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SMOOTH SAILING

Latest interest rate hike fails to jolt luxury apartment market

By Holly Dutton

Experts believe New York City's residential market won't be too shaken by the new interest rate hikes, and with the expected tax cuts for top-earning Americans, the luxury market could get a boost.

GREG MCBRIDE

JONATHAN MILLER

Last week, the Federal Reserve announced an interest rate hike by 0.25 percentage points, just the third raise the Fed has announced since the financial crisis. The rate was raised to a range of 0.75 percent to 1 percent. But New York City market insiders aren't worried.

The hike is actually a sign that the economy is growing stronger. The Fed lowered interest rates to historic lows following the financial crisis in 2008, in order to help the collapsed housing market.

"The simple message is the economy is doing well," said Federal Reserve chairwoman Janet Yellen in a press conference March 15 announcing the hike. Yellen also forecasted two more hikes for 2017, as well as three in 2018. "We have confidence in the robustness of the economy and its resilience to shocks."

Greg McBride, chief financial analyst at Bankrate.com, an online aggregator of financial rate information, said the Fed is gradually normalizing interest rates at a level more appropriate for where the economy is right now.

"What they're effectively adjusting is the price of money," said McBride. "When the economy was in really bad shape during the financial crisis and with a very sluggish recovery, the Federal Reserve kept interest rates at rock bottom levels to encourage activity. Now the economy is doing better, we don't need emergency levels of interest rates."

The overriding factors are the health and stability of a household from a financial perspective, and when people are working and making more money, they will buy houses - whether the interest rate is 4.5 percent or 3.5 percent - they might buy a different sized house, but the underlying fundamentals for why people buy houses is on the rise, said McBride.

Appraiser Jonathan Miller, who has been tracking the market in NYC for nearly 30 years, said for the rate hike to make any real difference, they'd have to be much higher than they are now.

"In 2007, the market had the highest sales volume in the 27 years we've tracked the market, and interest rates were at almost 6.25 percent," said Miller, adding that even with rate hikes in the last nine years, there is still a record volume of sales.

At the beginning of the year, the Federal Reserve projected they would hike interest rates two more times in 2017, but Miller is somewhat doubtful.

"I'm skeptical about that," he said. "I think rates have to climb much higher before they become a significant factor."

Miller also pointed out that in the Manhattan market, 48 percent of transactions in the 4Q of 2016 were all-cash, which goes to show that mortgage lending doesn't have the same footprint in Manhattan as other housing markets that are more dependent on it.

According to Douglas Elliman's 2016 fourth quarter Manhattan sales report, 34 percent of all co-op sales and 61.7 percent of all condo sales were all cash in the fourth quarter, and higher-priced properties had an even higher share of all cash buyers.

For apartment sales under $500,000, 35 percent were all cash, while those over $5 million, 82.1 percent were all cash.

The interest rate hikes could have about an $18 dollar increase every month on the typical home buyer's mortgage, while in pricier housing markets like San Francisco and New York City, that number could be $77 and $40 per month, respectively, according to Zillow economist Aaron Terrazas.

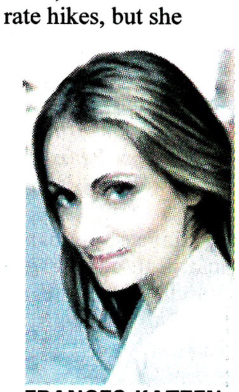
"While we don't think this is going to be much of a headwind for the vast majority, we do think higher-priced markets are more vulnerable," said Terrazas, who added that the rates aren't going to dissuade anyone looking to buy, but it may affect where in a metro they buy, and the size of the home.

And if rates do continue to be hiked as many expect the Fed to do, at the higher end of the market, the monthly mortgage increases will take more of a hit. However, expected tax cuts to individuals in the highest tax brackets could offset this.

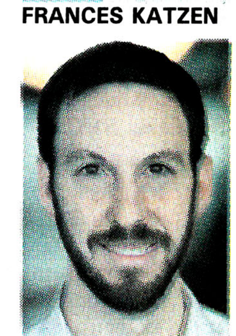
President Donald Trump as well as congressional Republican leaders have proposed tax cuts across the board, but those earning $200,000 or more per year would see a nearly 7 percent cut to their taxes, from the current rate of 39.6 percent to 33 percent.

"I think that if this tax cut across the board, the luxury section will benefit," said Douglas Elliman broker Frances Katzen. "That's putting 7 percent back into pockets in discretionary income to high net worth individuals."

But what about the entry market?



FRANCES KATZEN



AARON TERRAZAS

Katzen admitted that those not in the top-tier tax brackets "have the least to spend and the most to lose," and will be more sensitive to the rate hikes, but she believes people will still buy if they feel there is value, even with an interest rate increase.

"At the end of the day, they're throwing away [income spent on renting]," she said. "I think everyone is sort of driven by the same impetus of getting the maximum amount for the least to spend."

Katzen said she was initially worried about what the interest rate hike could mean for the residential market, but she expects that the tax cuts will give prospective buyers "a sense of confidence again" and return on hard work, which will help offset the increase.

"I think it's going to boost and help fill in the sector," she said.

"There's an oversupply and people are very driven by value propositions. I think quite frankly that the rate hike is historically low compared to the 16 percent in the 1980's. I don't think it will smash it apart."