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A look at the recovery of the multifamily property sales sector in New York City - by Brandon Polakoff

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Flash back 12 months ago. The summer was coming to an end with fears of a second wave starting to surface. While the majority of property owners were understandably hesitant to market their properties for sale, a handful decided enough was enough and it was time to pull the trigger. The feedback from buyers was consistent. The 10-15% discount was not enough. With a budget deficit, property taxes were certain to rise. The rental market was going to take years to recover and this needed to be priced in. It was the perfect storm (let's not forget about political risk) for values to continue declining to a new rock bottom.

Fast forward 12 months. On January 15th, 2021 the Department of Finance released its 21/22 Notice of Property Values and we observed assessments decrease across almost all tax class 2 & 4 properties. Additionally, there was a reduction in tax rates across all residential properties. Residential rents drastically rebounded across the board due to dwindling supply. This was confirmed by Douglas Elliman's latest market report that announced, "New lease signings in Manhattan rose to their highest level for an August since at least 2008. Listing inventory continued to fall precipitously, down by more than half since January." The main reason for the spike in demand is that New York City has never experienced four different tenant bases entering the market at the same time. This group includes two sets of graduating classes, college students, and professionals of all ages returning from the suburbs.

I do not pretend I saw the speed of the recovery coming. I also recognize that when the market experiences a shake up and prices drop, there is a justifiable reason buyers grow hesitant. But if you were and are a believer in the NYC comeback, you would have had to expect rents were going to recover in the relatively near future. The reality is that most buyers were arriving at values using overly conservative underwriting assumptions as opposed to taking a step back and recognizing a proper discount when they saw one. Maybe this was a lesson learned for all of us when the next dip comes, or for opportunities that currently remain on the table.

Accordingly, how can we use what we have learned over the last two months and still take advantage of the current marketplace by better predicting the near future?

According to Nancy Wu, an economist at StreetEasy and Zillow, "We are seeing that the inventory numbers in East Village, in a lot of areas of downtown Manhattan, are dropping way faster than they are in Upper East Side, or even areas in Brooklyn, where we're seeing generally less demand from the younger, more mobile renters." At the height of the pandemic, I strongly encouraged buyers to focus on neighborhoods with a young demographic as I felt they would be the first to bounce back in value. Nancy Wu's findings confirmed this belief. Of course, very few were able to act on this with conviction and simply asked for a larger discount. In fact, when selling a 72-unit multifamily property in the East Village just three to four months ago, there was only one buyer willing to hit a seller's substantially reduced price using this thesis. The ultimate purchaser, who closed at the end of August, told me that net rents on new leases climbed 27% between contract signing and closing, which improved the going in cap rate by 100 basis points.

I believe that investing today in prime downtown locations and on the Upper West Side is still a smart strategy. Interest rates remain low, markets outside of New York City have reached levels that no longer make financial sense, and we are still climbing our way back from the trough. However, I also think in the short term, investors can take advantage of neighborhoods where property values have not rebounded as quickly due to a slower rental recovery. As the rental supply in prime neighborhoods continues to be absorbed at record levels, and demand can no longer be met, I am confident rents in "second-tier" neighborhoods are going to rise faster than we can blink, reaching or exceeding pre-COVID-19 levels depending on the rate of inflation. I believe there is a great opportunity to get more aggressive today using 2019 rent rolls as a baseline as opposed to hopping on the band wagon after the ship has already sailed. If you are a believer in New York City, now is the time to act.

Brandon Polakoff is principal and executive director of tri-state investment sales at Avison Young, New York, N.Y.