



2022 New York Upstate Apartment Market - by Brian Heine

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M&T Realty Capital, Buffalo-based M&T Bank's commercial banking subsidiary, plans to increase its multifamily financings to double its real estate loan volume in two years in response to the

increasing demand it is receiving from apartment investors. New mortgages to include balance sheet loans, a traditional bank mortgage that the bank keeps in its portfolio, and loans for life insurance companies and Fannie Mae and Freddie Mac that M&T also originates. These are all permanent mortgages that will be offered in addition to its construction loan business. The Federal Reserve has begun its long-anticipated increase in the federal funds rate. So far, the ten-year treasury, the industry benchmark for mortgage interest rates, has moved up a full point in reaction to and in anticipation of future tightening; mortgage rates are correspondingly above 5%, up from 3% and lower. More important for investors is the impact on capitalization rates as the slack is taken up in the gap between mortgage interest rates and cap rates. Owners and managers must make sure that rents are at market, referred to as revenue management, to maximize income and maintain Net Operating Income (NOI) as the Fed moves ahead. Expect cap rates to remain steady; prices to increase as gains in NOI from higher rents match or exceed higher debt service costs.

The Climate Leadership and Community Protection Act (Climate Act) was signed into law in New York in 2018. The law created the Climate Action Council which has recently released a draft plan to chart the implementation of the Climate Act. The objectives include the banning of the use of natural gas to heat new and existing homes and apartment buildings and bans on the replacement of natural gas appliances in new and existing homes and apartment buildings. These bans will start in 2027 or sooner and will hit the upstate New York apartment market very hard, with its overwhelming use of natural gas for heating and a very cold winter heating season. Upstate apartment owners should plan for massive costs to comply as the decade progresses and then higher electric expenses thereafter. Heating systems will need to be retrofitted with more expensive and less reliable electric heat pumps including a necessary upgrade of the property's electrical service. Expect the abandonment of competing properties at the lower end of the rent scale, especially the large inventory of century old inner-city doubles (two-family apartment properties) in Buffalo and Rochester where the cost to retrofit will be uneconomical and not recoverable with future rents. There will be overwhelming tenant demand for apartments through the decade and the challenge will be to keep NOI ahead of these new costs.

Ithaca, in central New York south of Syracuse, is one of the most active multifamily markets in Upstate New York. Arnot Realty from the Elmira area paid \$14.5 million for the 38-unit Seneca Way Apartments in the city of Ithaca at the end of 2021. The market rate apartments sold for \$381,000 per unit including some first-floor retail space. Rents are \$2.25 per s/f per month for one- and two-bedroom apartments. Arnot is also building the Ironworks Ithaca, a five-story urban infill project with 129 market rate apartments, at a cost of \$39 million. Two-bedroom, two-bath rentals are advertised at \$3.20 per s/f

per month, comfortably above the \$3 rent figure necessary to justify new construction without rent subsidies and one the few markets in upstate New York that does. Ithaca has a strong college-town economy, and is not overly landlord friendly. The left-wing common council passed a rent cancellation bill during the pandemic (but not signed into law) and has an aggressive Green New Deal building decarbonization program, and despite a growing list of regulations, investors and developers continue to look for new opportunities in this market.

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