UrbanDigs.COM

Is Investing In A Fixer-Upper In New York City Worth The Hassle In 2022?

Written by John Walkup of UrbanDigs

January 27, 2022

Market: Manhattan
Timeline: 2012-2021

Bring your architect! This, along with similar code phrases, means that the apartment you're about to view needs work — and probably a lot of it. To compensate for future headaches, sellers tend to offer buyers a lower price upfront. Since the pandemic, however, interest in fixer-uppers has waned considerably compared to move-in ready units due to additional obstacles the current environment brings to the already uncertain course for renovations.

Mental Math

Consider how the variables in the typical buyer's mind have changed in the past 18 months:

$$Unrenovated\ Value = Renovated\ Market\ Price - (Unrenovated\ Price + Renovation\ Costs)$$

In other words, to price fixer-uppers, buyers look at the price of move-in ready units and back out the cost (and headache) of renovation. For example, if renovated units are selling for \$1M and an unrenvoated unit can be had for \$800K with an expected renovation cost of less than \$200K, then a buyer can sense the value proposition.

The issue, of course, today, is the hassle of renovating. But first, let's start with what we mean by "hassle". Roughly defined, it looks like this:

$$Hassle = Costs + Effort + Time$$

The higher it rises, the more the property's price has to be reduced in order to make sense for a buyer. And these days, almost everything is a hassle. In fact, looking at its three variables, you can see easily see how "hassle" is increasing across the board:

> $Time$
>
> Pre-pandemic, the old adage of three to six months, doubled (meaning that renovations usually take double the time you expect when you get started) pretty much captured the timeline and its associated unpredictable factors. Plans, factors like approvals at the city and building level, supplies, appliances, labor could all be reasonably estimated, albeit with a somewhat hefty overage allowance. Since the onset of the pandemic, however, almost every one of those timelines is in flux. So if you expect the renovation to take three months, it could end up taking six, nine, or even twelve months. While plans can still be drawn up somewhat quickly, getting them approved is another matter. Regarding supplies, kinks in the global logistics chain can mean quoted lead times for appliances or cabinets can go from a specified number of weeks to an unspecified number of months. Finally, with Covid still an issue, many general contractors find themselves constantly

scrambling to keep their crews together (due to a labor shortage in the industry), adding another layer of complexity.

Costs

The consumer price index spiked 7% in 2021 as the aforementioned global supply chain issues forced higher prices, and prices appear to be still heading higher. As the cost of goods rises, so does the cost of labor. Again, pre-pandemic, most costs were known upfront with reasonable overages within the range of mental math. Unfortunately for those planning renovations, today's price based on yesterday's costs may not accurately capture tomorrow's final invoice. There is simply a lot more wiggle room to the upside.

Effort

At the risk of a circular definition, effort is hassle in the corporeal form. While imaging layouts and finishes is enjoyable for many, most underestimate the thousands of picayune decisions that must be made. From choosing drawer pulls to tile width to shade of ceiling white, the nitty-gritty details have to be dealt with. Add to that the business of managing contractors, submitting building paperwork, chasing down insurance forms, wrangling suppliers, tracking down appliances, and locking down working periods, and you quickly begin to understand why renovated units trade at a premium.

In the end, many buyers did the mental math over the past 18 months and realized that whatever value a renovation could bring to an estate condition home, the hassle was just too great while the discount was just too small. Hence, as the real estate market gained steam, more and more buyers competed for renovated properties pushing up prices, while renovated units saw their prices generally stagnate.

Blurry Value

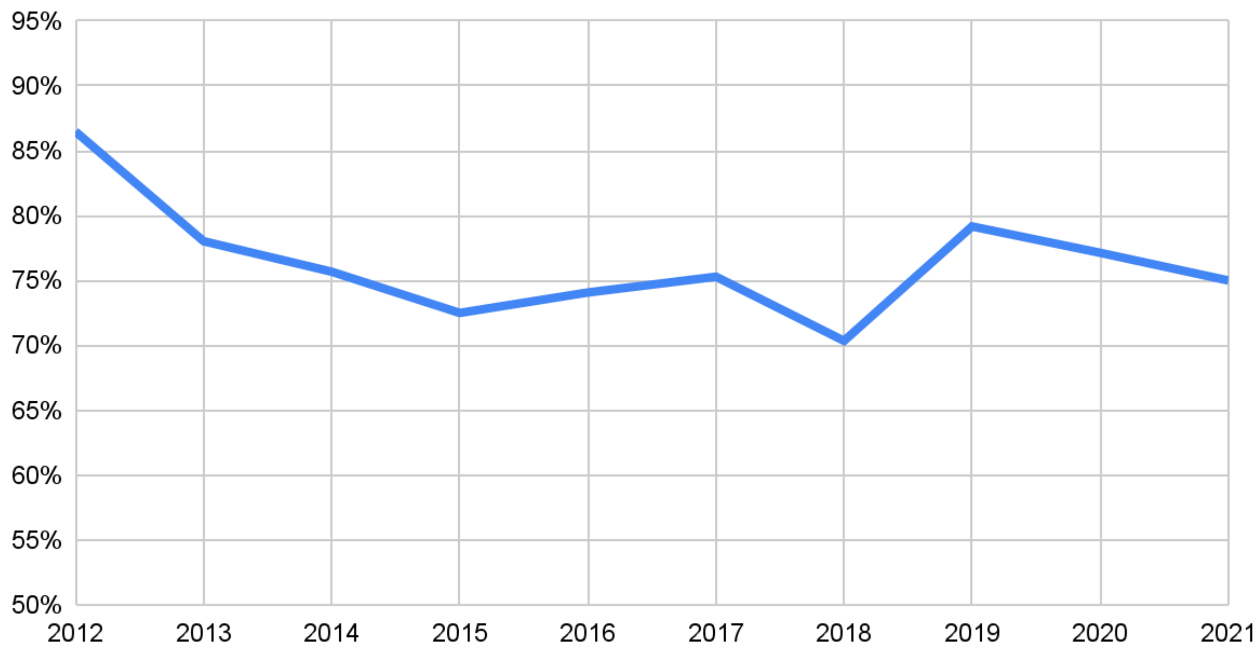
A decade ago, in 2012, the median selling price of an unrenovated apartment was approximately 86% of the price of a renovated apartment. Over the years, that same ratio has mostly fallen and last year it was roughly 75%, further reflecting the increasing desire of buyers to avoid headaches. Price action confirms this trend, with the median price for unrenovated units rising 17% during that time, while renovated units saw double that with a 35% increase. In that sense, the preference for ease is not part of the pandemic's aftermath. Instead, the pandemic brought focus to many buyers' priorities: they wanted bigger units, and they wanted them immediately. Or, to put it another way, renovations are simply not worth the hassle.

The Return of Value Investing?

Entering 2022, the discount for unrenovated units suggests buyers might want to take another look at this currently overlooked sector. As Covid fears don't affect the market nearly as much as they did before, as new patterns and practices turn into a new normal, and as supply chains finally begin to recover, the cloud of uncertainty may finally start lifting from planning hefty renovation projects. With price trends most likely heading higher as 2022 gets underway, the potential value to be realized by doing your own work may finally offset the hassle.

UrbanDigs.COM

Ratio of Unrenovated Price to Renovated Price



Median Price: Renovated vs Unrenovated Units