

Why the Prices of NYC Office and Rent-Stabilized Apartment Buildings Are Tumbling

BY [REBECCA BAIRD-REMBA](#) JUNE 28, 2023 9:00 AM



OLDER OFFICE AND RENT STABILIZED BUILDINGS IN NEW YORK CITY HAVE SEEN DRAMATIC DECLINES IN PRICES AND VALUATIONS ON THE INVESTMENT SALES MARKET. WILL THEY EVER BOUNCE BACK?

ILLUSTRATION: KEVIN FALES

discount on New York City's investment sales market: namely older office buildings and rent-stabilized residential buildings.

David Schechtman, a broker at Meridian Capital who handles about \$200 million worth of Class B office sales annually, said that prices on older, less amenitized office buildings have come down by as much as 50 percent over the past few years. With the sharp rise in banks' benchmark borrowing rate from near 0 percent to almost 6 percent over the past year, New York City office properties that were already struggling have hit an even bigger stumbling block.

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It's become increasingly clear that workers may never return to the office five days a week, with average weekly attendance hovering around 49 percent of the pre-pandemic average for much of this year, according to Kastle Systems, which tracks ID card swipes at office properties in major markets. Many office owners are discovering they cannot lease their buildings, and interest rates are too high to comfortably refinance their properties. In some cases, office owners end up giving back the keys to their lenders.

Schechtman said he'd been marketing a building near Rockefeller Center that fetched a \$60 million offer before the pandemic. The owner turned it down. Now, the property is likely to sell for \$36 million or \$37 million, in a significant price cut.

"If this contract gets signed at \$36 million, it would be a record at \$600 per square foot [for Class B] this year," he said. "Knotel signed a lease for most of

market.”

Most buyers in the market these days are either office occupiers — big financial, tech and law firms — or out-of-town investors looking for a good deal.

“When sentiment shifts, you have people from San Francisco, Chicago, who say, ‘We’re looking at your offering memo,’ ” said Schechtman. “And I’m like, ‘Wow these people are real, but I never even knew about them.’ ”

He added that most Class B and Class C office buildings are unlikely to be good candidates for residential conversions.

“Office is still a dirty word in terms of how it’s viewed in the market,” said the broker. “Do I think office will ever return to the boom days of record leases signed daily? I do not. Notwithstanding the good intentions of some politicians and office owners, you’ll see very few office buildings converted to other uses. What we fail to realize is the inefficiency of these buildings, especially the Class B, our most inferior stock. It wouldn’t surprise me if our most inferior stock was sold as teardowns to be rebuilt. To buy a 100,000-square-foot building, even at \$300 a square foot, you may have to match that \$300 a square foot just to convert it.”

This spring, the New York State Legislature debated incentivizing more office-to-residential conversions through tax breaks in exchange for affordable housing, but lawmakers couldn’t reach an agreement on policy with Gov. Kathy Hochul.

“As we plod along over the next few years, lenders are not in the business of owning real estate, so the question becomes: What happens to these buildings?” Schechtman explained. “It can’t be that you’re going to have millions of square feet of office vacant in perpetuity. We just need the laws to match that desire. I

zombified.”

However, lenders tend to be more forgiving of Class A office properties in good locations such as the Plaza District.

“What we’re seeing in office is that if you have a Class A office building that’s well-tenanted and well-located, and you have a mortgage or CMBS loan that’s coming due, in many cases the servicer will probably work with you, if you’re a good sponsor or have a clear path,” said Shimon Shkury, president of investment sales brokerage [Ariel Property Advisors](#). “Those sponsors that gave up on their buildings and are giving the keys up — RXR, [Brookfield \(BN\)](#), Blackstone — the servicers would rather have them keep operating the buildings. We are just starting to see it, but the repricing in office is going to be the strongest.”

Lenders, Shkury said, don’t want to manage office buildings. They’d often rather owners keep the property or stay on as a manager.

“When [a landlord] gives up the keys, they’re not going to play a game,” said Shkury. “The servicer maybe comes to them and is like, ‘Keep the keys and we’ll extend.’ Or if the servicer comes to them and says, ‘Why don’t you manage the building for a fee?’ and someone will say, ‘Well, it better be a big enough fee for it to be worthwhile.’ If I’m a lender, I would be incentivized for them to get me out of there. If the valuation has sunk to a level where it’s no longer worth it, I would want them to keep operating the building for me.”

Citywide, investment sales transaction volume overall was down by about half compared to last year, Shkury noted. Ariel’s research found that roughly \$5 billion worth of sales closed across New York City in the first quarter of 2023, compared to \$11 billion in the first quarter of 2022.

“very little sales activity, very little loan origination activity” these days, especially for Manhattan’s largest and most expensive office buildings.

“In the good days, you came to the table with 35 percent. Now it’s hard to get a 50 percent loan,” the broker said. The broker had also noticed a number of occupiers buying buildings, typically in all-cash deals.

“We’ve represented three different users buying properties this year,” the broker said. “Users tend to be all-cash buyers, and they’ve avoided the increased cost of capital by using cash.”

Things have gotten trickier on the residential side, too, but for very different reasons. The state Housing Stability and Tenant Protection Act of 2019 dramatically altered New York’s rent-stabilization laws, making it harder for landlords to raise rents through renovations or after a tenant vacates a unit. The law effectively made it impossible to deregulate any of the city’s roughly 1 million rent-stabilized apartments, stymying many landlords’ ability to bring regulated units up to market-rate rents.

“The minute that happened, there was the notion of repricing,” said Shkury. “There were very few transactions as a result of the law. What we haven’t seen is enough transactions to know enough about repricing, but we can estimate it around 20, 25 percent [discount].”

Then interest rates shot up, and one of the city’s go-to mid-market residential lenders, Signature Bank, was shut down in May by financial regulators. Investors willing to purchase a rent-stabilized building now may struggle to find financing in the wake of Signature’s collapse.

Previously low borrowing costs put off any reckoning from the 2019 law. “Some of the impact of those changes in the law were masked by the low interest rates

investment sales broker with [Cushman & Wakefield \(CWK\)](#). “Values of rent-stabilized apartment buildings have been dramatically impacted.”

The changes in the law have slashed valuations of rent-regulated apartment buildings by 30 to 50 percent since 2018, according to O’Brien.

In addition, the state legislature this month passed two bills that would make it easier for rent-stabilized tenants to bring rent overcharge cases against landlords in court, potentially making it even harder for landlords to sell their rent-stabilized assets.

One bill allows tenants to claim that a landlord has committed rent fraud by failing to register stabilized apartments in the building if they are receiving two particular tax abatements, J-51 and 421a. The other piece of legislation extends the lookback period for rent overcharge cases beyond the current four-year period.

O’Brien added that he had marketed residential development sites that were struggling because of expensive construction lending and the expiration of the 421a/Affordable New York tax exemption a year ago.

“Land sites are being repriced today given the cost of debt capital and the lack of 421a,” he said. “Land sites without a footing in the ground to qualify for Affordable New York and the ability to complete the development by June of 2026 — anything that is not a high-end condominium site — I would estimate pricing is off by about 30 percent.”

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KEYWORDS: [Ariel Property Advisors](#), [Brookfield](#), [Cushman & Wakefield](#), [Meridian Capital Group](#), [RXR Realty](#)