A Look at Our Report Card. (It's Weird.)

Now that the first half of 2016's (1H16) New York City investment sales statistics are in the books, it is time for me to report them to you as I typically do at the end of every quarter. While there have been signals of the beginning of a transitional market, there are some events which demonstrate infidelity to a looming correction. I have written in this column for about nine months now that the correction had begun, led by weakness in the land and hotel markets (historically the first sectors to turn), but the shift has been slow and mixed signals have led to an opaqueness we haven't seen since 1998.

Robert Knakal

Current market conditions in the city's sales market remind me of a quote from the famous American business management writer, Tom Peters: "If you're not confused, you're not paying attention." That sums the current market up succinctly and accurately. Here's why:

In 1H16, the dollar volume of sales was $31.5 billion, on pace for $63.1 billion if annualized. This would result in a yearly total 18 percent below last year's all-time record of $77.1 billion. While an 18 percent drop seems like a lot, it is important to remember that at $63.1 billion, this would be the second best year ever, narrowly eclipsing the $62.2 billion of sales in 2007, the previous record which stood for eight years. It would also be about 5 percent above 2014's $57.9 billion, which was viewed as epic by the industry.

With regard to the number of properties sold, 1H16 produced 2,257 trades, on pace for 4,514 for the year, which would be 13 percent below last year's 5,191. This total would be well below 2014's all-time record of 5,532.

At the beginning of the year, we forecast a 15 to 20 percent reduction in dollar volume and a 30 to 40 percent reduction in the number of properties sold. We believe the statistics for 1H16 overstate the actual activity as many of the transactions that closed in the first half of the year had contracts signed last year. The forecast is not on track, thus far, but we remain confident it will come close to our predictions.

We also projected a reduction in value for the year with average prices per square foot ending the year lower than at the start of the year. However, values so far have increased this year.

In 1H16, the average price per square foot citywide was $566 per square foot, up 15 percent from last year's $492 average. This average is somewhat misleading as two retail property transactions in Manhattan skew these numbers. They occurred at 109 Spring Street and 139 Spring Street ($17,000 and $30,000 per square foot respectively) and, without them, the average drops to $527, an increase of 7 percent over last year.

Cap rates are, remarkably, continuing to compress as the citywide average in 1H16 dropped to 4.55 percent from last year's 4.74 percent, a compression of 19 basis points. It is noteworthy that this compression is the smallest since 2010. So cap rates are compressing but at a decelerating rate.

In the Manhattan sub market, often used as a leading indicator of the broader market, dollar volume is on pace for $45.3 billion, a 24 percent drop from last year and the number of properties sold is off 2015's pace by 29 percent, on track for 778 sales, a mediocre year by historical standards. Excluding those two astronomical Spring Street sales, values are up just 4 percent over last year, at $1,384 per square foot. Cap rates are down just 4 basis points from last year, which is essentially flat.

These market conditions reinforce the assumption that the market is in the early stages of a correction. Even though values are rising, the rate of increase is decreasing and volumes are dropping tangibly. This is because sellers who are getting their price are selling, and those that are not are simply not selling. The next condition we should see is an actual drop in pricing.

This is the case in the land market where values thus far in 2016 the average price per buildable square foot citywide is $261, down 12 percent from last year's $295 average. However—and importantly—the number of transactions is down 29 percent to 448, and the dollar volume is down a whopping 50 percent from 2015. Here, I also believe volume is overstated because of contracts signed last year where the deals are closing this year. Again, this dynamic is indicative of a correcting market.

The confusion comes from the occasional transaction where a top of the market price is obtained for a property that may, or may not be, deserving of such a price. This can be explained by buyers simply not understanding the market or that the correction is happening at such a slow pace that it will take an extending period of time to play out.

In either case, the confusion is palpable and makes for a most interesting market. Too bad crystal balls are mythical!

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