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Squeeze in supply could stabilize prices for luxury condos

MULTIFAMILY MARKET

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Sales of million-dollar-plus single-family homes peaked in 2007, with more than 250 transactions in Seattle's in-city neighborhoods. Then the Great Recession hit.

By 2009, this luxury cohort fell back to just 155 home sales, declining 38 percent over two years. Clearly there were fewer high-end buyers, and many of the houses that did trade closed with fewer digits in their price tags.

But conversely, the sale of million-dollar-plus condominiums in downtown Seattle grew from 48 units in 2007 to 85 units in 2009 – that's a 77 percent increase over the same period.

This illustrates some potential shifts in demographic preferences but also tests the balance of supply and demand (and the potential interdependencies) between single-family and multifamily housing in Seattle.

Buyers' desires

More than 10,000 baby boomers celebrate their 65th birthday every day in the U.S. Many will retire and change where and how they live, oftentimes preferring to downsize their domestic responsibilities while upsizing their lifestyle.

This demographic remains an obvious pool of buyers for luxury condominium homes in downtown Seattle, but it's by no means the only group. High-end condo demand is also composed of move-up buyers who have already embraced urban living and now seek the next generation of product.

It helps, too, that Washington is income-tax friendly — retirees from Southern states are buying primary residences in downtown Seattle while keeping second homes for the winter months. Fortune/CNN Money recently ranked Seattle a top retirement destination for "urbanites."

Housing cycles

It wasn't until 2005 that Seattle finally joined the condominium boom, which had hit most metro areas several years earlier.

In 2006, higher density zoning was adopted in downtown Seattle, and condominium deliveries multiplied from an average of 250 units per year during the first half of the decade to more than 600 per year in the latter half.

Increased competition fostered design innovation, and larger, more premium product met with pent-up demand for luxury lifestyles in the city. As developers wrestled with protracted permit and construction schedules, condo prices skyrocketed and so did speculation.

But just as the bubble inflated, the global credit crisis effectively saved Seattle from overbuilding (a favorable byproduct of being a late-bloomer market). At least a dozen high-profile condominium towers were deferred or canceled.

Given the lack of construction financing for speculative development, only apartments are being built today. The in-city condominium market has a significant runway to recover because the current development cycle doesn't include new "for sale" condominium towers in the pipeline. (Bank owned inventory is on the rise, but that product is typically limited to entry-level price points.)

Supply and demand

A year ago, there were approximately 560 unsold new-construction condos in downtown Seattle. Available new inventory has since shrunk to about 350 units today — a 37 percent absorption rate in one year, as developers (and their lenders) repositioned prices for today's home buyers.

About a quarter of this supply is priced above a million dollars, which must satisfy increasing demand over the next several years.

Although at lower prices, single-family home sales in Seattle's most coveted neighborhoods are rebounding, and the waterfront sector is on track to eclipse 2007 peak sales volumes this year.

These sales bring greater liquidity to the market, and affluent buyers are on the move. Luxury real estate brokers are reporting a flight to quality as the best values are being cherry-picked.

Unlike the surrounding single-family markets, where million-dollar-plus inventory is commonplace, it would appear the supply of luxury condominiums is fixed. Therein lies the challenge with high-rise construction — demand can rise much quicker than the supply.

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