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Investment opportunities persist in Connecticut despite economic downturn

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Connecticut businesses continue to trim payrolls, with broad-based job cuts taking a moderate toll on the state's apartment market. While a 7,000 worker reduction in the professional and services sector during the first quarter has taken center stage, manufacturing losses and construction cuts are also impacting the local apartment market. Even so, persistent demand, positive demographics and the supply-constrained nature of the regional multifamily market will keep vacancy from accelerating to problematic levels as much of the state's renter population remains locked in by high home prices, and growth in those employment sectors that support renters will not be entirely deficient.

Indeed, the concentration of financial services companies in the southernmost areas of the state will continue to impede Hartford's ability to record a swift economic recovery, which could impact the area's Class A assets. Nonetheless, education and health services firms remain bright spots in the overall state's economy. While other sectors are cutting jobs, companies in these fields are expanding, adding more than 1,300 jobs so far this year. Moreover, the sector is forecast to expand by almost 1.4% for the entire year, with the creation of 4,000 positions in 2009. As such, the New Haven apartment market will get a strong boost from continued expansion among biotechnology firms and solid growth in health care employment. The already strong-performing New Haven County apartment market will see fewer concessions, improved occupancy and a quicker return to positive rental growth.

Additional expansion, albeit slight, is also expected this year in leisure and hospitality, and other services sectors. Consequently, New London's casinos, including two of the world's largest, will safeguard area demand for Class B/C assets with lower-paid service workers, while growth among pharmaceutical firms such as Pfizer, will have a similar (much needed) impact on Class A properties, primarily in southeastern Connecticut where occupancy in some properties dipped below 90% in the past nine months.

Vacancy and rental rates will get a much needed assist from reduced development levels this year, and construction will be limited primarily to the Hartford area. Developers are reacting to economic uncertainty by slowing apartment deliveries in 2009, which has been compounded by elevated land and construction costs. After approximately 900 units were delivered statewide in 2008, less than 550 units are expected to come on line this year, an increase in inventory of less than 1% and there is nominal new product in the development pipeline over the next couple years.

After rising 80 basis points in the first quarter, statewide vacancy will continue to increase through year end, finishing in the low-6% range. While this is about 200 basis points higher than the average in Connecticut over the past eight years, it is still fairly strong as compared to many other national markets. As a result of the jump in vacancy, asking rents are forecast to post a modest 3% drop this year to $1,275 per month. These short-term changes represent the first negative trends for the state in over a decade; however, the Connecticut apartment market in general remains reasonably fit compared to the East Coast overall and we anticipate healthy improvement by early 2010.

Proximity to New York will underpin the state's largest vacancy increase in Fairfield County, with rates climbing 200 basis points to 6.9% this year, and asking rents are expected to finish the year down 3.6% to $1,744 per month. Losses within production, manufacturing and distribution companies in Hartford will effect an 80 basis points jump in vacancy by year end to 6%, while rents are expected to fall 4.2% to $926 per month. Rising vacancy in New Haven will be eased by solid renter demand, as vacancy finishes the year at a respectable 4.5%, the lowest level in the region. Local rents are thus expected to remain flat in 2009 at approximately $1,100 per month.

While Connecticut investors have been faced with a shortage of quality for-sale product, sales activity has remained fairly steady. Transaction volume for the past three years has held flat at around 40 sales per year, while dollar volume has fluctuated, a result of the size and quality of assets trading hands.

Based upon the supply-constrained, high barrier characteristics of the regional apartment market, demand from investors for A and B-quality assets with reasonable cash flow expectations persists, as do opportunities for such properties. Additionally, capital flows from regional banks in Connecticut and New York could benefit buyers, as funds are available with spreads below that of most national lenders and agency debt is also available at almost record low rates.

Steven Witten is first vice president and senior director of the National Multi Housing Group in the New Haven office of Marcus & Millichap Real Estate Investment Services.