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Multifamily Fundamentals Soften

By Paul Bubny

NEW YORK CITY-Wall Street's ailments have begun to infect the city's residential market, with apartment prices dipping in Q4 2008 and two reports predicting a rise in the rental vacancy rate this year. The result could be a softening of fundamentals in the formerly ironclad multifamily category, although rental buildings will maintain much of their investment appeal.

"Despite the downside risks to the multi-family market, the local reliance on rental housing is expected to prevent significant revenue declines," says a report from Marcus & Millichap Real Estate Investment Services. "Additionally, vacancy is forecast to remain in check in popular Manhattan and Brooklyn neighborhoods such as the Upper East Side and Upper West Side, the Village, downtown Brooklyn, and Park Slope as distressed renters take on roommates rather than move out of desirable locations."

In contrast, Marcus & Millichap cites neighborhoods including Long Island City, Midtown West, the Financial District and southeastern Harlem, "where deliveries will be elevated and the threat of shadow rentals persists." The report predicts a 130-basis point rise in the vacancy rate this year.

As part of its 2009 Global Real Estate Forecast, Grubb & Ellis notes that the housing slump and recession have produced "countervailing forces that will both help and hurt" the city's multifamily market this year. "Apartments are seeing some new renters who have lost their homes to foreclosure, while landlords are able to maintain existing renters who are waiting for prices and mortgage rates to fall further," the report states. "However, new graduates who can't find jobs are doubling up with a roommate or moving in with a relative to conserve cash."

At the same time, according to Grubb's report, "the apartment market faces competition from an increasing supply of unsold condos and foreclosed homes returning to the market as rentals." Grubb says "the negative forces are expected to have a slight edge" and result in slowly rising vacancies for the multifamily market in '09.

Grubb's report notes that as in other markets across the US, New York residential condominium projects coming online in the next couple of years may have to be converted to rentals "as prospective purchases are reluctant to buy in a down market and financing is difficult for certain buyers to come by. Recent appreciation in the value of the dollar discourages foreign buyers as well, which could help rental apartment building prices to outperform other types of real estate in the New York market."

Marcus & Millichap expects the local buyer pool for multifamily properties to change "significantly" this year, even as local transaction velocity remains modest. "Experienced New York property owners who have waited on the sidelines for the froth in the investment market to dissipate are poised to re-enter the market. Sovereign wealth and opportunistic investment funds are also expected to increase their presence this year as economic and financing issues provide easier entry for buyers with cash."

Going forward, the Marcus & Millichap forecast says that investment speculation will gravitate

toward location and strong historical performance, "although the trickle of distressed property sales that has begun in tertiary locations like Brownsville/East New York, Bedford-Stuyvesant, South Bronx and East Harlem will likely offer buying opportunities."

Fourth-quarter reports from residential brokerage firms have yielded mixed signals in terms of pricing and sales velocity. A Prudential Douglas Elliman/Miller Samuel report observes a 9.4% year-over-decline in sales overall and a 24.8% year-over-year drop in re-sales. The report notes that the average sales price on a Manhattan apartment was up 3.1% year over year to \$1,485,102, but adds, "this gain was caused by an increase in closings of new developments properties, which generally are more expensive."

Halstead Property's Q4 market report shows a 3% year-over-year increase in co-operative prices but an 8% decline from Q3. The report says that a 7% decline in the average condominium price from Q4 2007 was due primarily to fewer closings at the ultra-high-end 15 Central Park West and the Plaza. In Q4 '08, the average time on the market for apartments sold was 100 days, 16 days more than Q4 '07. Sellers received nearly 95% of their asking price, as compared to 98% a year earlier.

"While we show a decline of 2% from the third to fourth quarter of this year, our real estate market is still holding up relatively well when compared to some parts of the nation," says Halstead president Diane Ramirez in a release. "We are clearly in a buyer's market and there are a number of great deals out there. Combined with low interest rates, this is a really good market for someone looking to buy real estate."

At Brown Harris Stevens, whose Q4 report offers similar figures, president Hall Willkie notes in a release that Q4 '08 figures "largely reflect closings of sales that went to contract months earlier, and are therefore indicative of the market at that time. Despite the current economic environment, we should remember that New York City is unique. As we have learned, we are certainly not immune to economic woes, but the fundamentals of our market are stronger than most."

On the rental side, brokerage firm the Real Estate Group of New York notes declines in asking rents across all classes of apartments except two-bedroom doorman apartments. The declines range from 2.04% for non-doorman studios to 9.2% for doorman studios.

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