NYC commercial real estate market sees encouraging start to 2023 as inflation drops and lending rates decrease - by Jakub Nowak

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In last month's column, I examined the challenges that New York City commercial real estate is facing in 2023 due to high inflation and the impact of recent rate hikes. However, this month I am pleased to share that after a challenging second half of 2022, the year is off to an encouraging start. It seems that last year's aggressive rate hikes are finally having their intended effect. December's inflation fell to 6.5%, an impressive 2.7% drop from a high of 9.1% in the summer of 2022. The Fed seems to be taking advantage of its new-found breathing room to scale back on the size of near-term increases with its recent decision to raise the short-term federal funds rate by a modest 0.25%. As a result, we have seen commercial lending rates drop by as much as 1% across different loan products since the fourth quarter of 2022. Let's take a closer look at what impact lower rates and the prospects of a more dovish near-term monetary policy are having on activity in the city's commercial real estate market.

Seeing last year's peak in inflation in the rear-view mirror marks an important turning point for many NYC commercial real estate investors. Numerous would-be buyers who were afraid that committing capital before the Fed took its foot off the gas would mean catching "a falling knife" are now willing to place a bet that any further value erosion will be limited as the Fed embarks on a path of more modest increases. We are seeing investors who had been sitting on the sidelines over the last few months re-enter the market eager to deploy stored up dry-powder and take advantage of a more favorable lending environment. In some cases, there are two to three times as many bids for our exclusive listings. For some, it seems that the fear of loss is giving way to a fear of missing out on buying opportunities before rates continue their upward trajectory. As a result, the bid-ask spread between buyers and sellers seems to finally be narrowing.

Interestingly, while most lenders stayed in relative lock-step on lending rates for most of last year and rarely deviated by more than twenty-five basis points from one another, this is no longer the case in today's volatile environment. Due to a shortage of reserves, certain high-volume lenders have been forced to stop lending on NYC assets completely. This has brought new lenders into the market and as treasure yields have stabilized, lenders with sufficient capital reserves have been able to drop rates while others have not been able to keep pace. Consequently, we are seeing rates offered by different lenders on the same asset vary by as much as 1.5%. With that in mind, it is critical for investors shopping for financing to engage multiple lenders simultaneously to make sure they can capitalize on the best possible loan terms available to them in today's dynamic environment.

The recent drop in rates represents a window of opportunity for buyers to transact at favorable terms, but the Fed's rate increases are not over. Sellers in particular need to make informed decisions about their short- and long-term plans with their asset if they want to benefit before rates resume an upward trajectory. For starters, sellers need access to market intelligence and a trusted team of advisors who can provide timely insights.

With inflation now on a downward trajectory, and assuming we do not enter into a major recession, I anticipate deal velocity and dollar volume to start to recover as we continue through 2023. For now, market participants have a unique opportunity to capitalize on lower rates if they act quickly and decisively. Let's see how things play out over the coming weeks. In the meantime, stay informed, keep raising rents and lowering expenses, and I look forward to seeing you at my next monthly column.

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