Did You Really Expect Sales Volume to Increase?

In the third quarter of 2020, investment sales activity in Manhattan continued on its downward trajectory. Given the impact the pandemic has had on New York City, this should come as no surprise.

Many hotels are closed, and tourism is on pace for 4.2 million visitors this year, a 93 percent drop from the 60 million tourists last year. (In January, estimates were for 67 to 68 million this year.) Many stores are still closed, and estimates range from 25 percent to 40 percent that will close permanently.

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Physical office occupancy, which was 7 to 8 percent in August, is now averaging about 13 percent post-Labor Day. Luxury residential rental occupancy is at its lowest point anyone can remember. And the jury is still out on how the work-from-home experiment will impact office space utilization and absorption moving forward.

As I always like to do in this column, we will first take a look at the entire cycle, before looking at 3Q20 performance, in order to provide some perspective.

It is clearer than ever that the cyclical peaks in New York City investment sales market volumes were in 2014 and 2015. The volumes we look at are the dollar volume of sales and the number of properties sold. While both of these metrics are important indicators, we have always felt that the number of properties sold was a much more illustrative metric, as a few mega transactions can skew the dollar volume significantly, particularly when the total dollar volume is on the low side.

In 2014, there were 5,534 properties sold in New York City, an all-time record by more than 10 percent. This was followed up with $80.1 billion in sales volume in 2015, another all-time record. The bull market in investment sales, which began in 2010 from a volume perspective and in 2011 from a value perspective, ended in 4Q15 when it became apparent that the market was about to turn.

We are now more than five years into an investment sales market correction in New York. From October 2015 through February 2020, the correction was mainly a volume correction.

If we look at the sales market for transactions above $10 million in Manhattan south of 96th Street on the East Side and south of 110th Street on the West Side, we see a market peak of $57.5 billion in 2015, and $28.7 billion in 2019, a 50 percent drop. Over that same period, the number of properties sold dropped from 484 sales in 2015 to 220 in 2019, a reduction of 54.5 percent. During this period, values dropped by an average of only about 10 percent. Clearly, it was different for each product type, but the average was only about 10 percent.

This is a relatively benign drop compared to the 38 percent drop we saw during the Great Recession from 2007-2010, and the 58 percent drop we observed during the Savings and Loan Crisis in the early 1990s.

In March, COVID-19 turned the correction mostly from a volume correction to a value correction. It would be irresponsible to try to quantify the drop in value over the past eight months, as the low number of transactions are effectively statistically insignificant.

However, it is safe to say that significant downward pressure has been exerted on property values, particularly in Manhattan. Values in the outer boroughs are also experiencing downward pressure, but to a lesser degree than we are seeing in Manhattan.

In 3Q20, there was $1.37 billion in sales volume in Manhattan, the lowest quarterly total since 4Q09. This performance puts 2020 on pace for about $10.4 billion, which would reflect a 64 percent reduction from 2019 levels, and would be 82 percent below the 2015 peak.

Also, in 3Q20, there were 16 sales over $10 million, the lowest quarterly total in 44 quarters, going back to the 13 sales in 3Q09 during the height of the financial crisis. This puts Manhattan on pace for 101 sales this year, which would be down 54 percent from last year's total, and down 79 percent from the 484 sales in 2015.

The drop in volume we have seen is not at all unexpected. When downward pressure is exerted on property values, discretionary sellers are slow to capitulate and that is what we are seeing now. In New York City, there is always a market-clearing price. The slow volume is a result of sellers not being willing to accept that market-clearing price.

But those of us who rely on transaction volume should take heart. At some point next year, the volume of sales will pick up as stresses in market fundamentals will force transactions to happen. That increase in activity will be a welcome shift from the downward trajectory we have been on for what has been a very long five-year period.

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