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Sizing up the Second Avenue Subway bump

After decades of false starts and eight years of construction, the UES starts to reap the rewards of a real estate game changer

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Amit Doshi, Krishna Rao and Teri Noren

Barring any unforeseen catastrophe, the Upper East Side should have a new subway line in 2017. As of late last month, the \$4.4 billion project — which has been nearly a century in the making — was set to open on New Year’s Day. “If we’re not done January 1, I will stand up and say we failed to make the deadline, and I’m disappointed,” said Gov. Andrew Cuomo, who personally visited the new stations and oversaw details. But whether construction crews actually make that deadline or not, the new transit line is already being factored into the UES market, according to experts. In November, StreetEasy released a study that showed that median rents along Second Avenue had increased 27 percent over the last five years, significantly more than rents along First and Third Avenues. That suggests more optimism than might be expected, according to Krishna Rao, StreetEasy’s economist. “The history of the Second Avenue Subway is a bit tortured, so we had a sense people wouldn’t believe it was real until it was built,” he said. “Our suspicion was perhaps the news wouldn’t see impact until opening day of the subway, because it could have been pushed back again.” Brokers are already seeing price hikes on condos, and developer Ben Shaoul, who earlier this year launched sales at 389 East 89th Street, told *The Real Deal*

that he is shopping for more sites in the neighborhood. To find out what kinds of buyers and investors are flocking to this market and what other changes are in store for the UES, we turn to the experts.

Krishna Rao

Economist, StreetEasy

Walk us through the methodology of StreetEasy's study on the impact of the Second Avenue Subway line on rents. What was the most surprising finding?

The main part of the study was looking at apartments around Second Avenue, how they appreciated over the last five years, and comparing that to what we've seen around First and Third Avenues between 72nd and 96th. Then we looked at what sorts of appreciation rates we're seeing. The main thing that surprised us was the pace of appreciation we've seen on Second Avenue, especially compared to First or Third. In the last five years, we have seen rents increase by about 14 percent on Third, but that figure was 27 percent for Second Avenue.

Obviously once the subway line opens, that should impact prices, but construction is ongoing, and it was surprising that we are already seeing evidence that the Second Avenue area is outperforming other avenues around there based on anticipation of this subway line and how it might change the neighborhood.

Can you compare the market bump of the Second Avenue Subway market to that of other infrastructure projects in NYC?

The High Line and the impact of the High Line on the West Side is one. If you look at how it changed West Chelsea and homes and their values in that area, it's a similarly large impact. I do tend to think there are two things in New York real estate that drive home values: convenience to commuting and also amenities like a park, such as the High Line. Supply and demand of new buildings can come up or down, but those are two of the things we tend to see.

How much of an impact will there be on the market once the subway actually opens?

Once it does open and things are final, you will see a big impact. What we saw in the study was how much exactly New Yorkers do value shorter commutes. The average New Yorker is generally willing to pay about \$33 a month in extra rent to shave a minute off their commute. With the opening of these new subway stations, depending on the area, you're looking at reducing the time it takes you to travel to 42nd Street by about 10 to 14 minutes. That adds a big convenience premium in the neighborhood when subway stations open. We expect to see convenience premiums priced into the area more and more.

It's a little tough to look too far into the future. One of the things we're going to look at is how the opening of the Second Avenue subway changes the character of the neighborhood. As rents increase, you start to attract a different type of renter. This often influences dining and retail options there. There's also a lot of long-time residents of the area who established a life there and might not want to be uprooted and were planning on staying for the long haul. The pace at which something like a new subway can change a neighborhood is unknown, since it has been so long since we've seen the establishment of new line in the area on this scale.

How does Yorkville's standing as one of the relative bargains in Manhattan change going forward?

Yorkville was the least expensive part of the neighborhood, but bargains depend a little on who the renters are. Certainly, [once prices go up], other areas will be attractive for some of

these renters, whereas some might be a little more tied to the neighborhood. Yorkville is still the least expensive place to live out of all the Upper East Side neighborhoods.

Frances Katzen

Principal broker and founder of Katzen Team, Douglas Elliman

You've been working on the Upper East Side for roughly a decade. What are you seeing in the UES market now that the highly anticipated subway is set to open?

The Upper East Side east of Third Avenue was typically considered the "nosebleed section." People didn't want to live over there; it was too far over. But people really believe the subway is happening now, and there is an affluent group of people who want chic, well-made apartments. And what we're finding now is that people do have an interest in seeing what's coming to life on places like East End Avenue and York Avenue. Restaurants are shifting up there, and retail too.

What types of residents are you seeing moving into the neighborhood, and what types of investors are interested?

A broad range: young, hip professionals; Europeans who want to be near the best schools, people who want the loft lifestyle like Downtown but don't want 8-foot ceilings or co-op boards. They want the Downtown feel and have Uptown needs and sensibilities. I do see foreign investors who show an interest especially next to schools. Foreigners are looking for condos they can rent out, a pied-a-terre. They are specifically looking for ease and a clean acquisition that doesn't have any hair on it. It's a slam dunk on the Upper East Side, and the pricing has different entry points. The market now in Downtown is very expensive and the Upper East Side is more opportunistic, with a bigger width and deviation on either side of Lexington. There are a lot more opportunities to enter, and the investor likes it because the numbers make more sense for buyers.

Where are the relative bargains in the neighborhood going to be?

Yorkville will not remain the relative bargain. Right now, people find it noisy, inconvenient, and people want silence when they move in. But the ones looking now may be missing that market by virtue of the fact that it's going to get very pricey very quickly when there's no more risk, noise, dirt and fuss. If you're an entry buyer or investor with a limited budget, ultrasmart people looking for value are looking at First Avenue: it's not such a dumb idea. I'm seeing a shift and going to bet that 10 years down the line those people will not regret putting their liquid assets into an apartment, because this thing will perform. We feel that is the natural progression. This island ain't getting any bigger and the population is growing, and the only way to go is up. So on the Upper East Side, there's a new buyer in town who doesn't need to have a prewar on Park. They want good product and value.

Ben Shaoul

Developer, Magnum Real Estate Group

There are a slew of luxury condo projects coming up on the Upper East Side — 12 of them east of Lexington. You currently have a condo project at 389 East 89th Street.

How much does the Second Avenue Subway opening help sell the units? What slew?

I don't see much coming at all, as I don't see construction loans coming. But with that said, the Second Avenue Subway has been a major selling point on the Upper East Side, which once completed will provide residents with easy access to Downtown for the first time in history.

How quickly are your units selling right now?

The traffic and sales velocity at 389 East 89th Street is evidence of how well buyers are responding to the accessibility of the neighborhood, as the building is approaching 50 percent sold with an average of 40 appointments per week.

Which condo projects are best positioned to sell in this market?

What sorts of properties are in high demand? Properties that are priced well at the \$1 million to \$3 million range while maintaining the element of luxury, as we have done at 389 East 89th Street.

Where do you see the market six months from now once the Second Avenue subway opens?

I see much of the \$1 million-to-\$5 million market all being sold in the next six months. I think the media has gotten it all wrong when they state that there is too much inventory coming to market. I see us shifting from a buyer's market to a seller's market at this price point.

Are we seeing a demographic shift for the neighborhood? What types of people are moving in and considering the neighborhood now?

We've seen interest from both current Upper East Side residents as well as those who potentially would not have considered the neighborhood before. There has been a variety of different people migrating to the area, from young professionals to families to empty nesters.

Do you have any other projects in the pipeline in the neighborhood?

Currently 389 East 89th Street is our sole Upper East Side project, but with how successful this building has been, we are looking in the area and have identified a few other sites that could fit with market demands on the Upper East Side.

Amit Doshi

Executive Director, Besen & Associates

Extell last summer closed on a \$93 million contract to buy a former Gristedes supermarket at 350 East 86th Street. What kind of development interest is there right now in the Upper East Side? Do you expect to see more projects in the pipeline following the opening of the new subway line?

There is interest in streets such as East 86th Street and East 79th Street. No developer can go wrong on cross sections along major avenues. Developers are more and more bullish, but the Upper East Side is for a select category of owners and investors. The younger single crowd is moving elsewhere and finds the Upper East Side too staid for their taste.

Where do you see the condo market moving six months from now?

Six months is too short a period for a defined change, but if the buyer financing for condos opens up a bit more, there is going to be a ton of aggressive buyers, both foreign and domestic, for all segments of Manhattan and fringe areas of New York City. There is also a ton of \$2,000-per-square-foot condos in the pipeline and as product available in today's market. The developer has to create a signature product to distinguish themselves from others. Ultimately, the end buyer is the winner, especially if you are thinking long-term, and one should be.

What effect will the new subway line have on retail? What are retail rents right now, and where do you see them moving in six months?

Retail rents vary from Madison Avenue to First Avenue. On Madison rents can fluctuate from \$600 per square foot to \$300 per square foot, while other avenues range from \$300 per square foot all the way down to \$100 per square foot. Frontage, corner, proximity to transportation, pedestrian traffic are factors. Rents have suffered due to the subway

construction, and those rents will come back up slowly but surely. Corners and location close to main intersections are about \$200 to \$300 per square foot; the rest fluctuate from \$100 to \$200 per square foot.

Perception of where the economy is heading is a big factor in determining where rents are headed, but one can safely assume 5-6 percent increase in the next two years. There is still a vast amount of space available throughout New York City to be absorbed before rents move up into the double digits.

Stephen Glascock

Developer, Anbau

How big an impact will the Second Avenue Subway have on the UES market in general?

Due to its lack of public transportation, Second Avenue hasn't historically been the most popular part of town. Now, with the opening of the Second Avenue Subway, nearby restaurants and retail purveyors are coming back to life. Yorkville is one of Manhattan's best-kept secrets, and the lack of nearby transportation has preserved its authenticity. The new subway will add convenience for those who value the charm of the neighborhood yet want to access different parts of the city, especially the West Side. I'd describe Yorkville as the Upper East Side with a bit of East Village thrown in, and now it will have the first new subway in 100 years, making it an even more attractive place to live.

Are we seeing a demographic shift in the neighborhood? What kind of buyers are you seeing?

We are primarily seeing young professionals starting families and empty nesters moving to the Upper East Side, as well as people who want the prestige of an Upper East Side address and the schools. Interestingly, we've noticed many people moving from Tribeca and Brooklyn Heights, people who need to reverse-commute to suburbs north of Manhattan and people who want quick access to the Hamptons.

How are sales going at Citizen360?

Anbau launched sales for our new luxury condominium Citizen360 earlier this year. The property offers 84 one- to four-bedroom residences in Yorkville. Exteriors have been designed by SHoP Architects to reflect the surrounding streetscape, with remarkable attention to detail. People who value the SHoP Architects design and Clodagh interiors combined with the convenience of the neighborhood have been especially attracted to the project.

Steve Maschi

Vice president, Glenwood Management

You own 11 rental properties on the Upper East Side. How much has the lack of transportation affected the Yorkville rental market over the years?

We have been dealing with not having the subway here since the company started. I've been here for 30 years and we're accustomed to not having the Second Avenue Subway, so what's frustrating is not so much the wait but the disruption the construction has caused in the neighborhood while waiting for it to be completed. It caused traffic problems, and retailers are having problems. Our York Avenue properties provide shuttle transport to the subway for tenants, but now they have another choice. We will likely continue to provide shuttles. Just having another transportation option makes the neighborhood a little more desirable.

Where are rents going?

Rents are cyclical. During the course of a year rents go up and down; typically this time of year rents get a little softer, that's normal. Spring and summer they go up a bit, in fall and winter they go down a bit. That cycle repeats itself, but in the long term rents are going up. So if you take the long view, over the 30 years I've been here I anticipate they will continue to rise. Of course, not always straight-line.

Teri Noren

Broker, Bond

How has the long wait for the Second Avenue Subway affected prices on Second Avenue?

The long wait depressed prices and rents for a while. There has been a huge change in prices from three years ago to now because people didn't want to live with construction. Now you don't hear it that often because certain phases are complete, and, as a result, prices have increased. What you can get for a one-bedroom now, you could have gotten a three-bedroom three years ago. Even though buyers see the mess, they know the subway is coming. I tell them that once the subway is built, the prices will go even higher.

How much are prices going up?

An apartment I sold a year ago for \$750,000 is now \$830,000. I think prices aren't going to go up that much more, because interest rates are starting to rise. They'll need more money to buy the same property. Sellers are starting to hear that, and there's not that much more wiggle room to go up. Let's see what happens once Trump takes over. I've been telling my clients to buy now so as to lock in this interest rate.

What sorts of buyers are you seeing coming into the neighborhood?

I've been getting young families and foreign investors, mostly from China. One couple asked me to take them to the new Second Avenue Subway because they wanted to see the entrance. They were very interested in that East 86th Street entrance. It gives investors an opportunity to buy something if they want to be on the UES at some point down the line. The UES still has the cachet of wealth and accomplishment. Schools are good there. I'm seeing families with young kids who want to be there and want to mingle with other young families. Once the subway comes in, there will also be more retirees coming in from the suburbs.

Will Yorkville remain a relative bargain?

Yorkville is still cheaper than lots of places in Brooklyn. I had a couple looking at Park Slope, and the initial prices there have been higher than things in Yorkville — although maintenance is still less in some areas of Brooklyn. I would say families who want a three-bedroom apartment can get one for under \$1.5 million, where they couldn't get that anywhere else in Manhattan. The area is still not as fancy as other parts below 79th Street, but it has a very relaxing vibe. Nobody gets angry if you don't look proper when you live in Yorkville. You don't have to play that "Upper East Side role." The relative bargains are in the 80s and 90s east of Lexington.