

3 Year Hold Multifamily Value Add Assumptions

Property Description

- 240-unit, class B, garden-style apartment built in 1996
- Unix Mix
 - Studio – 70 units, average size: 650 SF
 - 1 Bedroom – 90 units, average size 750 SF
 - 2 Bedroom – 60 units, average size 900 SF
 - 3 Bedroom – 20 units, average size 1150 SF
- Parking: 110 carport spaces, 210 surface spaces

Acquisition Assumptions

- Purchase price of \$42,500,000
- Closing and Due Diligence costs equal to 0.5% of the purchase price (excluding financing costs)

Capital Improvement Program (i.e. Value-Add Renovation Plan)

- Zero units have been renovated to date
- 10 units to be renovated per month, starting in month one of the analysis
- Units under renovation down for one month; thus, no rent generated in month unit is down. Next month, that unit is occupied but at the rental rate for renovated units
- Model change in total rental revenue from non-renovated to renovated rent as a percent of total units, rather than calculating which specific units were renovated each month
- Common area renovation takes place over 12 months (month 1 – 12); costs forecasted straight-line
- Renovation costs as follows:
 - **In-Unit**
 - \$10,000/unit in hard costs, \$800/unit in soft costs
 - **Common Areas**
 - \$1,800,000 in hard costs, \$125,000 in soft costs

Financing Assumptions

- Senior loan
 - 65% of purchase price
 - Financing costs equal to 0.5% of the loan amount (paid in month 0)
 - 5.25% fixed interest rate; calculated 30/360
 - Interest-only
 - 3-year term
 - First to fund, followed by equity
- Mezzanine loan
 - 20% of purchase price
 - Financing costs equal to 2% of the loan amount (paid in month 0)
 - 10.0% fixed interest rate; calculated Actual/365
 - Interest-only
 - 3-year term
 - Last to fund after equity
 - Interest does not accrue; meaning no interest reserve and debt service is payable each month

Timing and Exit Assumptions

- Analysis start – Month 0 in December 31, 2019
- Acquisition occurs in month 0
- First 10 units renovated in month 1, with 10 units renovated each month thereafter
- Common area renovation completed in month 12, in-unit renovations completed in month 24
- Stabilization occurs in month 25
- Sale occurs at end of year three (month 36)
- Sale value based on year four NOI (months 37 – 48)
- Exit cap rate of 5.50%
- Exit selling costs equal to 2.0% of the sales price

Operating Assumptions

- Growth Rates
 - Both non-renovated and renovated rents grow at 2.5% per year (assume monthly increases/compounding);
 - Parking Income grows at 2.0% per year (assume annual increases)
 - Operating Expenses and Capital Reserves grow at 2.0% per year (assume annual increases), except for property taxes
 - Property taxes grows by 8.0% per year
- Rental Rate
 - Non-renovated units
 - Studio –1,250/month
 - 1 Bedroom –1,400/month
 - 2 Bedroom – 1,650/month
 - 3 Bedroom – 2,000/month
 - Renovated units
 - Studio –1,450/month
 - 1 Bedroom –1,600/month
 - 2 Bedroom – 1,850/month
 - 3 Bedroom – 2,200/month
 - No concessions offered
 - Do not include adjustments for loss-to-lease (i.e. assuming monthly increases rather than annual increases accounts for loss-to-lease element)
 - Assume an adjustment (i.e. subtraction) to Gross Rent of 0.75% per month for two model units
- Other Income
 - RUBS - None
 - Parking Income - \$50/carport/month; surface parking is assumed to be free
 - Misc. Income - 4.0% of Gross Rent (before adjusting for downtime and model units)
- General Vacancy and Credit Loss
 - Assumed 5.0% General Vacancy (on Potential Gross Income)
 - Assume 1.0% Credit Loss (on Potential Gross Income)
 - When modeling In-place and Stabilized pro forma, don't include Downtime Vacancy from units under renovation
- Operating Expenses (In-Place and Stabilized)

- Repairs and Maintenance – 350/unit/year
- Security – 200/unit/year
- Contract Services – 250/unit/year
- Landscaping – 150/unit/year
- Utilities – 900/unit/year
- Marketing – 350/unit/year
- Insurance – 275/unit/year
- Administrative – 250/unit/year
- Payroll – 1,200/unit/year
- Management Fee – 3.00% of Effective Gross Revenue
- Property Taxes – use 1.00% of Purchase Price for In-Place pro forma and then grow that amount by 8.0%/year in DCF; use 1.25% of Purchase Price when calculating untrended Stabilized pro forma only
- Capital Reserve – 200/unit/year (assume above NOI)

Partnership Structure

- General Partner – 5% of ownership
- Limited Partner – 95% of ownership
- Partners to contribute equity capital pari passu, based on each partners' respective ownership share
- A preferred return of 10.0% paid to the partners, distributed pro rata based on each partners' respective ownership share
- Once each partner has achieved a 10.0% internal rate of return and received a return of 100% of their contributed capital plus any accrued preferred return, the partnership shall distribute 75% of the excess cash flow to the partners pro rata based on their respective ownership share, with the remaining 25% being distributed to the General Partner as a promoted interest

Solve for the Following Outputs

- Property-level unlevered and levered internal rate of return and equity multiple
- Stabilized (i.e. after 100% of units are renovated), untrended (i.e. before applying income/expense growth) yield-on-cost
- The difference between the untrended yield-on-cost and the exit cap rate (i.e. the development spread)
- Required contribution for both partners
- Internal rate of return and equity multiple for both of the partners

Notes

- Sources fund as follows:
 - 1st senior debt to partially fund purchase
 - 2nd equity to fund portion of acquisition costs
 - 3rd mezzanine loan to fund remaining acquisition and renovation costs