Salem Inclusionary Zoning
Update | Monday, January 14th, 2019

FINANCIAL FEASIBILITY MODEL

To test the market implications of various inclusionary zoning scenarios, MAPC is developing a financial feasibility model. This model is based on a pro forma analysis that is typically used by a developer to understand whether a real estate project is financially feasible. A development pro forma takes into account dozens of project-specific real estate development variables (many of which are listed below) to arrive at a projected level of profitability. As each of these variables changes – for example, as construction costs decrease or interest rates increase – profitability goes up or down. If profitability falls below a certain level, the project is considered infeasible.

At the January 14th Advisory Committee meeting, we will be using a working draft of the model to understand how different inclusionary requirements might impact development feasibility. We will start with a baseline scenario: a typical mid-sized Salem rental development project with no inclusionary zoning. From there, we will explore the ways that different iterations of an inclusionary policy (for example, number of affordable units required or bonus incentives offered) might impact the project's bottom line. **Our goal will be to understand the tradeoffs involved in the different aspects of an inclusionary policy and to arrive at consensus of how these different aspects should be prioritized.**

WORKING ASSUMPTIONS – 01/10/19

An important part of financial modeling involves market research to ensure that the model's inputs reflect Salem's local development conditions. MAPC is in the process of interviewing developers and lenders about Salem's local development conditions, which will inform the model inputs along with information from industry real estate database CoStar. Below is a working list of assumptions based on these sources. Please note that this is a working document and that many assumptions will likely change as we continue to gather information and refine our understanding of development in Salem.

<u>Development basics</u>

- Unit mix: 40% 1-bdrm units, 55% 2-bdrm units, 5% 3-bdrm units
- Unit size
    - 850 sq.ft. 1-bedroom
    - 1,200 sq.ft. 2-bedroom
    - 1,500 sq.ft. 3-bedroom
- Common area: 15% of total building area

- Parking: per zoning (generally 1.5 spaces/unit; 1 space/unit for existing buildings in B5)

Construction costs

- Construction costs (new construction)
    - Stick construction: $220/sq.ft.
    - Podium construction: $250/sq.ft.
- Parking costs
    - Surface parking: $10,000/parking space
    - Podium parking: $25,000/parking space
- Land costs: in progress
- Soft costs: 20% of construction costs

Operating

- Rents:
    - $1,800/month 1-bedroom
    - $2,200/month 2-bedroom
    - $2,400/month 3-bedroom
    - Inclusionary rents per HUD requirements
- Condo sales
    - $290,000 1-bedroom
    - $325,000 2-bedroom
    - $375,000 3-bedroom
    - Inclusionary sales prices per HUD requirements
- Operating costs: $8,500 per unit annually/$9 per sq.ft.
- Vacancy rate: 5%
- No separate parking charge

Financing requirements

- Debt /equity: 70% permanent debt, 30% equity
    - Equity from small, non-institutional investors
- Permanent debt interest rate: 5.75%
- Construction period: 1 year
- Mortgage term: varies
- Inflation: 3%
- IRR: 12-15%