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Developers diversify with mixed rental/condo buildings

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The condominium and rental markets continue to travel parallel paths, with rates increasing steadily. However, the future of this extended bull market is hard to predict and some residential developers are considering projects that offer both rental and condo units within one building.

Diversifying the types of units in the building reduces the risk of unexpected shifts in the rental market or condo market while also balancing benefits of short-term and long-term profits.

In the short term, condominiums tend to offer greater immediate returns for developers because sales can commence before or shortly after construction begins. The development firm receives a revenue influx sooner than it can in a rental building, whose leases pay out steadily over a long period



of time. While rental properties are best matched to those with long-term horizons, they also provide a great hedge against potential future volatility in the sales market. Rental properties are especially attractive now, when the vacancy rate for rental apartments in Manhattan is 0.8 percent.

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By combining both types of properties, developers can reduce risk while achieving a balance of both short- and long-term returns.

The hybrid strategy works best, however, in larger buildings with a greater number of apartments.

Projects in the range of 150 units may not be positioned to properly absorb a rental-condo mix, while larger projects, those in the range of 300 units or more, may benefit from the mix.

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Both rental and condo units can share a similar marketing approach. The Related Companies’ One Carnegie Hill on the Upper East Side was one of the first projects in the new wave of mixed rental-condo buildings and has seen success in marketing the rentals and condominiums with comparable offerings to similar audiences.

Rental-condo hybrids do raise several issues. What is the best way to locate and manage the condominium and rental units? Should renters and owners be mixed together, or should they have separate common areas such as lobbies/entrances, elevators?

Developers pursuing mixed rental-condo buildings with shared common spaces must consider adopting similar amenities and finishes for both rentals and condos, so as not to create a divide among residents.

Other issues arise. For example, a condo purchaser pays for a

portion of the common areas in the purchase price – this structure may become complicated when common areas are shared with renters.

Likewise, the management company must accommodate two different types of residents — one that is more transient and another that is more invested in the building.

Potential buyers may question the value of a property with tenant neighbors moving in and out regularly.

They may also express concerns that tenants, despite paying high rents, are not as invested in the building environment and are less concerned with long-term quality of life issues.

If it is not feasible to offer equal amenities and services to tenants and owners, the building

may require separate entrances and common spaces for each group. This alters the cost of construction and building management.

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