

San Francisco Market Update: Q4 2009

4Q 2009 Notable Sales:

- 805-811 27th Avenue: This **vacant** fourplex listed at \$995,000, and sold for \$1,050,000, or \$230/sq ft. With smaller houses needing updating selling in the \$700K's in Central/Outer Richmond, this property is a great opportunity for a homeowner to buy an additional three units for about \$350,000.
- 55 Manchester: This small, six unit building suggests that investors should look at District 9 more closely this year. Nicely renovated, the sale price of \$1,353,000 equaled a 10.45 multiple for a small investor.
- 2900 Franklin: This 11 unit mixed-use building with parking, a good tenant mix and individual heating (i.e. no boiler) was probably the best value for apartment buildings in 4Q. Priced too high at \$3.4M, this building languished and then sold for a nice 10.38 multiple at \$2.7M. Bought by a 1031 exchanger, this price should have satisfied an ordinary investor.
- 2240 Golden Gate: This was a distressed Lembi building in good condition and in a good rental area, but with a boiler. The lender held out for months in hopes of a sale over \$4M. It finally settled for \$3.9M, or a 10.26 multiple.

In contrast to the above sales, there were several buildings that drew a premium. Location was key. 1758 10th Avenue in Inner Sunset and 3110 Clay were 7-8 unit buildings that sold at multiples of 12+. In addition Jordan Park/Laurel Heights had a five-unit sale at 85 Palm at a 16.67 multiple, or \$1.4M. Two-unit 136-138 Palm sold for \$1.6M. Both properties needed updating.

Also, 735-737 Chestnut finally sold after 171 days on market, but still for over \$2.1M. The unit mix was an uncertain duplex or triplex with plenty of parking and in need of updating. A large building with tax records showing 4,370 sq ft, it sold for \$492/sq ft.

Q4 2009 Report

After a tumultuous year, property owners are seeking touchstones and direction. However, 4Q activity showed us a shifting market that has not yet stabilized and many sales indicated property specific pricing.

The only evidence of stabilization is in the 10+ unit market. Seven sales in 4Q cannot confirm a trend, but compared with the ten sales in 3Q, pricing moved from an average 9.936 to 11.19 X gross annual income.

Having watched several sales of Lembi properties in 2009, owners saw a Lembi property successfully flipped: 2050 Powell sold at 11.18X gross or \$3,010,000 in 3Q and then resold at 12.49X gross or \$3,395,000 in 4Q.

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Accordingly, some non-Lembi sellers began listing at higher multiples in 4Q to test the market. So far, their success has been muted. Two buildings in Districts 1-8 sold for over 12X gross. Four sold for less than 10.5X gross.

It is doubtful this pricing will degrade significantly, except in two instances: location and deferred maintenance. A multiple of 10-11 should generally give an investor a 5%-5.5% cap rate. This is attractive compared with fixed income vehicles and marks a ten year low in San Francisco.

Location: Larger buildings in the Bayview and the Tenderloin will sell for much lower than 10X gross. Short sales and bank owned properties in the Bayview are giving smaller investors an opportunity to buy smaller buildings (2-4 units) at a GRM of less than 10:

- *1656-1658 Newcomb:* This 3,350 sq ft triplex sold for \$369K. Even with rents projected just at \$1,500/unit, that's \$54,000 in annual gross rents.
- *1201 Revere:* This 2,057 sq ft duplex sold for \$350K. Actual yearly gross rents are \$45,600.

These smaller units will erode pricing for larger buildings. 1501 Kirkwood still could not sell last year despite a \$125K gross annual income and a price drop to \$995K.

The foot traffic in the Tenderloin continues to affect pricing downward. 620 Eddy is pending at a 7.94 multiple. 381 Turk has been on the market for over two and a half years, originally at \$3.85M and now at \$2.7M or at a 7 multiple.

Deferred Maintenance: Buildings with old boilers, roofs, electrical systems and/or dry rot could sell slightly lower. Buyers make large down payments (50%-100%). They will be reluctant to pay more for capital costs.

Duplex sales ranged from as low as \$203/sq ft to as high as \$832/sq ft. The only conclusion in this market is that it will be hard to sell duplexes at over \$600/sq ft, but few will sell below \$370'ish/sq ft. Otherwise, there is no real trend that stands out despite 51 sales in 4Q.

The 3-4 units and the 5-8 units sub-markets will be the most interesting to watch in 2010.

The sale of 972 Dolores, a fourplex with two vacant units and two rented at \$467/month and \$309/month respectively, might be close to the bottom for properties with below market rate rents. This building sold for \$1,030,000, or \$230/sq ft.

For **3-4 units**, will we see a few more value sales like 805-811 27th Avenue? 27th Avenue harks back to pricing where it made sense for homebuyers to buy a multi-unit instead of a house or condo.

Property owners are probably disappointed at current market values. However, the rarity/unavailability of 3-4 unit properties could also act as a floor to pricing for this property group.

It's unclear if we'll see more **5-8 units** selling at below 11X gross that are in decent neighborhoods and in decent condition. If another 55 Manchester comes around, investors should act. These properties will be priced affordably, generally well below \$2M, and many below \$1.5M.

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