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Letter of Intent - Apartment Sector Surge

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The residential sector has exploded across the country, with close to 170,000 class A units coming to market in major metros in 2013, and an additional 220,000 expected in 2014. A vast number of class C assets are expected to be renovated into class A/B, as has been the value add proposition for many national investors for the past few years, thus narrowing the spread between asset classes. Since class A cap-rates have dipped, savvy investors have found a solid opportunity to class B/C asset renovations. Fear not though, New York has retained its status as the lowest vacancy rate in the nation, hovering around 2.5%, and the future is looking bright. The newfound technology and start-up boom in New York City, (along with the elevated salaries tied to those jobs) has led to a strong demand for high end product. The projected 30,000 new professionals to that field alone will add to the frenzy for quality housing in New York City.

One of the main drivers is the competition amongst investors to snag a piece of the action before their neighbor does, and the desire to do so will push owners to sell their current holdings. Cap-rates in Manhattan for market-rate assets are 5%, while rent-stabilized buildings or assets with upside have traded closer to 3%. For the risk-to-reward type investors, there are plays in secondary and tertiary markets in the Bronx and Brooklyn that will yield 7% unleveraged returns, but require far more tolerance to the market and demand relentless building and tenant management. As the service industry in New York continues its boom, those risk tolerant investors will find comfort in the belief that employees in such industries will keep up the demand for low-tier apartments, especially those close to transit.

All in all, most agree that the trend should continue for at least the foreseeable future, of course that is, if interest rates don't escalate too much, but we can save that topic for another time.

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