expansion.

The trend of increased volume of sales and meandering values mirrored what we saw across all product type segments. On a positive note, the rate of decline in value reduced

significantly as we progressed through 2010, and in some sectors, we saw metrics turn upward as we approached year end.

Below is a summary of all multifamily building sales activity in 2010.

In 2010, there were 543 multifamily apartment buildings sold in New York, up 25 percent from the 435 properties sold in 2009. The 543 buildings sold had 15,011 individual apartment units, up 52 percent from the 9,888 units sold in 2009. The dollar volume of sales showed the largest increase, as there was approximately \$2.33 billion in sales activity in 2010. This total was up 84 percent from the \$1.26 billion in sales transaction volume in 2009.

Last year, 77 percent of the apartment buildings sold were walk-ups as opposed to elevator buildings, which is consistent with the composition of the market. Elevator property sales, however, performed much stronger than walk-ups relative to 2009 levels. In 2010, there were 417 walk-up buildings sold, up approximately 20 percent from the 348 buildings sold in 2009. The number of units sold was also up approximately 20 per-

cent, as 6,069 were sold in 2010, versus 5,022 in 2009. The dollar volume of walk-up sales showed a larger increase, of 23.5 percent, to approximately \$788 million last year, versus \$638 million the year before.

Comparing elevator buildings to walk-ups illustrates the relative strength of that sector; 126 elevator buildings were sold in 2010 versus 87 in 2009, a 45 percent increase. A trend, which is illustrated by the following two statistics, indicates that the larger properties were being traded in 2010. The 126 buildings sold last year contained a total 8,942 apartments, an increase of 84 percent over the 4,866 sold in 2009. The dollar volume of sales in the elevator sector showed the largest increase. Here, volume more than doubled, from \$627 million in 2009 to \$1.55 billion last year, an increase of 146 percent.

As demonstrated by the volume statistics, it is apparent that the activity in the multifamily sector has been rising steadily since the low point in the first half of 2009 (2H09). Value trends demonstrate mixed signals when comparing 2010 to 2009. When we look at longer-term trends, we see that since the peak of the market, in 2006 and 2007,

value has been steadily decreasing. During this period of time, capitalization rates have clearly been trending up, and gross rent multiples have clearly been trending down.

When analyzing values within the multifamily sector, we look at four major metrics: capitalization rates, gross rent multiples, prices per square foot and prices per unit. We will now take a closer look at each of these metrics for walk-up and elevator buildings within each of the submarkets that we cover.

The Manhattan market started to show clear signs of improvement in 2010. Even though capitalization rates rose by 59 basis points in the walk-up sector from 2009 levels, we saw decreases in cap rates in the second half of 2010 versus the first half. The same was true in the elevator sector. The average walk-up cap rate in 2010 was 5.78 percent. At its lowest point in 1H07, this capitalization rate was at 4 percent.

In the elevator sector, the average cap rate was 4.84 percent in 2010. This figure represents a large expansion from the low point in 1H06, when the average cap rate was just 2.8 percent. In 2006, cap rates were so low because properties were being purchased for their condominium conversion potential, not their cash flow.

Gross rent multiples in Manhattan are also showing positive trends. In the walk-up sector, we saw average multiples decrease in 2010, versus 2009; however, there was a clear jump of almost a full multiple in 2H10 versus 1H10, indicating that this market is correcting. The same pattern holds true for elevator properties, with year-over-year decreases but strong second half performance relative to the first.

On a price-per-square-foot basis, we see that values were relatively unchanged in 2010 versus 2009, with walk-up buildings averaging \$525 per square foot and elevator buildings averaging \$438.

Once again, we see the counterintuitive trend of walk-up buildings having a higher value per square foot than elevator properties. This occurs because the tenancy turnover within walk-up buildings is significantly higher than that in elevator properties, which allows owners to benefit from the upside potential created by artificially low rent-regulated rents. Additionally, typical unit sizes in walk-up buildings are much smaller than their counterparts in elevator buildings. Therefore, while the rent check written each month for a one-bedroom apartment in an elevator building will be higher than that for a one-bedroom in a walk-up, the rent in the walk-up building is often higher on a price-per-square-foot basis than in an elevator property. These dynamics lead to higher values per square foot for walk-up buildings than elevator properties.

In northern Manhattan, walk-ups saw a 55 percent increase in the dollar volume of sales, rising from \$83 million in 2009 to \$129 million in 2010. The number of properties sold

Multifamily Analysis • GRM

	Walk-Up			Elevator		
	2009	2010	Change from 2009	2009	2010	Change from 2009
Manhattan	12.48	11.87	-0.61	13.30	12.74	-0.56
Northern Manhattan	8.22	7.51	-0.71	8.47	8.75	+0.28
Bronx	6.74	6.62	-0.12	6.58	7.36	+0.78
Brooklyn	9.58	10.12	+0.54	8.66	8.19	-0.47
Queens	10.77	9.77	-1.00	9.14	9.56	+0.42

Multifamily Analysis • CAP RATES

	Walk-Up			Elevator		
	2009	2010	Change from 2009	2009	2010	Change from 2009
Manhattan	5.19%	5.78%	+0.59	4.71%	4.84%	+0.13
Northern Manhattan	7.04%	7.48%	+0.44	5.53%	6.27%	+0.74
Bronx	7.43%	8.04%	+0.61	8.10%	7.93%	-0.17
Brooklyn	7.64%	7.10%	-0.54	6.41%	7.09%	+0.68
Queens	6.43%	7.55%	+1.12	6.04%	6.03%	-0.01

Multifamily Analysis • PRICE PER SQUARE FOOT

	Walk-Up			Elevator		
	2009	2010	Change from 2009	2009	2010	Change from 2009
Manhattan	\$530	\$525	-1%	\$438	\$438	0%
Northern Manhattan	\$163	\$164	0.8%	\$124	\$120	-3.6%
Bronx	\$88	\$87	-0.8%	\$69	\$67	-2.3%
Brooklyn	\$160	\$172	7.4%	\$121	\$192	58.4%
Queens	\$218	\$203	-6.7%	\$133	\$181	36.0%

increased 71 percent, from 38 in 2009 to 65 in 2010. In the elevator sector, the dollar volume increase was a startling 175 percent, hitting \$319 million last year from \$116 million the year before. The number of properties sold increased from 22 in 2009 to 35 in 2010, an increase of 68 percent.

Cap rates rose in 2010 from 2009 levels in both the walk-up and elevator sectors. GRM, prices per square foot and prices per unit showed no consistent trends, with some rising and some falling.

The markets in Manhattan and northern Manhattan clearly performed better than other submarkets. The trends in the Bronx, Brooklyn and Queens were also relatively positive versus 2009, just not to the same extent.

In the Bronx, the dollar volume of sales in the walk-up sector was up just 5 percent, increasing from \$100 million in 2009 to \$105 million last year. The number of buildings sold in this sector was up to 67 in 2010 from 53 in 2009, a 26 percent increase. In the elevator sector, the dollar volume was up 52 percent from \$139 million in 2009 to \$211 million in 2010. The number of elevator buildings sold in the Bronx last year rose 32 percent to 41, from 31 in 2009.

Price per square foot was down in 2010

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from 2009 levels in both the walk-up and elevator sectors. Cap rate, GRM and price per unit metrics were mixed, demonstrating a market that is still volatile.

In Brooklyn, the dollar volume of sales in the walk-up sector rose 36 percent, from \$152 million in 2009 to \$206 million in 2010. The number of properties sold increased from 123 in 2009 to 152 last year, a 23 percent rise. In the elevator sector, the dollar volume of sales increased just 11 percent, from \$92 million in 2009 to \$102 million in 2010. Surprisingly, the number of buildings sold dropped from 18 in 2009 to 17.

With respect to value in Brooklyn's multifamily sector, even though GRMs were down in both the walk-up and elevator sectors, and cap rates were mixed, prices per square foot and prices per unit were up across the board. This indicates that, on average, a better-quality building was sold in 2010 versus 2009, with a higher percentage of free-market apartments. These characteristics would explain the value increases observed.

Lastly, in Queens, we saw walk-up dollar volume increase 48 percent over 2009 levels, reaching \$98 million in 2010. The number of walk-ups sold rose 17 percent, to 67 last year from 57 the year before. In the elevator sector, the dollar volume rose by 40 percent, from \$55 million in 2009 to \$77 million. The number of elevator properties sold was up by 160 percent over 2009 levels, but that was due to an extraordinarily low total of just five sales in that year.

Each of the four main multifamily metrics were mixed in Queens, with the exception of price per unit, which rose by 21 percent in the elevator sector and was up just 1 percent for walk-ups.

When we review all of the data presented above, we clearly see that the multifamily market is making tangible strides toward recovery. The Manhattan submarket has already turned into positive territory, with northern Manhattan not far behind. This is not surprising, as Manhattan always leads New York's submarkets out of downturns. In the outer boroughs, we see volatility, with some metrics continuing to slide while others move in positive directions. Here, we continue to bounce along a rocky bottom but, based upon recent trends, we believe all metrics will be in positive territory by the middle of this year.

One factor that could pose a problem for the multifamily sector in 2011 is the pending expiration of current rent regulations, which are set to sunset in June. No one actually believes these guidelines will sunset, so the question becomes: In what form will they be renewed?

Governor Cuomo has indicated that there are many other issues far more pressing to deal with than rent regulation. However, knowing that many of the governor's agenda items work against his constituency, Sheldon Silver is likely to try to obtain something in return for agreeing to most of the governor's positions. Rent regulation is vulnerable here. Many feel that Mr. Cuomo has a presidential run on the back burner and effectively dealing with public-sector unions, health care, education, budget deficits and spending cuts are résumé builders for that lofty job application.

Anything done to New York's rent-regulation system (for better or worse) would not help or harm a presidential campaign. The question on the minds of many participants in the multifamily sector is whether rent regulation will be a sacrificial lamb to ensure support on more macro issues. We certainly hope it is not.

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Robert Knakal is the chairman and founding partner of Massey Knakal Realty services and in his career has brokered the sale of more than 1,125 properties, having a market value in excess of \$7 billion.

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