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A Developer Outwitting the Slump

The careening market has forced Related to rethink how to sell—and finance—its buildings

Ross: With $1.4 billion in fresh capital, he can fund an ambitious lineup of projects

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By Christopher Palmeri

As the mortgage industry was melting down last year, real estate mogul Stephen M. Ross lay awake in his 8,200-square-foot condo overlooking New York's Central Park pondering his next moves. He kept thinking about a shrewd deal his late uncle, gas station magnate Max M. Fisher, cut with Marathon Oil in the Great Depression to lock in a source of petrol. When supplies later shrunk, Fisher prospered, with plenty of gas for his pumps. "I applied that to our business," Ross says. "They ran on crude; we run on money."

These days money is tight in real estate. But Ross cannily has managed to find a long-term supply of cash. On Dec. 17 his real estate development and management firm Related Cos. secured $1.4 billion from five prominent investors, including Michael Dell, Goldman Sachs, and the government of Abu Dhabi—Related's first outside investment. He'll use that cash to fund what may be the most ambitious lineup of new construction projects in the country, $9 billion worth of giant condo, hotel, and retail towers he's building from New York to Los Angeles. "You have to look to the future," says Ross. "But make sure you can survive the present."

With that funding, Ross is confident he can bob and weave his way through the challenging real estate terrain. As necessary, he can retool his marketing tactics and even his building designs to attract buyers. He's also better positioned for the tough financing environment. Many banks now want developers to cough up more money for projects up front. And few banks are willing to back a project on their own, so developers must scramble to find multiple financiers.

Ross seems unfazed, despite having some of the biggest projects in the U.S. He's building a $3 billion village at the base of the Snowmass ski area in Colorado. Related also has teamed up with Vornado Realty Trust on the expansive redevelopment of New York's Pennsylvania Station, including Madison Square Garden and the Farley Post Office.

The 66-year-old started far from Gotham's gilded towers, building low-income housing. His first project in 1972 was a $3 million, 150-unit apartment complex in Rhode Island. Ross rose to world prominence in 2004 with the Time Warner Center, a $1.7 billion office, hotel, mall, and residential complex on New York's Columbus Circle—a trophy project that helped make him one of the biggest developers of mixed commercial-residential projects.

TOUGH CONDITIONS

Ross had plenty of doubters in that case. For one thing, financing for the project was hard to find. After every major bank in the city turned him down, Ross got a loan from General Motors' financing arm.

Then the condos, a critical part of the plan, went on sale three weeks before the 2001 terrorist attacks. So Ross refinanced the project, bringing in $360 million in new money from private equity investor MacFarlane Partners. That deal lowered his interest payments, giving him more breathing room. "The Time Warner Center looks like a no-brainer now," says Victor B. MacFarlane of MacFarlane Partners. "But it was a difficult time."

It's not unlike the problems he faces today. At the peak of the boom in 2004 Related paid $120 million for the struggling St. Regis Hotel in L.A.'s Century City neighborhood. Ross planned to turn the building into condos. But he decided he could get a higher price by tearing down the hotel and building a new high-rise. As a result, his costs have swelled to $1,000 a square foot. So, in one of the weakest housing markets ever, Related must sell the new condos at near-record highs for the city in order for Ross to recoup his costs and make a decent profit. (The asking price for the penthouses is $30 million.)

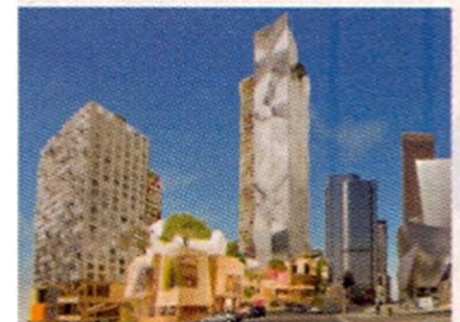
There's no turning back on these monoliths. That means Ross has had to find creative ways to attract buyers. With the dollar falling, for example, he's shopping properties overseas. His salespeople will trek to London this year to pitch prospects on the L.A. tower.

Ross also is ripping up business plans for some properties. At Snowmass, Related has asked for permission from local officials to sell fractional interests to multiple buyers rather than one condo to a single person. Ross hopes that will make the condos more affordable: Eight shares go for $300,000 each, compared with millions for an entire condo.

Ross's cash cushion is also allowing for some opportunistic buying. In South Florida, where he and partner Jorge M. Perez are prominent condo builders, prices are plunging, and buyers are walking away from their down payments. So Ross and Perez, who think the market is undervalued, are buying up competitors' condos—if they can get them for less than the cost of new construction, or roughly $500 a square foot. Says Thomas J. Barrack, chairman of Colony Capital, a large real estate investment fund: "[Ross] is courageous in the face of fear." |BW|

BUILDING A PRIZE PORTFOLIO

Mega-developer Stephen Ross tweaks his strategy depending on the market



The Grand Avenue Project

Los Angeles, $2.6 billion

The Frank Gehry-designed complex will be built in three stages. That way Related can lock in land costs up front but has to pay for only one parcel now.

The Clarendon

Boston, $275 million

The 285-unit complex, designed by architect Robert A.M. Stern, will have condos on the upper floors and rental units below—giving Related a source of income even if condo sales are slow.

Icon Vallarta

Puerto Vallarta, Mexico, $200 million

Ross and partner Jorge Perez are marketing the Philippe Starck-designed condos as second or third homes to owners in their South Florida buildings.