

Building Slowdown

Will Covid-19 stall construction for long?

By: Brian Bandell | July 2, 2020



PENN-FLORIDA COS. | The construction of Penn-Florida Cos.' Residences at the Mandarin Oriental, Boca Raton.

If it seems like construction activity held steady during the Covid-19 crisis, that's because it did.

But it's important to note that, while existing projects mostly moved forward, developers kept their golden "breaking-ground shovels" out of site.

Construction starts in the tri-county region plummeted 53%, year-over-year, in March, and then 33% in April, according to Dodge Data & Analytics. That's mainly because some developers delayed breaking ground to reassess the market, while others were stymied by a lack of construction lending.

That has cost thousands of jobs in the local construction sector, and has architecture and engineering firms concerned they won't have enough new work to maintain staff.

But while there was a pause in new project starts at the beginning of the pandemic, some developers are more confident about restarting work now, said Patrick Murphy, executive VP of Miami-based Coastal Construction.

Solid projects with subpar locations and lacking an experienced developer are struggling to gain traction, Murphy said.

"Well-conceived projects – whether hospitality, mixed use, residential or commercial – in choice locations with [top-notch developers] are moving forward," he added.

And for projects already under construction, delivering them now is a major challenge.

Developer Jeff Greene said he will halt construction of his One West Palm project after topping off at 30 stories this summer. The two towers were slated to be a mix of high-end residential, hotel and offices. But the Palm Beach billionaire said he's no longer confident in the hotel and office components, so he's asked the city to allow him to make both towers residential before resuming construction.

"Building a big spec office building makes no sense whatsoever," Greene said. "And building a new hotel in a market that's glutted [with them] makes no sense, either."

Some developers are pushing ahead with their projects.

In downtown Miami, One Commercial Real Estate CEO Daniel de la Vega has ramped up marketing efforts in the Northeast to sell office condos in Creative HQ. The project, part of the Natiivo residential condominium, is still expected to break ground later this year.

"People in cities highly effected by Covid are relocating to South Florida in a manner they never have before," de la Vega said. "You have a new wave of people moving here who are OK with moving their offices, as well."

Retail tenants pray for delay

Urban-X Principal Andrew Hellinger is almost ready to open the River Landing Shops and Residences in Miami. Tenants such as Publix Super Markets, Ross and Burlington are moving forward with interior buildout, but some retailers asked for more time or new lease terms.

“Soft goods retailers have to make a decision,” Hellinger said. “Do they open this year? Is there demand for what they are selling?”

He's put lease negotiations with restaurants on hold because he wants to make sure their concepts survive. He doesn't want to commit capital to tenant improvements until he's confident the tenant will do well, and he expects restaurants won't return to full strength for at least a year, he said.

Many tenants building out spaces face tough decisions, said Scott Sherman, managing principal of Miami-based retail developer Tricera Capital.

They invested a lot of money into the facility, but had no income for months and want free rent until they can hire staff and open, he said. He's working with tenants so they can be successful in the long term, but at least one tenant is likely to cancel its lease.

Office tenants hesitant to commit

With no leases signed after a year of marketing, Greene was already struggling to line up office tenants for One West Palm. Securing tenants was harder than he thought, as companies in the Northeast weren't quick to relocate their families. The pandemic, which popularized working from home, further added to that challenge.

“Instead of needing all these conference rooms, firms will have one conference room and then utilize Zoom and other methods,” Greene said. “There will be less demand for office.”

In downtown West Palm Beach, the Related Cos. is still moving full speed ahead with its 360 Rosemary office tower. Senior VP Gopal Rajegowda said 40% of the building is preleased, although it was difficult to reach prospective tenants during the first few months of the pandemic.

One of the selling points of 360 Rosemary is its health-conscious features. The air filtration systems, antibacterial surfaces and outdoor green spaces could help it compete with older office buildings.

“Maybe it will take a little longer to lease up, but we remain confident about the long-term strategy,” Rajegowda said.

Many office buildings under construction are really struggling because they can't secure the Class A rents they were hoping for, said Adam Mopsick, CEO of Miami-based Amicon, which manages commercial properties and construction. It will be difficult to fill those buildings unless rents are adjusted, but that would reduce the value of the properties.

One Commercial has focused on big U.S. cities with expensive office rents in marketing the CreativeHQ office condos. Smaller suites can be used by professional firms relocating or downsizing.

“We have seen demand for smaller units because they are more rentable,” de la Vega said. “We are seeing interest from Latin American buyers on the commercial side more than on the residential side.”

Condo sellers focus on Northeast

De la Vega, also the president of One Sotheby's International Realty, said demand for condos from Latin American buyers is down about 70% due to the pandemic and currency devaluations.

It would be extremely difficult to launch a 350-unit condominium on Brickell and sell out in a reasonable

amount of time. However, condos marketed to buyers who intend to live in their units versus rent them out, such as in Coral Gables or Boca Raton, tend to sell faster, he said.

Activity at Villa Valencia, now under construction in Coral Gables, picked up in early June with \$12 million in presales. Rishi Kapoor, CEO of developer Location Ventures, said he directly marketed to wealthy Chicago and New York residents, and emphasized the boutique size of his 39-unit project. The private elevators, air purification systems and wellness platform have become big selling points.

“We’ve seen a noticeable uptick in people from dense urban northern cities considering a move to South Florida,” Kapoor said.

Penn-Florida Cos. inked five contracts in the last three months at Residences at the Mandarin Oriental, Boca Raton, where most units cost \$4 million to \$5 million, said Frank Weed, VP of development and construction. There have been more inquiries from the Northeast and California, but they missed the prime selling months of March and April. So, while activity has resumed, it’s not at pre-Covid levels.

“We expect to catch up with the sales,” said Weed, who will deliver the building in late 2021 or early 2022.

With fewer Latin American buyers looking at Miami condos, OneWorld Properties CEO Peggy Olin has shifted her focus to the Northeast to sell projects like Paramount Miami Worldcenter. She’s had success with a rent-to-own program, so people can experience the building before making a long-term commitment.

Olin said she’s converted dozens of presales to contracts at the Legacy Hotel & Residences, planned at Miami Worldcenter, because the average price is less than \$500,000. Selling multimillion-dollar condo units is a much greater challenge because people would rather have a single-family home for those prices, which is why some projects are on hold.

“There were projects I have been working on to launch this year, and we put a stop to it to reanalyze the market,” Olin said. “People will be more cautious about which projects they launch.”

Future cloudy for hotel projects

Ronald Finvarb, principal of the Finvarb Group, would like to begin construction of the Thompson South Beach Hotel in late 2020 or early 2021, but expects it will be harder than usual to obtain financing.

He said lenders will request more equity, a lower loan-to-value ratio, and a guarantee from strong loan sponsors before funding new hotels.

Finvarb expects that hotels in hot tourism spots will have a better shot at funding compared to hotels that rely on business travel.

“The pipeline of new hotel supply will slow significantly,” he said. “But leisure markets such as South Florida are expected to bounce back quicker than other cities.”

International travel is being significantly impacted, but the region will likely see a bump in domestic travel, which will help, he added.

Still, it’s going to be challenging to obtain hotel construction loans, said Dev Motwani, president and CEO of Merrimac Ventures, which operates and develops hotels. While his company owns land for new hotels, he’s not going to move forward until he sees the hospitality market improve.

“Next year might be a great time to start a hotel because you will be building when nobody else is, and delivering when nobody else is,” he said.