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February 1, 2023

Karla Henderson
Community Development Director
City of Bloomington
1800 W. Old Shakopee Road
Bloomington, MN 55431

Re: Request for Extension of Final Development Plan
3700 American Boulevard East
Case PL202200055
Our File No. 41,912-00

Dear Ms. Henderson:

This firm represents Rosa Development Company, LLLP ("Rosa Development") with regard to this request to extend the approval of the Final Development Plans for the Rosa Apartments (the "Project") for property located at 3700 American Boulevard East. Please accept this letter as our client's formal request to extend the approval of Final Development Plans for the Project for one year.

Background

As you know, the global pandemic and has disrupted the supply chain for everything from furniture and fixtures, to building materials and steel. This disruption and the Fed's aggressive inflation fighting efforts have dramatically increased the cost price of the Project. As a result, the City Council approved new milestones for the Project at its meeting of August 8, 2022. However, the Final Development Plans could not be extended until the City Council acted on amendments to Section 21.501.03(f) of the City Code to provide administrative authority to do so based upon a finding that "the applicant is making a good faith effort to make progress on the final development plans." Those amendments were adopted by the City Council at its regular meeting of November 28, 2022.

To underscore our client's good faith efforts, Rosa Development has worked diligently with City staff to finalize its entitlements, construction plans and to apply for a building permit for the Project. This work included review of the final plat, title work, sidewalk and bikeway easements, and an application to vacate existing easements. The investment in these entitlements is substantial and would be lost without extension of the Final Development Plans. In this request, we make reference to our most recent financial profroma (provided to the Port Authority staff under a confidentiality agreement). That financing document was prepared for private lenders and the Port Authority before the Federal Reserve enacted a series of aggressive rate hikes, raising the federal funds rate from 0.5% to 4.5%. The returns under the proforma were below market prior to the rate hikes and financing projects has only gotten more difficult. (I have included a couple of recent articles which highlight the uncertainty that interest rate hikes have created for financing markets.)

Request

With the submittal of this letter, Rosa Development hereby requests extension of the approval of the Final Development Plans for Project for one additional year to allow the Applicant to secure financing for Project, file the Plat and begin construction. The effect of your approval would be to extend the Final Development Plans for the Project from April 6, 2023 to April 6, 2024.

We are grateful for the assistance that City staff has provided under difficult and extraordinary circumstances. Please let me know if you have any questions.

Sincerely,

William C. Griffith, for
Larkin Hoffman
Direct Dial: 952-896-3290
Direct Fax: 952-842-1729
Email: wgriffith@larkinhoffman.com

Enclosure

cc: Kristin Muir
Glen Markegard, Planning Director

How the Fed’s Sixth Interest Rate Hike Will Impact CRE Development in 2023

northspyre.com/blog/how-the-feds-sixth-interest-rate-hike-will-impact-cre-development-in-2023

December 2, 2022
Written by: Northspyre
In early November, the Federal Reserve raised interest rates for the sixth time this year to curb soaring inflation. The interest rate for federal funds to 3.75 to 4%, its highest level in 14 years. The Fed indicated more rate hikes are coming in 2023. The government’s fiscal policy shift has significant implications for the commercial real estate market.

The biggest issue is capital becoming less available to developers. Mortgage loan terms have increased alongside interest rates, making the debt used to finance projects more expensive. Moreover, Moody’s Analytics found interest rates have eclipsed capitalization rates for many commercial properties for the first time since the 1980s.

While the Fed’s efforts to relieve inflationary pressure are generating headwinds for the entire industry, it’s also disrupting certain specific asset classes.

Here’s a closer look at how rising interest rates will shape the commercial real estate market of 2023.

The Negative Leverage Problem

When considering new projects, developers must calculate a property’s cap rate to find its long-term value. The formula divides a site's projected net operating income by its total cost. So, a project with a $15 million price tag that generates $750,000 in yearly net income has a 5% cap rate. Unfortunately, the recent interest rate spikes have exceeded predicted returns on over 30% of commercial mortgage-backed securities (CMBS) in Q3.

In commercial real estate, that condition is known as negative leverage.

Moody’s believes the surge in negative leverage CMBS loans will prompt a slowdown in commercial real estate lending and sales. The firm also predicts that the situation will drive property values down. It further notes that while the negative leverage problem affects all asset classes, it’s hitting the industrial (35.9%) and multifamily (30.8%) segments the hardest.

The analytics firm forecasts that the loan-to-value imbalance will continue expanding until the Fed successfully curbs inflation and normalizes interest rates.

The industrial property market has been due for a correction because of its rapid, unsustainable growth during COVID-19. The segment will bounce back as e-commerce providers and retailers need warehouses to sustain their operations. But recession anxiety means that consumer purchasing won't drive the market's revival in the near term.

The big takeaway for developers is their project planning needs to account for the market's increasing volatility. Many opportunities that might have been sure things in the summer now carry significant risk. In the current landscape, project teams would be best served by pursuing deals that involve recession-resistant property types.

As for the multifamily segment, the situation is ... complicated

Multi-Family Segment Faces Uncertainty

In a recent post, J.P. Morgan Chase offered some meaningful insights regarding the immediate future of multifamily properties.

First, the bank noted that demand for affordable housing greatly surpasses available inventory. It also pointed out that Americans are migrating to the center of the U.S. to escape the higher cost of living on the coasts. And it highlighted the growing need for workforce housing, homes for families and young professionals that earn too much to qualify for affordable housing but don't earn enough to buy luxury properties.

The undersupply of affordable and workforce housing in America represents an obvious opportunity for real estate developers. However, the multifamily segment has significant risks in the current economic environment.

The most prominent issue is that high-interest rates mean less favorable lending terms for potential tenants.

ATTOM, a real estate data provider, reported a 47% year-over-year decline in mortgage origination in Q3 2022. Refinancing activity also fell by 68% during the same period. Rick Sharga, ATTOM's EVP of market intelligence, said the combination of high home prices and "unprecedented jump" rates had priced many consumers out of homebuying.

Until conditions improve, launching a successful multifamily project will be tricky. J.P. Morgan recommends carefully examining the particulars of a local market before investing time and resources in new apartment complexes or housing developments. A comprehensive view of a major American city's local real estate development dynamics is essential to a project's success.

That said, finding actionable, meaningful insights about the real estate market can be a challenge. A good best practice is to cultivate sources with proven track records and industry experience. It's also valuable to have a good mix of national trend reporting and regional development happenings to gain a proper 30,000-foot perspective on the market.

Check out Northspyre's library of project delivery resources made specifically for real estate developers and owner's reps to help bring projects in on time and under budget.

Healthcare is Doing Well Despite Multiple Challenges

Because of strong nationwide demand, medical and healthcare facilities are effectively recession-proof property types. Even with soaring interest rates, JLL anticipates the segment will post record sales this year, as transactions totaled $9.2 billion in the first half. However, the Fed's efforts to reduce inflation have negatively impacted parts of the commercial real estate market.

JLL noted the healthcare industry is still grappling with the ongoing effects of the coronavirus pandemic. Declining patient volumes, staffing shortages, and the payer mix becoming dominated by low-reimbursement government healthcare programs have prompted many medical providers to enter cost-cutting mode. Since real estate accounts for up to 40% of hospital and healthcare systems' costs, making changes to reduce that burden – like lease restructurings and portfolio overhauls – is seemingly inevitable.

In addition, Bisnow recently published an article explaining that capital becoming more difficult to acquire is hurting smaller medical service providers. Following the outbreak of COVID-19, specialists have sought to upgrade their facilities to serve their patients better, but debt is increasingly expensive, and limited inventory has exacerbated the problem. Developers have investigated converting traditional office space into healthcare facilities, but the requirements for certain features like fireproof structures have made that option exceedingly expensive.

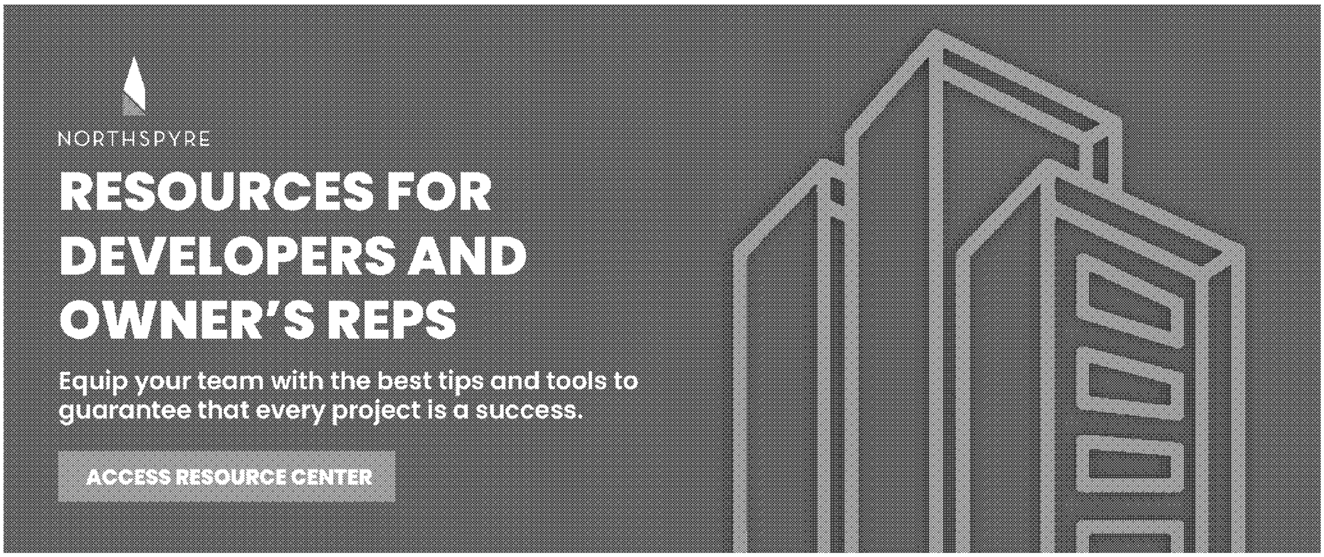
Although financing challenges are a nationwide problem, new opportunities are emerging within the segment.

Trask Leonard, CEO of Bayside Realty Partners, has seen growth in smaller leases for discretionary medical providers. He believes plastic surgeons, fertility clinics, and behavioral health facilities will occupy a more significant position in the marketplace. Similarly, Unity Medical Properties CEO David Lynn noted his organization successfully financing its projects with the help of local banks.

The Fed's recent and future interest rate hikes will create challenges and opportunities for real estate developers. Firms will need to tap robust data resources to create bulletproof proposals for institutional lenders. And project teams must harness modern technological resources to keep their projects on track in a demanding environment.

Ultimately, commercial real estate's strong fundamentals mean that companies can achieve meaningful growth in 2023, but only those that take a forward-thinking approach.

Interested in getting an edge on the market amid unprecedented economic uncertainty? Check out our Resource Center to download reports, whitepapers, eBooks, and infographics that can help outpace the competition.



Tag(s): Real Estate Development

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Commercial Property Executive
(https://www commercialsearch com/news/)

Another Interest Rate Hike: What's Ahead for CRE

By Jordana Rothberg
(https://www.commercialsearch.com/news/author/jordanarothberg/)

December 13, 2022

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Industry experts weigh in on how the Fed's move will affect markets in 2023.

Image by mohamad_hassan via pixabay.com

The consensus was correct: **The Federal Reserve** has again raised interest rates. The most recent increase was smaller than the previous four consecutive meetings that resulted in a jump of three-quarters of a percentage point (https://www.commercialsearch.com/news/cre-braces-for-interest-rate-hike-no-6/).

Wednesday's meeting went as predicted, resulting in a short-term interest rate raise by half a percentage point, bringing the federal funds rate to a range of 4.25 percent to 4.5 percent. This is the highest range seen since 2007.

The decision of how much to raise rates was a reflection on the latest data on the Consumer Price Index, including wage growth, consumer goods pricing, consumer demand, housing prices and shipping costs. Fed Chair Jerome Powell also said in past meetings the Fed's decision is impacted by the tightness in the labor market.

READ ALSO: How a Looming Recession Impacts CRE Deals (https://www.commercialsearch.com/news/how-a-looming-recession-impacts-cre-deals/?utm_source=WhatCountsEmail&utm_medium=CPE%20Daily&utm_campaign=NEW%20CPE%20Daily)

Experts agreed that the Fed would raise rates by 50 basis points this week. Inflation remains higher than the central bank's goal, indicating this raise will likely not be last. Powell said in his Wednesday speech that he anticipates ongoing increases in rates.

CRE economic slowdown

As real estate lenders and developers adapt to the new environment, deals and transactions (https://www.commercialsearch.com/news/how-deals-will-fare-in-2023-pwc/) are slowing across most major markets. Uncertainty about how high rates will go and the impact on the economy makes it difficult to assess property values.

"The slowdown in CRE is already being felt in all segments of the market," said Shlomi Ronen, Managing [redacted]pal at **Dekel Capital** in Los Angeles. "The big question is how long will it last and if there's a potential [redacted]me easing of monetary policy from the Fed sometime next year."

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Jon Fhima, CEO of **F2**, noted that even with a lower interest rate hike, such as 50 basis points, the general market and developer sentiment will likely not get development back to pre-COVID level activity. "Developers still seem skittish to put shovels in the ground," said Fhima. "Construction costs coupled with interest rates are still a little too high to palate."

Until a sense of "normalcy" is returned to the market, CRE must navigate the uncertain future with the information given on the current economy. While certain deals are still actionable, some asset classes and property types are feeling the pressure more than others.

"Rate hikes make deals harder to get done, especially with the uncertainty with retail and office markets," said Marc Norman, Associate Dean, **NYU School of Professional Studies, Schack Institute of Real Estate.** "That said, as rates increase, alternative lenders and investors' capital becomes more competitive and more flexible."

Financing in the foreseeable future

The rate hikes are roiling the commercial mortgage market. Rising rates increase the cost of debt for borrowers, while banks worry about how rising rates affect the value of their portfolios.

"Banks must be careful writing loans in a rising rate environment," Paul Fiorilla, Director of Research for **Yardi Matrix** said. "Portfolio lenders worry that the value of the loans on their books will decline, plus higher rates could make the take-out of the loan more difficult. For CMBS and CLO issuers (https://www.commercialsearch.com/news/2022-cmbs-delinquency-rate/) the problem is more acute. Although they hedge, their book loses value when rates increase between the time loans are originated and sold."

According to Fiorilla, because the rates only went up slightly this week and may continue suit in following rate hikes, the impact on the market will be relatively small. However, should the Fed raise by another 100 basis points, lending will be discouraged as originators will have to be more conservative because they will reduce leverage and ensure debt service is sound.

Rate hikes not only impacts the future of deals in CRE due to the difficultly that may stem from trying to find financing, but also affect existing funding already in play.

"Existing loans with maturities or resets in 2023 and 2024 will feel the brunt of the rate increases and likely struggle for new financing given the triple whammy of higher rates, higher expenses and higher vacancies," said Norman.

As the outcome of this rate hike was an increase by 50 basis points, Fhima believes general investor sentiment should be positive, as the message conveyed is that inflation is slowing. "The hope is that we'll begin to see far greater volume and liquidity in the marketplace considering it has drastically slowed down over the last six months," said Fhima.

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