

## Endeavor rides out the downturn

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At 1.6 million feet of retail space, Southpark Meadows is Endeavor Real Estate Group's largest development to date. Although Endeavor has a long record of retail development in Central Texas, the Austin firm now has a 'very conservative' view of speculative projects, one executive says.

Four years ago, Austin-based Endeavor Real Estate Group was the leading developer of shopping centers across Central Texas, the power behind nine projects that had added 4.5 million square feet of retail space during the past decade.

By late 2007, the U.S. residential mortgage market had melted down, and the housing market had cratered. The global downturn deepened during 2008 and 2009. Credit shrank dramatically, along with demand for retail and other projects. Speculative commercial development came to a near halt locally and nationally.

Endeavor mothballed plans for large retail centers in Bastrop and in the Manor area. It delayed two proposed office projects and postponed the retail phase at its 170-acre Domain development in North Austin.

From its offices on the 13th floor of Chase Tower downtown, the Endeavor team watched the economy turn from bad to worse.

"You're programmed as a real estate developer to always be looking for the next deal, the next opportunity," said Chris Ellis, 43, a managing principal who joined the firm in 2001, two years after it was formed. "And we all had to reprogram ourselves to be patient, because there have been no deals."

But Endeavor had a strategy to survive the downturn and to grow its business. In doing so, it has ventured into new territory.

Since September, the firm has participated in a federal lending program designed to restore credit and liquidity to the commercial mortgage-backed securities bond market, which is collateralized with loans on hotels, office, apartment, retail and industrial buildings, and other types of commercial real estate. Endeavor and its investors have bought more than \$600 million worth of the securities. Most of those purchases were financed by the Federal Reserve Bank of New York under the Term Asset-Backed Securities Loan Facility program, or TALF, which provides loans for financing up to 85 percent of the price.

Andy Pastor, an Endeavor co-founder and managing principal, said Endeavor and its investors in the bonds are expecting percentage returns in the mid-teens.

When the federal financing ends this month, Endeavor, using other financing sources, will continue buying the bonds "to the extent they remain compelling investments," Pastor said.

"We view this as an ongoing long-term investment for Endeavor," said Pastor, 48.

In addition, Endeavor is raising money from outside investors for potential real estate acquisitions in Central Texas, should opportunities arise to buy undervalued properties. To date, however, none have been identified, Ellis and Pastor said.

Pastor said the real estate and securities funds were seeded with Endeavor money, with other money coming from investors, including high net worth individuals, family foundations and to a lesser degree, smaller institutional investors and private pension funds.

Pastor said more than \$30 million has been raised for the real estate fund in the past 90 days toward an eventual goal of more than \$100 million.

### **Standing apart in several respects**

Those aren't the only changes Endeavor has made. Instead of building its own projects, Endeavor is now developing them for third parties.

The firm recently was tapped to build a 500,000-square-foot shopping center at Fort Sam Houston in San Antonio for the Army and Air Force Exchange Service, which oversees retail and restaurant operations at military facilities. That is Endeavor's first major new retail project in several years. In the private sector, Endeavor will develop a 6,800-square-foot auto repair center for Lamb's Automotive in Round Rock.

Endeavor is well-capitalized and diversified, and didn't overextend itself during the recession, its bankers say, noting that the company hasn't defaulted on any loans.

"We were conservative in the amount of debt we put on our properties and in the amount of speculative construction we undertook," Pastor said. "And we were lucky that we didn't start a couple of our projects that we had under pursuit."

At a time when many in the real estate industry are struggling, "these guys aren't," said Brian Tuerff, a senior vice president in Austin with BBVA Compass, which has been Endeavor's lead lender for 10 years.

"They're very visionary," Tuerff said. "They don't react to the news; they create the news. They're always looking out on the horizon; they're not looking in the rearview mirror."

Even on a national scale, Endeavor is "fairly unique" in its TALF participation because the company is a developer, "whereas most of the firms doing the same thing are institutions or big investment managers," said Ben Thypin, senior market analyst with Real Capital Analytics Inc., a commercial real estate research firm based in New York.

The program only applies to triple A-rated securities, the highest quality bonds.

"It's a pretty conservative strategy, especially compared to the development work they typically do, which can be more lucrative but is not viable in this market," Thypin said. "It's an opportunity to invest in the commercial real estate market and generate stable returns without the risk of developing or owning properties."



Principals and managing partners of Endeavor Real Estate Group: from left, Jamil Alam, Chris Ellis, Billy Osherow, Kirk Rudy, Brian Lent, Charlie Northington, Becky Heston, Chad Marsh, David Roche, David Robert, Andy Pastor, Bryce Miller and Jeff Newberg. They are outside Endeavor's development at the Domain in North Austin, where the firm decided to postpone a retail project.

### **Make right call at right time**

Endeavor was founded in 1999 by five Trammell Crow veterans: Pastor, Kirk Rudy, Jeff Newberg, David Roche and Bryce Miller. The company expanded during Austin's growth spurt in the following decade, planting retail projects across the region. To date, Southpark Meadows is the largest, with 1.6 million square feet of stores.

In 2003, Endeavor announced plans for the Domain, a high-end outdoor shopping center with apartments in North Austin. Simon Property Group later became a partner and now owns the project.

In 2005, Endeavor announced that it and a partner were buying the adjacent 175 acres at the Domain, envisioning shops, hotels, offices and housing and stores. Endeavor later announced a lineup of major retailers, including Whole Foods Market Inc., Saks Fifth Avenue and the region's second Nordstrom.

But as the recession worsened, Endeavor hunkered down on the development side. Along with canceling the Bastrop and Manor projects, Endeavor put on hold plans for office projects in Rollingwood and Northwest Austin. Endeavor also has pushed back the retail phase at the Domain.

"Walking away from projects," Ellis said, "is part of the business. You've got to make the right call at the right time."

At the Domain, "the worst thing in hindsight would have been to plow forward, because we wouldn't have leased up the project and it would have been saddled with huge debts and no way to lease it up," Ellis said.

Endeavor has continued to build during the downturn, Pastor said — retail buildings are under way at University Oaks in Round Rock and at 1890 ranch in Cedar Park — but he added that the firm has remained "very conservative" on speculative retail construction.

Endeavor has sold several of its retail projects in recent years. Ellis said the company has been fortunate to have its four remaining shopping centers performing well, with strong anchor tenants it didn't lose during the downturn.

Besides reining in development, Endeavor made other moves internally.

It increased staffing for its service business, which entails leasing and managing a portfolio of more than 5 million square feet of retail, office and industrial space in Central Texas and San Antonio.

Among the firm's own projects, Endeavor's retail leasing team, led by Billy Osherow and Brian Lent, brought its centers to 95 percent leased "in the worst retail environment in the last 20 years," Ellis said.

Endeavor's office division signed two large leases, including the largest local deal of 2009, the OneWest Bank lease that filled Endeavor's 174,000-square-foot Domain Gateway building.

Endeavor also downsized its staff from 122 in 2007 to its current 68. More than half of the departures were through attrition, Ellis said.

"With revenues down, and revenue opportunities down, we've had to make some very difficult decisions," Ellis said.

### **Waiting for upturn, bargains**

Other developers also have had to adjust to the new realities.

"We have all had to retrench and refocus, but that is a healthy exercise," said Beau Armstrong, CEO of Austin-based Stratus Properties Inc., developer of the W Austin Hotel & Residences under construction downtown. "Real estate is a cyclical business, and we are currently moving through the most difficult part. It's certainly not as much fun as it was three or four years ago, but you have to learn to take the good with the bad. When it looks the worst, it's probably the best time to invest."

Stratus, like Endeavor, has been looking for potential acquisitions.

Armstrong said Stratus has "evaluated a limited number of new opportunities but, quite frankly, we have not seen the volume of distressed situations that were widely expected by most experts in our business."

Ellis said that starting last year, there's been a "major influx" of commercial investors, including private individuals, pension funds and insurance companies, looking for buying opportunities in the local market. The big unknown, he said, is whether there will be "huge bargains."

So far that hasn't been the case, Ellis said, as Central Texas "hasn't taken as much of a beating" as many other places. It remains to be seen whether the renewed investor interest will push prices up, he said.

There are, however, signs of an emerging upturn.

In December, Catellus Development Group sold the regional retail portion of its Mueller development in Northeast Austin to Phoenix-based Cole Real Estate Investments. The sale price wasn't disclosed.

Ellis said that sale marked "the first positive in the investment market we've seen in over two years."

On the development side, predictions vary on how long it might be before demand and the economy pick up. Ellis thinks it could be 12 to 18 months before retail and office demand return; it all depends on job growth.

Tuerff, with Compass, said it could be two or three more years before demand comes back to build new shopping centers.

Stratus' Armstrong said that, "considering the dearth of real estate financing, it is likely to be several years before we see any significant new construction. And when we do, it will be conservatively underwritten and heavily pre-leased or pre-sold."

As for whether and when Endeavor might revisit its Bastrop and other retail projects or set its sights on new ones in Central Texas, Ellis said the firm "will continue to monitor the whole market for any opportunities."

"But when or if they make sense," Ellis said, "is still up in the air."

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