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# Real estate values and COVID-19 - by John Rynne

September 22, 2020 - Spotlights

The recent trends in real estate valuation has been heavily influenced by COVID-19. It's been five months since the first major lockdown due to the COVID-19 virus which started to raise havoc not only in the United States but throughout the world. New York State continues some of of the biggest lockdowns because of the early severity in mainly New York City and Westchester County. The Finger Lakes Region which encompasses Rochester was one of the leaders in opening up commerce. Other Upstate regions that followed included Albany, Buffalo, Syracuse, Binghamton, Watertown, Rome/Utica, etc. However, certain properties that still have substantial restrictions include entertainment sites such as stadiums, arenas, concert sites, churches, work out gyms, banquet facilities etc. So the market value of these types of facilities have been more negatively affected.

The banning of some out of state visitors unless they quarantine for 14 days has created a disincentive for travel. Currently, travelers who fly into NYC must get tested. All this is devastating to the travel industry especially the airlines, bus companies, railroads, cruise lines, etc. The real estate that gets negatively affected the most are hotels, rental car properties, restaurants,and malls. As an example, a local developer in the Buffalo area has postponed construction of four new hotel projects. The negative effect of the virus on single-family, multifamily housing, industrial, and warehouses has not been as evident. Office space has been negatively affected primarily due to more workers having the flexibility of working remotely. However, this has been partially offset since more social distancing will be desired by office occupants which will increase the need for more office space. The federal government's Payroll Protection Program (PPP) did help tenants to pay rent or owner occupants to pay mortgages. However, the PPP has ended, so low debt service is a real necessity.

Another factor in neutralizing some of the negative effects of the virus and the end of PPP translates directly to overall capitalization rates because of an historic decline in interest rates. (Visit our Rate Survey at www.rynnemurphy.com). At the beginning of January, 2020 the 10-year treasury rate was at 1.81%. When restrictions were put on travelers from China by the federal government at the end of January, the 10-year treasury started a significant decline. By April 30th the 10-year treasury had dropped about 120 basis points. This substantial decrease in debt service prevented overall capitalization rates to escalate dramatically. With low interest rates and without the pandemic, overall capitalization rates would have taken a favorable substantial decline. However, there is higher market equity return requirements for real estate. The lower debt service neutralized the increased risk which is reflected in the equity side of the property investment.

Another double edged sword is the increased cost of new construction components due to a backlog caused by a shutdown of production lines along with some consequences of tariffs. As an example, lumber prices have been escalating due to a lack of supply. This helps maintain the core value of the existing inventory of buildings because the cost of replacement increases. A very glaring example of this is in the single-family residential market. Besides increasing construction costs, there is a lack of available listings in lower and middle parts of the market. Therefore, there is a bidding war on available listings. The most outrageous example that I have heard about is a property with 48 offers in the Buffalo area. Although, this is an extreme case, there are many cases of multiple offers. So given the historically low mortgage rates, rising material costs, and lack of inventory, there is surge in the certain parts of the single-family market. This doesn’t translate 100% to the multifamily market, but it takes tenants out of the rental market. Obviously, all this has put an extra burden on appraisers in regards to lack of comparable sales.

Many appraisers realize some of the uncertainty and add an extraordinary assumption which is outlined as follows: “The global outbreak of a “novel coronavirus” known as COVID?19 was officially declared a pandemic by the World Health Organization (WHO) and a state of emergency declared by national, state, and various local governments. It is currently unknown what direct, or indirect, effect this event may have on the national economy, the local economy or the market in which the subject property is located. The conclusions presented in this appraisal report apply only as of the effective date(s).”

All this translates into overall rates and values which have not changed significantly in many property categories. The most noteworthy property categories which have changed are hotels, restaurants, banquet facilities, malls and to a lesser extent offices. The COVID-19 pandemic appears to be diminishing, so normalcy may be just around the corner.

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