# Table of Contents

Executive Summary 2

Market Analysis 5

Product and Leasing Strategy 23

Site Analysis 26

Due Diligence and Regulation 30

Redevelopment and Construction Costs 34

Property Input Assumptions 37

Financing 40

Investment Analysis and Risk Factors 43

Feasibility Analysis 46

Summary Conclusion 51

Financial Analysis

Market Analysis Addendum Exhibit A

Site Analysis Addendum Exhibit B

Redevelopment Supporting Documents Exhibit C

Market Leasing Assumptions Exhibit D

Argus Reports Exhibit E
Executive Summary

Introduction:
Tanya Slesinger has been retained to complete a market and feasibility study for the purchase and redevelopment of 266 Border Street, a 35,000 sf warehouse in East Boston, Massachusetts to be converted to luxury rental loft units to be known as Border Lofts. Situated on one of the cleanest and most picturesque harbors on the East Coast, directly across from Boston’s Financial District and with immediate access to the interstate highway systems, mass transit options and Logan Airport, Border Lofts would significantly contribute to the waterfront rehabilitation goals of this neighborhood.

Project Summary:

**Building Description:**
266 Border Street is an existing owner-occupied warehouse built in 1950 located at Princeton and Border Street in the East Boston neighborhood of Boston.

**Address:**
266 Border Street
Boston, Massachusetts 02128

**Property Type:**
Conversion of warehouse into 30 luxury rental loft units, including 4 “affordable” units.

**Project Size & Land Area:**
Border Lofts is 4-story, 34,579 square foot building on 0.36 acres.
Border Lofts  
Boston, Massachusetts

Building Construction: Solid brick construction

Parking: Sufficient parking for one rented space per unit.

Building Features & Amenities: Open floor plans, 14’ ceilings, hardwood floors, exposed brick interiors with exposed raw finishes, skylights, stainless steel appliances, shared laundry facilities

Access & Visibility: Direct harbor and Boston skyline views and access to all public transportation options.

Zoning: Zoned Waterfront Commercial, proposed usage permitted, with conditional approval required for first floor residency.

Development Schedule: It is estimated that the entire project will take eighteen months through due diligence, permitting, construction and lease-up.

Financial Summary:

Required Returns: Financial feasibility is defined by a required 15% IRR on the equity investment.

Financing: East Boston Savings Bank will underwrite comprehensive financing including construction loans through permanent financing.

Project Costs: The property purchase price is $3.3M, total redevelopment costs are $4.9M ($139 psf).

Valuation: Stabilized value as of June 2007 is $5.53M at 7% going-in capitalization rate and 10% discount rate.
Development Issues:

- East Boston is an “up and coming” neighborhood with several major developments determining its success for high-end residential product. These developments are both critical to the neighborhood’s transformation, however pose to over saturate the East Boston residential market.
- East Boston neighborhood politics are highly volatile due to the history of this area of Boston, coupled with significant development opportunities affecting the East Boston’s future.
- The regulatory limitations and conditions to comply with historical renovation and affordable housing requirements add significant risk to the development; both however are critical components for financial feasibility.
- The industrial neighborhood and previous site use suggests a prolonged due diligence process to rule out environmental liabilities and to prepare the site for residential occupancy.
- While zoning regulations are relaxed for usage regulations, the waterfront location will require additional due diligence to ensure compliance with Chapter 91 Tideland Requirements of the East Boston zoning code.
- Uncertainties associated with the rehabilitation of an old structure threatens feasibility with an already maximized budget in an expensive and union driven market.
Location Overview –  
266-268 Border Street is located in the East Boston neighborhood of Boston, Massachusetts. The City of Boston serves as the capital of the Commonwealth of Massachusetts and stretches 48.4 square miles across the eastern portion of the state on the Atlantic Ocean. Boston was first incorporated as a town in 1630 – it is one of the nation’s oldest and wealthiest cities. It served as the third busiest port in the British Empire and its economy was heavily reliant upon the seaport long after the Revolutionary War. The city’s history is a critical element of its cultural landscape as seen in the dated brownstones and twisting streets of a downtown devoid of a formal urban plan. Central Boston was for a long time set back from the waterfront and separated by the John Fitzgerald Expressway which connects Interstate 93 across the downtown portions of the city and was the inspiration for Boston’s infamous and controversial Central Artery Tunnel Project (the “Big Dig”). The once conservative city has been replaced by a progressive culture and attitude drawing a young and vibrant population to its numerous educational institutions. Its once maritime economy has been replaced by education, finance, healthcare and high technology sectors.
Boston is comprised of sixteen distinct neighborhoods, each exhibiting characteristics of its long history. East Boston is one of the oldest neighborhoods in the city and has a land area of 4.51 square miles, 2.5 square miles of which is dedicated to Logan Airport. The neighborhood is a peninsula made up of five islands in the Boston Harbor that have been connected through filling operations over the past 150 years. It is still separated from the city by the Boston Harbor and is bordered by the towns of Winthrop, Revere and Chelsea Creek. The development of this neighborhood for residential and commercial use began in the 1830’s under the control of the East Boston Company, making East Boston one of the city’s few neighborhoods created with a formal urban plan. Historically, it was a popular resort community due to its expansive views and access to Boston Harbor. The neighborhood was the home of New England’s first major horse race track, Suffolk Downs. Its economy was heavily reliant upon marine industries and was the center for Boston trade and clipper shipbuilding. While remnants of this seaport exist today, the East Boston economy is anchored by Logan International Airport. The airport’s construction commenced in 1923 and inextricably altered the face of the neighborhood.\(^1\) East Boston is generally considered a blue-collar neighborhood, historically it was the arrival point for thousands of immigrants – first Irish and Canadians, then Russians and Italians, followed by Southeast Asians and most recently Central and South Americans.

---

Market Demand –

Population:²

The City of Boston has a population of 589,141 with a gross population density of 12,172, according to 2000 Census data. The city’s population grew by 14,859 or 2.59 percent, making it one of only two older northern and mid-western cities to gain in population over the last two decades. Boston’s racial composition is comprised of 49 percent White, 24 percent Black, 14 percent Hispanic/Latino and 8 percent Asian Pacific. The white population dropped 10 percentage points from 1990, while the overall non-white population rose. The number of whites increased in only three Boston neighborhoods, Central Boston, the South End, and Fenway-Kenmore. The Hispanic and Latino population is experiencing the most rapid growth, registering an increase of 3.2 percentage points from 1990 to 2000.

Boston’s cultural landscape is also defined by its population of 20 to 34 year-olds, drawn to the city by the presence of higher education institutions, job opportunities, and many social, cultural and recreational attractions. This age bracket makes up approximately 33 percent of Boston’s population, ranking the city second in the country for concentrations of residents in this bracket. A closer look at changes in this bracket from 1990 to 2000 suggests a slight decline; however a recent report released by the Boston Redevelopment Authority contends that this trend is a national phenomenon due to the aging of the “Baby Bust” generation.³ While this bracket slightly declined since 1990, populations between 35 and 59 all showed an increase, with declines again of 60 to 85 year-olds.

Of the sixteen defined Boston neighborhoods, East Boston and Dorchester account for 80 percent of the city’s population gain. East Boston had the largest total population growth of any Boston neighborhood, gaining 5,472 residents or 16.6 percent between 1990 and 2000 to total 38,413. The racial composition in East Boston is 49.7 percent white, 3 percent black, 39 percent Hispanic and Latino and 4 percent Asian Pacific (refer to Chart 2). East Boston has become home to the largest Hispanic and Latino population in the city, with an increase of nearly 10,000 residents in the past decade. Unlike its parent city, East Boston experienced an increase in residents 21 years old, 25 to 29 years old and 30 to 34 years old. The largest increase however occurred in the 35 to 39 year-old bracket – adding 1,182 residents from 1990 to 2000. Like the City of Boston, East Boston also experienced an increase in the population of 40 to 59 year-olds and a decline of older groups between 60 to 85 years old.
Economy:

Boston is the economic center of not only Massachusetts, but also of New England. Its economy accounts for approximately 18 percent of the Massachusetts economy and 10 percent of New England’s economy. A 2004 report released by the Boston Redevelopment Authority states, “the ratio of jobs to population indicates that the City provides a direct source of employment and income for an area that extends well beyond its borders.” The Boston metropolitan area experienced an economic recession from 2001 to 2004 where economic indicators showed a loss of jobs with higher unemployment rates.

The current unemployment rate in Boston is 4.8, down from a high of 5.9 in May of 2003. Boston’s unemployment is typically above the state’s rate of 4.3 currently and 5.6 in 2003; however it also tends to be below the national average. From 2000 to 2003 an estimated 54,409 jobs were lost, unemployment estimates today suggest slow growth and recovery. According REIS, forecasts for the Boston economy are mixed. Employment is anticipated to grow 4.1% or 91,300 jobs, from 2004 to 2009. However, this still does not place Boston at pre-recession employment levels. The

---

Manufacturing, Telecommunications and Financial Services sectors are still showing losses; however a rise of temp-hiring is a hopeful sign of industry confidence\(^5\).

**Chart 3.**

![Boston Employment by Sector Chart](image)

**Labor Force, Income and Wages\(^6\):**

Boston has a labor force of 296,293, forty-three percent of which is employed in management or professional positions. The largest industry sector in the Boston economy is educational, health and social services (27 percent), followed by professional, scientific, management and administrative (15 percent) and finance, insurance and real estate (10 percent). Of the City’s ten largest private employers, seven are research/medical related, while two are educational institutions – illustrating the critical role these industries play to the local economy. According to 2000 Census data, the median household income in Boston was $39,629.

East Boston has a labor force of 17,801 and an unemployment rate of 7.3 percent, significantly higher than both the state and city’s figures. Thirty-two percent of neighborhood residents are employed in service occupations that are almost equally divided among all industry types – with education, healthcare and social services

---


representing the largest proportion of 13.3 percent. Ultimately, Logan International Airport anchors the East Boston economy. East Boston represents the lowest-income Census tract in the metropolitan Boston area. The median household income, according to 2000 Census data, is $30,013 – significantly below both the city’s median at $39,629 and the state’s at $50,502. The poverty coincides with these figures with 24.5 percent of the neighborhood’s households living below the poverty level, while the national figure is only 9.8 percent. These figures illustrate the enormous demand for affordable housing, which is discussed further under Supply Considerations.

_Education:_

The abundance of higher education institutions dominates the metropolitan’s educational system. The city has a long held a reputation of being one of the intellectual centers of the world. There are 36 colleges and universities within the city of Boston, including 4 public and 32 private. This figure does not include numerous other colleges in surrounding communities, such as Harvard University in Cambridge, which greatly contributes to the higher education community. Considering only the institutions within the city limits, there were 132,125 students enrolled in the fall of 2000. This concentration of students ranks among the top in the nation and the world and plays a critical role in the Boston economy. The Boston Redevelopment Authority quantified a $4.8 billion economic impact from these institutions, with direct student spending amounting to $773 million. The academic institutions provide numerous employment offerings, increase the out coming workforce and support the regional housing market.

Transportation:

The City is a major national and international air terminus, a seaport and serves as the hub for New England’s rail, truck and bus service. Three major interstate highways serve the city and connect it to national highway systems:

- US 90 (‘Massachusetts Turnpike) runs 138 miles east-west between Boston and the New York State border.
- US 95 is the primary north-south route between Portland, Maine and Washington DC.
- US 93 is a regional north-south route connecting Northern Boston to New Hampshire and Maine.

The city’s internal road system has been continually tested by the Central Artery Tunnel Project, which has had an enormous impact on transportation trends since its beginnings in 1983. The $15 billion project has been wracked with delays and budget problems, making this capital project dominate Massachusetts’ political climate. Its evolving completion status produces ever-changing traffic patterns throughout the city and will ultimately alter the face of Boston and all real estate markets along its path. As of March 2006, the project is considered 98 percent completed, with the following milestones being completed (refer to Exhibit B for East Boston “Big Dig” project map):

- I-90 extension connecting the Ted Williams Tunnel to Logan Airport and extending I-90 to 138 miles.
- The demolition of the old elevated Central Artery (I-93) to be converted to 27 acres of open space.
- After 14 years of construction all tunnels and bridges and their connections/ramps to surface roads are open to the public.

Construction continues on the I-90 and I-93 interchange, on the Dewey Square Tunnel, Logan Airport and Causeway Street ramps. In addition to the “Big Dig” the
Massachusetts Port Authority (Massport) has developed a long-range capital improvement program of approximately $250 million per year. The funds will be allocated to improvements to Logan Airport, the Toban Bridge, port facilities and other properties.\(^8\)

For residents of East Boston, access to the Boston’s Central Business District and points West, requires using Route 1A through the Sumner (accepting southbound traffic) or Callahan Tunnels (northbound traffic). Route 1A stretches one mile from the portals of these tunnels as a six-lane expressway over the streets of East Boston, then touches down at the McClellan Highway through Revere. It is approximately a five-minute drive from 266 Border Street to Government Center in downtown Boston. Despite this short time, both tunnels are tolled at $3.00 per car. However, East Boston residents who regularly take this route are eligible for the Resident Discount Program through the FastLane toll system, which reduces the fare to $0.40 per car.

\[\text{Big Dig Construction outside of the Callahan Tunnel} \quad \text{Ted Williams Tunnel}\]

The Massachusetts Bay Transportation Authority (MBTA) with commuter rail, subway and buses serving 1,038 square miles in eastern Massachusetts controls public transportation options. The “T” is comprised of five subway lines: the red line, green line, orange line, silver line (Boston’s first Bus Rapid Transit System) and the Blue Line. The Blue Line runs from downtown Boston at Cambridge and New

Chardon Street to Revere and through East Boston including Maverick Station, which is 0.6 miles from the subject site. Residents of East Boston can be in Boston’s downtown and financial district (Government Center) in seven minutes using the “T” system. There is also access to numerous bus lines, specifically the 114, 116, 117, 120 and 121, which crosses the entirety of East Boston. The fare for a single subway token is $1.25 with monthly passes costing $44.00. Almost 45 percent of East Boston residents take advantage of public transportation options, while 36 percent drive to their employment. Complete MBTA maps are included in Exhibit B.

Market Supply –

*Housing Stock, Housing Values and Land Use:*

The City of Boston has 251,935 housing units, an increase of only 1,070 units added since 1990. Total occupied units are 239,528, 30.7 percent of which are owner-occupied and 64.4 percent renter-occupied. As of 2000 census figures, Boston had a vacancy rate of 4.9 percent down from 8.9 percent from 1990. The mean household size has also decreased over the last ten years from 2.37 to 2.31 in 2000 for both owner and renter-occupied units. East Boston has a total of 15,078 housing units, which experienced a 1.8 percent growth since 1990. The neighborhood has a higher proportion of renter-occupied units than the city, with 71.9 percent and 28.1 percent owner-occupied. Utilizing 2000 Census figures, East Boston had a vacancy rate of 5 percent, roughly equal to the city’s, however down from 9.4 percent in 1990. The average household size also decreased in East Boston over the past ten years from 2.65 to 2.43.
While Boston has one of the largest populations in the nation, it is the second smallest major city when it comes to land area. Encompassing only 48.6 square miles, the city’s residential land use reflects its small geographic size and diversity. Residential land use totals 114,529 parcels or 36 percent of the total land in Boston. Of this 36 percent, East Boston represents 7 percent of the residential land use in the city, making it the fourth largest neighborhood in terms of residential land. While the city is predominately comprised of single-family units (35 percent), East Boston is comprised predominately of three-family units (28 percent) known as triple-deckers. Both the city and East Boston neighborhood account for roughly ten percent of land use dedicated to apartment dwellings\(^9\).

With a strong presence of students the metropolitan’s housing market is consistently strong. Many students prefer off campus housing options, while many recent graduates remain in the metropolitan area for employment. The shortage of dormitory beds, however, also contributes to the city’s housing demand. As students are forced into rental options, many of the neighborhood’s residents are displaced. This trend has created a ripple effect throughout the city as residents relocate due to

displacement and perceived neighborhood quality issues originating from the collegiate lifestyle.

While students sustain a great deal of the rental market, the residential ownership also remains strong. Residential sales prices showed an 11.8 percent increase since 2003 to $380,000. Despite rising costs, the city experienced a 52 percent increase in sales from 2003 to 2004. The majority of this increase is attributed to the rising demand for condominiums, which increased 61 percent since 2003. Triple-deckers experienced the largest increase in median sales price up 12.7 percent. East Boston has the highest concentration of this type of property in the city with sales having increased 115 percent over the past ten years. Triple deckers have become a popular investment choice as owners can occupy one unit, while renting the other two for income – yet this trend makes tracking housing data difficult in this neighborhood. East Boston specifically has experienced a 13 percent rise in median sales price from $331,750 in 2003 to $375,000 in 2004. This rise in cost was matched by a 35.3 percent increase in sales volume. Following its city lead, it was condominium sales that experienced the most volume growth, up 63.5 percent from 2003.\(^\text{10}\)

<table>
<thead>
<tr>
<th>Land Use</th>
<th>Boston</th>
<th>East Boston</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Square Feet</td>
<td>Land Parcels</td>
</tr>
<tr>
<td>Single Family Dwellings</td>
<td>153,637,364</td>
<td>29,660</td>
</tr>
<tr>
<td>Two-Family Dwellings</td>
<td>90,038,472</td>
<td>18,458</td>
</tr>
<tr>
<td>Three-Family Dwellings</td>
<td>57,300,968</td>
<td>15,801</td>
</tr>
<tr>
<td>Apartment Buildings</td>
<td>40,807,566</td>
<td>5,276</td>
</tr>
<tr>
<td>Condo Buildings</td>
<td>31,302,999</td>
<td>36,270</td>
</tr>
<tr>
<td>Vacant Land</td>
<td>38,192,083</td>
<td>8,395</td>
</tr>
<tr>
<td>Urban Renewal</td>
<td>10,808,353</td>
<td>669</td>
</tr>
<tr>
<td>BHA</td>
<td>16,332,242</td>
<td>n/a</td>
</tr>
<tr>
<td>Total Residential</td>
<td>438,420,047</td>
<td>114,529</td>
</tr>
</tbody>
</table>

With a small land area in the region, vacant residential land is rare. The City of Boston has a total of 38,192,038 square feet of undeveloped land, however only 52 percent of this is suitable for development. East Boston has 2,119,194 square feet of undeveloped land (or 5.5 percent of total undeveloped land in the city), however only 464,253 square feet or 22 percent is deemed “prime undeveloped residential land.” Of the sixteen Boston neighborhoods, East Boston ranks ninth in available developable land. Given this shortage, redevelopment options are increasingly becoming competitive options for financial success.\textsuperscript{11}

The Development Pipeline:
The East Boston neighborhood is currently undergoing an enormous transition, as developers are taking advantage of redevelopment opportunities along the Boston Harbor waterfront. This interest is slated to bring over 1,000 luxury units to East Boston by 2011. Currently there are five major residential and mixed use projects underway that will reshape the East Boston landscape. The Atrium Lofts, located less than one mile from the subject site was recently completed in the fall of 2005. With 217 condominium lofts, this property is the 218,200 square foot Goddess Bra factory that before redevelopment was surrounded by rusted and graffiti-splashed airport access ramps and a rundown adjacent soccer stadium. On a scale more comparable to

the Border Lofts, the Paris Flats located 0.8 miles away is another redevelopment of an existing 25,000 square foot warehouse into condominium loft units.

The remainder of new construction in East Boston is large scale projects that may not serve the same user as Border Lofts, but will serve as critical projects in the revitalization of this neighborhood and will ultimately serve as a further catalyst for attracting residents to this neighborhood. Portside at Pier One, less than one mile from Border Lofts, is a 585-unit residential community that is a key part of the planned East Boston waterfront revitalization. The project will redevelop an existing shipyard on Marginal Street, with a marina expansion and greenway for pedestrian and bicycle access. Both condominium and rental units will be available, with first floor retail. The Boston Redevelopment Authority considers this project to be the “flagship” of the East Boston Waterfront, however construction was significantly delayed due to appeals to the Environmental Protection Agency after the project threatened Essential Fish Habitat (EFH). The adjacent Clipper ship Wharf has also met with design delays, but is slated to offer 400 condominiums with ground level retail. The project will include 1,715 linear feet of harbor walk that will connect to Portside. Finally, the Hodge Boiler Works, a smaller project of 116 condominium units, is to be built around an atrium on a site once used to build ships’ boilers.

**Competitive Analysis** –

The massive revitalization attempts may alter the type of residents the neighborhood attracts; however triple-deckers, small apartment buildings and rehabilitated warehouses still dominate the landscape. Data associated with these properties are difficult to track given that they are generally not professionally managed nor advertised. The most advertised rental communities in proximity to the site are Maverick Landing and Chapman House Apartments. Maverick Landing, at 48 Border Street, offers one-bedroom apartments for $1,395 monthly and two bedroom units for $1,625. The property was the recent conversion of the former subsidized housing complex Maverick Gardens, greatly reducing local affordable housing and pressuring housing policy to compensate through new developments. Maverick
Landing is perhaps the most competitive and comparable property to this development due to its rental format, new units, waterfront views, proximity and price range. Next, Chapman House, located on Eutaw Street offers one, two and three bedroom apartments for $935, $1100 and $1500 respectively.

There are several other loft communities in East Boston, such as the Atrium Lofts and Paris Flats, both currently under construction and The Gumball Factory, a previously converted warehouse. However, all of these communities offer condominium ownership structures. It is anticipated that these properties, while providing similar product types, will not reach the same user, as Border Lofts will attempt to reach those unable or unwilling purchase property. Because these properties have some investor owners who consequently rent their units, it is still critical to understand these properties’ structures and amenity offerings.

Rental Analysis and Amenity Offerings:
Boston is known for its high cost of living and thus there is a persistent demand for affordable housing. During the 1994 to 2001 period, annual gains for both asking and effective rental rates averaged in the mid-7.0% range, with some years seeing double-digit increases. Rental rates however declined 3.3 percent across the city in 2004. The Department of Neighborhood Development suggests declining rates are due to a stabilizing market and increased housing supply.

East Boston rental rates dipped further, declining 4.3 percent from $1,150 to $1,100. The neighborhood currently has the lowest rental rates in Boston, significantly below the city’s average of $1,450. A compilation of East Boston classified rental listings revealed the average price of a one bedroom, two bedrooms and three bedrooms to be $926, $1,251 and $1,315 respectively. This compares to the median current asking rent of $1,773 according to REIS. Current asking rent per unit type is summarized below (for the complete REIS Apartment Asset Advisor Report please refer to Exhibit A).

---

Analysis of recent loft rentals throughout the Boston area reveals that the majority of loft floor plans are “open” allowing for no distinct sleeping quarters. Of these open lofts, the average rental rate was $2,505 monthly for 1,267 square feet of space. One-bedroom lofts had an average rental rate of $2,067 monthly for 1,000 square feet, while two-bedroom units on average charged $2,922 for 1,500 square feet of space. These rental rates are significantly above the averages for East Boston apartment rentals, however it can be assumed that the quality and amenities of these lofts far exceed the offerings of local triple-deckers and small apartment complexes.

### Community and Political Climate –
Community reaction to the renewed interest in East Boston development has been mixed. As discussed above, the displacement of low-income residents has been a consistent concern as affordable units are replaced by luxury developments. Community organizations such as NOAH (Neighborhood of Affordable Housing) have begun to purchase a great deal of East Boston real estate in an attempt to preserve low-income housing options and to ensure small business growth despite the real estate surge in the neighborhood. Acting on concerns over gentrification, East Boston residents have shown support for waterfront revitalization in exchange for public amenities packages, such as Pier One’s harborwalk. Waterfront access and density issues have dominated the neighborhood-developer negotiations. Numerous community organizations have formed in attempt to cleanup the Boston Harbor, surrounding green space and Chelsea Creek, currently the most polluted tributary flowing into Boston Harbor.

<table>
<thead>
<tr>
<th></th>
<th>Studio</th>
<th>1 BR</th>
<th>2 BR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Asking Rent/Unit</td>
<td>$1,228</td>
<td>$1,778</td>
<td>$2,283</td>
</tr>
<tr>
<td>Unit Size (sf)</td>
<td>526</td>
<td>751</td>
<td>1,069</td>
</tr>
</tbody>
</table>
The East Boston community is also well known for its public conflicts with Massport, which owns and operates Logan Airport. Local residents have battled MassPort for years over persistent attempts to expand airport runways – one expansion resulted in the community’s loss of Wood Island Park, a space designed by the famous landscape architect Frederick Law Olmsted\(^\text{13}\). Local citizens continue to battle the proposed addition of a fifth runway. The community’s activism was further displayed when a group of local women blocked Logan’s noisy construction trucks with their baby carriages. Noise as a result of airline traffic will be critical issue to manage during site marketing campaigns and will be discussed further with the full site analysis.

**Market Summary:**

Housing demand remains strong throughout metropolitan Boston and specifically in East Boston, where populations are growing rapidly. The decreasing household size throughout the region will also support housing demand, as more housing units are required per family. Further, improving economic conditions coupled with the declining housing affordability in Boston will serve to bolster the region’s rental market. Unmet demand is also apparent throughout the region’s colleges and universities. Insufficient supply for dormitory housing has created a ripple effect

throughout the city as students seek alternative options, slowly displacing neighborhoods residents. Demand indicators are moderately tempered by a full development pipeline for the East Boston waterfront, threatening to flatten rental rates in the coming year. These developments, however, will provide minimal rental product and should primarily serve to revitalize the area rather than reduce capture rates.
Product Recommendation and Design Elements:

After a thorough market and competitive analysis, it is recommended that the warehouse at 266 Border Street be redeveloped into mid-level luxury rental loft units. The need for this product is not only supported by market research, but further acknowledged by the East Boston Master Plan:

Upper income households appear to be reasonably well served by the ownership market but underserved in the rental markets… The feasibility of new luxury waterfront rental housing development is positive…Pricing is relatively affordable and there exist niche market opportunities such as water views, history, architecture, and tax credit eligibility potentials.\(^{14}\)

The suggested unit mix is as follows according to market data and a preliminary structural evaluation. To maximize rentable area and to stay true to loft architecture, each unit may have a unique floor plan and spatial arrangement. Suggested unit rents are slightly below the REIS rent comparables for Boston City to account for location and market conditions.

<table>
<thead>
<tr>
<th>Unit Type</th>
<th>Quantity</th>
<th>Size (sq. ft.)</th>
<th>Rent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Studio</td>
<td>4</td>
<td>750</td>
<td>$1,215</td>
</tr>
<tr>
<td>Affordable Studio</td>
<td>1</td>
<td>750</td>
<td>$900</td>
</tr>
<tr>
<td>One-Bedroom</td>
<td>14</td>
<td>950</td>
<td>$1,525</td>
</tr>
<tr>
<td>Affordable One-Bedroom</td>
<td>3</td>
<td>950</td>
<td>$1,050</td>
</tr>
<tr>
<td>Two-Bedroom</td>
<td>7</td>
<td>1500</td>
<td>$2,150</td>
</tr>
<tr>
<td>Affordable Two-Bedroom</td>
<td>1</td>
<td>1500</td>
<td>$1,400</td>
</tr>
</tbody>
</table>

\(^{14}\) East Boston Master Plan, Boston Redevelopment Authority, April 2000.
All units will have open floor plans and accentuate the design and architectural characteristics of the 1950’s warehouse, including but not limited to:

- 14’ ceilings
- Exposed brick interiors
- Exposed raw surfaces/ventilation ducts/beams
- Skylights on upper floors
- Rooftop garden/deck
- Stainless steel appliances
- Concrete countertops
- Open Shelving
- Walk-In closets
- Shared laundry center
- Assigned Parking

Sample Design Elements for Border Lofts
Leasing Strategy and Marketing:

The targeted consumer for Border Lofts is the young to middle-aged urban professional for whom living in a centrally located, upscale apartment in a rehabilitated warehouse holds fashionable appeal. It is anticipated that this market will include single professionals and ‘DINKs’ (dual-income no-kids) that are status driven, seeking unique living formats with convenient access to urban life – however those that lack the financial means or interest in purchasing. The lofts are equipped for live/work environments – with ample light and equipped with modern telecommunications – however the units will not be marketed specifically to this user. Because the units are rented not owned, there are restrictions for unit improvements and general wear that may not be suited for this market.

To reach the target market, promotional efforts for the redevelopment will focus on assets similar to the neighborhood. The East Boston Master Plan states, “East Boston’ current and future market positioning relies to a great degree on its competitive strengths, which include its proximity to downtown Boston and Logan International Airport, its waterfront location and facilities, its established businesses and institutions, its physical quality, and its relative affordability.” Advertising efforts will be primarily through independent channels. A banner will be displayed throughout construction to provide contact information for rentals. The majority of renters will be drawn from outside of the neighborhood and leasing will be heavily reliant upon rental agents. Local brokers and specialty Loft brokers such as A Boston Loft Company and Paragon Properties will also be contacted with the listings. This provides them with the opportunity to earn a commission of one-month’s rent for approved leases (standard Boston commission structure). It also allows for Internet advertising on company sites. In anticipation of weakened market conditions, funds to cover the commission costs are budgeted for which will serve as a rental incentive.
Site Analysis

East Boston has two main centers, Maverick Square on Sumner Street and Central Square on Porter Street. Maverick Square is serviced by the Blue Line “T” service and opens onto the Lewis Mall pedestrian way, featuring many of the small and family owned retail in the area. Central Square, 0.5 miles to the north of Maverick Square, is the home of 266 Border Street. Central Square is the major commercial center for East Boston; the “square” is in reality a traffic circle bordering open space and pedestrian walkways. The area is anchored by a major strip center, including Shaw’s Supermarket, CVS, and AJ Wright, plus there are numerous surrounding restaurants. Next to Shaw's is Liberty Plaza, which boasts access to the Harborwalk, where landscaped areas abut a small swatch of lighted path. This area allows the public wharf and harbor to mix, one of the few areas of its kind in East Boston.

The subject property is located on the west side of Border Street near the cross street of Lexington. The site is constrained by commercial uses to the south, including Shaw’s Supermarket and Liberty Plaza directly behind the site, and Institutional zoning to the north (the Umana Barnes Middle School, Umana School Park and Harborside Community Center). To the East across Border Street is a mix of triple-
deckers, small commercial and institutional uses such as the East Boston Branch Public Library. To the west of the site is the Boston Harbor; a single story warehouse stands between the site and direct harbor access.

Site constraints for 266 Border Street are primarily a result of a blighted community in need of infrastructure revitalization, rather than rezoning. Border Street, primarily serves as access to the “big box” commercial center of Central Square, however the majority of high traffic is routed down the parallel Meridian Street. Despite Border Street’s narrow and minimal traffic environment, the area is not pedestrian friendly. Site walks are only passable near the center of Central Square and along the west-side portions of Border Street. Road conditions are in need of updates as well. Street lighting is currently adequate for the site’s current use, but would need to be extended to serve a residential user. Noise as a result of local traffic is minimal; however a critical concern for the neighborhood is noise issues emanating from Logan airport.

---

To address noise issues, Massport’s Noise Abatement Office was established in 1977 to implement noise regulations and monitor neighborhood complaints. The Boston metropolitan area has 30 listening stations that gather data for Massport – 5 stations are located within the East Boston neighborhood. In 2004 East Boston logged 75 noise complaints as compared to Jamaica Plain and Hingham, which had the highest complaint level at over 375 complaints. Further, through flight path, carrier and runway use restriction and soundproofing technologies, Massport has reduced the number of people exposed to more than 65 decibels from 67,000 in 1987 to 7,200 presently. Given the full pipeline of new projects and a consistent residential population in East Boston, it does not appear that Logan airport noise will adversely affect absorption.

The site boasts numerous benefits despite the aged neighborhood and perceived issues surrounding Logan’s proximity. Most notable is the site’s proximity to the Boston Harbor waterfront and views. The waterfront is a wholly under utilized asset; attempts to rectify this are outlined below through East Boston’s Master Plan. An adjacent warehouse blocks the first two floors of the west building. However, upper

---

floors boats breathtaking views of the harbor and the Boston skyline. It is hoped that
in the near future an option to purchase the waterfront parcel will increase visibility
and projected long term returns. While sidewalks and pedestrian access needs
updating, the site is located within walking distance of all major services and
transportation needs, in addition to Liberty Plaza’s entrance to the Harborwalk for
waterfront enjoyment and exercise.


Due Diligence and Regulation

*City Planning and Zoning:*
There are four regulatory agencies regulating zoning and planning in the city of the Boston:

- Boston Redevelopment Authority which is the city’s Planning and Economic Development Agency
- Boston Zoning Commission is in charge of maintaining the zoning code and making textual or graphic changes
- Inspectional Services Department grants building permits and change in use or occupancy
- Board of Appeals hears appeals for changing the application of the zoning code

The Boston Redevelopment Authority, which anchors the planning of Boston, has a reputation for selectivity without justification. With no master or comprehensive plan for the city, developers and related contractors have little understanding of future goals as the BRA’s vision is unreleased until single developments are approved. The authority is slowly attempting neighborhood plans however and the first phase for East Boston was recently released. The Master Plan has set forth numerous goals to revitalize the neighborhood, most of which are hinged upon the success of the waterfront’s rehabilitation. Specific plans for Central Square include the rehabilitation of Liberty Plaza, which includes a proposed ferry dock to provide for water transportation to other East Boston waterfront attractions as well as the financial district. This will also serve to refresh access points to the Harborwalk that have been compromised by lack of upkeep. Central Square has also been active in the City of Boston’s Main Streets Program, which has promoted local business through marketing, signage and physical improvements like façade renovations.¹⁷

¹⁷ East Boston Master Plan, Boston Redevelopment Authority, April 2000.
The property at 266 Border Street is currently zoned “WC” or Waterfront Commercial, the purpose of which is to “ensure that the commercial areas located near the waterfront develop in a manner that is sensitive to and compatible with the goals for the waterfront.”\textsuperscript{18} Article 53 of the Zoning Code outlines permitted uses for this property; Multi-family is conditionally permitted in the Basement and First Story and allowed for the second story and above. This permitted use will require a conditional use for first floor residential units. With this zoning comes Tideland Requirements outlined in Chapter 19 of the East Boston zoning code, including waterfront open space requirements, specific environmental protection and safety standards and waterfront development reviews.

\textit{Easements and Utilities:}

It will be critical to examine easements affecting this property due to its configuration. This parcel of land between Border Street and Boston Harbor has two other warehouses each currently using the same entrance on Border Street. This will be a development issue to maintain isolated parking and to minimize interference from warehouse vehicles. Multiple owners own both warehouses; further information could not be obtained. Utility availability will also need to be researched in depth to ensure there is adequate support for the redevelopment. Utilities for the 30 units will have a much heavier storm/water/sewer requirement as compared to the previous industrial use. This factor will also increase construction costs, as the current property is not outfitted sufficiently for the mechanical and electrical needs of supporting 30 units.

\textit{Environmental:}

A phase I assessment will be required to determine the existence of any environmental liabilities, followed by a phase II assessment containing the recommendations for regulatory compliance and remediation should any issue be

uncovered. The environmental concerns associated with this redevelopment centers around previous tenancies. The building has historically been occupied for industrial and commercial uses, as do many of the neighboring properties. Each tenancy creates potential environmental liability concerns for current and prospective owners through the Comprehensive Environmental Response Compensation and Liability Act (CERLA).

Super Laundra-A-Mat most recently occupied the property on the first floor and A&M Paper Converting in the remainder of the property. Super Laudr-A-Mat functioned solely as a coin-operated laundry service, with no on-site dry cleaning operations, thus eliminating the risk of environmental contamination due to such chemicals as Perchloroethylene, Petroleum solvents (Stoddard solvents) and Trichloroethane. A&M Paper Converting is involved in the mechanical process of converting bulk paper to commercial uses and does not have the capability of pulping or bleaching on-site. Therefore there is little risk of contamination from sodium hydroxide, sodium sulfides, chlorine dioxide, peroxide or chlorine. It is anticipated that the highest risk for environmental liability will originate from tenants prior to the laundry mat and paper converter.

Further environmental compliance will be required due to the age and renovation activities planned for the property. Due to the probability of both lead paint and
asbestos being disturbed by the renovation process, both will need to be removed. To improve the site for residential use, all lead paint will be removed to comply with Massachusetts Lead Paint laws. Massachusetts requires the removal or covering of lead paint in residential properties built before 1978. The state has the second highest percentage of pre-1950’s rental housing in the country; therefore the state spends a great deal of resources ensuring compliance with state regulations.  

Asbestos removal will be another consideration due to the renovation of the site. Currently the asbestos is considered in “good repair” and non-friable, however due to the age and use of this warehouse. Construction and repair activity could cause damage to the asbestos containing material; it may be required to be removed prior to renovation. Compliance will be regulated through the Department of Environmental Protection (DEP) and Department of Occupational Safety (DOS). Further, a certified remover will also be required by EPA’s NESHAP (National Emission Standards for Hazardous Air Pollutants) to file waste shipment record.

Redevelopment and Construction Costs

Purchase Analysis –

266 Border Street has been on the market since March 2005 at an asking price of $3,749,000 ($107.42 psf). The Boston/Suffolk County Industrial Warehouse market posted 11.9% vacancy in third quarter 2005, a mild decrease from the YTD high of 12.4% in the first quarter. Warehouse deliveries have been consistently between 600,000 and 800,000 sf per quarter, with positive net absorption of 151,000. According to Costar’s Boston Industrial Market report, industrial properties between 25,000 and 99,000 sf have an average sales price of $69.44 psf with a 9.28% cap rate\(^\text{20}\). The average sales price has continually declined over the past year at a high of $80 psf. Boston area warehouse sales comparables show an average sales price of $118.02 psf for properties built between 1900 and 1950.

<table>
<thead>
<tr>
<th>Address</th>
<th>Neighborhood</th>
<th>Year Built</th>
<th>Size</th>
<th>Land Area</th>
<th>Sale Price</th>
<th>Per SF</th>
</tr>
</thead>
<tbody>
<tr>
<td>169-299 A Street</td>
<td>Boston</td>
<td>1916</td>
<td>107,780</td>
<td>2.047</td>
<td>$16,100,000</td>
<td>$149.38</td>
</tr>
<tr>
<td>121-127 Portland Street</td>
<td>Boston</td>
<td>1918</td>
<td>70,668</td>
<td>0.272</td>
<td>$6,600,000</td>
<td>$93.39</td>
</tr>
<tr>
<td>1001 Commonwealth Ave</td>
<td>Boston</td>
<td>1940</td>
<td>31,320</td>
<td>0.276</td>
<td>$4,258,100</td>
<td>$135.95</td>
</tr>
<tr>
<td>154-158 W. 2nd Street</td>
<td>Brighton</td>
<td>1920</td>
<td>48,624</td>
<td>0.961</td>
<td>$3,300,000</td>
<td>$67.87</td>
</tr>
<tr>
<td>126 N. Washington Street</td>
<td>Fort Point Channel</td>
<td>1910</td>
<td>10,800</td>
<td>0.050</td>
<td>$1,550,000</td>
<td>$143.52</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td></td>
<td></td>
<td><strong>53,838</strong></td>
<td><strong>0.721</strong></td>
<td><strong>$6,361,620</strong></td>
<td><strong>$118.02</strong></td>
</tr>
<tr>
<td><strong>Median</strong></td>
<td></td>
<td></td>
<td><strong>48,624</strong></td>
<td><strong>0.276</strong></td>
<td><strong>$4,258,100</strong></td>
<td><strong>$135.95</strong></td>
</tr>
</tbody>
</table>

The property is currently not functionally competitive in the market. Built in 1950, it has had few structural and capital upgrades and has poor ingress/egress for warehouse purposes. A purchase price of $3.3M is recommended based on sales comparables as listed above, market statistics and an assessment of the properties condition.


\(^{21}\) All Comparables found at [http://www.costar.com](http://www.costar.com).
AVERAGE WAREHOUSE SALES PSF | 266 BORDER PURCHASE PRICE
--- | ---
Costar Average Sales PSF | $69.44 | $2,423,456.00
Boston Warehouse Comparables | $118.02 | $4,118,898.00
**AVERAGE** | **$93.73** | **$3,271,177.00**
**Rounded** | **$3,300,000.00**

**Construction Costs**22 –

Construction costs for this project have been estimated at $6.1 million ($160 psf) based upon specific project needs, in addition to construction comparables from similar redevelopments. Review of several Urban Land Institute case studies of similar projects yielded an average cost of $135 psf. This figure, while below Border Lofts’ cost estimate, is reflective of less costly markets such as Pittsburgh and Cincinnati. Please refer to Exhibit C for detailed cost comparables and itemized development budget. Tax credits of $1.2M (20% of qualified rehabilitation expenditures) were deducted from development costs because this project qualifies for historical rehabilitation.

**Development Budget Estimate -**

<table>
<thead>
<tr>
<th>Border Lofts Development Budget</th>
<th>Cost</th>
<th>$/PSF</th>
</tr>
</thead>
<tbody>
<tr>
<td>Site Improvements (including purchase):</td>
<td>$5,616,450</td>
<td>160.84</td>
</tr>
<tr>
<td>Construction Costs:</td>
<td>$350,715</td>
<td>10.04</td>
</tr>
<tr>
<td>Soft Costs:</td>
<td>$119,480</td>
<td>3.42</td>
</tr>
<tr>
<td>Financing Costs</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Development Costs:</td>
<td>$6,086,645</td>
<td>174.30</td>
</tr>
<tr>
<td>Less 20% Tax Credit</td>
<td>$1,217,329</td>
<td></td>
</tr>
<tr>
<td><strong>Net Development Costs</strong></td>
<td><strong>$4,869,316</strong></td>
<td><strong>139.52</strong></td>
</tr>
</tbody>
</table>

---

22 Construction estimates from compiled loft redevelopment case studies through the Urban Land Institute at [http://207.86.218.154/dcs_frameset_master.html](http://207.86.218.154/dcs_frameset_master.html), accessed 31 August 2005.
Redevelopment Schedule:

It is estimated that the entire project will take eighteen months through due diligence, permitting, construction and lease-up. Leasing should begin approximately 6 months prior to completion. Again this estimate is based on the specific variables for this project including due diligence, as well as estimates from comparable loft redevelopments.
Property Input Assumptions

All property assumptions used to value this redevelopment and estimate stabilized cash flows are included below. Please refer to Exhibit E for a complete set of Argus reports.

Vacancy and Collection Loss:
A vacancy rate of 5% was used to estimate revenue loss due to market conditions as estimated from 2000 census overall apartment vacancy figures for Boston. It is noted that any higher occupancy rate does not allow for adequate rollover and rental escalations. Collection loss is estimated at 2% due to the difficulty of assessing credit risk for residential renters, including the young age group the property will be marketed to.

Operating Expenses and Fixed/Variable Rates:
(Please refer to Exhibit D for complete inflation indices – all CPI indices used for the Boston-Brockton-Nashua MSA):

- General Inflation was calculated at 3.37%, using the CPI index for all urban consumers.
- Insurance is estimated at $320/unit in year one and will use the general inflation rate of 3.37%. This is a 100% fixed expense.
- Property Management is estimated at 3% of the Effective Gross Income, it is a 100% fixed expense.
- Utilities for common areas are estimated at $2,200/unit in the first year of analysis and will inflate at 4.12% based on CPI for fuels and utilities. Common area utilities are a 100% fixed expense. All unit specific utilities (except for water) are paid directly by the tenant.
- Repairs and Maintenance are estimated at $2,457/unit and will inflate at 3.33 yearly based on U.S. Cities average CPI household operations inflation.
• Real Estate Taxes are $594/unit. Real Estate taxes are 100% fixed and will not vary by occupancy level.

**Capital Expenditures:**

It is assumed that this building will be fully restored and all major capital items including HVAC, roof, and apartment appliance upgrades will not be necessary in the first ten years of the analysis. A replacement reserve of $185 per unit was applied to the analysis to allow for unforeseen repairs and maintenance not included in operating expenses and as suggested by the loaning institution.

**Additional Revenue:**

• Application Fees – A nonrefundable fee of $50 will be charged to each applicant to cover credit and administration costs to process incoming tenants. This revenue however, will not be received if the tenant applies through a private broker.

• Parking – One assigned parking space per unit is available for $125 monthly for $3,750 of additional miscellaneous income.

**Market Leasing Assumptions:**

All market-rate units are assumed to renew at a 95% probability, while affordable units are assumed to renew at 100% probably, both at 12-month terms. Market rents inflate at the global rate (3.37%) and preparation costs are estimated at $100 per unit at rollover. For the purposes of this analysis, a half-month downtime was assumed between tenant rentals.

**Capitalization Rates:**

A going-in capitalization rate of 7.00% was applied to the financial analysis. This figure is supported by interview with Boston area brokers and Chris Chandor, a Trammel Crow Development Manager specializing in this market. Korpacz’s Fourth Quarter 2005 Investor Survey also reports rates between 4.50% and 8.00%, with an average of 6.13% for the national apartment market. A 7.25% was applied as the
reversionary capitalization rate for the ten-year analysis. Korpacz reports this rate
between 5.50% and 9.00% with a national average of 7.31%; this report can be
accessed in Exhibit D.
Financing quotes were obtained from East Boston Savings Bank (“EBS”), local to the site, and BB&T, a national lender. Below are the quoted financing structures for construction, permanent, “mini-perm” and mezzanine financing. EBS quoted a recourse construction loan at 8.5% (Libor plus 100 basis points) for 80% loan-to-cost of total project costs through lease-up. The quote included two extension periods, which are critical given the unknown of redevelopment timelines. BB&T offers a slightly lower rate of 7.85% for a construction loan, at 75% loan-to-cost, requiring more equity investment upfront.

Permanent loan quotes were provided from both lenders, with EBS offering 25 basis points lower than BB&T and all other terms remaining identical. After review of these financing costs, EBS was chosen for its locality and relationship with regional political and development figures. EBS has quoted a higher rate for construction financing however will cover a greater proportion upfront. EBS also stands to offer a lower rate on take-out financing. Using one lender for comprehensive funding will benefit this development, in that East Boston Savings Bank will have an increased stake in the project’s success and should exhibit more flexibility through the development process.
### Construction Loan Quotes –

<table>
<thead>
<tr>
<th></th>
<th>East Boston Savings Bank</th>
<th>BB&amp;T</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost Structure</td>
<td>Prime + 100</td>
<td>Libor+300</td>
</tr>
<tr>
<td>Actual Cost</td>
<td>8.5%</td>
<td>7.85%</td>
</tr>
<tr>
<td>Fee</td>
<td>1.00%</td>
<td>1.00%</td>
</tr>
<tr>
<td>Extension</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Extension Cost</td>
<td>0.50%</td>
<td>0.25%</td>
</tr>
<tr>
<td>Number of Extensions</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Maximum LTC</td>
<td>80%</td>
<td>75%</td>
</tr>
<tr>
<td>Acceptable Mezzanine</td>
<td>10%</td>
<td>To be</td>
</tr>
<tr>
<td>Debt</td>
<td></td>
<td>determined</td>
</tr>
<tr>
<td>Required Cash Equity</td>
<td>10%</td>
<td>15%</td>
</tr>
<tr>
<td>Recourse</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Non Recourse</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

(As of 1/06)

Prime 7.25%

Libor 4.85%
### Permanent Loan Quotes –

<table>
<thead>
<tr>
<th></th>
<th>East Boston Savings Bank</th>
<th>Laureate Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan Term (Years)</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Amortization (Years)</td>
<td>25</td>
<td>25</td>
</tr>
<tr>
<td>Cost Structure</td>
<td>10 Yr. Treasury</td>
<td>10 Yr. Treasury</td>
</tr>
<tr>
<td></td>
<td>+220</td>
<td>+250</td>
</tr>
<tr>
<td>Actual Cost</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fee</td>
<td>1.00%</td>
<td>1.00%</td>
</tr>
<tr>
<td>Maximum LTV</td>
<td>80%</td>
<td>80%</td>
</tr>
<tr>
<td>Acceptable Mezzanine Debt</td>
<td>10%</td>
<td>5%</td>
</tr>
<tr>
<td>Required Cash Equity</td>
<td>10%</td>
<td>15%</td>
</tr>
<tr>
<td>DSCR</td>
<td>1.25x</td>
<td>1.25x</td>
</tr>
<tr>
<td>Recourse</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Non Recourse</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

(As of 1/06)
10 Yr. Treasury 4.35

### Mini-Perm Quote –

<table>
<thead>
<tr>
<th></th>
<th>East Boston Savings Bank</th>
<th>Laureate Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Term (Years)</td>
<td>3-5</td>
<td>5</td>
</tr>
<tr>
<td>Amortization (Years)</td>
<td>25</td>
<td>25</td>
</tr>
<tr>
<td>Cost Structure</td>
<td>3 or 5 Yr. Treasury</td>
<td>N/A</td>
</tr>
<tr>
<td>Loan Cost</td>
<td>2.75%</td>
<td>N/A</td>
</tr>
<tr>
<td>Fee</td>
<td>0.50%</td>
<td>1.00%</td>
</tr>
</tbody>
</table>

### Mezzanine Debt

<table>
<thead>
<tr>
<th></th>
<th>East Boston Savings Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan Cost</td>
<td>12%</td>
</tr>
<tr>
<td>Fee</td>
<td>2%</td>
</tr>
</tbody>
</table>
Investment Analysis and Risk Factors

To determine an appropriate discount rate for this analysis, the formula \( RFR + B \times (R_m - RFR) \) was used to calculate the cost of capital with an adjustment for risk factors specific to this market and the Border Lofts redevelopment. The following risks have been quantified into a total of 50 basis points to total a discount rate of 10.01. This figure remains consistent with fourth quarter 2005 national apartment market rates, which were reported to be between 6.00% and 13.00% by the Korpacz Real Estate Survey found in Exhibit D.

- Economic Risk is composed of demand and supply factors influencing the Boston multifamily market. As presented in the market analysis, demand factors remain strong. Boston has a consistent user base for multifamily product allowing vacancy rates to remain stable at roughly 5% over the past decade. East Boston specifically has experienced rapid population growth; however the region is forecasted to see little employment and population growth as a whole. While demand remains consistent, East Boston is threatened with oversupply due to the substantial increase of multifamily construction in the region. With a local economy that is small in size, the fortunes of individual companies, property owners and industries are vulnerable.\(^23\)

- Liquidity risk is a critical consideration for all real estate investments as there is no guarantee of disposition, especially at favorable conditions. Difficultly with liquidation brings the risk of lower returns if there is weak demand for multi-family property in this submarket. Border Lofts, being a unique and specialized product could be more susceptible to market reactions because this product cannot be easily adapted to alternative uses. Boston has consistently remained a strong market for multifamily product given its consistent user

\(^{23}\) East Boston Master Plan, Boston Redevelopment Authority, April 2000.
base, however East Boston’s market remains hinged upon its “up and coming” status proving successful.

- Location risk comprises local, state and federal regulations pertaining to the political, legal, environmental and zoning mandates affecting this project. These factors while highly uncontrollable can be sufficiently monitored to reduce risk. Political and regulatory risk is sufficient for Border Lofts given the nature of the redevelopment and an involved entitlement process. Further risk is associated with ensuring compliance to gain tax credits, which are critical to financial feasibility of this project. Environmental risk, as briefly described earlier, is palpable due to contamination risk associated with previous tenants and the risk of unforeseen redevelopment costs associated with the physical rehabilitation of this structure. Zoning risk is mild due to relaxed zoning codes in the East Boston submarket; further there exists political and community support for neighborhood revitalization projects.

- Business and Management risk is defined by factors affecting the income and operating of Border Lofts. Because this is a small property, minimal support staff for management would be required and the majority of leasing responsibility falls upon private brokers in the Boston market. It is recommended that this project be structured through a joint venture partnership, thereby decreasing personal risk to the equity investor; however this increases business risk as management power is compromised.

- Long Term Cash Flow Risk is mild due to the stable nature of the multifamily market in Boston. Cash flows will show little volatility due to consistently low vacancy rates, however rental rates are at risk of flattening due to new unit deliveries. Because most new product is condominiums, rental rates should not decline. Lease expirations poses a significant risk to operations as all lease terms are 12 months leading to a high probability of multiple units rolling in the same month or timeframe. This risk should decline the longer
the property is held, as leases will naturally become staggered with unanticipated lease terminations. Operating expenses are primarily built into rental rates and risk should be minimal, as the property should be operating efficiently due to functional upgrades.
Border Loft Valuation and Summary of Cash Flows:

Based upon the loan quotes obtained from EBS and the Argus assumptions previously outlined an unleveraged present value of $5.53M ($158 psf) was concluded using a 7% going-in cap rate as supported by local brokers and national apartment indices. Of the value, 41% is reliant upon prospective income and 59% of value is upon resale – making this a stable income producing property with little risk of cash flow volatility after stabilization. The present value was based upon stabilization in June 2007. Net Operating Income in year one is $157,000 with five-year NOI growth of 34.5%; year one Cash Flow before Financing is $148,000. The average cash-on-cash return over the holding period is 9.3%.

<table>
<thead>
<tr>
<th>Pro Forma Stabilized Operating Statement</th>
<th>1st Stabilized Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Potential Revenue</td>
<td>$511,670</td>
</tr>
<tr>
<td>Operating Expenses</td>
<td>$129,817</td>
</tr>
<tr>
<td>Net Operating Income</td>
<td>$381,853</td>
</tr>
<tr>
<td>Leasing &amp; Capital Costs</td>
<td>$2,822</td>
</tr>
<tr>
<td>Cash Flow Before Debt Service</td>
<td>$379,031</td>
</tr>
<tr>
<td>Debt Service</td>
<td>$360,049</td>
</tr>
<tr>
<td>Cash Flow After Financing</td>
<td>$18,982</td>
</tr>
</tbody>
</table>

Cash flows throughout the holding period show no volatility due to the stable multifamily market in Boston, consistently low vacancy rates and no major capital improvements required in the first ten years. The challenge will be to secure affordable construction financing through lease-up to support the lack of income.

No multi-family sales comparables were available for the East Boston market; however an analysis of Boston area sales comparables reveals an average
sales price of $5.9M ($211 psf). The average sales price is significantly above Border Loft’s valuation due to the higher rents obtained in the represented markets, specifically in Brookline and Cambridge.

<table>
<thead>
<tr>
<th>Address</th>
<th>Neighborhood</th>
<th>Year Built</th>
<th>Building Size</th>
<th>Land Area</th>
<th># of Units</th>
<th>Sales Price</th>
<th>Sales per SF</th>
</tr>
</thead>
<tbody>
<tr>
<td>89-95 Park Drive</td>
<td>Boston</td>
<td>1910</td>
<td>29,128</td>
<td>0.308</td>
<td>48</td>
<td>$8,245,581</td>
<td>$283.08</td>
</tr>
<tr>
<td>149-151 Park Drive</td>
<td>Boston</td>
<td>1910</td>
<td>34,092</td>
<td>0.303</td>
<td>48</td>
<td>$7,466,561</td>
<td>$219.01</td>
</tr>
<tr>
<td>37-41 Wendell Street</td>
<td>Cambridge</td>
<td>1930</td>
<td>35,415</td>
<td>0.610</td>
<td>39</td>
<td>$7,250,000</td>
<td>$204.72</td>
</tr>
<tr>
<td>94 Queensberry Street</td>
<td>Fenway</td>
<td>1919</td>
<td>21,310</td>
<td>0.151</td>
<td>33</td>
<td>$5,280,000</td>
<td>$247.77</td>
</tr>
<tr>
<td>48 Glenville Ave</td>
<td>Allston</td>
<td>1910</td>
<td>30,785</td>
<td>0.205</td>
<td>37</td>
<td>$5,200,000</td>
<td>$168.91</td>
</tr>
<tr>
<td>15-17 Lothian Road</td>
<td>Brighton</td>
<td>1930</td>
<td>32,535</td>
<td>0.206</td>
<td>29</td>
<td>$4,900,000</td>
<td>$150.61</td>
</tr>
<tr>
<td>17-21 Worcester Square</td>
<td>Boston</td>
<td>1910</td>
<td>16,200</td>
<td>0.146</td>
<td>15</td>
<td>$4,800,000</td>
<td>$296.30</td>
</tr>
<tr>
<td>10 Armington Street</td>
<td>Allston</td>
<td>1920</td>
<td>31,644</td>
<td>0.440</td>
<td>25</td>
<td>$3,800,000</td>
<td>$120.09</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td></td>
<td></td>
<td>28,889</td>
<td>0.296</td>
<td>34</td>
<td>$5,867,768</td>
<td>$211.31</td>
</tr>
<tr>
<td><strong>Median</strong></td>
<td></td>
<td></td>
<td>31,610</td>
<td>0.306</td>
<td>44</td>
<td>$7,358,281</td>
<td>$233.39</td>
</tr>
</tbody>
</table>

24 All Comparables found at [http://www.costar.com](http://www.costar.com).
Investment Structures and Returns:
Financial feasibility is defined as the ability for this project to generate enough cash flow to able to pay its debt service and provide a 15% minimum return on the invested equity to justify the associated risks defined above. To determine the maximum yield for this redevelopment, four financing/investment structures were analyzed. Each capitalization strategy assumed financing from East Boston Savings bank at the terms discussed on pages 37-38. With construction costs determined to be $4.9M, based upon an 80% LTC, a construction loan of $3.9M would be financed. Assuming an average outstanding balance on this loan of 50% and interest only payments, total interest carry through the development phase is estimated at $250,000. Upon completion and lease-up, EBS permanent financing would offer 80% LTV. Argus cash flow assumptions yield an unleveraged present value of $5.53M at stabilization using a 7% cap rate as suggested by local brokers and national indices. Total construction costs are below the maximum LTV of the project and results in $470,000 in appreciation upon take-out.

<table>
<thead>
<tr>
<th>Total Construction Costs</th>
<th>$5,529,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction Loan (80% LTC)</td>
<td>$4,423,200</td>
</tr>
<tr>
<td>Unleveraged Present Value (7% Cap Rate)</td>
<td>$4,944,000</td>
</tr>
<tr>
<td>Permanent Financing (80% LTV)</td>
<td>$3,955,200</td>
</tr>
<tr>
<td>Appreciation</td>
<td>$468,000</td>
</tr>
</tbody>
</table>
I. **100% Equity**

An investment structure with a full equity contribution would require $5.53M of investment. The direct capitalization of year 11 Net Operating Income produces a resell value of $6.73M less 4% selling expenses for $6.46M in net proceeds from sale. This investment structure produces an 8% IRR, significantly below the investor’s required return.

II. **80% Debt + 20% Equity**

This investment structure utilizes $4.42M of leverage with $1.11M of equity to fund this project. Net proceeds from sale would be $3.2M after the senior debt payoff of $3.8M. This use of leverage results in an equity IRR of nearly 12% with $2.42M in gross profit on equity. This structure successfully supports the annual debt service of $360,000, however underwriting requirements of a minimum Debt Service Coverage Ratio (DSCR) of 1.25x are not satisfied until year 7. The average DSCR over the analysis period is 1.22x; escrowed reserves will most likely be required by the lender to compensate.

III. **80% Debt + 15% JV Equity + 5% Equity**

A joint venture equity partner would be introduced in this structure to contribute $830,000 (75% of required equity), reducing the investor’s equity contribution to only $275,000 (25% of required equity). This structure assumes a 10% preferred return, with equal split of returns thereafter. Preferred returns are distributed to the equity positions, however this project does not provide surplus returns. The JV equity partner will receive a gross profit upon sale of $1.25M and an equity IRR of 9.2%, most likely considered to be below a reasonable hurdle rate given the risk. The return on investor equity is 20.5% with $1.64M in gross profit. This return surpasses the minimum required return, however the project stands to be significantly complicated by management and decision making compromises.
IV. 80% Debt + 10% Mezzanine Debt + 10% Equity

The introduction of mezzanine financing, reduced the equity contribution to $550,000, however the cash flows from this project do not support the cost of $95,000 for additional mezzanine leverage at 12%. An 11% IRR is achieved upon sale, however, this structure could not be underwritten as the junior debt service is not covered until year 9.

To achieve a 15% return on equity invested it is recommended that this project proceed with a JV equity partner. If management control is deemed to be a priority, it is suggested that the appreciation upon take out be applied to the senior loan to reduce debt service and increase annual cash return to the investor. When the total debt is reduced $460,000, the yearly debt payments are reduced from $360,000 to $322,000 and the average DSCR is increased from 1.22x (below the minimum 1.25 underwritten DSCR) to 1.36x. This strategy would allow the investor to maintain management control over this project while reaching the required 15% return.
Summary Conclusion

It has been determined that East Boston is an evolving market that will support this redevelopment due to Border Lofts’ superior harbor-side location, convenience to Boston’s central business district and its unique rental format. This project, however, must overcome the challenge of the high cost of converting this warehouse to a more productive use. The regulatory limitations and conditions to comply with historical renovation and affordable housing requirements will add significant risk to the development. These factors, however, remain critical to maintain community support and ultimate benefit to neighborhood revitalization.

Border Lofts is financially feasible under the assumptions utilized in this study, however financial returns are reliant upon JV equity contributions or the reduction of senior debt payments through further investor equity contributions of property appreciation. The project remains highly susceptible to changing economic fundamentals and it is recommended that a Cap and Collar policy be purchased to reduce interest rate sensitivity as the property’s cash flows are already stretched to support debt service. In addition, due to the inherent risk of redevelopment in a highly charged political community, it is recommended that further sensitivity analyses be completed prior to project approval.

This project is recommended to proceed and should positively contribute to neighborhood revitalization while providing adequate investment returns. With limited land options for new development in the city of Boston, risk tolerance must be adjusted to tolerate the challenges of urban redevelopment.