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Luxury condo overload?

Behind NYC's new development craze — a look at the soaring prices and whether today's strong market is sustainable
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From left: Stephen Kliegerman, Shlomi Reuveni, Andrew Gerringer and Izak Senbahar

New York City's new development condos have been breaking price records and making headlines for their over-the-top, boom-time-like amenities. But there is still concern about just how sustainable the market for these new luxury condos actually is.

In this month's Q&A, *The Real Deal* talked to new development marketing brokers and developers about the residential development landscape, including whether there's an emerging oversupply of luxury condos after a long spell of tight inventory.

While the vast majority of the new development condos being built in the city are in the luxury sector, sources denied that there was an oversupply of high-end units, noting that there are only about 3,000 new units launching this year compared to about 8,000 during the previous peak.

"The new development market is maintaining near-record pricing, but there has been extreme lack of product, which has held the market back from realizing its full sales potential for several months," said Kelly Kennedy Mack, the president of Corcoran Sunshine Marketing.

Soaring land prices, particularly in prime areas of Manhattan, are pushing up average luxury prices into the $3,000-a-square-foot-range and also steering developers away from building rentals.

"You certainly can't make rentals work anymore in prime areas," said Andrew Gerringer, managing director of new business development at the Marketing Directors. "Everyone is going to be doing condos at these new pricing levels. The only people doing rentals are people who have had the land for a long time."

And while the current bumper crop of projects is helping meet demand at the top of the market, there is a hole of new inventory in the middle of the market.

For more on the role foreign buyers — particularly the Chinese — are playing in the new development world, on which locations developers are likely to target next and the impact that a wave of new soaring towers could have on the market, we turn to our panel of experts.

Stephen Kliegerman
president, Halstead Property Development Marketing

New residential developments are being built all over the city. How would you characterize the new development landscape in NYC and what do you predict going forward?

There are obviously numerous ultra high-end condos in the works throughout Manhattan. Although we are not seeing the same number of units being built [as during the boom] because many of the planned sites are smaller, the prices are record-setting. … With such high demand, still-limited inventory and continued low interest rates, I predict at least two to three years of positive growth in the new development sales arena.

***TRD* reported recently that less than 30 percent of the planned condo units in the Manhattan pipeline are expected to be priced below $2,000 a square foot. What are you seeing in terms of per-square-foot asking prices for new development?**

Overall, I am seeing the majority of new Manhattan developments asking over $2,000 per square foot and, really, it's more like over $2,500. That's due more to the high cost of land and construction in Manhattan than to developers wanting to only build super-luxury products. With land prices doubling over the past year and construction costs increasing, developers have been challenged to provide a product under $2,000 per square foot south of 110th Street. That, coupled with the demand for top-quality larger residences, has pushed the average price-per-square foot in Manhattan to new levels — and if you want a view, it is now $4,000 and up.

We're hearing rumblings that developers are more eager to sell units because they're concerned that today's market is not sustainable. Is that the case and are they allowing units to go into contract at lower prices?

We have not sold one unit in any of our developments at less than ask in quite some time and we continue to amend prices upwards. I am not seeing any concern from our [developer] clients that the market is not sustainable and [given what they are willing to pay for land right now], I do not think most developers are that concerned with the longevity of today's market.

At our recent new development showcase you mentioned that foreign buyers are actually not playing as big a role as many think. What kind of ratio of foreign-to-domestic buyers are you seeing in the market?

Overall, I do not see the foreign buyer making up more than 15-to-20 percent of the market, at most. Some developments have reported up to 35 percent of their units selling to foreign buyers, but others see almost none. Overall, the Manhattan market is still a domestic market, which means there is still a lot of room for growth.

Nancy Packes
president, Nancy Packes Inc.

How would you characterize the new development landscape in NYC?

It's focused primarily on established neighborhoods in Manhattan, Brooklyn and, to a lesser extent, Queens. The overall projects are, for the most part, smaller than new development projects prior to Lehman [crashing.] Going forward, we believe that the locations of new development condos will expand to less desirable locations in Manhattan and to the "outer-outer" boroughs — beyond the already gentrified areas of Downtown Brooklyn, Williamsburg and Dumbo. We also foresee a time, in the very near future, when the expansion of demand for new development condominiums increases the price of land in gentrified areas of the outer boroughs such that it will be difficult to build rentals. This follows the pattern we have seen in core Manhattan areas where it's virtually impossible to buy land for rental development.

How big a role do you think Chinese buyers, who were just named the most active group of foreign purchasers, are going to play going forward?

A bubble has been forming in the Chinese real estate market for some time. For several years, wealthy and influential Chinese investors have been seeking a safe haven from their real estate market and economy. In March, [there were] steep price declines and a slowdown that characterizes a market crash. It's to be expected that Chinese nationals will continue to try to export capital now that the local market has reached this critical phase. Also, Russian nationals are largely reputed to be the second-largest group of foreign buyers in the New York new development market. Russia's aggression in the Ukraine has resulted in an increasing isolation of the Russian economy. Thus, it's also to be expected that Russian nationals have an even greater emphasis to seek a safe haven. For the moment, the New York new development landscape should be the beneficiary of these trends. However, an economic fiasco in either of these countries might affect the New York new development market.

What are the most surprising new trends in the NYC new development world?

The higher absorption for new development projects averaging more than $3,000 per square foot as compared to lower-priced new developments. Also, the mix of the most expensive new developments contains a much higher proportion of three-bedrooms, four-bedrooms and even five- and six-bedrooms than ever before. … In addition, we are seeing the return to buying from plans.

Kelly Kennedy Mack
president, Corcoran Sunshine Marketing Group

How would you characterize the new development landscape in NYC?

Though more new properties are opening, Manhattan is still very much feeling the effects of an inventory shortage, with inventory down 19 percent compared to the same time last year. The new development market is maintaining near-record pricing, but there has been extreme lack of product, which has held the market back from realizing its full sales potential for several months. In the first quarter of this year, only 9 new properties with 159 units entered the market, the lowest since 2012's third quarter. More than 3,000 new units are expected to launch this year. While there are a similar number of buildings coming to market in 2014 as we saw during 2007, these developments are significantly smaller, continuing the condition of undersupply. Far fewer units will enter the market when compared to the previous peak, when we saw more than 8,000 residences open for sale in a single year.

We know that the new development market is going strong. But which areas of the new development market are struggling the most?

Very little is struggling in terms of sales velocity or pricing. The true challenge is in neighborhoods where supply is exceptionally low compared to demand. The Upper West Side, Downtown, and brownstone Brooklyn are the three most acute areas. Not only is this lack of inventory frustrating for buyers, but it means there are fewer sales taking place compared to the previous year. On paper, that doesn't look great, but it sets the stage for new development introductions coming later this year.

What kind of ratio of foreign-to-domestic buyers are you seeing? And how big a role do you think Chinese buyers are going to play going forward?

Within our portfolio, approximately 35 percent of sales were to international buyers over the past year. That's a significant increase over what we saw in the previous cycle when foreign buyers represented 10-to-15 percent of the market. Nearly half of these buyers are from the Asia Pacific region and about 20 percent come from mainland China, which is the single most active country outside of the U.S. in our portfolio. [But] the local New York market remains the absolute most significant buying population. At trophy buildings like the Greenwich Lane and 56 Leonard, the vast majority of buyers have come from within the city.

What are the most surprising trends in the NYC new development world?

The soaring condominium tower is back. While 2013 saw an increase in units brought to market in boutique buildings, this year we are going to see several developments that will reach over 700 feet tall and contain more than 100 residences. We're in the midst of an incredibly important quarter that has signaled the return of the large-scale tower with the opening of buildings like 30 Park Place Four Seasons Private Residences.

There's been a lot of talk about the all-cash buyer. Are you seeing fewer buyers who need financing?

Cash remains very dominant in the market. With inventory very tight, cash can be a powerful advantage in making a competitive offer.

Shlomi Reuveni
managing director, Town New Development

How would you characterize the new development landscape in NYC?

The new development arena is the most active I've seen it in my 28 years in Manhattan real estate. We're seeing escalating land values and record-breaking transactions on development sites. The lack of development sites is creating competition among developers.

What are you seeing in terms of per-square-foot asking prices?

Most of the new pipeline projects I know of are projected to price and sell above $2,000 per square foot. Escalating land and construction costs are creating a new floor for break-even costs for developers, which translates into higher prices for end users.

What kind of ratio of foreign-to-domestic buyers are you seeing?

With the exception of Russian buyers, possibly due to recent political events in the Ukraine, I am not seeing a slow down with foreign buyers. We are seeing approximately 15 percent of inventory in our current projects sold to foreign buyers. Asian buyers are very active in New York. We are also seeing strong presence by South American, European and Middle Eastern buyers. In addition to purchasing individual condos, foreigners are also very active with investing and developing projects.

What are the most surprising new trends in the NYC new development world?

The Upper West Side and East Village are the most undervalued neighborhoods in Manhattan. There is an abundance of buyers for each location and smart, well-designed product is lacking.

Susan de França
president and CEO, Douglas Elliman Development Marketing Group

What kind of ratio of foreign-to-domestic buyers are you seeing? And how big a role do you think Chinese buyers are going to play going forward?

We do continue to see interest from foreign buyers. In many cases it's dictated by the type of property and location. We recently opened a new sales center in Midtown on the East Side, which is attracting South Americans as well as Asian and European buyers; however, local residents make up the majority of purchasers. A new launch in the West Village surprisingly is not attracting Asian purchasers. The Chinese market continues to dominate interest from overseas buyers now.

Is there any concern about an oversupply of new development inventory in any segment?

Compared to the height of the market in 2007 when there were approximately 8,000 units in new development properties, the forecast is a total of approximately 3,000 units for 2014. We do not believe we are at that point yet where we are facing oversupply.

We're hearing that developers are starting to reach out to brokers more and calling back potential buyers who have just looked at units. Doesn't that suggest some concern about the market among developers?

It's always our policy to actively follow up with prospective purchasers who have visited sales centers and not to wait for them to contact us. We do not see that as a sign of weakness, rather as sign of proactive sales strategy. It's our duty to our clients to actively market their properties; otherwise, they could hire order-takers.

We've also heard that some developers are shifting to more outside agents rather than using in-house brokers. What are you seeing?

We have been approached by developers, who wish to energize their sales efforts. We are collaborating with several developers — Alchemy Properties and Macklowe Properties, for example — and their in-house teams to increase awareness and increase their sales conversion rates.

Andrew Gerringer
managing director of new business development, the Marketing Directors

How would you characterize the new development landscape in NYC?

There's a hole in the market in the $1,800-to-$3,000 category and there is big demand there. As far as the ultra-luxury, $3,000 range, there seems to be decent supply and demand. There's a lot of product in the pipeline. And the foreign buyers are really fueling that ultra-luxury market.

Do you think there's a ceiling on land prices that either has been reached, or will be soon, that will stop or slow down new development transactions?

Land prices have gone up dramatically for prime Manhattan areas to $800 to $1,100 a foot, give or take. For off-prime locations in Manhattan, they're probably in the $500 to $600 range. Land in Brooklyn and Long Island City is going for over $200 a foot. The market changed this past year-and-a-half very rapidly. But I don’t think it’s going to continue that way. You certainly can’t make rentals work anymore in prime areas. The only people doing rentals are people who have had the land for a long time.

What is the biggest challenge in marketing new development right now in NYC?

The challenge is that a lot of these developments are high priced and we don’t have enough product for the middle-luxury market.

What are the most surprising new trends in the NYC new development world?

Renters staying in apartments for much longer because a lot of kids are coming out of school with high debt and can’t afford to buy their first condo right away. Financing is not available like it used to be. As a result, the amount and dedication of space to the amenities within rentals have just changed dramatically. You’ve got bocce ball courts, BBQ grills, movie theaters — everything that is suggestive of wanting to retain a rental tenant.

Plans for new developments are popping up in places that were previously ignored — like Staten Island and the Bronx. Do you think these locations will be marketable?

We’re proving right now that Staten Island is very marketable. We’re on our second project there — the Accolade. We’re already up to almost 50 percent sold since April. There’s a lot of demand and there’s a lot of good stuff coming to the area. There’s the Homeport project that Ironstate is doing. And Triangle Equities is building a site over [by the Staten Island Ferry in St. George.] Then you have the Ferris Wheel and the retail that’s coming with that. The Bronx hasn’t seen that kind of activity yet. As these other areas get more expensive, I think things will catch up there, but most of what gets built in the Bronx is affordable.

Izak Senbahar
president, Alexico Group

What kind of ratio of foreign-to-domestic buyers are you seeing?

It’s very project and location specific. For example, at 56 Leonard, it’s mostly domestic whereas at the Mark Hotel we see more international. Foreigners are much more familiar with Uptown than Downtown.

We’re hearing developers are more eager to sell units because of concerns that today’s strong market is not sustainable. Are you concerned?

Having over a billion dollars of sales under our belt at 56 Leonard Street feels really good. Maybe we didn’t price it as aggressively as we should have. … I think a little insecurity about the market and where the market is going made us a little concerned. Land prices, construction prices going up — those are all things that concern me.

There’s been a lot of talk about the all-cash buyer. Are you seeing fewer buyers who need financing?

I’m always surprised by the amount of all-cash buyers. It’s way above 50 percent. And in our units those are big [dollar figures]. There used to be a time when people would put their cash in the stock market. Nowadays, I see people putting it in real estate and not financing it. They have more trust in the real estate market than in the stock market.

Correction: In a previous version of the “Luxury condo overload” Q&A, the name and photo of Susan de França, president and CEO, Douglas Elliman Development Marketing Group, was omitted due to an editing error. As a result, her comments were incorrectly attributed to Shlomi Reuveni of Town New Development, along with his own. The item has since been corrected.