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2009 may be the year to build on

Developer knows credit is still tough, but hopes changes will help

Robert Freed vividly recalls the first house he saw under construction. When he was in second grade, his parents built a home in Saratoga.

“There was a point in time when the foundation had been poured,” he said. “I walked it with my grandmother and grandfather; they put coins in the corners of the foundation to bring us good luck. It was the first time I knew of such a tradition; I remember the experience being so wonderful.”

Since then, Freed has gone on to mastermind the building of umpteen homes around the United States as a senior executive at KB Homes, Davidon Homes and Blackhawk Corp.

These days, Freed has returned to his Bay Area Roots as CEO of builder SummerHill Homes of Palo Alto, which has projects under way in San Jose, Palo Alto, Menlo Park, San Bruno, South San Francisco, Fremont and Union City. Its focus is infill development—using land within build-up areas – which he considers the right approach for the Bay Area. SummerHill projects range from smaller, single-family detached homes to condos, with density per acre ranging from “north of 30” to six units.

Freed joined SummerHill in September 2007 – just after the credit crunch really walloped the already-foundering real estate market.

“My timing could be considered either impeccable or unfortunate,” he said dryly.

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He sees his role as guiding the company through the turbulence and positioning it to emerge strong amid a shrunken field of competitors.

While the entire real estate market is reeling from the foreclosure crisis, plunging home prices, drastically tightened lending and this year's Wall Street meltdowns, home builders are among the most affected.

"It's been a brutal year for new home builders, especially for private builders," said Patrick Duffy, principal of consulting firm Metro Intelligence Real Estate Advisors in Los Angeles. That's because private builders rely heavily on bank financing, which has been effectively shut off in recent months, he said. Public firms have more options, such as lines of credit and selling stock.

The industry's own trade group, the California Building Industry Association, said home building is in "dire straits." The pace of home sales in October, for instance, was "extraordinarily bad," it said, down 63 percent from a year earlier. New-home starts have plunged to record lows. CBIA projects that only 66,000 new homes and condos will be built in California this year, compared with 160,500 in 2006.

Duffy said SummerHill's saving grace likely is that it's owned by Marcus & Millichap, a national real estate investment brokerage from Encino (Los Angeles County.) "I would think having Marcus and Millichap behind them would be analogous to having a public company behind them," he said. "That leverage probably helps."

Freed doesn't mince words when talking about the obstacles.

"This is definitely the most challenging and most severe downturn I've experienced," he said. "It gets tougher and tougher to secure financing. Revenues are clearly down. Absorption rates-the rate at which one sells-are clearly down. There are fewer buyers, and they're looking for what they perceive to be bargains at the expense of the seller. It's like daily hand-to-hand combat."

Like most of its competitors, SummerHill has had to reduce staff significantly, shrinking from about 125 positions to 80. At the same time, "We've taken the opportunity to hire some very senior people who became available to us because of the downturn," Freed said.



every moment counts

In another move to be rebound once the market turns around, “We’ve made a conscious decision to maintain staffing levels in land acquisition and forward planning”-obtaining government approval, for instance.

The homes now in the sales pipeline are part of the projects initiated in 2005 and 2006. “They have very little profit,” Freed said. “We’re trying to recapture any equity left in the deals to generate cash, reduce our debt and position the company with leaner balance sheet as we move forward.”

He’s not optimistic about the \$700 billion bailout loosening banks’ purse-strings any time soon.

“I think 2009 will be difficult time for firms such as ourselves to close on properties where the closings need to be financed with bank debt,” he said.

His workaround? “ To look at controlling a few good properties in 2009 where the close of escrow is not calendared until 2010 and beyond.”

The development timeline is so long, with so many months of city and environmental permits, that that kind of planning is necessary anyway.

The one exception would be if “distressed assets” come on the market. In that case, SummerHill would try to snap them up-and he thinks the financing would be available.

“The money sitting on the sidelines in residential real estate is waiting for distressed sales where there is more profit.” He said.

Freed has some thoughts about steps the government could take to address the housing market and economy.

In assessing how to tackle the foreclosure crisis, he thinks it’s important to distinguish people who bought homes they simply cannot afford, and those who can continue to make payments but are discouraged because their home values have declined. For the former group, “we have to recognize that we can’t save their homes.” He thinks facilitating the foreclosure process

through a simple way for them to sign over their home, perhaps in exchanging for renting it for 12 to 18 months, make sense.

For the latter group “ those people who made good decisions” but now own homes worth less than their mortgages, he thinks the government could give them a tax credit for the next five years to facilitate their staying in their homes and keeping current on their mortgage.

Like virtually everyone in the building and real estate industry, he thinks lower mortgage rates will help revive sales.

“What will clean up the housing mess more quickly than anything is affordability,” he said. “When these homes become more affordable because of lower interest rates and decreases in value, that’s where we will find the bottom. People will buy houses because they can see they can afford them.”