I-Sales Supply and Demand Dynamics, 2Q19

As students of the investment sales market in New York City, we are constantly tracking supply and demand metrics to try to gain a better understanding of where the market is headed.

The relationship between the supply of available properties for sale and the demand from various groups that want to purchase properties is as basic a fundamental economic relationship as exists. Low supply and low demand generally yields low prices and low volume. High supply and low demand yields very low prices and very low volume. Conversely, low supply and high demand yields very high prices, but low volume and high supply and high demand yields high prices and high volume. Got it?

Robert Knakal.

The extent to which the highs are high and the lows are low is dependent upon the magnitude of each of the metrics.

Historically, in the New York City investment sales market, the supply of available properties for sale is almost always relatively low and demand is almost always strong. When looking at the relationship between the two, over the last 35 years, demand has exceeded supply with the exception of 1992 when the Resolution Trust Corporation (RTC) was dumping what seemed like hundreds of properties per week on the market from failed banks in the wake of the savings and loan crisis.

In the average year in the Manhattan submarket, 2.6 percent of the total stock of properties trades. If we assume that half of what goes on the market actually sells, this means only one out of every 20 properties is on the market at any one time. Furthermore, the 2.6 percent turnover ratio means that, on average, a property sells every 40 years or so. This is clearly a low volume market.

Additionally, when downward pressure is exerted on property values, fewer properties go on the market as sellers decide not to sell for less today than they could have gotten yesterday. Compounding this is that when downward pressure is applied to price, a lower percentage of properties placed on the market will actually trade.

Looking at the broader investment sales market today would lead one to think that the overall market is slumping. After all, sales volumes, both in terms of dollar volume and number of properties sold, dropped by about one-third in the first quarter of 2019. However, this downturn seems to have been caused primarily by a disruption in multifamily sales as pending rent regulation renewal has stifled the market.

It appears that the supply of available properties has not dropped all that much. At JLL, our sales platform has consistently obtained about 90 leads per month over the past six months from potential sellers who want to know what their properties are worth to make a decision about a possible sale. While a lower percentage of these potential sellers are actually going to market, the percentage reduction is only slight. The more impactful trend is that, because multifamily buyers are hesitant, with many blatantly sitting on the sidelines, a much lower percentage of the available supply is trading. Because the majority of properties in the city are multifamily, this disruption is greatly impacting the broader market.

Demand drivers for all other product sectors remains healthy and diverse. This is positive and very surprising as a troubling trend has been emerging over the past year or so in which many local investors, who for decades have only purchased assets in New York City, are increasingly looking to deploy their capital around the country. Consistently low yields and an increasing anti-business political class are pushing investment dollars out of the local market. Add to this a real estate tax policy that seems to be out of control, a 50 percent increase in state transfer taxes and a new progressive mansion tax that quadruples the tax in some cases and it's no wonder some investors are fed up.

Fortunately, new domestic buyers from around the country are coming into the market and offshore buyers continue to seek investments here. Because of this, demand is strong and, after 42 months of a correcting market, signs are appearing that, in some sectors, values are experiencing upward pressures. If supply and demand dynamics keep on track, we expect to see a positive shift later this year.