

Multi-Family Continues to Thrive as Market Faces Demand

In recent columns, I have been reviewing the state of the New York City investment sales market with a focus on third-quarter 2016 results. As we have discussed, the volume of sales is slowing down both from dollar volume and number of properties sold perspectives. Simultaneously, values are remaining relatively strong as market wide they are appreciating both in Manhattan as well as in the outer boroughs.

While the general trend in value has been up, it is apparent that different product types are performing very differently. Land and hotels have been facing the biggest challenge; office buildings and multifamily properties are doing the best, leaving retail assets somewhere in the middle. This week we will focus on the ever-resilient multifamily market, which, despite significant headwinds, continues to surprise to the upside.

Decade after decade, multifamily assets are always at the top of the list in terms of the product type that is in heaviest demand, and they attract the largest pool of potential investors. There have been several reasons for this, including the fact that rent regulation has created artificially low rents, which limit downside and create tremendous upside when tenancies rollover. Given the

perceived safety of these investments, this product type has also attracted the largest amount of available financing from the widest array of lenders.

Remarkably, demand for this product type continues to be enormous notwithstanding the fact that this market is facing significant headwinds. These challenges have been in the form of court decisions and a Rent Guidelines Board (RGB) that has been extraordinarily pro-tenant over the past several years. The Roberts decision impacting J-51 buildings, the Altman decision impacting deregulation thresholds and the

Altschuler decision impacting the look-back on overcharge complaints have made operating multifamily assets much more difficult. Even the best landlord-tenant attorneys in the city are often unable to give definitive advice to clients in terms of how they should proceed administratively in many circumstances. Two consecutive years of rent freezes on one-year regulated leases from the RGB have also made things more challenging for property owners, particularly in the outer boroughs. Therefore, to see demand continuing to be strong, and values continuing to rise, is surprising.

As we look at 2016 results thus far, we will eliminate 2015's Stuyvesant Town/Peter

Cooper Village transaction as it skews number of buildings and dollar volume metrics very significantly. Interestingly, the Stuy Town deal does not impact price per square foot or cap rate metrics as that transaction was effectively at those market averages.

Through third-quarter 2016, the city is on pace to sell 1,615 multifamily assets, down 2 percent from the 1,652 sales in 2015. Dollar volume is on pace for \$12.7 billion this year, 4 percent below the \$13.2 billion that occurred in 2015 (remember, that is without the Stuy Town transaction). These reductions in volume are relatively modest compared with other product types, which are seeing much more significant reductions.

Meanwhile, prices per square foot have eclipsed \$400 per square foot for the first time ever. Thus far in 2016, the average price per square foot of a sold New York City multifamily asset is \$402 per square foot, 7 percent above last year's \$374 average. Not surprisingly, capitalization rates have compressed to a cyclical low of 4.37 percent citywide, 19 basis points below last year's average.

In the elevator sector, the number of sales is on pace for 287, 16 percent below the 2015 total. The dollar volume is on pace for \$7.6 billion, 9 percent below last year's total of \$8.4 billion (these percentage drops are 28 percent and 45 percent, respectively, if Stuy Town is included). The average price per square foot in the sector

has hit a new all-time record of \$492 in 2016, a 2 percent increase over last year's \$483 average. Capitalization rates have also hit a cyclical low at 3.95 percent so far this year, down 17 basis points from last year's 4.12 percent average.

In the walk-up sector, the market is on pace for 1,328 sales this year, up 1 percent from last year's 1,312. The dollar volume is on pace for \$5.1 billion, a 4 percent increase over the \$4.9 billion that occurred last year. The average price per square foot is up to an all-time record of \$383 per square foot, a strong 8 percent increase over last year's average. Capitalization rates have also compressed to a cyclical low of 4.57 percent, down 19 basis points from 2015's average.

The multifamily market in New York City is continuing to thrive and, on a relative basis, is the shining star of the market. There are some market participants, however, that have given up on this sector given the headwinds that it faces. To date, this small segment of market participants has not had an impact on the broader sector. Whether it will in the future will be dependent upon future legal decisions and legislation, both of which have made it much more difficult to effectively operate these assets. Time will tell...

Robert Knakal is the chairman of New York investment sales for Cushman & Wakefield.

