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Commercial real estate value increase remains slow but steady in the current market

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According to commercial brokers and investors I have talked to recently, the commercial market may be bottoming out. I have observed many other indicators including but not limited to market transactions. Based upon Real Capital Analytics larger commercial real estate closings were down 75.78% when comparing 2007 and 2010 on an average weekly basis. This was confirmed in part by the CoStar Group who estimated that the total volume of commercial sales in New York City in 2009 decreased to approximately $4.58 billion or a decrease of approximately of 83.65% from 2007. The number of commercial transactions decreased approximately 66.41% from 2007. One of the reasons was the withdrawal of Commercial Mortgage Bask Securities (CMBS) market. In the period 2002-2007, the CMBS market accounted for 37% of all large commercial mortgages. In 2008, the CMBS market accounted for 1% and only 1.5% so far in 2010.

Based upon Yardi Systems, Inc. the median sales price for commercial transactions in New York City reached a peak in the mid 3rd quarter of 2008 to almost $1.9 million. However, at its lowest point which was in the middle of the first quarter of 2009 the median price of commercial transactions in New York City was approximately $900,000. It fluctuated slightly upward for a year but dropped below $900,000 at the end of the first quarter in 2010. Ironically in Manhattan the highest average median price was early in the 4th quarter of 2007 in the amount of approximately $5.3 million. However, by mid 3rd quarter it had fallen to approximately $2.8 million. It did rise to approximately $4.2 million in the middle of the 4th quarter of 2008 but dropped substantially after the late September, 2008 economic disaster through the late 4th quarter of 2009. By the end of the first quarter 2010 the median sales price of commercial properties was up to $3.1 million in Manhattan.

One of the other concerns is delinquency rates. Based upon the Mortgage Bankers Association, CMBS loan delinquencies increased from 1% in the 1st quarter of 2009 to 7.1% in the beginning of the second quarter of 2010. In addition, many commercial loans are coming due in each of the next five years. Another significant national statistic between 2007 and 2010 show that industrial, office and retail new construction was down over 80%. The good news is, supply is down which will eventually even out the supply and demand curve over the next 5-10 years. Many high end properties were and will continue to be substantially affected because the CMBS market is still severely diminished. Of course, this has more substantially affected the downstate New York, Boston and the extreme southwest sector of Connecticut because the dollar size of the properties are at extremely high levels. In upstate New York, most of western and central New England region was not as severely affected by the decline of the CMBS market. Much of the financing in upstate, etc. was being supplied by regional banks which remained relatively healthy throughout the 2008 and 2009 economic national crisis. These regional banks are still a good source of financing for commercial real estate transactions in upstate New York, western and central New England.

Therefore, values have been more insulated and stable from a financing prospective.

There is still some hesitancy on the equity side in all markets which has reduced sales activity. However, the value levels have remained relatively strong because of the extremely low interest rates and low debt service. Because of the various factors of low interest rates, more stability in the financial markets and reduced building over the past two years, overall capitalization rates have diminished slowly since the fourth quarter of 2009 from the higher levels of the last quarter of 2008 and most of 2009. Of course, rentals and occupancy are also recovering after declines. The improvements in occupancy and rents started in early 2010. Thus, commercial real estate value increase remains slow but steady in the current market.

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