The State of Real Estate

An Interview with Kent M. Swig,
Co-Chairman, Terra Holdings, LLC and President, Swig Equities, LLC

Kent M. Swig

EDITORS' NOTE *In addition to his ownership of and responsibilities at Swig Equities and Helmsley Spear, Kent Swig is an owner and Co-Chairman of Terra Holdings, LLC, a company that owns and operates several real estate service firms, including Brown Harris Stevens and Halstead Property. Swig is also a principal in The Swig Company, a family-owned real estate and hotel company based in San Francisco and New York. Swig earned a degree in Chinese history from Brown University and attended UC Hastings College of the Law (San Francisco).*

COMPANY BRIEF *New York-based Swig Equities (www.swigequities.com) is a real estate development, investment, and management firm that purchases and develops prime residential and commercial buildings, operating companies, and securities.*

Terra Holdings is the parent company of Brown Harris Stevens and Halstead Property.

How is the New York real estate market faring today?

The commercial market is a reflection of the greater economy as a whole, and employment, in particular. As companies hire new employees, they need more office space and, thus far, the job market and new hirings are doing well in New York City.

We have gone through four significant downturns since 1945: In the mid- to late '70s, New York City lost about 768,000 jobs. In the next downturn, from 1989 to 1991, we lost approximately 350,000. From March 2001 to December 2001, we lost approximately 250,000. During the recent Great Recession, we lost about 140,000 jobs. The pattern is clear: New York City is losing fewer jobs during each recession and the recovery tends to be faster than in earlier recessions.

In New York State, 80 percent of those who had jobs experienced the loss of at least 10 percent or more of their income in this Great Recession. So it was an impactful recession – less so because of job losses and more so because of lost income, which prior to this recession, were typically directly linked.

This resulted in a compressed recovery. The downturn was rapid as was the upturn; the shape looked like a "V" when put on a graph. Layoffs that were anticipated did not occur and, consequently, the commercial market did not decline to the extent of previous recessions.

Also, prior to the Great Recession, commercial rents had spiraled upwards to as high as $200 per square foot in some cases. When the decline occurred, rents did dip, but to a level that was still high. Rents in New York City still remain inexpensive compared to the rest of the world's financial capitals.

The vacancy rate is under 11 percent right now. Somewhere between 9 and 10 percent is where economists consider that an equilibrium exists where tenants and landlords have equal negotiating strength in the marketplace.

On the investment side of the commercial market, in many cases we have not only returned to the previous values but we have exceeded them. This is a result of several factors: the stock market is at record levels causing investors to look to other investment opportunities; there is an enormous amount of cash that corporate America has retained and they are encouraged by real estate investments because of the inherent "groundedness" of real estate in that you can't "Madoff" a building; and real estate is basically a transparent and easily understandable investment.

With worldwide instability, New York City real estate is a safe investment with relatively few restrictions on buying and selling, and located in a transparent and fairly liquid market. So while rental rates in the commercial sector haven't gotten back all of their value, with the large amount of cash out there and the strong demand, prices are reaching historic levels.

How has the residential side fared?

In terms of the residential segment, the market had one of its more severe downturns in New York City's history. From July 2008 to July 2009, the market fell some 23 percent in value. In 2006, we had peaked at about 19,000 transactions per year – typically we average about 14,000 – and during this one year drop, transaction volume fell to just under 9,000.

Among those who were most adversely affected were those who are dependent on volume, which are brokerage companies. Yet it was also a great opportunity to grow because brokers and brokerage firms become available during weak economic periods.

For Halstead Property and Brown Harris Stevens, we grew by some 40 percent; we had cash and no debt and we were in a strong position. In the downturn, we made cuts selectively but also grew our base in Terra Holdings, so when the market came back in July 2009, we had more market share and found ourselves as a more dominant player.

There are several reasons that the residential market rebounded so quickly: the job losses were much fewer than expected and they weren't substantial enough to force people to move or sell their homes, which meant that an inventory build-up did not occur. Consequently, when income returned, people were able to re-enter the sales market rather quickly and, combined with a lack of new buildings and low inventory, sales prices soared to some of the highest prices ever achieved in New York City.

The issue is that, if demand continues, New York City has only about a three-month supply of product. If we don't begin to add units to the sale market or stimulate more re-sale inventory, there will be nothing to buy and prices will continue to escalate.

Are too many people being priced out of this market?

This is a problem. In the 1970s, the impact of the 768,000 job losses was that 1.1 million people left the city. It took us until 2003 to regain that population and the result was that the supply of housing was enough to maintain moderate and steady price growth.

Yet, during the recent Great Recession, our population continued to increase and we now have 8.3 million people living in New York City with just 3.1 million housing units. Two-thirds of the market is rental and one-third is home ownership – that equals just 1.1 million homes to buy. New York City has a local, domestic, and international following yet we have very little available product and we're not adding enough supply to keep prices from escalating at a fast pace. In the past, New York City added approximately 55,000 homes (both rental and for sale) each year between 1952 and 1975, whereas last year, we added a mere 4,800 homes to the marketplace. This resulted in steep increases in price, which is certainly having a negative impact on "affordable housing." ●