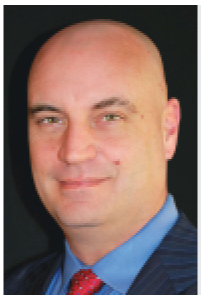
SOUTHEAST REAL ESTATE BUSINESS®

May 2016 **Circulation: 20,074**

MARKET HIGHLIGHT: MIAMI

DOWNTOWN MIAMI'S CONDO MARKET IS APPROACHING SUPPLY-DEMAND EQUILIBRIUM



Anthony Graziano
Senior Managing Director,
Integra Realty Resources

The colossal fall of the downtown Miami condominium market in 2007 to 2008 became an emblem of excessive developer exuberance. The memory of "see-through" buildings, and nearly 21,000 vacant condo units is burned bright in the minds of locals and non-locals alike; so much so that when cranes emerged in 2010 to commence construction of Brickell City Centre, Miami's largest under construction urban development project, everyone thought the folks at Swire had lost their minds. All of this while pundits were giving speeches and columnists were quoting them that the market would take a decade or more to absorb the excess inventory.

Adding to those cranes in 2011 was Related's Brickell House project, followed shortly thereafter by Millicento, and then more cranes emerged in Edgewater. Almost overnight, by 2012 there were dozens of cranes and downtown Miami development commenced in earnest. By 2013, those same pundits with the "lost decade" predictions immediately started heralding a new boom while whispering the dreaded phrase, 'But when will it bust?'

Developers have made billions since the first whisper of this cycle's bust. Some analysts have called the bust four times already, and yet the development market marches on. More cautiously, more diligently, but onward ho.

By early 2015, weakness in the global economy began to affect sales velocity, not only in downtown Miami, but generally throughout South Florida. The pundits and media returned in force calling a bust imminent. The problem with predictions is that no one ever fact checks the predictions that were wrong. There is never any penalty in calling for bad weather because if it doesn't materialize, everyone is happy it's still sunny.

So what is really happening? Integra Realty Resources Miami issued the Miami Downtown Development Authority report in the first quarter of 2016, and there are some key metrics supporting our prediction that the preconstruction condo market remains in balance:

1.) Resale condominiums (those not sold by developers) continued to see price increases through 2015. If the market supply of condominium units was out of balance, this would negatively affect pricing in the resale market.

2.) The number of units under construction is less than 50 percent of the inventory under construction in 2006. If history is any teacher, we are nowhere near the level of construction which might lead to a tipping point of over-supply with 7,300 units under construction versus 16,000 in 2006.

3.) The pipeline of pre-construction sales has narrowed significantly since 2014. Of the inventory under construction and projected for delivery in 2016, this product is 85 percent presold with 50 percent buyer deposits.

4.) There is a tremendous level of equity in the overall market. In 2015, over 64 percent of the resale condo inventory was purchased all cash. About 78 percent of transactions purchased from developers were bought all cash. Of the transactions using financing, the loan-to-value ratios average 67 percent (33 percent equity down payments). This leaves lenders far less exposed to systemic default in the sector as a whole.

5.) The under construction multifamily market is a separate, but related component, adding new inventory to the downtown market. This may draw rental demand away from condominiums purchased for investment. With 4,145 conventional apartment units currently in the construction pipeline, IRR expects 2016 to 2017 to offer some rent relief to downtown renters who have been experiencing 5 to 6 percent year-over-year rent growth. This is a healthy addition to the rental inventory, and will require condo buyers who expect to rent to be cautious in their rent assumptions.

The rent growth within the condo inventory is slowing moderately in Brickell and Midtown, but other submarkets are still exhibiting more than 4 percent rent growth year-over-year. The conventional apartment inventory rents are 10 percent less than the existing condo inventory, but maintenance costs and taxes are also lower.

The downtown Miami market is important because it serves as a bellwether to the broader market dynamics. Absent a national recession or other black swan event that clobbers the debt and equity markets, the downtown market remains healthy. This is not to say that every vacant site downtown should start development tomorrow, but business conditions remain strong, downtown employment continues to rise, and assuming continued economic strength in the region, the urban multifamily landscape remains solid.

The for-sale condominium pipeline is mostly pre-sold, and the projects under construction at 7,000 units will deliver over a three-year time horizon. This delivery and absorption is far from past conditions indelibly burned into everyone's memory.

In spite of hyperbole and headlines, the downtown Miami market is coming of age. Ever-increasing pricing and unwavering unlimited foreign demand is as unlikely as ever. But a major market-wide correction in pricing need not be a foregone conclusion. The market is allowed to reach equilibrium, and in fact should do so to remain healthy. The metrics demonstrate we are nearing such an equilibrium. Slowing construction is not a bad sign. In fact, it's a healthy sign in light of global economic conditions.

Anthony Graziano of Integra Realty Resources wrote this article on behalf of the Miami Downtown Development Authority, an independent public agency of the city of Miami funded by a special tax levy on properties in its district boundaries.