



St. Louis Development Corporation
DRAFT: Sample Financial Analysis
September 6, 2022

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1. Executive Summary

Note: This is a draft sample financial analysis of a hypothetical project prepared to illustrate the proposed format and content of an updated financial analysis. The intent of this draft is to illustrate the concept of how future analysis of projects could be completed and summarized. It is not meant to be a report analyzing a specific project. Certain hypothetical project information is included for illustration purposes.

Project Overview

The _____ project proposes the creation of a new multi-family building creating approximately 302 new residential multi-family units, and a projected 936 sf of commercial retail space. In addition, the project proposes the construction of a 386-stall parking garage. The Developer will be undertaking the acquisition and development of the project incurring costs related to the construction of the vertical improvements, along with sitework and other infrastructure improvements necessitated by the project. The Developer is seeking assistance for the project in the form of LCRA tax abatement and a sales tax exemption on the purchase of construction materials.

Community Benefits Scorecard

The project was evaluated using the residential Community Benefits Scorecard. The project scored **42** points placing it in the Tier 1 category (30-50 points). Tier 1 projects are eligible for a maximum level of abatement assistance of 80% for the first 10-years and 50% for the second 10-years.

The project received points in the following categories:

Capital Investment: **7** points for a total investment of \$132MM.

Walkability: **5** points for a walk score of 82 – “Very Walkable”.

Transit Access: **7** points for being located adjacent to a transit stop.

Public Infrastructure: **10** points for a private \$200K investment in public streetscape.

Geography: **5** points for being located in EJI-4.

Infill Development: **3** points for being an infill project that increases density.

Affordable Housing: **5** points for including 10% of the residential units at 80% AMI.

Total Points: **42 Points** – Tier 1 (30-50 Points)

Need for Assistance Analysis

Shown in the tables below are the calculated internal rates of return with and without the subsidy request, based on the project costs and operating revenues of the proposed project. Determining if a project would occur without subsidy requires the testing of various assumptions which have a material effect on a project's feasibility. We have tested the sensitivity of the return without assistance by varying the cost and the revenue assumptions, each independently and then collectively. The reason for testing sensitivity is to illustrate the magnitude with which project assumptions would have to change for the project to be considered feasible without assistance. For the purpose of this analysis, we have used the Midwest Investment Criteria IRR Return threshold of 6.0% as a feasible benchmark.

Table A

Without Assistance Sensitivity Analysis	Change Necessary to be Feasible	Unleveraged IRR without assistance
Decreased Costs	10% Decrease	6.08%
Increased Revenue	11% Increase	6.07%
Combined Cost and Revenue Changes	5% Decreased Costs 5% Increased Rev	6.01%

The table above indicates the magnitude at which project assumptions would have to change for the project to achieve a feasible IRR without assistance. Based on typical return thresholds the project would need to realize a return of approximately 6.0% to be considered feasible. Absent the requested assistance, without changes of the magnitude outlined above, the Developer would be unlikely to proceed with the project.

Table B, below, illustrates the Developer's projected rates of return with and without assistance:

Table B

Pro Forma	With 15-Years @ 80% Request	Without Assistance
Unleveraged	6.42%	4.81%

Fiscal Benefit of Project

Table C below identifies the projected fiscal benefit to the City and the School District from the project being undertaken and tax abatement assistance being provided for an initial period of 10-years at 80% followed by a second period of 10-years at 50% of the increase over the base level of taxes. The fiscal benefit identified below is the calculated Net Present Value of revenues generated over the identified time period, based on an interest rate of 3%.

Table C

City Fiscal Benefit over Base (NPV 3%)	10-Year	15-Year	20-Year
Net Revenue to City	\$2,743,045	\$4,468,235	\$6,103,920
-Baseline Revenue (if no project)	-\$129,613	-\$187,662	-\$241,417
=Net Revenue to City	\$2,613,432	\$4,280,573	\$5,862,503
School Fiscal Benefit over Base (NPV 3%)	10-Year	15-Year	20-Year
Net Revenue to School	\$2,195,317	\$5,059,402	\$7,047,379
-Baseline Revenue (if no project)	-\$469,192	-\$719,170	-\$873,922
=Net Revenue to School	\$1,726,125	\$4,340,232	\$6,173,457

Incentive Amount

Table D below identifies the projected value of the requested assistance, based on tax abatement assistance being provided for an initial period of 10-years at 80% followed by a second period of 10-years at 50% of the increase over the base level of taxes. The table illustrates the present value of the incentive request, as well as the nominal value of tax abatement savings.

Incentive Value to Project	10-Year	15-year
Present Value of Incentives (5.5%)	\$10,006,000	\$14,537,000
Percentage of Project Costs	7.6%	11.0%
Nominal Value of Incentives	\$13,978,384	\$25,102,629

3. The Project

The Developer is proposing the construction of an approximately 302-unit apartment building, located at _____. The proposed building is projected to be 418,645 square feet, and in addition to the 302-apartment units the building is also proposed to include 946 square feet of retail space and a 386-stall parking garage. Additionally, the Developer will be constructing necessary site improvements and related improvements.

The Developer anticipates construction commencing on the project in 2024 with 2025 being the first year of operations. The building is anticipated to be fully leased by 2026.

4. Redevelopment Costs

The total cost of the project is detailed in Table E below. The costs reflected below are before an estimated savings of \$3,008,584 provided by the requested sales tax exemption on construction materials.

Table E

Total Project Costs	Total Cost	% of Total Project Costs
Land Acquisition	\$9,785,000	7.41%
Hard Costs	105,000,000	79.46%
Soft Costs	17,353,632	13.13%
Total Project Costs	\$32,138,632	100%

Acquisition

The Developer acquired the building site for a cost of \$9,785,000. This cost equates to 7.41% of the total project cost and is equivalent to \$23.37 per building square foot.

Hard Costs

The total cost grouped together as hard costs are detailed in Table F below.

Table F

Total Hard Costs	Total Cost	% of Total Project Costs
Core, Shell & Rehabilitation	\$105,000,000	79.46%
Total Hard Costs	\$105,000,000	79.46%

The Developer provided a preliminary estimate for the total cost of hard construction of \$105,000,000, on which their pro forma was based. The total hard costs equate to 79.46% of the total project cost, which equates to \$250.81 per square foot or \$347,682 per unit.

To provide a comparison, we compared the cost estimates to the Marshall and Swift Swiftestimator for estimated construction costs for an apartment building in the St. Louis metropolitan area. The Swiftestimator provided an average cost estimate of \$_____

PSF, with a range from \$_____ to \$_____ depending on construction material type. In comparison the Developer's per square foot cost assumption for vertical improvements, net of site costs, was \$250.81. Based on this the Developer's hard cost estimate appears reasonable.

The construction cost category is the largest segment of the development costs, accounting for 86.83% of the total project costs. Consequently, this is a segment where project costs savings could have a positive effect on the rate of return realized by the Developer, while higher than estimated costs would have the converse effect. In the return analysis section of the report, we discuss the sensitivity of the rate of return to changes in the project costs, and the effect on the return without assistance of a decrease in project costs.

Soft Costs

For purposes of this review, we have grouped the cost categories in Table G below as Soft Costs:

Table G

Total Soft Costs	Total Cost	% of Total Project Costs
Architect/Engineer/Design Costs	\$3,733,405	2.83%
Inspection Fees	824,254	0.62%
Legal Fees	450,000	0.34%
Title/Recording/Disbursing	200,000	0.15%
Property Taxes	190,569	0.14%
Insurance Builders Risk	281,700	0.21%
Advertising/Marketing	1,384,600	1.05%
Other Development Soft Costs	627,500	0.47%
Soft Cost Contingency	587,153	0.44%
Mortgage Loan Commitment Fees	823,153	0.62%
Construction Period Interest	3,227,877	2.44%
Developer Fee	5,023,421	3.80%
Total	\$17,353,632	13.13%

The total amount of the cost categories grouped under the soft cost heading is \$17,353,632, which equates to approximately 13.13% of the total development costs or approximately \$41.45 per square foot.

Reviewing the soft cost categories for largest percentage of the total project costs to smallest, the largest portion of the soft costs is for the Developer Fee of \$5,023,421. This amount equates to approximately 3.80% of the total project costs. For purposes of the rate of return analysis this amount was reduced by \$819,014, to bring the amount to 3.5% of the total project costs.

The next largest line-item is the Architecture/Engineering/Design line-item of \$440,700, which equates to approximately 2.83% of the total project costs. This is a reasonable percentage for this type of line-item.

The next most significant soft cost line item is the Construction Period Interest Expense of \$3,227,877, which equates to 2.44% of total project costs. This cost estimate is a reasonable amount based on its portion of total project costs.

The remaining soft cost line-item greater than 1% of total project costs is the advertising/closing cost line item, which is \$1,384,600 and represents approximately 1.06% of the total project cost.

The other remaining soft costs line-items, all of which represent 1% or less of total project costs, in total are \$3,984,329 which equates to approximately 3.02% of the total project costs.

In the “Return Analysis” section of the report we discuss the sensitivity of the rate of return to changes in the project costs, and the effect on the return of a decrease in project costs.

Table H provides the anticipated sources that will be utilized to fund the development project.

Table H

Sources:	
Developer Equity (35%)	\$46,245,521
Permanent Financing (65%)	\$85,890,111
Total Sources*	\$132,138,632

*Prior to savings from sales tax exemption.

5. Assistance Request

The project has requested assistance in the form of a LCRA Tax Abatement. The project was scored using the Community Benefit Scorecard, which resulted in a score of 42 points placing it in the Tier 1 category making it eligible to receive a maximum tax abatement of 80% of the new value for an initial period of 10-years followed by a second period of 50% of the new value for 10-years.

The post-development property tax estimate for the project upon completion is projected to be \$110,391,426, resulting in a total property tax amount (prior to abatement) of \$1,827,406. The market value is assumed to increase at 2.0% annually over the life of the abatement. The post-development market value equates to a value assumption per-unit of \$365,535 and a per-unit tax amount of \$6,051.

Based on the scoring of the project, the maximum abatement eligibility is for 80% of the post development market value amount for 10-years followed by 50% for years 11-20, resulting in a taxable value of approximately \$22,078,285 (prior to inflation) during the abatement period. The resulting annual property tax amount paid during the initial 80% abatement period is \$423,441.49 prior to inflation. The taxing jurisdictions will continue to realize this level of taxes during this initial abatement period.

In Table I below we show our estimate for the gross value of the abatement as well as the net present value of the requested tax abatement assistance based on a 5.5% interest rate.

Table I

Tax Abatement Scenario	Total Abatement Savings	Total Abatement Savings Net Present Amount @ 5.5%
10-Years @ 80% and 10-years @ 50% of increase over base amount	\$25,102,629	\$14,537,000

The Net Present Value of the tax abatement savings is \$13,988,996 which equates to approximately 9.8% of the total project cost. In the return analysis section, we will illustrate the impact on the projected rate of return with and without the requested tax abatement assistance.

Additionally, the project is seeking an exemption on sales tax on the purchase of construction materials. The estimated net benefit to the Developer from this exemption is \$3,008,584 and equates to approximately 2.3% of project costs, bringing the total assistance request to approximately 12.1% of the total cost.

6. Return Analysis

Utilizing project cost and operating information prepared by the Developer we evaluated the need for assistance for the project by comparing the potential return with and without assistance. This information was used to calculate an unleveraged Internal Rate of Return (IRR) calculation after 10-years of operation. The IRR calculation is a measure of return on investment that accounts for the time value of money and allows for a measure of the potential financial return generated by the project. By calculating the potential IRR return generated by the project with and without the requested financial assistance we are able to draw comparisons regarding the potential feasibility of the project with and without the requested assistance.

The return realized by the Developer is a result of the assumptions used in the creation of the operating pro forma, therefore a number of steps must be performed to analyze the reasonableness of the assumptions used.

The first step in analyzing the return to the Developer is to determine if the costs presented are reasonable. We have discussed a portion of the costs above and have commented on the mechanics whereby cost savings on the private side could occur. If cost savings for the Developer's share occur absent any other changes, the Developer would realize a greater return than projected.

The second step in calculating the return to the Developer is to determine if the operating revenues and expenses of the proposed development are reasonable.

- The Developer has projected the following average lease rates for the multi-family units:
 - \$2,669/Month (\$3.14 psf) – blended average across all unit sizes
 - The Developer has assumed a 7% vacancy factor upon stabilization.
- For the Retail space the Developer has assumed a NNN lease rate of \$24.00 psf.
- The Developer has projected annual operating expenses (net of taxes) which are equivalent to approximately 17.3% of annual revenues upon stabilization.
- Operating revenues to inflate at 2% annually and operating expenses are proposed to inflate at 2.5% annually upon stabilization.

Based on a review of third-party market information, we feel the Developer's operating assumptions outlined above appear reasonable.

The calculation of an internal rate of return requires the assumption of a hypothetical sale of the asset in the final year of the operating pro forma. The inclusion of this hypothetical sale is used purely for purposes of evaluating the return on the Developer's investment. The determination of the potential market value of the project, through a hypothetical sale, is necessary as it allows for the inclusion of the value of the asset into the rate of return calculation. The calculation of an IRR without the hypothetical sale would result in an understated return, as the return would not be taking into account the value of the real

estate asset. The use of a hypothetical sale assumption is not indicative of the Developer's intention to sell the development in the final year.

The third step in analyzing the return to the Developer is to determine if the assumptions for the hypothetical sale of the asset are reasonable. A critical assumption when valuing the asset at the time of the hypothetical sale is the capitalization rate. The available net operating income divided by the capitalization rate results in the assumed fair market value of the asset. For purposes of our analysis, we utilized a capitalization rate of 6.64%, to calculate the hypothetical sale value based on current market information.

An unleveraged IRR calculation is used in order to compare the potential return to the Developer to available third-party market data, which provides a market comparison on which project feasibility can be judged.

Table J below, shows the Developer's base pro forma rate of return without assistance and the return with the tax abatement and sales tax exemption assistance.

Table J

Developer Pro Forma	Unleveraged IRR
Without assistance	4.81%
With tax abatement 15-years @ 80% and Sales Tax Exemption	6.42%

To evaluate the rate of return a project of this nature would require to be considered "feasible" we used the Midwest Investment Criteria Range for First-Tier Investment Properties in Prime to Good Locations. This provides a resource for comparing the Developer's rate of return to a market benchmark to help determine feasibility. According to the resource, the typical unleveraged market return necessary for a project of this nature falls in a range from 6.0% to 8.5%; with an average return of 7.2%.

Sensitivity Analysis

In order to answer the question "is the development likely to occur without public assistance" we analyzed the project on the basis of the Unleveraged Rate of Return with Assistance. For the purpose of this sensitivity analysis, we utilized the MidWest Investment Criteria low IRR range of 6.0% as a feasibility benchmark for evaluating the rate at which project assumptions would need to change for the project to result in a feasible rate of return without the requested assistance.

Presently without assistance, the projected unleveraged IRR for the project is 4.81% which falls significantly below the feasible return threshold of 6.0% used for this sensitivity analysis.

In order to understand the sensitivity of the project to changes in assumptions, we have prepared a sensitivity analysis to illustrate the rate at which assumptions would have to change for the project to have a feasible IRR equal to or greater than 6.0%. To understand the impact of the project cost assumptions, we have performed a cost sensitivity analysis to determine the rate at which costs would have to be reduced for the project to be feasible without assistance. Table K illustrates the development would need to realize a 10% reduction in project costs to achieve a feasible IRR without assistance.

Table K

Project Costs Sensitivity	Reduction in Project Costs	Unleveraged IRR without assistance
	10%	6.08%

To understand the impact of increased operating income, we have performed a sensitivity analysis to determine the rate at which project net operating income, would have to increase for the project to be feasible without assistance. Table L illustrates the development would need to realize a 11% increase in net operating income in order to realize a feasible IRR.

Table L

Project Revenue Sensitivity	Increase in Operating Income	Unleveraged IRR without assistance
	11%	6.07%

As a final step in the sensitivity analysis, and to understand the impact of a combined change in project costs and project revenues, we have performed a sensitivity analysis to determine the rate at which these areas would have to change for the project to realize a feasible DCR. Table M illustrates the development would need to realize both a 5% decrease in project costs and a 5% increase in operating income for the project to realize a feasible IRR without assistance.

Table M

Combined Sensitivity	Reduction in Project Costs	Increased Operating Income	Unleveraged IRR without assistance
	5%	5%	6.01%

The three tables above (Tables K, L, and M) indicate the magnitude at which project assumptions would have to change for the project to have a feasible IRR without assistance which we feel is approximately 6.0% for this type of project. Absent changes of the magnitude outlined above the project would have an insufficient return to draw market investment. Only by assuming either increases in project revenues, decreases in project costs, or a combined change of the two does the projected IRR increase to a feasible level without public assistance.

Need for Assistance Conclusion

The Developer will bear all the risk until project completion and permanent financing is in place, and continued operating risk thereafter. This level of risk typically demands a positive return with a range between 6.0% and 8.5% based on the MidWest Investment Criteria, with an average return of 7.2%. The unleveraged rate of return with assistance is 6.42% and without is 4.81%.

Without assistance the project would realize an unleveraged IRR (4.81%) that is significantly outside of the third-party benchmark range identified above. As illustrated by the sensitivity analysis outlined above, it would take significant changes to assumptions for project costs and operating revenues for the project to achieve a feasible return without assistance. Based on the review of the Developer’s assumptions, changes of this magnitude are unlikely to be realized, and therefore it is concluded the project would be unlikely to occur on this site at this time without a public subsidy.

7. Fiscal Impact Analysis

In order to calculate the projected fiscal impact to the City and the School District, future tax revenues were projected related to City and School District captured taxes. These tax calculations incorporate the property taxes generated by the project due to the 20% of market value not being abated. In addition to the property taxes, future taxes generated by the development were projected related to the following categories:

- Earnings Taxes (Residents & Workers)
- Retail Sales Tax (City & School)
- Payroll Tax
- Parking Tax

Additionally, consideration was given for the potential substitution effect realized by the future tax projections, and in order to ensure that future revenue projections are not being overstated, the following Substitution Rates were utilized in the calculation of future tax revenues:

- Payroll: 15%
- Retail Sales: 15%
- Residents: 41%

Utilizing these assumptions, future tax revenues were projected for the City and School District, with Table N below illustrating the benefit to each jurisdiction over a 10-year period, the 15-year period of the abatement, and over a 20-year period.

Table N

Fiscal Benefit over Base (NPV 3%)	10-Year	15-Year	20-Year
Gross City Revenue	\$6,382,174	\$9,458,320	\$12,376,701
-City Portion of Incentive	-\$2,265,390	-\$2,960,821	-\$3,619,201
-Revenue Lost to Substitution	-\$1,373,739	-\$2,029,264	-\$2,653,580
=Net Revenue to City	= \$2,743,045	= \$4,468,235	= \$6,103,920
-Baseline Revenue (if no project)	-\$129,613	-\$187,662	-\$241,417
=New NPV Revenue to City	= \$2,613,432	= \$4,280,573	= \$5,862,503
NPV Fiscal Benefit to School District	\$1,726,124	\$4,340,232	\$6,173,457

Table O below identifies the Estimated Fiscal Impact of Tax Abatement related to the project on all of the Taxing Jurisdictions.

Table O

Estimated Fiscal Impact of Tax Abatement					
Residential rate=\$8.2756/\$100** Commercial rate=\$9.9156/\$100**	Est. Annual Share of Property Tax Fractions	Total Nominal Abatement Value	Average Annual Abatement Value (1st 5 Years)	Revenue Collected During Abatement (Nominal)	Baseline Revenue If No Project (Nominal)
State - Blind Pension	\$0.0300	\$90,269	\$4,445	\$103,491	\$6,199
School District - General Fund	\$5.0342	\$15,147,664	\$745,856	\$17,366,463	\$1,040,268
Community College District	\$0.2112	\$635,491	\$31,291	\$728,576	\$43,642
Metropolitan Sewer District (MSD)	\$0.1159	\$348,737	\$17,171	\$399,820	\$23,950
Library District	\$0.5496	\$1,653,720	\$81,427	\$1,895,953	\$113,569
Zoo, Museum, & Botanical Garden	\$0.2694	\$810,612	\$39,914	\$929,348	\$55,669
Community Mental Health District	\$0.0883	\$265,690	\$13,082	\$304,608	\$18,246
Sheltered Workshop District	\$0.1472	\$442,918	\$21,809	\$507,795	\$30,417
Senior Services	\$0.0500	\$150,448	\$7,408	\$172,485	\$10,332
Community Children Service Fund	\$0.1865	\$561,169	\$27,631	\$643,368	\$38,538
City of St. Louis					
Municipal Operation	\$1.4600	\$4,393,069	\$216,310	\$5,036,557	\$301,695
Interest and Public Debt	\$0.1333	\$401,093	\$19,749	\$459,845	\$27,545
M & M Surtax (Commercial Only)	\$0.0000	\$0	\$0	\$0	\$0
Total Nominal Values		\$24,900,879	\$1,226,094	\$28,548,310	\$1,710,071
Net Present Value of the Tax Abatement				\$14,537,186	

ASSUMPTIONS:

Estimate based on Net Operating Income projections from developer. Assumes that tax rates stay constant over the entire period. Discounted at 6%.

**Tax rates are subject to change