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DAILY BUSINESS REVIEW

SPECIAL REPORT Business Advisory Board



IN SEARCH OF CERTAINTY

Our experts weigh in on federal budget cuts, an improving but still tough lending climate, Latin America's growing influence, and why schools are failing to prepare students for a 21st century economy.

By Paola Iuspa-Abbott

THE PANELISTS (FROM LEFT)

Thomas Lehman: Founding partner, Levine Kellogg Lehman Schneider + Grossman

Francisco Cerezo: Partner, Foley & Lardner

Vanessa Grout: President and CEO, Douglas Elliman Florida

Bruce Foerster: Founder, president, South Beach Capital Partners

Jim Kaufman: CEO and co-founder, Kaufman Rossin

Michael Maxwell: Real estate program director, Huizenga School of Entrepreneurship, Nova Southeastern University

Scott Baena: Partner, Bilzin Sumberg Baena Price & Axelrod

Antonio Villamil: Dean, St. Thomas University School of Business

Richard Dailey: President and CEO, Apollo Bank



While forced cuts to the federal budget are contributing to an uncertain economic climate, participants in the Daily Business Review's quarterly Business Advisory Board panel are far from panicking.

They noted some businesses put hiring on hold, but others could benefit from an increase in public-private partnerships resulting from sequestration.

Just as important to the panelists: the availability of capital for business expansion, Latin America's growing influence

on our economy and the real estate industry, education and the health of South Florida law firms.

Banks have started to loosen their business lending to real estate developers and others that once had easy access to capital. The experts say lenders and customers are still grappling with the Dodd-Frank Act passed in the wake of upheaval in the financial markets.

Our experts also say many companies with jobs to fill struggle to find qualified workers. Many lack skills to survive in a

high-tech economy. Educators, they said, need to rethink how they prepare students for the work force. They also urged vocational schools to play a larger role in turning out workers who aren't interested in a college degree.

Meanwhile, many South Florida law firms are experiencing "a cultural shift" by hiring contract workers. The firms save money because the pay scale is lower, and they don't have to provide benefits.

ECONOMY

Federal budget cuts cloud outlook, but sky isn't falling

Sequestration is creating economic uncertainty, but no one's ready to panic over the mandated federal budget cuts yet.

Still, "I am concerned about how the sequester could affect the unemployment rate here," Francisco Cerezo said.

Other panelists were more upbeat. Sequestration could have a positive side. Since the federal government has less money to spend on infrastructure upgrades, it might choose to partner with the private sector to create more private-public partnerships, Scott Baena said.

"They proliferate when government isn't able to spend money," he said.

Entering the second quarter, the region's employment data are giving mixed signals.

In Miami-Dade, the unemployment rate in February was 9.4 percent compared with 9.2 percent a year earlier, the state Department of Economic Opportunity reported.

Broward County's jobless rate was 6.2 percent in February versus 7.8 percent in February 2012. Palm Beach County reported a 7.4 percent rate, down from 9.1 percent a year before.

Overall, Florida had an unemployment rate of 7.5 percent in February, slightly better than the national rate of 7.7

percent. The national rate for March dropped to 7.6 percent, the lowest in four years.

Some businesses haven't yet been impacted by sequester cuts. In fact, many are growing.

"By and large, our clients are expanding and feeling more optimistic," said Jim Kaufman, whose company bills about \$80 million in services in accounting and related fields, mostly in South Florida. "We added 60 jobs in South Florida in the last 12 months."

Vanessa Grout agreed some companies are expanding but said more companies could grow more quickly but for two

pressing challenges: one is finding talent.

"The other issue is being able to pay them because there are all these associated carrying cost with having employees that we can't seem to forecast right now accurately," she said. "There is a lot of uncertainty, and I don't know how to solve that."

Grout's concerns are based on the impacts tax policy, regulation and health care will have on employers.

Grout's company, which employs 35 full-timers, has put hiring on hold and is trying to maximize productivity until the cost of hiring new people becomes clearer.

EDUCATION

Schools need to rethink mission in a high-tech world

Unemployment is declining modestly but doing little to help the recovery. Part of the problem: Many workers lack skills needed to survive in the 21st century economy.

Echoing a consensus of his Business Advisory Board members, Antonio Villamil said the need for talent is critical.

"There is a mismatch between the needs in technology and knowledge-based economy and the pool of labor," he said. "In banking, we are fighting to get additional credit officers," and lenders often are forced to hire people away from competitors.

The best way to reduce unemployment is for high schools, colleges and universities to start teaching trades and offering programs that match the skills employers want, Michael Maxwell said.

Welders and mechanics are paid well and don't require a lot of training, he said. Yet, that training is rarely available to people who aren't in-

terested in a college degree.

Thomas Lehman, whose family owns car dealerships, said hiring and keeping good auto mechanics with the level of training required before "a mechanic can open the hood of a car" is very competitive and difficult.

The key to a better economy is when employment and education are in sync, Scott Baena said.

Bruce Foerster said government should redirect funds going to unemployment claims into education subsidies to retrain jobless people in areas of high demand.

"If we are going to throw money, let's just be creative," he said.

But creativity may be limited to visionary entrepreneurs in the private sector.

That's the case of Miami restaurateur John Kunkel, who founded and sold Lime Fresh Mexican Grill. He now owns Yardbird Southern Table & Bar and Khong River House

in Miami Beach. He isn't waiting for anybody to provide technical training to his kitchen workers. He is doing it himself, Lehman said.

"He is setting up a test kitchen, a laboratory on 60th Street and Biscayne Boulevard," he said. "He is doing it on his own nickel. He needs talented people, trained people. He doesn't need people with a college degree."

Jim Kaufman agreed. He said his accounting firm launched Kaufman Rossin University to retrain graduates in accounting and finance "to understand the aspect of the business they are in."

"Universities are not producing a business graduate capable of entering a professional firm and being effective without more training," he said.

Baena said law schools also are deficient in preparing law students for legal work. When a firm is looking to hire, one of the things it looks for is

someone with a book of business. Yet law schools aren't teaching students how to look for clients.

Law school "doesn't tell you 'you actually have to find the client,'" he said. "Everybody assumes there is a client. But productivity is not just doing well for the client. It is doing really well for the firm, too."

The solution would be for colleges to adapt their curricula to meet the demands of the labor market. But that solution won't be easy to achieve, Villamil said.

Schools can't change their curricula without the approval of accrediting agencies.

"The key is to teach them verbal skills, written skills, critical thinking and the ability to use technology to mine data," Villamil said. "But you have a very rigid [accreditation] approach at all levels that prohibits innovation."

More banks return to lending — even for residential

As the economy strengthens and property values rise, some South Florida banks are boosting their lending and resuming construction loans. That was unheard of less than a year ago.

Richard Dailey said more lenders are getting into residential lending even though they prefer commercial deals. That's because regulators limit how much a bank can lend in a particular sector.

"A bank's capital determines how much one can lend in commercial real estate, so now they are turning to residential lending," he said.

But most residential lending has become more challenging since the financial collapse of 2008. The passage of the Dodd-Frank Act made it tougher to obtain residential financing. Some lenders don't want to invest the time and resources to make loans.

"Some banks are saying we are not going to touch it. ... It is too complicated," Dailey said.

His bank is financing construction of homes, small hotels and just provided funding to a restaurant group, he said.

"But we are taking the time trying to understand a borrower's business," he added. "We are giving 75 percent financing and doing loans in certain situations where there is no recourse on new construction. It all depends on the borrower, the project and the circumstances."

Mercantil Commercebank is lending, said Antonio Villamil, who is on the bank's board.

Michael Maxwell, who sits on a Regions Bank advisory board, said the bank is lending as well.

"Our business is doing really well," he added. "We are one of the few banks in that area that will actually finance your custom-made home."

In its recent Beige Book report on the economy, the Federal Reserve said access to construction financing remained mostly tight in the region that includes Florida. The outlook for construction activity and new-home sales over the next several months is positive, the Fed said.

Scott Baena said his law firm recently helped close the largest construction loan since the housing crisis. The \$160

million loan will help build the Mansions of Acqualina, a Sunny Isles Beach condo project. Baena's firm represented the Trump Group led by Williams Island developers Eddie and Jules Trump. The syndicated loan was led by Regions Bank. Other participants were SunTrust Bank, Mercantil Commercebank, Sabadell United Bank and Israel Discount Bank of New York.

He said the lenders were not as interested in the value of the collateral compared with underwriting during the housing boom, but rather in the character of the borrower.

"It was clearly a loan that was made on the quality of the sponsorship, not on the collateral value," he said.

Small real estate investors have a hard time getting acceptable financing to develop or buy properties, said Maxwell, who is part of a private investment group. He said the loan-to-value and loan-to-construction cost ratios are working against domestic investors and in favor of foreign investors paying cash.

"It is so difficult," he said.

"The LTV and LTC are unsustainable on an investment basis. It is really sad. I can't build anything right now. I am looking at income-producing properties, but the deals are not there. You can't make it work because we need more liquidity."

When it comes to lending to small business owners, the sector is a challenge, Dailey said.

"Often, small businesses lack capital, and it is very difficult to borrow if you don't have the right amount of capital," he said. "And if you try to finance that capital, it is bad for the business. That's one of the challenges I see for small business owners."

Accessing debt can be critical to businesses trying to reorganize and emerge from bankruptcy. Yet, they are finding that to be almost impossible. Thomas Lehman said.

Lenders, most likely, won't refinance an owner's exit from Chapter 11 but will finance a person to buy the business, he added.

"Nobody is putting money into an existing management with a troubled company," Lehman said.

BUSINESS OF LAW

In time of uncertainty, 'hedging' means controlling costs

The economy may be improving, but uncertainty about the speed of the recovery is impacting how law firms operate in South Florida.

One trend: Firms are increasingly turning to contract lawyers to do the jobs that associates used to do in the good old days. Firms save money because the pay scale is lower and they don't have to provide benefits.

"There has been a cultural shift in law firms," Scott Baena said. "This isn't true of outsourcing. We are bringing these people

in-house, but they are in an at-will relationship with the firm."

These lawyers "don't have the right to have an expectation" of becoming permanent, he said.

"It is the opportunistic approach that law firms are taking today," Baena said. "It is sort of hedging. ... [We're] not quite sure what the future brings."

Firms began hiring contract lawyers as law schools graduated more students than the industry could absorb.

"It is a buyer's market," Baena said of law firm hiring.

"We can't process the applications fast enough. There is an expectation, though, that that party will be over, too, because enrollment in law schools is really down."

Hedging seems to be the buzzword as law firms try to find ways to offset potential losses if the economy again goes south.

Francisco Cerezo said law firms continue to push more work onto legal assistants to cut costs.

Back in the day, there is used to be one assistant per attor-

ney, he said. That number has grown to one assistant for three attorneys, he said.

"Now there are some firms in Miami where they are going one to four and one firm is talking about one to five," he said.

Cerezo said technology is making that possible, but some firms may be going too far.

"At some point, something's got to give," he said. "You just can't keep piling it on ... and using technology as a way of hedging."

REAL ESTATE

Industry risks a return to boom-and-bust cycle

South Florida's condominium market is recovering, helped in a big way by hefty down payments many foreigners are willing to make on new units. But that strategy, which helps fund projects by limiting or eliminating the need for bank loans, has pros and cons.

The upside is developers can save up to 15 percent of the construction costs by not using banks, which require such things as fees and construction inspectors, Michael Maxwell said.

The downside is developers have to collect at least half of the condo purchase price up front to secure a construction loan.

That worries Scott Baena. Less-experienced developers could collect deposits to get a construction loan, then fail to complete a project. That would hurt condo buyers as happened in the housing crash when some projects didn't get built and some buyers-to-be lost part or all of their 20 percent deposit.

"Historically that led to abuses," he said. "The develop-

ers indebted the money that they shouldn't have indebted. The project didn't get complete. The buyers went without either a unit or their money."

The big-deposit strategy is creating a mini-condo boom in downtown Miami and along the coast. Meanwhile, the cost of construction materials and labor is creeping up.

Some projects are being priced and pre-sold based on today's construction costs, Maxwell said. Developers could be caught short if supply prices rise.

When the housing market collapsed in 2007, many construction workers left the region, creating a shortage of skilled workers and driving up the cost of labor.

"Over 50 percent of the people who were unemployed in that sector are gone," Maxwell said. "And the real problem is that if you brought all [the proposed condo projects] to market today, you wouldn't have enough people to build them."

"Are we going into a new bubble?" he asked.

Construction jobs increased 1.7 percent in the year ended Feb. 28, according to the Florida Department of Economic Opportunity.

Maxwell said he's also concerned about a trend taking place nationwide but is especially impacting South Florida. Hedge funds are buying hundreds of foreclosed single-family homes in the region to build rental portfolios. He fears the buying spree may fuel a bubble that could burst if the expected returns don't materialize.

Maxwell said he can't see how they can profit renting properties that need maintenance and whose property taxes will rise when values increase.

"I just don't see the yield coming out," he added.

Vanessa Grout disagreed. She said the funds are paying cash, which gives them flexibility.

"That market is cash driven, so investors don't have debt on their properties, allowing them to ride out any downturn that may occur," she said.

The region continues to see the number of homes on the

market decline. That, together with a voracious appetite for South Florida real estate by foreign buyers, is causing values to edge up.

For example, there were 4,406 single-family homes for sale in Miami-Dade County in February, down 74 percent from the peak of the housing bubble in July 2008, according to EWM Realty International. The median Miami-Dade single-family home price in February was \$200,000, a 50 percent drop from the peak of \$400,000 in May 2007.

In Broward County, 3,402 single-family homes were for sale in February, a 77 percent drop from April 2008. The median sale price in February was \$228,000, 42 percent below its peak of \$394,000 in July 2005.

The fewer homes on the market is pushing home-builders to get busy.

"A construction boom seems to be reigniting in South Florida and soon is going to start showing some positive contribution to the economy," Bruce Foerster said.

LATIN AMERICA

Economy benefits as Latin American flight capital lands in South Florida

Latin American investors are contributing to the revival of the South Florida housing market. Some bring money to Miami because their home economies — Brazil, for example — are flourishing. Others are seeking to shield capital from their countries' unstable economies.

There is little foreign investment heading to Argentina, said Francisco Cerezo, but there are plenty of Argentines looking for a safe haven in the U.S.

"Flight capital [happens] for different reasons," Cerezo said.

"Whether it is a good cycle or a bad cycle, we benefit" from it.

Antonio Villamil noted that Latin America is experiencing a growth rate of 3 percent to 3.5 percent. Chile, Colombia and Costa Rica are doing well; the economies of Argentina and Venezuela are scaring away investors.

Cerezo said high-profile Mexican investors also have become more prominent in South Florida.

"They invest in everything from Spanish media to real es-

tate and even banking," he said.

When it comes to acquiring real estate, the main reason Latin Americans shop in South Florida is housing is much cheaper than in their home countries, according to the Miami Association of Realtors. The industry group reports the region leads the nation in international real estate buyers.

Flourishing economies in South America aren't just benefiting South Florida. Some U.S. companies are investing in Brazil, which will host soc-

cer's World Cup in 2014 and the Summer Olympics in 2016. But despite the glamour of the sporting extravaganzas, investors are looking at the long-term economic fundamentals.

"Last year, we did three deals at very reasonable valuation for industrial Midwestern clients investing in Brazil for the long haul and not centered around the Soccer World Cup and the Olympics," Cerezo said.