

# Multifamily Research

## Market Report

Fourth Quarter 2016

New York City

### Divergence Between Market Participants Grows as Supply Proliferates

**Job creation still supporting positive outlook; robust delivery schedule weighs on vacancy and rent growth.**

New jobs are consistently being created in the New York City economy, even as the pace of hiring has slowed over the past year. As a result, demand for local housing has remained high, particularly in the core areas of Manhattan and Brooklyn where mortgage payments are far above rental rates. As a result, multifamily development has risen to a cycle high, with the vast majority of supply growth slated for Manhattan and Brooklyn. In addition to development in these two boroughs, construction is also reaching the other boroughs as property values have pushed high enough to support additional development. Underscoring this trend, the top three projects for 2016 will exceed 750 units, with a location in three separate boroughs: Man-

hattan, Brooklyn and Queens. The sheer scale of construction — more than 56,000 apartments are underway with expected deliveries before 2018 — is softening occupancy as the new supply is absorbed by the market. However, the long-term space constraints and high single-family home prices, combined with the recent repeal of 421-A regulation, will support outside price appreciation for years to come.

**Investors migrate toward Class C product as development rises; yield-oriented buyers active in outer boroughs.**

The near-constant appreciation associated with New York City metro properties is driving a steady investment market in 2016, with buyers active at a range of price points. While institutional investors have focused primarily on Class A offerings in Manhattan

and Brooklyn, the overwhelming majority of dollar volume in the metro is flowing toward more affordable product throughout all five boroughs, with an emphasis on Brooklyn assets. As average cap rates have fallen into the mid-4 percent range metrowide, buyers have been actively seeking opportunities to enhance returns through repositionings or re-tenanting of existing spaces. However, a widening gap between buyers and sellers has emerged over the past few months as operations have become more challenged, lengthening closing times and lowering deal prices. As a result, the volume of transactions has slowed somewhat as prices have moderately retreated. Buyers are likely to be more selective, choosing the best properties and shifting away from buildings in need of more investment.

### 2016 Multifamily Forecast

1.9% increase  
in total employment



**Employment:**

New York City employers will hire 80,000 new workers this year, with headcounts rising by 1.9 percent. Over the previous 12 months, 101,000 new positions were created, a 2.4 percent improvement year over year.

29,000 units  
will be completed



**Construction:**

Developers will complete nearly 29,000 new apartments in New York City this year, increasing the pace of deliveries from last year, with the majority of new stock targeting Manhattan and Brooklyn. In the previous year, 11,800 rentals were brought to market.

20 basis point  
increase in vacancy



**Vacancy:**

The largest supply growth of the current cycle will foster a transitory shift upward in vacancy to 2.5 percent, up 20 basis points from 2015. In the prior four quarters, vacancy rates were unchanged as the pace of net absorption fell.

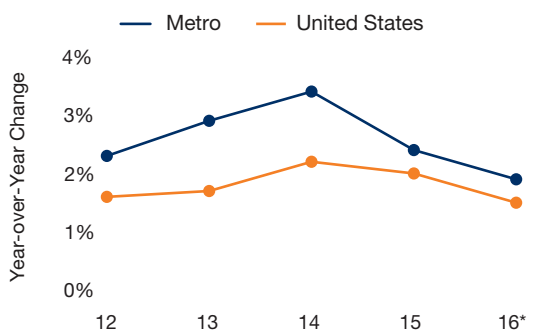
2.2% increase  
in effective rents



**Rents:**

Strong growth in net migration and new household formation will ensure sufficient demand to promote average effective rent growth of 2.2 percent to \$2,850 per month in 2016. Last year, average effective rents tacked on 2.9 percent.

### Employment Trends

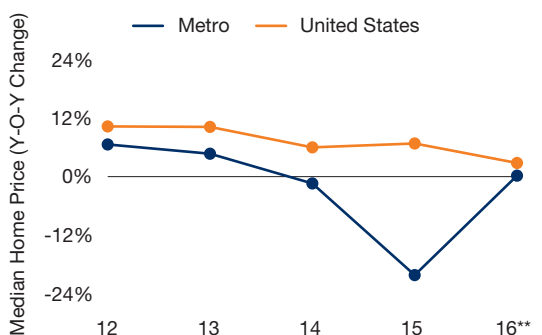


## Economy

- During the last 12 months ending in September, New York City employers created 85,200 new positions, expanding metro payrolls by 2.0 percent. This follows the hiring of 107,100 workers in the previous yearlong period, a 2.6 percent growth rate.
- Payroll additions over the last four quarters were driven by the education and health services and leisure and hospitality sectors, accounting for 26,100 and 24,300 positions, respectively. These sectors accounted for more than half of the workers hired in the metro.
- Although the financial activities sector shed 1,600 workers over the last year, the decline was offset by the creation of 11,300 jobs in the professional and business services sector and 4,100 positions in the information sector.

**Outlook:** The pace of hiring will slow to 80,000 jobs this year, a 1.9 percent growth rate. In the previous year, 101,000 positions were created, a 2.4 percent expansion to payrolls.

### Home Price Trends

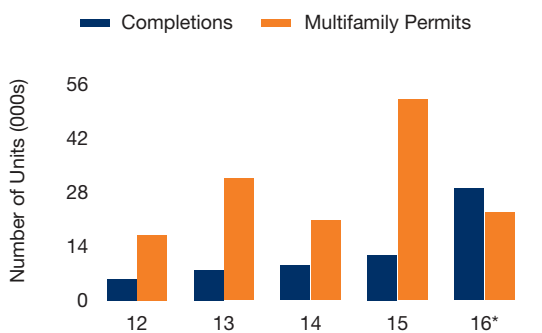


## Housing and Demographics

- For the full year of 2016, multifamily permitting is expected to decline roughly 50 percent as the expiry of the 421a regulations takes effect. Single-family permitting activity is also expected to fall 4 percent this year.
- During the past four quarters, the average price of a single-family apartment in Manhattan rose 13.4 percent to \$1.58 million. Median household incomes also appreciated, advancing 2.9 percent to more than \$65,000 per annum.
- After accounting for a downpayment, taxes and insurance, the average monthly mortgage payment is roughly \$8,200 per month in Manhattan. Meanwhile, the average effective apartment rent is \$3,375 per month. However, the cost of housing varies dramatically based on location; the most desirable neighborhoods are highly unaffordable for the average household.

**Outlook:** The high cost of housing, particularly in Manhattan, will leave the average household unable to afford a mortgage. While single-family homes are more affordable in the outer boroughs, the longer commute times may prompt households to continue renting.

### Construction Trends



## Construction

- By the end of the third quarter, metro builders had completed more than 12,000 new apartments, with more than 10,000 delivered in Manhattan and Brooklyn. Nearly 1,500 were completed in the Bronx, while 1,200 came to market in Queens.
- Development will remain substantial for the remainder of 2016, with more than 16,000 apartments under construction metrowide. The highest concentrations will be in Manhattan and Brooklyn, with more than 11,000 units slated for delivery in both boroughs.
- Builders have broken ground on more than 29,600 apartments for delivery in 2017, which would represent the largest supply of the current cycle. More than 11,600 units are slated for sites in Brooklyn.

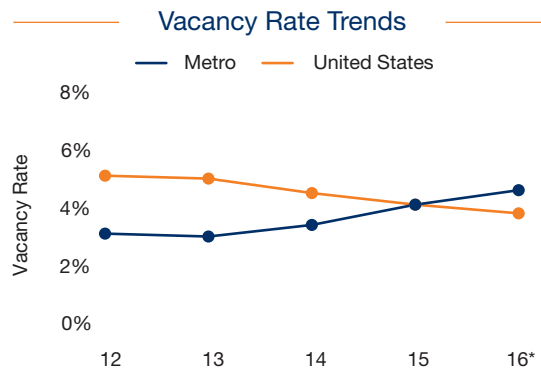
**Outlook:** Amid a need for additional housing, builders will complete roughly 29,000 new units this year, with plans for nearly 30,000 apartments slated for 2017. New supply will be concentrated in Manhattan and Brooklyn.

\* Forecast  
 \*\* Trailing 12 months through 3Q

## Vacancy

- Over the past 12 months, the metro vacancy rate was unchanged at 2.3 percent as a lack of affordable alternatives prompt significant absorption of new apartments. In the previous yearlong period, vacancy was also unchanged, indicative of the incredible demand for rental accommodations.
- While development surged in Manhattan, the borough remains in high demand, with apartment vacancy up 10 basis points over the past year at 2.5 percent. Midtown Manhattan registered the most pressure as vacancy rose 140 basis points to 3.7 percent.
- Intense construction is straining operations in Brooklyn, where vacancy ticked up 20 basis points to 2.5 percent. Apartment demand in Queens ramped up over the past year, with vacancy declining 60 basis points to 1.6 percent, while Staten Island vacancy vaulted 170 basis points to 3.2 percent.

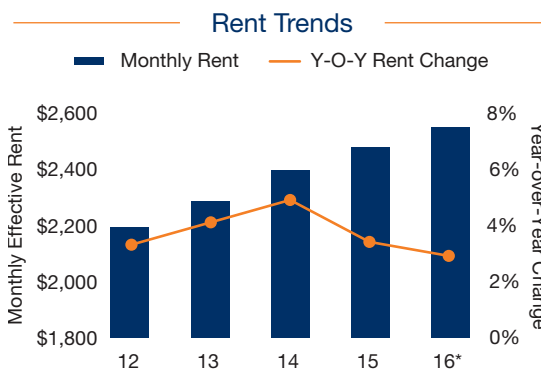
**Outlook:** The highest development pipeline of the current cycle will push up the metro vacancy rate by 20 basis points to 2.5 percent by year-end. This follows an unchanged vacancy rate in the previous four quarters.



## Rents

- During the last year, the average effective rent climbed 2.1 percent to \$2,580 per month by the end of the third quarter as heightened development activity elevated tenant options. Rents advanced 4.3 percent over the prior year.
- Soaring completions in Manhattan are weighing on rent growth in the market, with effective rental rates advancing 1.9 percent to \$3,544 per month by the end of the third quarter, slowing from the 4.0 percent growth achieved in the previous period. Brooklyn outpaced Manhattan properties over this period, with effective rental rates rising 4.4 percent to \$2,152 per month.
- Performance in Queens kept pace with both Manhattan and Brooklyn as average effective rents edged up 2.9 percent to \$2,029 per month. Meanwhile, assets in the Bronx ticked up 2.6 percent to \$1,325 per month.

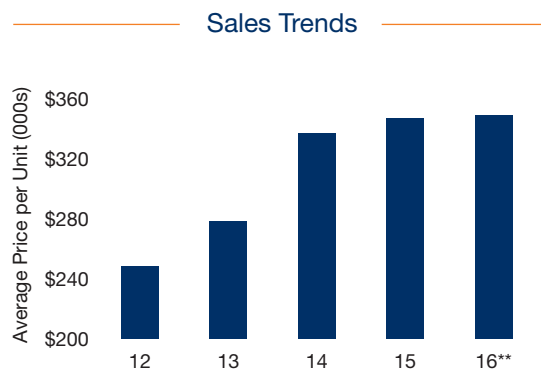
**Outlook:** One of the largest development pipelines of the current cycle will trim average effective rent growth to the low-single-digit level as high-end apartment builders discount available units to fill them.



## Sales Trends

- Over the past year, transaction volumes dipped moderately as a gap between buyers and sellers emerged. During this time frame, dollar volume also slipped marginally, indicating a slower pace of deal flow and a focus on properties at lower price points. While Brooklyn captured the majority of deal volume, total investment was highest in Manhattan, which rose above \$5.7 billion.
- The average price per unit for closed transactions over the past year reached nearly \$350,000 per door, up 2.8 percent from the prior year. Prices in Manhattan were above \$600,000 per unit, while Brooklyn topped \$310,000 per door.
- Cap rates in the metro have fallen to 4.6 percent during the last 12 months, down 10 basis points from the prior period. Properties in Queens and Brooklyn will trade near the average, while product in Manhattan can extend as low as the high-3 percent range.

**Outlook:** While yield-seeking buyers will deploy capital in the outer boroughs, capital-appreciation-oriented investors focus on Manhattan properties and Brooklyn assets located along the East River.



\* Forecast  
Sources: CoStar Group, Inc.; Real Capital Analytics  
\*\* Trailing 12 months through 3Q

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## Capital Markets

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

- The initial reading of third quarter GDP of 2.9 percent and consistent growth in employment are fanning expectations that the Federal Reserve will raise its benchmark short-term lending rate at its December meeting. Other economic data showing steady improvement in the housing market and the stabilization of oil prices around \$50 per barrel offer signals that the U.S. economy is growing at a sustainable pace.
- Increasing rental housing demand underpinned a decline in the U.S. apartment vacancy rate of 60 basis points to 3.5 percent year to date through the third quarter, the lowest level this cycle. Apartment builders have responded to growing demand and favorable demographic trends by ramping up construction. Completions will rise to 320,000 units this year and peak in 2017.
- Capital markets remain highly competitive, offering an assortment of fixed-rate products available through commercial banks, life-insurance companies, CMBS and agency lenders. Fannie Mae and Freddie Mac are underwriting loans of 10 years at maximum leverage of 80 percent. Rates will typically reside in the high-3 to low-4 percent range, depending on underwriting criteria. Portfolio lenders will also price in this vicinity but will typically require loan-to-value ratios in the 65 to 75 percent band. Floating-rate bridge loans and financing for asset repositioning are typically underwritten with LTVs 70 to 75 percent of stabilized value (80 to 85 percent of cost) and price 300 basis points above Libor for recourse deals and extending to 450 basis points above Libor for non-recourse transactions.

## Local Highlights

- JDS Development Group will deliver the largest new apartment tower this year. The 800-unit project at 626 First Avenue, known as the American Copper Buildings, will contain a sky bridge connecting the two towers, with other amenities including an indoor lap pool, rooftop deck and infinity pool, fitness center and spa.
- The Related Cos. is seeking a \$1.74 billion sellout at 15 Hudson Yards, one of the largest ever recorded in New York City. The first residential structure at the Hudson Yards site, the 88-story tower is slated to receive 285 market-rate condos and 106 affordable units. After breaking ground in 2014, the project is expected to be completed in 2018.
- After being neglected for over three decades, RKO Keith's Theater in Flushing was purchased by Xinyuan Real Estate with plans to convert the building into a 269-unit condo offering. The site has exchanged ownership several times in the last decade, with the sale highlighting the flow of foreign money into several notable sales over the past few years.
- Fetner Residential's Via 57 West will come online later this year. The 38-story, 709-unit project in the Lincoln Square submarket of Manhattan will contain multiple amenities including a 22,000-square-foot courtyard, poker room, gym, indoor half-basketball court and outdoor lounges with river views.