

Real Estate Development Report

by Kuponu Liu



Contents

1. Tenant Rollover	2
2. Tenant Clauses	3
A. Co-Tenancy Clause	3
B. Percentage Rent Clause	3
C. Other Tenant Clauses	4
3. Assessing Excess Demand using Vacuum Analysis	8
4. Ascertaining the Solvency of Major Tenants	9
A. Credit Risk of Tenant (Altman Z Score)	9
B. Credit Risk of Tenant (Dun & Bradstreet vis-à-vis Hoovers)	10
5. Reimbursable Expenses	11
A. Reimbursable Expense (No Vacancy)	11
B. Reimbursable Expense (3% Vacancy)	11
6. Rent Analysis	11
7. Pro-Forma Annual Operating Statement	11
8. Backdoor Approach	11
A. 0% Vacancy	11
B. 3% Vacancy	13
9. Market Rent	13
10. Cap Rate Front-door Approach	13
11. Conclusion	14
Appendix	18-33

has a justified price per square foot of \$172.94--- which is below the sold price.

If we hold our interest rate constant at 4.65% and decrease our cash on cash return from 12.20%, the deal is still feasible. As we decrease our cash on cash return from 12.20% to 8%, we see that our justified price per square feet increases from \$187.24 to \$203.82. Given that our justified price per square feet is larger than our sold price per square feet of \$176.21 (for this particular decrease in cash on cash return from 12.20 to 8%), we see that this deal is solvent.

8b. 3% Vacancy

At 3% vacancy, our justified price per square foot is \$184.87 (aka \$54,555,256 justified investment) (Appendix 8B). As we go from fully occupied to 3% vacant, we see that our justified price per square feet decreases by \$2.37 (from \$187.24 at 0% vacancy). We see that our justified investment decreases by \$698,183 (from \$55,253,439 at 0% vacancy).

Given that our justified investment of \$54,555,256 (at 3% vacancy) is larger than our actual sold price of \$52,000,000, we see

that the deal is still feasible from a backdoor perspective. A deal is feasible from a backdoor perspective if the justified value is greater than or equal to the sold price.

9. Market Rent

The asking market rent per square feet is \$17.99 (Appendix 9). The total asking rent is \$5,308,618. The total asking rent is the summation of total asking rent for anchor space (\$2,864,359) and total asking rent for pad and shop space (\$2,444,259).

10. Cap Rate Front-door Approach

Under both scenarios of full occupancy and 3% vacancy, we see that the deal is financially feasible (Figure 10). With full occupancy, the required base rent per square feet is \$13.74; with 3% vacancy, the required base rent per square feet is \$13.91. Given that both required base rents per square feet are below the market rent per square feet of \$17.99, this deal is financially feasible. As a

Figure 10:
Cap Rate
Front-door
Approach

	0% Vacancy	3% Vacancy
Assumptions (2013)	Scenario 1	Scenario 2
Dollar Vacancy	\$0	\$56,440
Frontdoor Cap Rate		
Purchase Price	\$52,000,000	\$52,000,000
+ Immediate Capital Improvements	0	0
Adjusted Purchase Price	52,000,000	52,000,000
* Market Going-In Cap Rate	7.70%	7.70%
Expected NOI	\$4,004,000	\$4,004,000
+ Operating Expenses	\$1,493,136	\$1,493,136
Income Before Vacancy	\$5,497,136	\$5,497,136
+ Dollar Vacancy	\$0	\$56,440
Required Potential Gross Income	\$5,497,136	\$5,553,576
- Percentage Rent	\$70,579	\$70,579
- Expense Reimbursement Income	\$1,371,165	\$1,377,324
Required Base Rent Revenue	\$4,055,392	\$4,105,673
Required Base Rent Revenue	\$4,055,392	\$4,105,673
÷ Total Rentable Area (sqft) (Owned)	295,100	\$295,100
Required Base Rent per SqFt	\$13.74	\$13.91
Market (Asking) Rent per sqft	\$17.99	\$17.99

rule, a deal is solvent in the front door approach if the required rent is less than or equal to the actual rent.

After stress testing the deal for both the 0% and 3% vacancy scenarios, the deal is solvent for the most part with a couple exceptions.

With 0% vacancy, there is one scenario where the required base rent per square foot is larger than the asking rent of \$17.99 (Appendix 10). At a 8.50% going-in cap rate and \$62,500,000 purchase price, the required rent is \$18.18 per square feet. In this instance, the deal would be insolvent since the required rent is greater than the asking rent of \$17.99. Other than this example, this deal is solvent at all other combinations of going-in cap rates (ranging from 6.25% to 8.50%) and purchases prices (ranging from \$40,000,000 to \$62,500,000) --- all resulting required rents from all these other combinations are less than the asking rent of \$17.99.

With 3% vacancy, there is one scenario where the required base rent per square foot is larger than the asking rent of \$17.99 (Appendix 10). At a 8.50% going-in cap rate and \$62,500,000 purchase price, the required rent is \$18.35 per square feet. In this one example, the deal would be insolvent because its required rent is greater than the asking rent of \$17.99. Other than this example, this deal at a 3% vacancy is solvent at all other combinations of going-in cap rates (ranging from 6.25% to 8.50%) and purchases prices (ranging from \$40,000,000 to \$62,500,000) - -- all resulting required rents from all these other combinations are less than the asking rent of \$17.99.

For both the 0% and 3% vacancies, this deal is solvent at all purchase prices within the range of \$40,000,000 and \$60,000,000. At

any purchase price within this range and at any going-in cap rate between 6.25% and 8.50%, the required rent is below the market rent of \$17.99.

At a purchase price of \$62,500,000, this deal is mostly solvent, but it depends on the going-in cap rate. Under the 0% and 3% vacancy scenarios, this deal is solvent if it has a purchase price of \$62,500,000 and going-in cap rate between 6.25% and 8.25%. However, at a going-in cap rate of 8.50%, the deal is insolvent at \$62,500,000 since the required rent is above \$17.99 in both the 0% (\$18.18) and 3% (\$18.35) vacancy scenarios.

11. Conclusion

Based on the front door-backdoor solvency analysis, vacuum analysis and my qualitative assessment of this building, I would not recommend purchasing this property for risk averse investors.

Advantages:

Front door-Backdoor Analysis

After conducting the front door and backdoor analysis, we see that this deal is solvent. In the backdoor analysis, we see that the justified investment of \$55,253,439 is greater than the actual sold price of \$52,000,000. Even after vacancy increases to 3% from fully occupied, our justified investment of \$54,555,256 is greater than the actual sold price of \$52,000,000. In the front door analysis, our required base rent per square foot is less than the asking rent per square foot (\$17.99) for both fully occupied (\$13.74) and 3% vacancy (\$13.91) scenarios.

Vacuum Analysis

In a 10-mile radius (5 to 10-mile radius) with \$303.43 per square feet (2013 sales per