

Case Study of a Typical Hotel Development

Introduction:

Staff analyzed the economic structure of a typical hotel development on District tidelands to discover how District revenues are impacted due to project delays and various rent ramp-up scenarios. The analysis in this case study is generic and could be applied to any hotel development on district tidelands.

Background:

A typical hotel development has many stakeholders both internal and external. Provided, the hotel project is desirable to the Board of Port Commissioners (Board), the District has an interest in receiving rental revenue from the project, the project meets all regulatory requirements and the Board elects to pursue the project¹, it is advantageous to have the project built as soon as possible. In certain circumstances, external stakeholders can delay the project after approval of the environmental review or the project by the Board. These delays have significant risks and costs as described herein.

Assumptions:

Staff used 100 as the stabilized market rent of a typical deal, as proposed by a developer, and made assumptions to create five different rent ramp-up and project delay scenarios or Deal Scenarios (DS 1 to 5 below).

Deal Scenario Assumptions:

- DS 1 is considered the base case with a standard three-year rent ramp-up to allow for construction and stabilization of the hotel within five years.
- DS 2 applies an additional 10% reduction in the rent over DS 1 for five years until full market rent is received in year six.
- DS 3 applies an additional 20% reduction in the rent over DS 1 for six years until full market rent is received in year seven.
- DS 4 is the same ramp-up as DS 1, but with a one-year delay in the project start date.
- DS 5 is the same ramp-up as DS 1, but with a five-year delay in the project start date.

Economic Assumptions:

- 30-Year Net Present Value (NPV)
- 7.0% Discount Rate
- All macro-economic assumptions are fixed for the purposes of this analysis

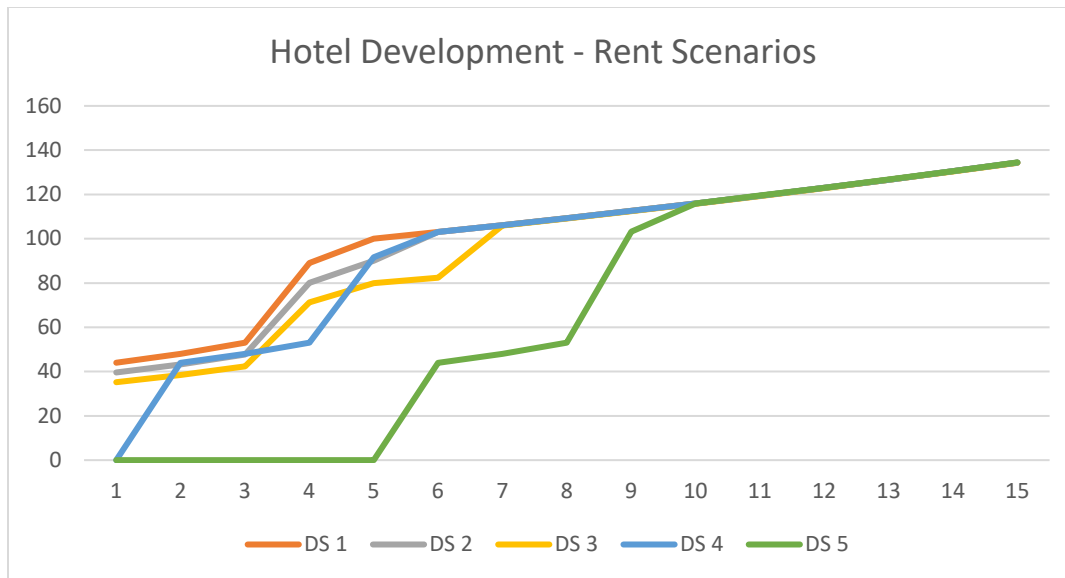
¹ This includes after the environmental impacts have been analyzed through environmental review and the Board approves the same in accordance with the California Environmental Quality Act.

- 3.0% annual inflation applied after stabilized market rent is achieved
- Hypothetical deal NPV of \$42MM used to show scale of impact to NPV

Year	DS 1	DS 2	DS 3	DS 4	DS 5
1	44	40	35	0	0
2	48	43	38	44	0
3	53	48	42	48	0
4	89	80	71	53	0
5	100	90	80	92	0
6	103	103	82	103	44
7	106	106	106	106	48
8	109	109	109	109	53
9	113	113	112	113	103
10	116	116	116	116	116
11	119	119	119	119	119
12	123	123	123	123	123
13	127	127	127	127	127
14	130	130	130	130	131
15	134	134	134	134	134

	Delay
	Full Stabilized Market Rent
	Rent Ramp-up

	DS 1	DS 2	DS 3	DS 4	DS 5
NPV Scale	100.0%	98.1%	95.1%	94.1%	72.8%
Deal NPV	\$42,000,000	\$41,199,583	\$39,958,266	\$39,524,944	\$30,596,420
NPV Loss		-\$800,417	-\$2,041,734	-\$2,475,056	\$11,403,580



Conclusions:

In DS 2 and 3, where the rent ramp-ups are greater and longer than the base case DS 1, the resulting NPV is lower by approximately 2% and 5% respectively. DS 4 has just one-year delay in the base case deal but has an even greater loss in NPV of approximately 6%. Predictably, the five-year delay in the base case deal has a substantial loss in NPV of more than 27%. The analysis shows that delays in the project start date, even for one-year, have a greater negative impact on the District's NPV than the longer and greater rent ramp-ups analyzed.