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## **The Current Environment is the Perfect Time to Consider Investing in NYC Real Estate**

Some may read the above statement and think I've either lost my mind or have spent the past 18 months on the dark side of the moon. The answer is neither. Warren Buffet once said something akin to, "My partner Charlie and I don't like panic, but we do like the prices it creates." Folks, none of us like what's happened over the past year, but these are the environments that create buying opportunities for those who have realistic views of the world going forward. If you believe that the economy will eventually rebound; that employment growth will return at some point; and that NYC will continue to attract business and international visitors then read on.

## **NYC Multi-family Market**

Several months ago I wrote that many of the people we were speaking to believed there would be a slew of distressed multifamily assets hitting the market in 2009, resulting in a 100% or more increase in cap rates. Although 2009 is far from over, we have yet to see evidence of such a wave of distressed multifamily product hitting the NYC market. Cap rates have risen, but there is still a disconnect between buyers expecting large increases in cap rates, and sellers who are adjusting to lower pricing, albeit at a much more measured pace than buyers would prefer.

Nevertheless, there have been a few offerings of distressed note sales that offer the potential to achieve significantly higher yields on completed buildings, versus what has been available the past several years. That being said, NYC Multi-family rental properties seem to be holding up relatively well with regard to valuation when compared with other asset classes, though many of the brokers we've spoken with have reported little to no transactional activity.

We are also starting to see some signs of life that

could potentially lead to more transactional activity in the near term. Many of the private equity firms, as well as other investors, with whom we have relationships are starting to be more open to looking at new deals. Some are more open than others depending on what shape they're in, however there seems to be a general shift in the psychology of many that Armageddon has been avoided, and although we are not sure as to when things will start getting better, we're cautiously optimistic that things are not going to get too much worse.

Multifamily has historically been the most stable asset class, which is one of the reasons we are not seeing values fall off a cliff the way they are in the office sector. Keep in mind that NYC still suffers from a housing shortage, and I have yet to see any statistics pointing to abatement in population growth.

In our multi-family portfolio we are seeing net effective rents on our market rate units down roughly 15% from 2008 levels. The actual numbers vary property to property, but overall this represents rent concessions in the form of both free rent and brokerage fees, in addition to lower gross rents at many of our properties. However, our vacancy remains relatively tight, due in large part to our willingness to adjust pricing in order to keep our buildings full.

In our rent regulated units we are seeing continued strength in the form of consistent rent growth and little to no vacancy (other than some minor transitional vacancies). This part of our portfolio has helped act as a hedge against some of the downward pressure we are feeling in our market rate units. In addition, lower fuel and energy costs have helped with profitability as well, both in our market rate and rent regulated areas of the portfolio.

We are also seeing an interesting paradigm unfold throughout our portfolio as there seems to be a significant contingent of tenants that are upgrading, both in terms of building class and/or neighborhood due to adjustments in pricing. One example of this shift is the large amount of applications we are receiving for our Manhattan apartments from renters who had previously lived in the boroughs. The decrease in rents throughout NYC has resulted in an influx of new tenants that had previously shunned Manhattan due to its relatively high rents when compared with Brooklyn or Queens. We are seeing more applications from tenants like these both in our low income and luxury buildings and we believe this is a testament to the fact that there is an aspirational facet to people wanting to live in Manhattan. If they can afford it, regardless of what they tell you, most people want to live in NYC.

### **Going Forward**

In our last issue we believed that the first two quarters of 2009 would be very challenging, and it certainly was. That being said, we are starting to see some signs of stabilization in the environment. Make no mistake, the environment is the most difficult one I've ever seen, but it does seem like its stopped getting worse. That being said, there are pockets in the market where new supply from failed condominium projects will continue to erode rental rates. As a whole, the market should be able to withstand these pressures, although in the short run these areas will suffer a bit more than others.

No one can tell you when the bottom of any market will occur and anyone who tries is just guessing. If you don't believe that, just think about all the "smart" people who thought 2008 would be another record year (this can apply to almost any industry, not just real estate). However, we believe that a solid value approach during these times will reap rewards in later years. As I said at the beginning of this letter, none of us have enjoyed the events of the previous year, but hopefully some of us will be able to enjoy the

opportunities the past year has and will continue to create.

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Simon Development Group owns a portfolio of residential buildings throughout the NYC metropolitan area. The firm is launching its first investment fund in 2009 which will focus on acquiring existing multifamily assets in the NYC metropolitan area. For any questions or comments, please call Matthew Baron at 212-400-0404 xt 14.