



Orange County Taxpayers Association

25 Orchard, Lake Forest, CA 92630
phone (949) 768-8131 • fax (949) 768-1601 • www.octax.org

This article, featuring OCTax Member Lennar Corporation, appeared in the Orange County Register.

For Developer, California Dream Is a Reality by Robbie Whelan

In the latest sign that financing is starting to trickle back into California's property market, a group of investors is pumping cash into a huge, but stalled, \$1.4 billion master-planned community being developed on the site of a former military base.

Under terms of the investment, Boston-based State Street Bank & Trust Co., a unit of State Street Corp., and a group of investors that includes several private-equity funds and pension funds will provide \$400 million in cash and credit to the project, called Heritage Fields at El Toro. The project, in Irvine, Calif., is being developed by Five Point Communities Inc., a company that is majority-owned by home builder Lennar Corp.

The transaction represents a significant step forward for Five Point, which like other developers has struggled to find financing for horizontal development, or the work that goes into building roads, sewers and other infrastructure that needs to be laid before homes and commercial buildings can be built.

By the end of 2010, the company had invested more than \$1.3 billion in the project, and needed at least \$400 million to get the development moving again. Emile Haddad, Five Point's chief executive and controlling partner, said construction of the first homes should begin in 2012.

The transaction also shows how nontraditional sources of capital are starting to migrate into California's housing market, one of the few markets in the country that is showing pockets of strength. Hedge funds, in particular, have emerged as a go-to source for the financing of land ventures.

"If you look at the folks in the housing industry who are actually putting construction dollars back to work for horizontal and vertical development, you can count them on one hand," said Tom Reimers, a Southern California land broker with Land Advisors Inc. "We're going to need private equity to move things along. It's new blood, new money."

Heritage Fields at El Toro calls for 5,000 new homes, 5.2 million square feet of commercial space and a public park twice the size of New York's Central Park. The development is being built on the site of a former naval air base in Orange County, which once was used by President Richard M. Nixon, who often flew on Air Force One to his home in nearby San Clemente.

(more)

Lennar purchased El Toro from the Navy at the height of the housing boom in 2005, borrowing \$775 million from Lehman Brothers Holdings Inc. to finance the purchase of the land. Lennar added about \$700 million more in equity from its own funds and from investors, including two affiliates of private-equity company Cerberus Capital Management LP, investment firm Rockpoint Group LLC, and computer tycoon Michael Dell's MSD Capital LP.

Under a separate agreement, Lennar will buy out Cerberus's stake in the project, although Mr. Haddad declined to provide details on the stake. "This is definitely one of the most complicated deals I've ever worked on," Mr. Haddad said.

An overleveraged Lehman, burdened by a number of huge commercial real-estate investments like the El Toro project, filed for bankruptcy protection in September 2008. In December 2010, a federal bankruptcy judge in New York approved the sale of the \$775 million Heritage Fields mortgage note to State Street for \$153 million.

After what Mr. Haddad described as several months spent crisscrossing the country for meetings in Boston, New York and California, Five Point closed on the restructuring deal two days before New Year's Eve. State Street agreed to reduce the outstanding debt balance on the deal to \$210 million, then gave the developers a \$180 million line of credit to complete land development.

By putting more money into the deal, State Street is taking a big bet that Mr. Haddad can get the project up and running in short order, and start producing strong cash flows from selling home sites and land for commercial buildings to builders, who will then construct and build homes and office and retail properties.

But the project isn't a slam dunk. The economy remains weak and while the California housing market has improved, it isn't clear that the market can support such a project.

"Everyone is talking about residential land deals as if they are all the same. My view on this is simple. Not all deals are the same. Not all locations are the same. And not all management is the same," Mr. Haddad said. "This is the right deal, in the right location."

Mr. Reimers, the Irvine land broker, said the Irvine area is expanding. Several companies have located in and around the nearby Irvine Spectrum commercial center, including drug-maker [Allergan Inc.](#), computer company [Western Digital Corp.](#) and the University of California, Irvine, providing jobs.

"Putting a significant amount of money to work in an Irvine master-planned community is probably as low risk as you can go," he said.