Can Retail Keep Up?

On the heels of the ICSC Convention in Las Vegas, this week we will look at the performance of retail property sales in the New York City marketplace.

As a backdrop, the investment sales market in New York City is coming off the two best back-to-back years in at least the last 32. In 2014, there were 5,533 buildings sold in New York City, an all-time record by more than 10 percent. In 2015, the dollar volume of sales was approximately $75 billion, also an all-time record, eclipsing the $62.2 billion sold in 2007 by more than 20 percent.


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Going into this year, we projected reductions in both dollar volume and number of properties sold as theses metrics moderate toward their long-term trend lines. We also anticipated that average prices per square foot would end the year lower than they began.

Within the mix of different product types, each segment typically performs differently as the market turns. Land and hotel properties are already seeing significant downward pressure applied to their values. These are typically the first two product types to feel a change in market direction. Office and multifamily assets are still selling very well. Multifamily buildings are typically the last to turn, and office properties are doing relatively better than they normally do at this point in the cycle, mainly due to the unprecedented job creation we have had in the city over the past six years. There have been about 650,000 jobs created here during that period of time that has bolstered the sector's underlying fundamentals considerably.

Retail assets have been somewhere in the middle. Capitalization rates are up slightly, and the number of properties sold is trending lower. However, the dollar volume of retail property sales is rising, and prices per square foot are higher through the first quarter.

In 1Q16, there were 95 retail properties sold in the city, on pace for 376 for the year. This pace is about 10 percent below last year's 416 sales. Dollar volume is slightly ahead of last year's pace. In 1Q16, there was $846 million of retail property sales, on pace for $3.39 billion, 4 percent above last year's pace.

The average price per square foot citywide reached $955, 5.7 percent above last year's $903 average. However, the $955 figure is 16.4 percent less than the $1,143 average in 2014. Cap rates in 1Q16 have averaged 5.06 percent, up slightly from the 4.95 average in 2015. It should be noted that in the Manhattan submarket, average price per square foot hit $2,661 in the first quarter, a new all-time record.

These retail metrics, with cap rates and values both rising, are indicative of a market in which rents are rising. The only way values can rise when cap rates are increasing is if net operating incomes are rising. That appears to be the case, at least through the first quarter. Recently, much has been written about the downward pressure retail rents are experiencing. In a market with rising cap rates, this trend, if it continues, will ultimately lead to reductions in values.

It is important to keep in mind that the averages reflected here are just averages. The best properties in the best locations continue to thrive, and those in tertiary locations are not doing quite so well.

So, the transition year we projected appears to be on track, but only time will tell in terms of the magnitude of the change.

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