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Dirt cheapens at building sites

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Land is often the crux of a great development deal, but in New York City, where developable land is scarce, it often comes with an expensive price tag. Now, some developers say they are seeing signs of change.

Ralph Trionfo, president/broker of Upside Ventures, a commercial real estate firm, said he is about to list an approximately 200,000-square-foot mixed-use development lot in Long Island City for $125 per buildable square foot. He said last year at this time, lots in the same area were selling for about $200 per buildable square foot.

Paul Massey, founding partner and CEO of Massey Knakal Realty Services, said changes in land values are starting in the outer boroughs.

"It's a little hard to tell exactly what's going on, because velocity has slowed down so much; there's not a plethora of comps and facts," he said. "But the outer markets have seen a definite dip in values ranging from 20 to 30 percent."

Because of the decrease in fourth-quarter sales volume, it's hard to point to specific instances of reduced prices, real estate experts said. It's possible that many sellers are still holding fast to unrealistic asking prices, they said.

John Reinertsen, senior vice president at CB Richard Ellis, said there is "probably" a 20 percent reduction in land prices in the boroughs. "But," he said, "It's going on in the negotiations. It's not in the asking price as yet."

At this point in the market downturn, brokers said they are trying to gauge when the expectations of sellers will drop to meet the financing capabilities of buyers, which have been greatly reduced by the credit crunch.

Land prices "are not spiking as they were in the last 24 months, and in some cases, landowners or sellers are recognizing that they have to adjust their expectations," Trionfo said. "We're currently in the process of educating our clients looking to dispose of sites or assemblages about this."

Massey said land prices in Manhattan, along with prime parts of Brooklyn and Queens, are holding much better than the rest of the city, because those properties are versatile.

"Interestingly, in the Manhattan market, values may have slipped a little, but some of these proposed residential uses, when the land didn't sell, could also be office or retail, and that kind of props up values," Massey said.

Prices may have fallen 5 to 10 percent in Manhattan, he said; some of the neighborhoods being hit are Chelsea and the East Village.

"We're starting to see the trades come in to prove that out," Massey said, though he could provide no specific examples.

Eric Anton, executive managing director of Eastern Consolidated, a real estate investment services firm, said prices have not "zoomed down."

"It's more the case that the velocity has zoomed down," Anton said. "If the seller is asking $400 or $500 a foot, and nobody shows up to buy, they don't drop it to $200 a foot. They just don't sell it."

Lenders who are fearful of making bad loans are asking potential land purchasers to put more equity into deals. Developers said that should eventually help to depress prices and open up opportunities for residential projects.

"Before, you used to build your acquisition financing at 80 percent loan-to-value," said Daren Hornig, managing partner of SAXA, a commercial real estate services and development firm. "Now, it's probably 50 percent.

"So if you went to buy a piece of land for $20 million, you used to be able to put down $4 million. Now you have to put down $10 million."

On top of that, loan interest rates are about 300 basis points, or three percentage points, higher than they were a year ago, Hornig said.

"It's almost come to the point where I won't even look at a raw piece of land to develop it, because with the difficulty financing it, the pricing is so out of whack to reality," he said.

Sources theorize that new restrictions on the 421-a property tax abatement will also exert downward pressure on residential land prices.

Effective July 1, developers in many areas of the city will qualify for the tax break only if they set aside 20 percent of the units in their developments for affordable housing. Many developers believe that makes what was once a lucrative tax break a wash.

"I think with the 421-a going away, people are going to pay even less for land because they're not going to be able to get as much money for non-421-a apartments," Hornig said.

Louis Dubin, the president and CEO of the Athena Group, a private real estate investment, operating and development company, said he hasn't seen a drop yet. But he predicted land prices are poised to fall significantly.

"I think the $400- to $450-a-foot price point that everyone's been talking about for your average, well-located site in Manhattan will come down by at least $100 a foot," Dubin said.

And with the 421-a tax break changing, that "will throw at least another $50 a foot to the diminution of land prices," he said.

The number of new residential projects in the pipeline is certainly dropping; as evidence, developers point to a 40 percent drop in the number of building permits issued in the first quarter of 2008 over the same period in 2007.

"There's no question there will be a slowdown in new construction for a while," said Steven Kohn, president and principal of Cushman & Wakefield Sonnenblick Goldman. "In markets like New York and Washington, D.C., and other strong central business district markets, there is still pretty much a shortage of good land, and sometimes it does lag — it takes a while for that pricing to move."

While smaller condo projects less than 100,000 square feet may still be bankrolled, lenders are shying away from anything larger, Anton said, especially with thousands of apartments already under development.

"I don't think the banks are going to get comfortable any time soon financing residential condominiums," he said. "Now they're more comfortable financing residential rentals; however, the prices of land are still too high. Most developers think you need to pay somewhere between $100 to $150 a foot, or $200 max is where you need to be for a rental project."

However, Kohn said he believes rental projects could possibly be done in certain pockets in Manhattan (such as the far West Side and the Lower East Side) and Brooklyn and Queens locations where land prices are below $200 a foot. Trionfo of Upside Ventures said affordable housing is currently an attractive and feasible option for developers, and will become more so as land prices drop.

Once sellers realize that they can't get as much for their land as they could have before the credit crisis, they may try to structure a different type of deal, Dubin said. They may "hypothecate" their land, meaning they would pledge it as a security to a developer without transferring possession or title.

"You're going to see many more deals where the sellers are staying in," Dubin said, meaning there may be more partnerships between landowners and developers.

But some sources said they aren't certain that land prices will fall much in Manhattan, partly because land there is such a scarce commodity.

"My feeling is that there are so many funds, so much money, so many well-heeled private established companies that are looking for these low-cost opportunities, that it's almost a safety valve for the market to keep prices from going too low," said Scott Singer, executive vice president of the Singer & Bassuk Organization, a real estate finance and brokerage company.

"As prices start coming down, each of these groups is going to have a strike price where they're interested, and at some point, they're going to be interested enough to where they're going to start competing to buy into these things," he said. "That's going to prevent prices from drastically dropping."
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