Investment Sales Market Moving in Expected Direction in 1Q18

In 2017, New York City's investment sales market showed continued declines in volume with values trending downward as well. The dollar volume of sales last year was $35.9 billion, the second consecutive year of sharp declines since 2015's record of $80.4 billion. The number of properties sold last year was 3,660, the third year of consecutive declines in this metric from the 5,534 sales that occurred in 2014 (an all-time record).


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For the first time in this cycle, values in all six major property type sectors in Manhattan moved into red territory. Land values fell by 18 percent, retail by 11 percent, office by 9 percent, mixed-use by 8 percent and multifamily assets held up the best with walk-up buildings losing 3 percent of value and elevator buildings just 2 percent. In the outer boroughs, there are seven major property types (we add industrial) and there are four submarkets, including northern Manhattan. In these 28 market sectors, 25 percent of them were in negative territory.

Heading into this year, we expected this current 32 month-long market correction to show increases in the volume of sales with values bottoming out. This came after an extraordinarily interesting 4Q17 which was either horrible or great depending upon your perspective. In terms of the number of buildings sold, we saw the lowest quarterly total citywide going back to 1Q13 and in Manhattan it was the lowest quarterly total going back to 1Q11. However, the activity with respect to contract executions was the best quarter that we had seen in more than two years. Our forecast for 2018 was impacted by this surge in activity.

Our forecast was also based on the way past corrections have played out. When corrections end, volume increases as values find their floor. Exactly the same market conditions existed in 1993 and again in 2010 when the market was coming out of its corrections. However, this time around, tax reform could have a tangible impact on market performance. As I have always said, commercial real estate market participants are highly sensitive to tax policy changes. This is illustrated by the spikes in sales volume that have occurred in 1986, 1998 and 2012, all years in which tax policy changes profoundly impacted market performance.

In 1Q18 the dollar volume of sales was $12.4 billion. This is on pace for $49.7 billion annually. This would be a 38 percent increase over last year's total of $35.9 billion. Notably, the volume in Manhattan was $8.9 billion, on pace to show a whopping 62 percent increase over last year's anemic $22 billion.

In 1Q18 the number of properties sold was 832, on pace for 3,328 for the year this would be a drop of about 9 percent from the 3,660 sales that occurred last year. While this metric is not moving in the direction we forecast, we believe it will turn the corner as we progress throughout the year and end up positive.

The big swing between the increase in dollar volume and the decrease in the number of properties sold demonstrates that larger properties were moving at a much better pace than they were last year. In 2017, the average price of a property sold citywide was $9.8 million. This year, the average price has risen to $14.9 million. In Manhattan, last year's average sale price was $35.6 million while this year the average has nearly doubled to $60.4 million. Pent up demand to sell these larger assets has precipitated this movement and the bid / ask spread is compressing because sellers are coming down to meet the market. As I wrote back in 2015, seller capitulation normally takes 18 to 24 months and market conditions are now illustrating this.

With regard to property values, on a citywide basis the average price per square foot this year has been $548, essentially flat from last year's $543 average. Interestingly, since 2013 the appreciation rates citywide have been decreasing consistently to the point where we are now flat. In Manhattan, values rose 2 percent to an average of $1,410 per square foot. While one quarter does not make a trend, value performance in 1Q18 was better than expected and we believe that tax cuts have played a hand in buoying property values. This is just one of the positive impacts that tax reform could have on the commercial real estate market.

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