Supply and Demand Dynamics in Today's Investment Sales Market

Occasionally, in this column, we look at the dynamics within the New York City investment sales market with regard to supply and demand. With the opaqueness of the market today, we thought it was time to take another look at this fundamental relationship that drives the marketplace. With regard to the supply of properties on the market, we see increases in supply coming for several reasons.

First, the volume of sales has been declining since the cyclically peak years of 2014 for number of properties sold and 2015 for the dollar volume of sales. As of the end of 2019, those metrics were down 55 percent and 50 percent, respectively, from the peak year with each showing steady declines year over year. This persistent decline in sales volume has created significant pent-up selling demand that seems to be revealing itself on the supply side today.

Second, we have seen a large increase in the number of owners who are looking for the opinions of brokers on the values of what they're considering selling (commonly called Broker Opinion of Values, BOV). This metric is always a leading indicator of future supply trends and one that we monitor on a weekly basis. Our analysis shows that the number of weekly BOV requests thus far in 2020 is up about 47 percent from the flow of requests we saw in 2019. Given the pent-up selling demand we have referenced above, we have seen a greater percentage of BOV turning into on-the-market availabilities for sale. Today, a potential seller who requests a BOV is 22 percent more likely to put their property on the market for sale than we saw last year. Third, we have seen the number of properties coming on the market increasing as many potential sellers are looking to diversify their exposure to New York City's political headwinds. This is particularly true within the multifamily sector where many owners have all of their holdings in the local market. Which leads to the next point. Fourth, some potential sellers appear to be ready to just sell at the current market and deploy that capital into other asset classes within the city or into the multifamily space in other states. We are still in price discovery mode relative to multifamily assets and the expected increase in activity in this space will get us that price discovery sooner. The desire of some owners to move capital out of the space is tangible. This is probably the most troubling trend we are observing as many long-term investors who have not purchased anything outside of New York City for decades are increasingly looking to purchase assets elsewhere. Fifth, the extraordinarily low interest rate environment has some potential sellers feeling like buyers may be able to substantiate paying higher prices based upon lower borrowing costs. For all of these reasons, the supply of available properties has been steadily increasing and we expect this trend to continue as the above factors continue to play out.

Robert Knakal.

If we look at the demand side of the equation, it is important to see that demand is still relatively healthy which is why property values have not fallen as much as some market watchers have expected. There are many first time buyers who are looking for commercial real estate investments in New York City. These first timers are domestic as well as foreign investors. On the domestic side, many investors who have been successful investing in other parts of the country are looking to get a piece of the Big Apple to include in their portfolios. Foreign investors remain attracted to the relative political and economic stability that the U.S. offers and New York City is a place that everyone knows. True, many large foreign institutions have cut back on some large purchases but high net worth individuals are continuing to search for opportunities here and are helping to absorb some of the product that is coming to the market. On the local investor side, while it is true many investors are looking outside New York for the first time ever, many are also doubling down on their New York City exposure. With reduced prices on some assets, they are, as one investor told me, "implementing a cost-averaging strategy to lower the average basis" in their portfolios. Others believe that the political headwinds are only temporary and the factors that motivate people from around the globe to come live and work here will continue for decades to come. Lastly, the low borrowing costs, created by these extraordinarily low interest rates, are motivating some owners to invest based upon the much higher than usual leveraged cash-on-cash returns that are available today given the positive leverage that is available. As one investor told me, "Financing is basically free today. I am going to buy as much as I can in New York City." As we move forward into the year, the supply-demand balance would lead us to project a more robust volume year than we saw last year, welcome news for anyone who makes a living based upon transaction volume. Here's to hoping these trends continue.