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2010 Upstate New York apartment market report: Long-term prospects look good

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Apartment sale activity slowed dramatically across the upstate New York markets of Buffalo, Rochester, Syracuse, and Albany through 2009. Heightened uncertainty from the past years financial crisis left buyers and sellers with little incentive. Owners are unwilling to discount assets with good long term prospects in order to attract buyers looking only for discounted prices; buyers are caught up in the all pervasive fear of the great recession. With little new construction in recent years, supply and demand remain in balance. Without an excess inventory of vacant apartments to work off occupancy has remained stable and tenant demand for existing units remains strong. Sunrise Management and Consulting in its Fall 2009 Multifamily Rental Market Report finds flat rents across upstate New York State, the exception is the Albany market with a $15 average monthly rent increase. Stable rents reflect stable occupancies and with values here protected owners aren't feeling pressured to sell. Financing for multifamily properties is available; maturing debt is readily handled through smaller and regional lenders along with Fannie Mae and Freddie Mac.

Also supporting prices is the increased spread between mortgage interest rates and cap rates; higher equity returns are available without a change in property pricing or income. Taking advantage of long term mortgage interest rates in the 5 percent range buyers can earn cash on cash returns in excess of 10% with current capitalization rates in the 8% to 9% range. In conservative markets like upstate New York value is created through higher rents and income; consistent income coupled with today's lower mortgage rates produces a better return with level or unchanged property pricing.

The past years events have also demonstrated the advantages of apartment investment here versus other areas of the country that until recently where considered superior. As values fall from unrealistic heights in southeastern and southwestern markets those properties with maturing debt in the form of balloon CMBS mortgages will find refinance debt unavailable at any price and cause complexes in these markets to be sold into falling markets. Sale prices in Phoenix fell 27% last year. National merchant builders chasing population growth were never active here and the local dynamics of the multifamily business never factored in the large population growth projections which caused these other markets to overbuild and drove them into depression when these projections failed to materialize. The limited capacity of the existing apartment inventory in upstate New York has worked to keep occupancy stable and values protected.

The long-term prospects look good for apartment investment in the upstate New York market although the start of 2010 looks to be repeat of 2009. Slow activity to start with sales increasing as buyers ease back into the market. Private local investors with long term familiarity with the market and pricing will dominate.

Serious concerns exist with pending government legislation. The proposed changes in the tax treatment of carried interest aimed at punishing hedge fund operators by taxing carried interest income at ordinary income rates rather than at the capital gains rate has negative consequences for the apartment investment industry as a whole. Real estate acquisition partnerships have used a percentage interest in the capital gains of a partnership on sale (the carried interest) as compensation for the general partners in exchange for organizing and operating the partnership's property for the limited partners; a group of silent investors. This structure has been used for years and the near tripling of this tax rate will discourage the formation of investment partnerships and reduce the pool of available buyers in the market and consequently reduce the price sellers receive.

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