



City of Lakewood

Physical Conditions
Broker's Opinions of Value
Projected Future Values

JULY 27, 2015

Outline

- Project Background and Objectives
- Project Methodology
- Physical Conditions Overview
- Broker Opinions of Value Overview
- Projected Future Cash Flows Overview
- Conclusions

Project Background and Objectives

- Report focused on three properties:
 - Lakewood Hospital Professional Building (“POB”)
 - Lakewood Community Health Center (“CHC”)
 - Lakewood Hospital Parking Garage (“Garage”)
- Three components of report:
 - Physical Conditions Assessment (POB and CHC)
 - Broker’s Opinions of Current Value (POB, CHC, and Garage)
 - Projected Future Cash Flows (POB, CHC, and Garage)
- Project team:
 - Allegro Realty Advisors, Ltd.
 - Simplified Facilities Group, Inc.

Project Methodology

- Three distinct components, multiple methodologies employed
- Physical Conditions Assessment
 - Thorough on-site inspection of properties and building components
 - Assessed roof, exterior, interior, doors/windows, landscapes, electrical, HVAC, and building systems
 - Components are assigned risk and cost ratings from one to three
- Broker's Opinions of Value
 - Conducted on-site inspection/tours of currently vacant spaces
 - Documented current conditions of spaces
 - Reviewed submarket conditions, likely investor/user perceptions, recent transactions, and current properties on market
 - Employed net land value methodology for Garage

Project Methodology, cont.

- Projected Future Cash Flows
 - Tested different assumptions, modeled variety of scenarios
 - Aimed at understanding future cash flows of properties
 - For CHC and POB utilized Argus software – designed exclusively for commercial real estate, industry standard software for valuation modeling
 - For Garage developed Excel model – able to be manipulated at later date by City based on performance
 - Financial modeling (CHC & POB)
 - Four different scenarios modeled: Status Quo, Intermediate, Recapitalization with Market Rents, and Recapitalization with Below-Market Rents
 - Aimed at capturing a variety of potential eventualities

Physical Conditions Overview (POB & CHC)

- Risk Ratings ranging from one to three (High to Low)
 1. Immediate concern or needs immediate attention
 2. Will need attention in the near term or regularly
 3. Not a significant concern
- Cost to Repair Ratings from one to three (High to Low)
 1. High Cost – over \$15,000
 2. Medium Cost – between \$5,000 and \$15,000
 3. Low Cost – less than \$5,000
- Determined that both properties were well maintained
- Neither required immediate attention related to structural components or systems
- Recommendations made to extend useful lives of current components, but no significant capital improvements required

Broker's Opinions of Value Overview

- Not formal appraisals, premised on what a reasonable buyer would pay for the properties
- Assumes properties are not subject to a master lease with Lakewood Hospital Association
- POB tour notes:
 - Suites outdated, configured for medical use, challenged for natural light
 - Common areas well-kept and updated
- CHC tour notes:
 - Updated finishes, outdoor space, good natural light, variety of configurations
 - Commons areas well-kept and updated
- Limited comparable office market data available for inclusion in analysis
 - Submarket appears stable

Broker's Opinion of Value Overview, cont.

- Utilized net land value methodology for Garage value
 - Fundamental premise – user of real estate would not pay more than it would cost to construct an equivalent condition
 - Utilized vacant land sales + projected demo costs to derive value
- Summary of building values
 - Completed transactions range in price from \$10.63 to \$21.88 per foot in submarket
 - Properties currently on market demonstrate higher than expected asking prices, considerable days on market
 - Expect a price per square foot premium for CHC over POB given interior finishes
- Conclusions
 - POB: \$1,300,000 to \$1,475,000
 - CHC: \$625,000 to \$700,000
 - Garage: \$75,000 to \$100,000

Projected Cash Flows Overview (CHC & POB)

- Modeled variety of scenarios to allow City to understand future cash flows based on different outcomes
- Four Models
 1. Status Quo:
 - Lakewood Hospital remains in place during term of lease
 - Existing leases remain intact
 - No significant capital investments are required
 2. Intermediate:
 - Lakewood Hospital exits property
 - Replaced by 50-60,000 square foot family health center
 - POB and CHC derive some occupancy benefits from proximity
 - Owner required to make capital investments to attract new tenants
 3. Recapitalization with Market Rents & 4. Below Market Rents
 - Lakewood Hospital exits property
 - POB and CHC do not derive occupancy benefits from wellness center
 - Owner required to make capital investments to attract new tenants

Projected Cash Flows Overview (CHC & POB), cont.

- POB conclusions
 1. Status Quo Model:
 - Even after costs associated with ownership, property generates positive cash flows over 10-year period
 2. Intermediate Model
 - After capital investments and reserves, property generates negative cash flows over 10-year period
 3. Recapitalization Model with Market Rent & 4. Below Market Rent
 - After capital investments and reserves, property generates negative cash flows over 10-year period
- POB Summary Conclusions
 - Status quo generates positive future cash flows
 - Stabilizing property without tenancy benefits associated with hospital proximity would require significant capital investment and patience

Projected Values Overview (CHC & POB), cont.

- CHC conclusions
 1. Status Quo Model:
 - Even after costs associated with ownership, property generates positive cash flows over 10-year period
 - Modeled NOI generates significantly higher underlying value
 2. Intermediate Model & 3./4. Recapitalization Models
 - Initial losses require minor investments/improvements
 - By year 4 of models property generates positive annual cash flows, after additional expenses are included
- CHC Summary Conclusion
 - Property is likely to continue to generate positive cash flows for future owner, with or without hospital proximity

Projected Values Overview (Garage)

- Developed an Excel model in order to determine breakeven parking figures based on estimated capital repairs required (Makovitch report)
- Utilized Makovitch's Option #1 – repair existing structure and upgrade construction to current standards
 - Assumes \$5,186,000 in repairs
 - Assumes \$100,000 in annual improvements thereafter
- Analysis did not include a parking demand component
- Two data points available for decision making
 1. Tool to determine how many daily parkers are required to breakeven on annual expenses
 2. Allows City to determine how many daily parkers are required to generate various rates of return based on capital investment

Projected Values Overview (Garage), cont.

- Garage conclusions
 - While possible to breakeven on current operations, requires a considerable increase in daily parkers (i.e., 250 parkers per day)
 - Generating a 0% return on repair investment over 10-year period requires 90%+ occupancy
- Summary conclusion
 - Based on assumption of 50% occupancy (315 cars per day), Garage could generate positive NOI
 - However given repairs required at Garage, ownership would require considerable patience to recoup initial investment (e.g., 40+ years)