

**MARKET ANALYSIS AND FEASIBILITY STUDY FOR A  
MIXED-USE DEVELOPMENT  
IN SANTA CRUZ, CA**

by  
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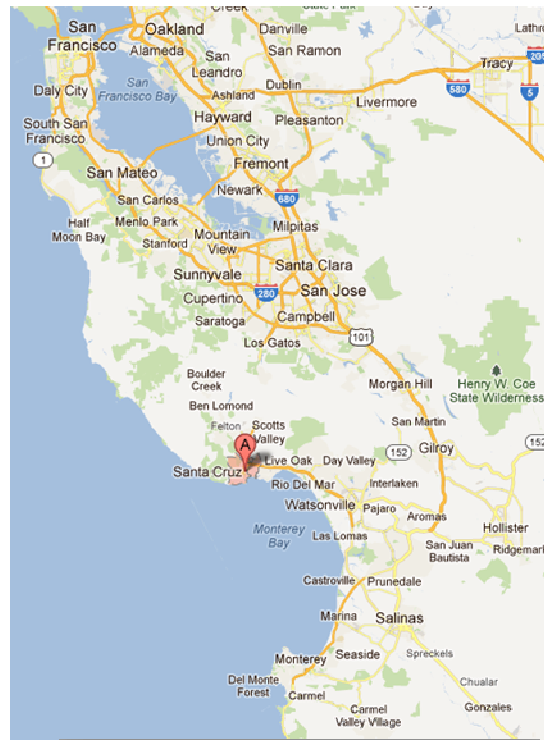
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## Executive Summary

Now is an excellent time to invest in Santa Cruz real estate. Prices are at 10-year lows, but have stabilized, financing is cheap, and rents are growing again. The population is growing with the expansion of University of California, Santa Cruz and the increase in tourism that comes with economic recovery. Yet despite the increased need for housing, supply is perennially constrained. Santa Cruz is surrounded by protected land (and ocean) that provides a bulwark against urban sprawl. Vacant land is scarce.

As a result, the City's General Plan encourages infill development and repurposing of existing structures, especially for mixed-use projects. It also identifies specific areas of the City, such as along the San Lorenzo River, where redevelopment is encouraged with higher density allowances.

A search of these areas identified 408 Front St as an ideal candidate for redevelopment. It is located in the Central Business District (CBD), on west bank of the San Lorenzo, and adjacent to Pacific Ave, the premier shopping district of Santa Cruz. The site is underutilized with a poorly designed, single-story retail building with a single tenant (Sherwin-Williams).



*Figure 1: Santa Cruz is in close proximity to, but separated from, nearby major metropolitan areas (Source: Google Maps)*

Its location and market conditions make it ripe for redevelopment into a mixed-use retail and residential building.

The following report describes the rationale used to zero-in on this investment opportunity and provides a comprehensive analysis to determine its feasibility. Presuming potential investors are unfamiliar with Santa Cruz, it begins with a macro-level market overview and an introduction to the City's land-use policies and goals,. Current real estate statistics and trends are reviewed, as well as opinions of local professionals, to confirm that now is a good time to enter the market. The report then narrows down specific geographical areas from which to select potential sites for development and ultimately identifies 408 Front St as the target property.

Review of current price trends, realistic estimates of acquisition, construction and finance costs are used to determine how best to develop the site to maximize return on investment while complying with local design requirements. Conservative assumptions are used to project income and expenses and determine the expected Net Present Value (NPV) and Internal Rate of Return (IRR).

Final analysis shows the 408 Front St to be an \$8.26 million project, requiring an investment of \$3.5 million of owner equity to provide a 15% IRR and \$780 thousand NPV using a 12% discount rate. It offers strong returns for a reasonable risk, making it an attractive investment opportunity.

## Market Overview

Santa Cruz, CA is located in Northern California on the northern edge of Monterey Bay. It is the county seat of Santa Cruz County and is renowned for its natural beauty, beach-side attractions, alternative lifestyles, and the liberal leanings of its residents.<sup>1</sup> Although it is within 65 miles of



Figure 2: City Seal (source: Wikipedia)

San Francisco and only 20 miles of San Jose, mountainous terrain, protected nature preserves, and limited transportation networks leaves the Santa Cruz separate and distinct from its larger neighbors.<sup>2</sup> The city proper is 12 square miles<sup>3</sup> and is home to the University of California, Santa Cruz (UCSC) and approximately 60 thousand people, including 16,000 university students.<sup>4</sup>

## Demographics

Santa Cruz's population racial mix is 75% white, 2% African American, 8% Asian, and 15% other. Approximately 32% of adults are married, 11% divorced, 3% widowed, and 54% single, never married.<sup>5</sup> The average age is 29.9.<sup>6</sup> Both the lower than usual average age and the high proportion of single, never married can be attributed to the UCSC student population.<sup>7</sup>

<sup>1</sup> Wikipedia, *Santa Cruz, California*, [http://en.wikipedia.org/wiki/Santa\\_Cruz,\\_California](http://en.wikipedia.org/wiki/Santa_Cruz,_California) (January, 2012).

<sup>2</sup> Google Maps, <http://maps.google.com/maps?hl=en&tab=wl> (February 2012).

<sup>3</sup> Santa Cruz County CA Press Room, *Facts, Stats, FAQs*, <https://santacruz.org/press/facts-stats-faqs.php> (February, 2012).

<sup>4</sup> University of California, Santa Cruz, *Facts & Figures*, <http://www.ucsc.edu/about/facts-figures.html> (February, 2012).

<sup>5</sup> U.S. Census Bureau, *Marital Status, 2008-2010 American Community Survey 3-Year Estimates*.

<sup>6</sup> U.S. Census Bureau, *General Housing Characteristics: 2010, Santa Cruz city, California*.

<sup>7</sup> U.S. Census Bureau, *Profile of General Population and Housing Characteristics: 2010, Santa Cruz city, California*.

The City is comprised of 22 thousand households with just over 10 thousand (46%) family households and 4,817 (22%) with children under 18. Non-family households numbered 11,652 (54%), and of those, 6,773 (31%) had single occupants.<sup>8</sup> Median household income is \$69,247 and approximately one-third have incomes over \$100,000.<sup>9</sup> (See Appendix A for detailed demographic data.)

## **Lifestyles**

Market researchers segment households by different lifestyles as a way to describe populations. A large proportion of Santa Cruz residents (44%) are characterized as “Urban Chic” by market researchers, meaning they tend to be white, affluent, well educated, professionals “[who] stay physically fit, own Apple computers, drink premium wines and Starbucks coffee, take advantage of city life, visit museums....” Many have families and own their homes.<sup>10</sup>

“Trendsetters,” the next largest group (22%), are similar to Urban Chic households, are also well-educated, white-collar professionals, but are more racially diverse, younger, mobile and on the “cutting edge of urban style.” They tend to prefer renting over home ownership and concentrate in upscale, urban, multi-unit housing.<sup>11</sup>

The last major lifestyle in Santa Cruz is referred to as “Old and Newcomers.” They make up 9% of the households and are typically renters found in neighborhoods in transition with more single-person and shared households than families. They tend to be less educated and

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<sup>8</sup> U.S. Census Bureau, *Profile of General Population and Housing Characteristics: 2010*

<sup>9</sup> Ibid.

<sup>10</sup> Gibbs Planning Group, Inc. , *City of Santa Cruz Retail Market Analysis*, Santa Cruz Redevelopment Agency, September, 2011.

<sup>11</sup> Ibid.

affluent than the other groups and are either young, at the beginning of their careers, or older, approaching retirement.<sup>12</sup>

## Employment

The main industries in Santa Cruz are education, government, tourism, and technology, employing 29,500 people.<sup>13</sup> The largest employer in the county is UCSC, with its 2,030 acre campus located on the northwest edge of the city.<sup>14</sup> The university employs 7,364 people, including 500 faculty, supporting over 16,000 students.<sup>15</sup> It is estimated to have an economic impact of \$960 million annually and supports an estimated 13,415 non-university jobs in the region.<sup>16</sup> (See Appendix B for employment statistics by job type and location.)

Since UCSC's founding in 1963, it has been the primary driver in the growth of Santa Cruz.<sup>17</sup> As the city's largest employer and with a student body that represents 29% of the population, UCSC is a major factor in practically every aspect of city management, including new development.

Santa Cruz and UCSC seem to have a strong partnership, but the City has no jurisdiction over the campus (which is governed by state law and University of California Regents' policy).<sup>18</sup> While the City's General Plan refers to many initiatives and partnerships with the University, it also defers to



Figure 3: UCSC Mascot, the Banana Slug (source: UCSC Admissions)

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<sup>12</sup> Ibid.

<sup>13</sup> City of Santa Cruz, California, *Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2011*, 175.

<sup>14</sup> UC Santa Cruz, *Long-Range Development Plan 2005-2020*, Final Draft, September 2006, 31.

<sup>15</sup> Wikipedia, *Santa Cruz*.

<sup>16</sup> University of California, Santa Cruz, Office of Planning and Budget.

<sup>17</sup> UC Santa Cruz, *Long-Range Development Plan 2005-2020*, 16.

<sup>18</sup> Ibid, 23.



the UCSC Long Range Development Plan (LRPD) on many issues and uses it as a foundation for projecting the future needs of the Santa Cruz community.



*Figure 4: Ariel View of UCSC Campus (Source: UCSC Long Range Development Plan)*

For its part, the LRPD also acknowledges the UCSC's partnership with the City and specifically cites cooperation on growth issues, such as infrastructure capacity, traffic, parking, and housing.<sup>19</sup>

In regards to housing, the LRPD acknowledges the increasing housing demand spurred by UCSC growth coupled with the paucity of vacant land available for development. Student enrollment is projected to grow 22% to 19,500 by 2020 with a corresponding increase in faculty and staff.<sup>20</sup> The aggressive growth of UCSC bodes well for the Santa Cruz economic future and the market for student housing.

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<sup>19</sup> Ibid.

<sup>20</sup> Ibid, 7.

## Tourism

After UCSC, tourism represents the second sector of the City's economy. Santa Cruz is a regional tourist destination, offering beach attractions (including wharf and boardwalk amusement park), vibrant shopping and dining venues, state parks with redwood forests, and many outdoor recreational activities (such as surfing, hiking, biking, etc.). Tourism contributes over half a billion dollars annually to the local economy.<sup>21</sup> The city draws 76% of overnight visitors from within California, 16% from other states, and 8% from foreign countries.<sup>22</sup>



Figure 5: A Local Landmark, the Downtown Clock Tower (Source: Localism.com)

## City Districts

For the purpose of market analysis, Santa Cruz can be subdivided into four main districts, each with its own characteristics:

**Downtown:** Highlighted by the distinctive clock tower on Pacific Ave, downtown Santa Cruz is a vibrant urban center that includes a historic shopping district with over 200 retail stores and restaurants, music venues, movie theaters, as well as the Museum of Art and History.<sup>23</sup>

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<sup>21</sup> Santa Cruz County CA Press Room.

<sup>22</sup> Lauren Schlau Consulting, *Santa Cruz County Visitor Profile*, presented to Santa Cruz County Conference and Visitors Council, March, 2010.

<sup>23</sup> Lauren Schlau Consulting, *Santa Cruz County Visitor Profile*.

East Santa Cruz: A densely populated, urban neighborhood with many re-purposed post-war buildings, East Santa Cruz offers many amenities to its residents, including several supermarkets (Whole Foods Market, Safeway, among others), home accessory and clothing stores, and many restaurants.<sup>24</sup>

West Santa Cruz: Divided from East Santa Cruz by the San Lorenzo River, West Santa Cruz has a more suburban flavor with amenities offered by many large shopping centers, which include supermarkets, big box stores (e.g. Costco), as well as many winery outlets and tasting rooms.<sup>25</sup>



Figure 6: Santa Cruz Districts (Source: Google Maps)

Waterfront: a regional vacation destination and tourist area, which includes a public beach, wharf, boardwalk, and amusement park. Other than a few restaurants, most of the neighborhood businesses, such as souvenir shops and motels, cater to vacationers and offer few amenities for permanent residents.<sup>26</sup>

<sup>24</sup> Ibid.

<sup>25</sup> Ibid.

<sup>26</sup> Ibid.



Figure 7: Santa Cruz Waterfront District (Source: Gibbs Planning Group, Inc.)

## Urban Planning

### Land Use

The City of Santa Cruz has established a General Plan, intended to be a “comprehensive, long-range, and internally consistent statements of [the] city’s development and preservation policies,” and is the main tool for managing city growth and conservation.<sup>27</sup> The plan includes the following major topics:

- Land Use, to include commercial, residential and industrial zoning, open space management
- Environmental Assessment, to include demographic and economic impact; cultural, historical, agricultural and natural resources; noise and air pollution; and hazards such as flooding and seismic activity
- Transportation and Circulation, to include major thoroughfares, pedestrian routes, bike access, and public utilities
- Housing Element, to include mixed use and housing density guidelines; promoting affordable housing; and regulating the subdivision of multi-family residences.<sup>28</sup>

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<sup>27</sup> City of Santa Cruz, *General Plan 2030 Administration Draft*, February 27, 2009, 5.

<sup>28</sup> *Ibid*, 4.

**Table 2. Existing Land Use in Santa Cruz**

**City Limits, 2006**

Land Use	Acres	Percentage of Total Acres
Total Residential	2,617	38.3%
Single-family residential	2,068	30.3%
Two-to Four Unit Residential	198	2.9%
Multifamily Residential	311	4.6%
Mobile Home Park	40	0.6%
Commercial/Mixed Use	252	3.7%
Office	61	0.9%
Industrial	197	2.9%
Public/Institutional	1,756	25.7%
Parks	654	9.6%
Open Space	1,068	15.6%
Parking	52	0.8%
Vacant	169	2.5%
<b>Total</b>	<b>6,826</b>	<b>100%</b>

*Source: County assessor, City of Santa Cruz GIS, 2006 as reported in General Plan 2030*

In addition to the General Plan, there are numerous other plans, from the City, County and State level, that govern specific areas in and around Santa Cruz. These too must be considered to gain a comprehensive understanding of the areas planning goals and restrictions. (See Appendix C for list of plans that affect Santa Cruz development.)

**Traffic**

Santa Cruz has many pedestrian friendly neighborhoods and biking is a popular mode of transportation. Regardless, with limited transit corridors and a large commuting population, traffic congestion remains a problem that is

projected to get worse. In response, the General Plan sets mobility as a high priority and seeks to “provide an accessible, comprehensive, and effective transportation system that integrates automobile use with sustainable and innovative transportation options—including enhanced public transit, bicycle, and pedestrian networks throughout the community.”<sup>29</sup>

Plans for growth are now focused on the downtown region where major traffic corridors can

<sup>29</sup> City of Santa Cruz, *General Plan 2030*, 58.

be made more efficient and bicycling and walking can be promoted as viable alternatives to cars.<sup>30</sup> As a result, land use regulations promote consolidating employment centers and new developments are encouraged to propose innovative parking solutions, improve access for pedestrians and bicycles, and provide “pedestrian-friendly frontage and streetscapes.”<sup>31</sup>

## **Regulatory Environment**

Local developers see the City of Santa Cruz regulatory environment as neutral, biased neither towards anti-development or pro-development. While past City Councils were perceived as being obstructionist, at least the last two administrations seemed to appreciate the association between new development and economic growth.<sup>32</sup> (See Appendix D for Zoning Map.)

Santa Cruz’s land use policies center on the concept of “sustainable development,” designs and methods that “promote harmony among people and between harmony and nature.”<sup>33</sup> The goal is to balance the need for economic growth, housing, and jobs while preserving the environment, natural resources, community character, and quality of life.

Land use policies also favor preserving current open, undeveloped space to preserve natural resources and wildlife habitats, recreational and park amenities, agricultural use, and city aesthetics. These areas include several parks and the UCSC campus to the north; the Santa Cruz Harbor and Arana Gulch to the east; and the Moore Creek Corridor, Younger Lagoon, Wilder Ranch State Park, plus agricultural and grazing lands to the west.<sup>34</sup> (To the

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<sup>30</sup> Ibid, 41.

<sup>31</sup> Ibid, 62.

<sup>32</sup> Mackens, Kristen, Principal, M Commercial Realty. Personal interview with Bryan Woolley via telephone. San Jose, March 23, 2012.

<sup>33</sup> City of Santa Cruz, *General Plan 2030*, Administrative Draft, February 27, 2009, 40.

<sup>34</sup> Ibid, 42.

south is the ocean.) Any development proposals that would impinge upon or otherwise impact these areas would likely be met with strong public outcry and ultimate disapproval by the City.

Existing land uses are characterized as either, single-family residential, two- to four unit residential, multifamily residential, mobile home park, commercial/mixed use, office, industrial, public/institutional, park, open space, parking, or vacant.<sup>35</sup>

Depending on location, housing density ranges from Very Low-density Residential (0.1-1 dwelling units per acre) for rural areas up to High-density Residential (30.1-55 dwelling units per acre) for high rise apartment buildings.<sup>36</sup>

Similarly, density for commercial developments is established using Floor-to-Area Ratio (FAR), with districts ranging from Neighborhood Commercial (0.25-1.5 FAR) for small scale, neighborhood developments, to Regional Visitor Commercial (0.25-3.5 FAR) districts, for larger enterprises intended to serve both local residents as well as attract visitors from surrounding communities. This highest density zoning only applies to the downtown and waterfront districts. Office zoning allows for densities from 0.25 to 1.75 FAR, and industrial zoning ranges from 0.1 to 2 FAR, depending on location.<sup>37</sup>

Due to the limited vacant land, growing population, and demand for new housing, the City encourages mixed use designs, especially in higher density areas (typically along the major transit corridors). Commercial and office development that include a residential component align well with the goals of the General Plan and are typically favored by City

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<sup>35</sup> Ibid, 43.

<sup>36</sup> Ibid, 45.

<sup>37</sup> Ibid, 46.

planning officials.<sup>38</sup> Further, most of the Central Business District (CBD) has been designated a High-Density Overlay zone, which promotes mixed-use developments by adding another 2 FAR for residential use, so long as the development is at least 60% residential.

For areas designated as Coastal Recreation, Parks, Natural Areas, or Agricultural/Grazing, development is limited to buildings deemed necessary to support and maintain these areas (0 to 0.1 FAR).<sup>39</sup> Notably, the City does not have zoning jurisdiction over UCSC campus properties; land use and densities are determined by the State of California.<sup>40</sup>

The Local Coastal Plan (LCP) is a land use plan which applies to areas of Santa Cruz designated part of the coastal zone, such as the waterfront district. It implements local ordinances and requirements of the California Coastal Act, which were established to manage and preserve coastal resources.<sup>41</sup>

In addition to density standards, the General Plan also establishes overarching goals and policies for new developments, in order to:

- Promote sustainable use of land and optimizing use of infill parcels
- Provide incentives for consolidating and better utilizing underdeveloped parcels
- Develop combined parking facilities and strategic locations
- Ensure “height, scale and bulk” of developments take into consideration the City’s character

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<sup>38</sup> Ibid.

<sup>39</sup> Ibid.

<sup>40</sup> Ibid,49.

<sup>41</sup> Ibid, 3.



- Protect and extend open spaces and wetlands, especially along the coast
- Promote pedestrian and bicycle access
- Require environmental impact studies to safeguard wildlife, preserve available water sources and limit air pollution
- Require new development to pay for proportional share of cost to expand supporting infrastructure
- Maintain City’s compact community and current boundaries (i.e. limit urban sprawl)
- Balance diverse land uses to support City’s economic, housing, community, and environmental needs
- Promote job creation through encouraging selective industrial and office development and economically viable commercial districts
- Protect and improve residential areas, especially historic districts, while encouraging higher density use
- Encourage land uses that reduce reliance on automobiles<sup>42</sup>

The General Plan also discourages the development of strip malls in favor of “clustered” commercial and mixed use developments and specifically limits the number and placement of fast-food restaurants.<sup>43</sup>

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<sup>42</sup> Ibid, 49.

<sup>43</sup> Ibid, 54.

## Current Market Conditions

### Office

According to Kristen Mackens, President and CEO of M Commercial, a real estate company that specializes in site acquisition, restoration and repurposing, “the Santa Cruz market is tight, especially the office sector.” She believes the market bottomed about October, 2011, and although there is little activity in new construction yet, pent-up demand is bringing vacancy rates down and rents up.<sup>44</sup>



Figure 8: Office Vacancy Rates (Source: Cassidy Turley)

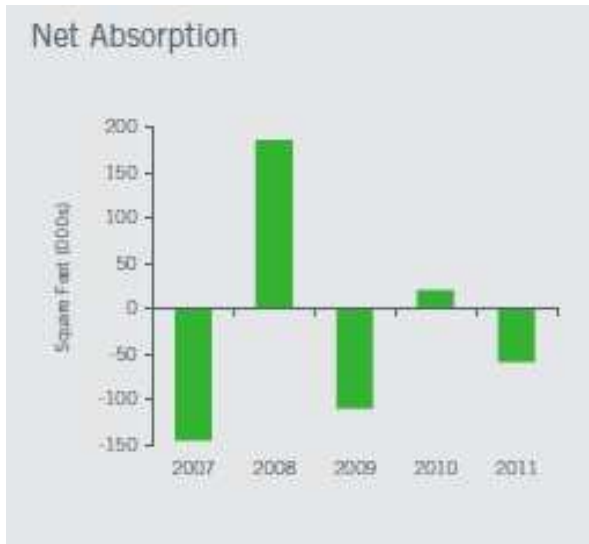


Figure 9: Office Net Absorption Rates (Source: Cassidy Turley)

However, Fred Antaki, broker for Main Street Commercial Realty, paints a different picture, “office [vacancy] rates have stabilized,” he concedes, “but it isn’t hot.”

Industry statistics seem to support Antaki’s assessment. As of fourth quarter, 2011, the office space inventory in City of Santa Cruz was 2.2 million square feet with

<sup>44</sup> Makens Interview.

a vacancy rate of 14.3%, well above the Santa Cruz County 10-year average of 10%. Nonetheless, vacancy rates have been stable for the last two years and are starting to trend downward. Net absorption was positive by 23,000 square feet in Santa Cruz for fourth quarter, and rents have been stable for over a year, averaging \$1.84 per square foot (full service) across all property classes.<sup>45</sup>

### **Commercial Residential**

Commercial residential also shows signs of strength with multiple offers on new listings. According to Antaki, “Days on Market is dropping big time, and we’re starting to see new projects in the pipeline.”

Jessika Soto, a local real estate agent with both residential and commercial experience, agrees, “The [residential] rental market is hot. Everyone is looking for rentals.” Rents are increasing as prior home owners, dispossessed by the housing bust, are looking to rent in the same areas. As a result, single family houses that were historically shared by students are now being leased to families, increasing demand for apartments. “Rents never really dropped much during the downturn;” said Soto, “there is always a need for student housing in Santa Cruz.”<sup>46</sup> Demand is expected to remain high with rents ranging from \$850-\$1200 per bedroom and vacancy rates consistently below 3%.<sup>47</sup> Her estimate of rent levels are corroborated by residential rental rate statistics published by the UCSC Housing Office (see Appendix E), and as of fourth quarter, 2011, apartment vacancy rates in Santa Cruz was at

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<sup>45</sup> Cassidy Turley Commercial Real Estate Services, *Office Market Snapshot, Santa Cruz County, Fourth Quarter 2011*, [www.cassidyturley.com](http://www.cassidyturley.com), April 2012.

<sup>46</sup> Soto, Jesyka, Agent with David Lyng Real Estate. In-person interview by Ted Woolley. Santa Cruz, April 2, 2012.

<sup>47</sup> *Ibid.*

2.6%.<sup>48</sup> In addition, rent growth is strong for multi-family residential properties, ranging from 6-12% annually.<sup>49</sup>

## Retail

In regards to space, the Santa Cruz market is dominated by properties with smaller footprints, with the greatest demand for office and retail spaces ranging from 500 to 5000 square feet.<sup>50</sup> Larger developments are uncommon due to lack of available raw land, the additional expense of consolidating and demolishing existing smaller structures, and political headwinds against “big box” developments.<sup>51</sup>

Central Santa Cruz County, has a

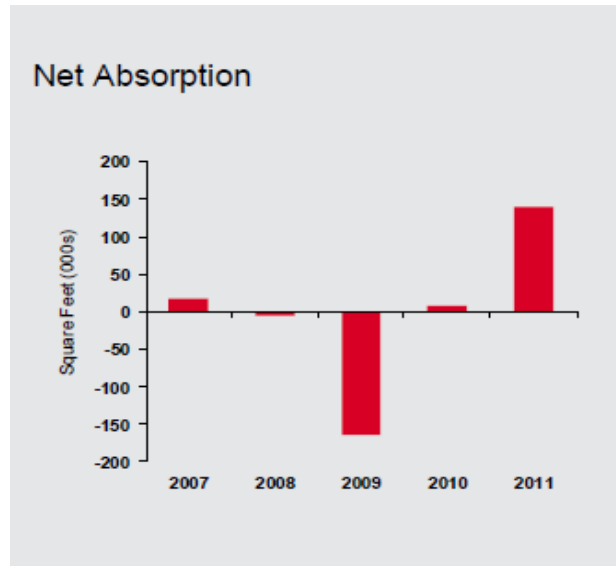


Figure 10: Retail Net Absorption Rates (Source: Terranomics)



Figure 11: Retail Vacancy Rates (Source: Terranomics)

<sup>48</sup> ReisReports, *Commercial Real Estate Report – Santa Cruz-Watsonville, CA [Apartment]*, <https://www.reisreports.com/Markets/California/Santa-Cruz-Watsonville/Apartment/>, April 2012.

<sup>49</sup> Daneshrad, Paul, *Multi-Family Looks to be the Investment Vehicle of the Future*, [www.cpexecutive.com](http://www.cpexecutive.com), 21 March, 2012.

<sup>50</sup> Antaki, Fred, Commercial Broker with Main St Realtors. Personal interview with Ted Woolley via telephone. Santa Cruz, March 23, 2012.

<sup>51</sup> Ibid.

retail space inventory of 2.4 million square feet, predominately in the City of Santa Cruz. As of end of fourth quarter, 2011, the vacancy rate was 3.6%, dropping from 9.8% a year before and below the 5-year average of 4.5%. Net absorption was positive 7,597 square feet fourth quarter and positive 149,311 square feet for the year. Average rent rose 12% from \$17.87 to \$20.03 per square foot, triple-net (NNN), and has been trending up in step with absorption since the beginning of 2011. Rents have large range though, varying from \$12.00 to \$36.00 per square foot. In addition to commanding higher prices, first-tier properties are experiencing annual growth rates of 5%.<sup>52</sup>

A recent study commissioned by the Santa Cruz Chamber of Commerce concluded that, based on an estimated \$43.9 million worth of unmet demand for retail sales, the CBD along Front St/Pacific Ave could support an additional 91,500 gross square feet of retail space, equating to 25 to 30 new retailers and restaurants.<sup>53</sup> Notably, no new retail construction is currently underway, so demand should remain strong with continued economic recovery. Further, sales of retail properties have stabilize in the last year, averaging \$196 per square foot, across all classes.<sup>54</sup>

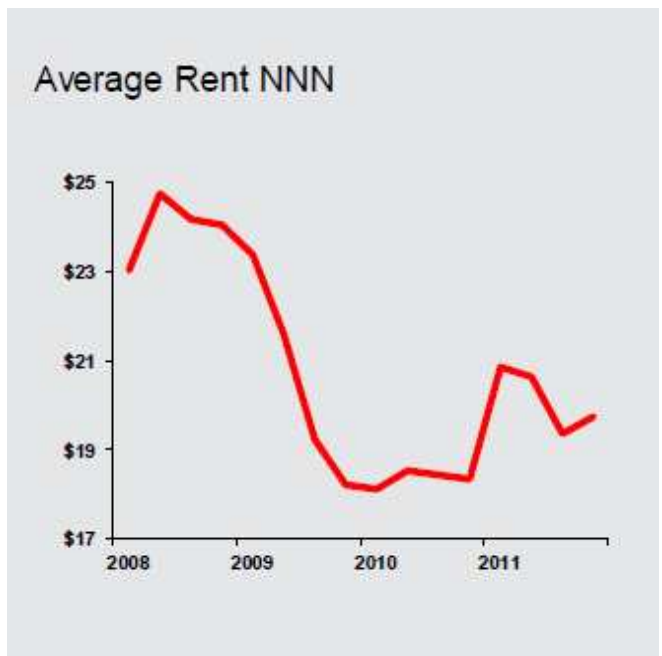


Figure 12: Retail Rent Rates (Source: Terranomics)

<sup>52</sup> Terranomics Retail Services, *Santa Cruz County Shopping Centers Report, Q4-2011*.

<sup>53</sup> Gibbs Planning Group, Inc. , *City of Santa Cruz Retail Market Analysis*.

<sup>54</sup> Loopnet.

## Retail Property Sale Prices - Sale Trends

Median Sale Price Retail Santa Cruz-Watsonville, CA (\$/SF)

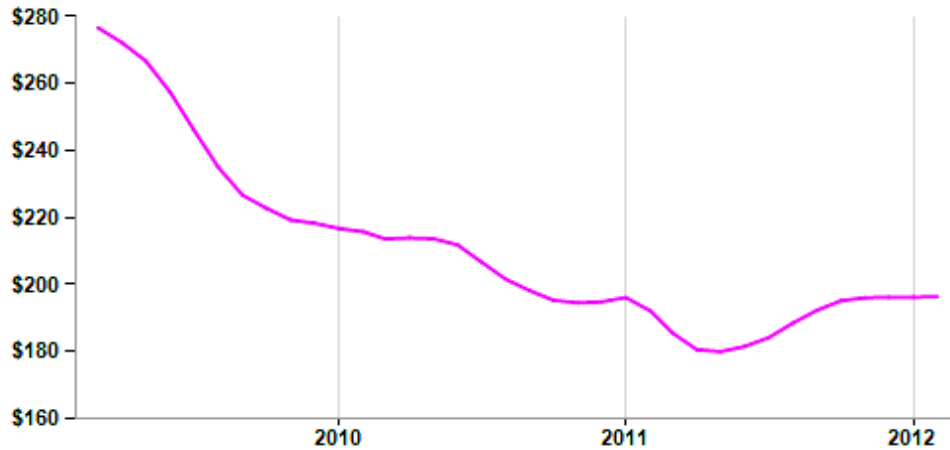


Figure 13: Retail Property Sales Trend (Source: Loopnet)

## Lending Environment

Local developers report that investment capital is flowing again after several years of constriction. “Financing is freeing up; Silicon Valley is tapping [Santa Cruz] again,” noted Mackens.<sup>55</sup> REITs “are flush with money” and have been especially active in the Northern California market, competing over investment opportunities and accepting ROIs as low as 3% in order to put capital to work. Bank rates are also low, for both construction and permanent lending, but developers “have to have some skin in the game.”<sup>56</sup>

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<sup>55</sup> Mackens Interview.

<sup>56</sup> Antaki Interview.

## Site Selection

Santa Cruz has well defined, immovable city boundaries due to the terrain, protected public lands and the Pacific Ocean. By 2006, there were few empty parcels available for new development. Since then, the focus of city planning has shifted to issues surrounding the redevelopment of existing structures and neighborhoods. Particular attention is being paid to infilling empty and

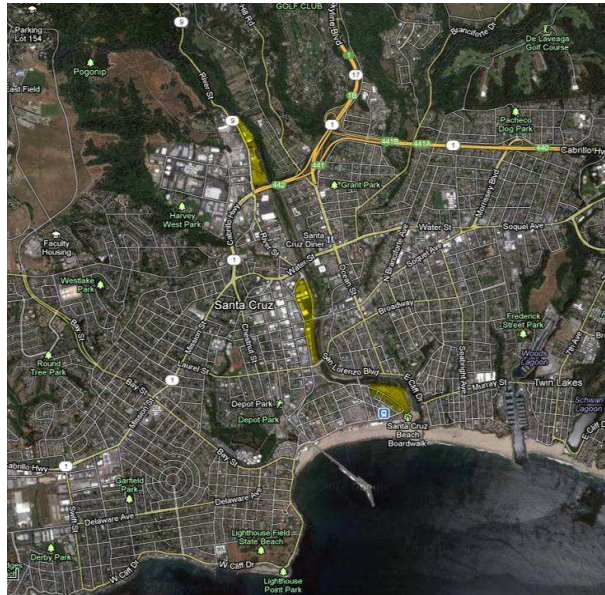


Figure 14: Satellite view of Santa Cruz with River Development Areas Highlighted (Source: Google Maps)

underutilized parcels of the city's commercial corridors and replacing or renovating older

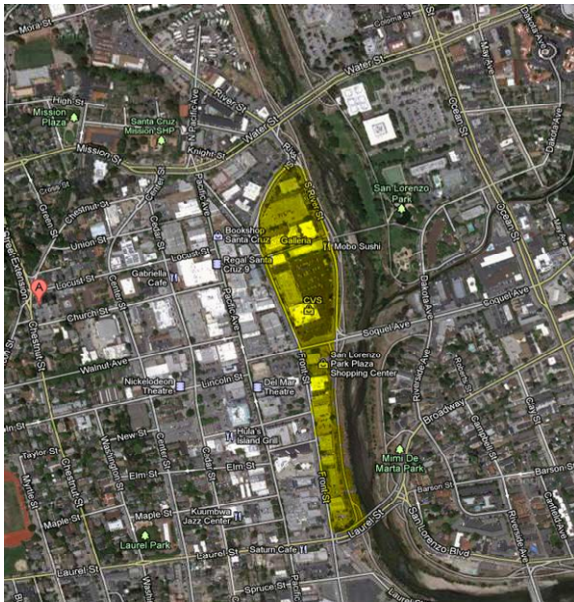


Figure 15: Close up of Front St River Development Area (Source: Google Maps)

commercial buildings that lack historical value. The General Plan 2030 specifically notes the desire for more and higher-density housing in these areas.<sup>57</sup>

### San Lorenzo Riverfront Opportunity

One of the City's goals, according to the General Plan is to improve, in various ways, the San Lorenzo River, which bifurcates Santa Cruz, flowing through its CBD.

Details regarding how to approach this goal

<sup>57</sup> Santa Cruz, *General Plan*, 29.



are detailed in the San Lorenzo Urban River Plan. In addition to addressing flood control, wildlife preservation, and recreational uses, one of the plan's goals is to "incorporate the San Lorenzo River...into the surrounding urban fabric of downtown and neighborhoods."<sup>58</sup>



Figure 16: Close up of Beach Flats River Development Area (Source: Google Maps)



Figure 17: Existing river trail along Front St (Source: Site visit)

The plan specifies three "Significant Riverfront Areas" ripe for redevelopment and recommends design guidelines and improvements for access and aesthetics.<sup>59</sup> Of the three, one area, designated the Saltz Tannery/Sycamore Grove Riverfront Area, is already undergoing redevelopment into a publicly funded, 8.3 acre Community Arts Center, with the first phase completed in 2009.<sup>60</sup>

Another designated area is the Beach Flats Riverfront Area, located where the San Lorenzo River empties into the Pacific. It is located along the river's west bank between the Riverside Avenue Bridge to the north and the beach to the south. The area includes both residential neighborhoods and commercial properties. The plan encourages development of

<sup>58</sup> Santa Cruz, *San Lorenzo Urban River Plan*, 2003, chapter 6.

<sup>59</sup> Ibid.

<sup>60</sup> Santa Cruz Wiki, *Saltz Tannery*, [http://www.scruzwiki.org/Salz\\_Tannery](http://www.scruzwiki.org/Salz_Tannery).



regional visitor commercial uses and high density residential use with designs that would improve pedestrian access to the river and beach.<sup>61</sup> However, the area is predominately residential parcels, which would increase development costs and timeline due to the need to get neighborhood buy-in and consolidate smaller lots.

The third designated area is the Front Street Riverfront Area, which is on the rivers' west bank between Laurel St on the south end and South River St on the north end. Although mostly commercial use and municipal parking lots, the plan encourages residential development in the area. In fact, an opportunities and constraints analysis completed by the Santa Cruz Planning Department determined the area could support up to 449 housing units.<sup>62</sup> Existing buildings face Front St rather than the river and adjoining parks and provide poor public access to both. Opportunities abound to renovate and repurpose an existing structure into a mixed-use building that offers river and park views and access as amenities.

### **Focusing on Front Street**

Developing a project on Front St offers several advantages over other areas of Santa Cruz:

- Focus on Riverfront development: Redevelopment of this area is a major tenet of the City's General and other long range plans. Any project that contributes to this goal should receive strong support from the Planning Department and fewer political obstacles.

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<sup>61</sup> Ibid.

<sup>62</sup> *San Lorenzo Urban River Plan*, chapter 6.

- Encouragement of mixed use/high density development: The City supports mixed-use development in this area by allowing for an increased height restriction, higher FAR. A mixed-use development would also provide sub-market diversification within a single project.
- Proximity to Pacific Ave Shopping District: Although both Front St and Pacific Ave are both part of Santa Cruz’s CBD, they have evolved into primarily a shopping district, though with some office and multi-family residential space available, mostly in multi-use buildings. Pacific Ave in particular has become a shopping Mecca for both residents and tourists, offering a mix of over 200 national retail stores and independent boutique shops and restaurants.<sup>63</sup> Front St, on the other hand, offers fewer boutique retailers. Some are lower-end (e.g. discount stores), and they are mixed in among more industrial-type stores, such as paint and auto parts stores. Although Front St has yet to develop the cache of Pacific Ave, it is located just one block east and is both visible and easily accessible by Pacific Ave shoppers via several intersecting streets. The higher end boutique shops have started to migrate onto Front St, and this trend should continue with the economic recovery, significantly increasing property values along the way.
- Availability of public transportation: The City’s central bus terminal is located on Maple St, between Front St and Pacific Ave. The local bus system is the main mode of transportation for UCSC students (along with bicycles). Its location allows the Pacific Ave area to be easily accessible by students despite the university campus being across town. It also makes the neighborhood ideal for student housing.

### **Target Property**

The 408 Front St property (parcel 005-151-32) stands out as an excellent candidate for redevelopment. It is currently underutilized as a single-story commercial building with Sherwin-Williams paint store as its sole tenant. Unlike the other buildings on Front St, the structure is set back approximately 40 feet from the sidewalk to provide on-site parking for 8

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<sup>63</sup> Gibbs Planning Group, Inc., *City of Santa Cruz Retail Market Analysis*, 34,35.

cars. This set back detracts from the buildings visibility and access, making it less desirable for retail space. Nor does the building take advantage of its proximity to or sight line from Pacific Ave, the primary retail thoroughfare in Santa Cruz. Also, it is oriented towards Front St and does not utilize its river and park views (from the back of building).



Figure 18: Target Property 408 Front St (Source: Site visit.)

The parcel is 0.22 acres, zoned “Regional Visitor Commercial” (RVC), which allows for a 3.5 FAR. Also, it is located within a high-density overlay zone, which allows for an additional 2.0 FAR of residential development in mixed-use projects, allowing a maximum FAR of 5.5 for development.<sup>64</sup> Existing improvements include a 5800 square feet (sf), single-story retail building with parking lots in front and along its side.<sup>65</sup>

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<sup>64</sup> City of Santa Cruz, *General Plan 2030, Land Use Plan*, 14,26.

<sup>65</sup> Loopnet.

## Acquisition of Target Property

The property is currently owned by Mr James Bierman of Santa Cruz and is assessed at \$545,152 for tax purposes with the land

assessed at \$201,591 (37%) and improvements at \$343,561 (63%).<sup>66</sup>

Based recent sales trends with retail space averaging \$196 per sf,<sup>67</sup> a figure supported by the most recent comps from the CBD (see Appendix F), the property

should be acquirable for approximately \$1.16 million. Adding closing costs, commissions, and lease termination costs, total acquisition costs for the property come to \$1.3 million.

**Table 3. Acquisition Information**

Acquisition Information	
Land Cost (based on avg sales psf)	\$ 1,160,000
Closing Cost as %	5.00%
Closing Cost	\$ 58,000
Brokerage Fees as %	1.50%
Brokerage Fees	\$ 17,400
Lease Termination (5%)	\$ 58,000
<b>Total Acquisition Costs</b>	<b>\$ 1,293,400</b>

The property is ideally located for a mixed use development that takes advantage of its proximity to the Pacific Ave shopping district, the downtown office district, a robust



Figure 19: Aerial view, looking west, of Subject Property and surrounding area (Source: Google Maps)

apartment rental market, and views and access to the San Lorenzo River. It is located

<sup>66</sup> Santa Cruz County, Geographic Information System.

<sup>67</sup> Loopnet.

cattycorner from the local bus terminal, making the location ideal for residents, especially UCSC students.

Since the property is at the Maple St and Front St intersection, it has the advantage of a direct line of sight from Pacific Ave, making it ideal for attracting shoppers to its ground floor retail space. On the river side, the property is easily visible from the Laurel St Bridge, a

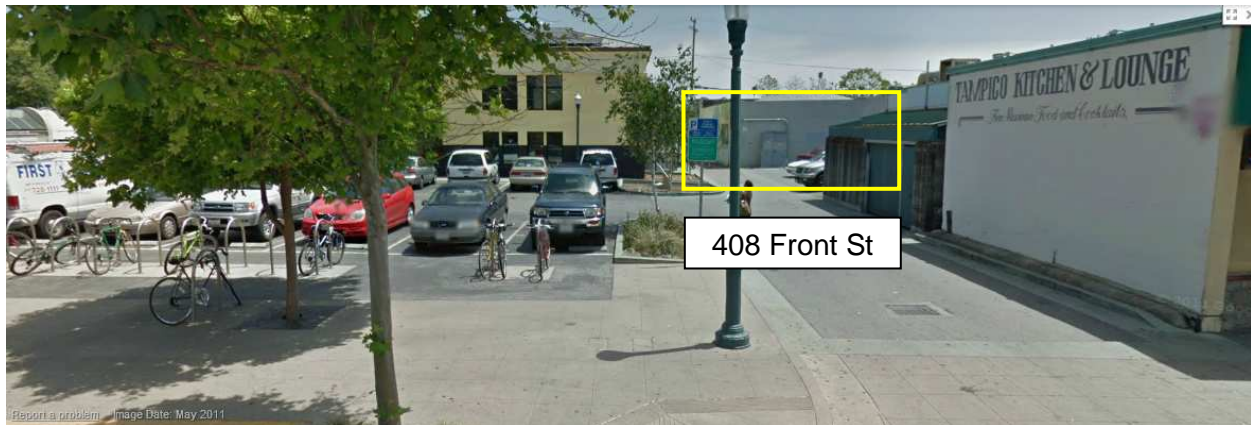


Figure 20: View of 408 Front St from Pacific Ave (Source: Google Street View)

major traffic artery, which would provide high visibility to any business on that side of the property. This would be an ideal space for a restaurant/bar tenant and would tie in with the City's goal of establishing a vibrant river walk along the San Lorenzo. Alternately, a single tenant could occupy the full ground floor with access from both Front St and the river walk.

Zoning and the General Plan encourages mixed use development and allows for structures up to four stories (50 ft) along the river. The proposed new development would then provide retail/restaurant space on the ground floor and residential apartments on floors 2-4, which would command desirable views of downtown, the river and nearby park.

Parking would be provided below level for residents, plus public parking is available a short walk down the street at the corner of Laurel and Front St. Metered on-street parking is also available for retail customers.



Figure 21: View of 408 Front St from Laurel St Bridge (Source: Google Street View)

## Due Diligence

Before purchasing the subject property, due diligence would be completed to develop a comprehensive picture of the physical, financial, legal, and environmental condition of both the site and structure, such as:

- Title search, deed, existing loan documents
- Document review (e.g. lease, permits, financial statements, insurance, etc.)
- Site inspection and survey
- Phase I environmental study, followed by phase II if indicated
- Geology engineering report <sup>68</sup>

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<sup>68</sup> Santa Cruz, *General Plan*, 122.

Costs related to due diligence are included in the development budget as part of the “soft costs” contingency.

## **Site Development**

### **Development Team**

The development team for this project was selected based on their experience in the Santa Cruz market and track record of success:

Design: Wald, Rhunke, & Dost Architects, LLP

Wald, Rhunke, & Dost Architects, LLP is the largest design firm in the Central California Coast region with 48 years experience in and around Santa Cruz. They boast a large portfolio of acclaimed designs for retail, office, and multifamily developments.<sup>69</sup> Their familiarity with design requirements mandated by the General Plan and vast experience with the Santa Cruz planning commission should facilitate the project approval process.

Construction: Bogard Construction, Inc.

Headquartered in Santa Cruz since 1947, Bogard Construction has a strong track record of major commercial construction projects in the Santa Cruz market, including Pacific Shore Apartments, the McPherson Center for Art and History, and the Orosco Office Building. Their areas of expertise include design, construction, LEED certification, project management, and post-construction maintenance.<sup>70</sup> The diversity

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<sup>69</sup> Wald, Rhunke, and Dost Architects, LLP, <http://www.wrdarch.com> (April 2012).

<sup>70</sup> Bogard Construction, Inc., <http://www.bogardconstruction.com>, (April 2012).



of their past projects, knowledge with local building codes, and experience with the local planning officials will help ensure the 408 Front St project proceeds smoothly.

Leasing Agent/Property Management: Sheldon Wiseman Commercial Real Estate

Sheldon Wiseman is a full service commercial real estate firm and the dominant broker in the Santa Cruz market. Their experience includes representing landlords in the office, retail, and multifamily markets for both leasing and managing properties.<sup>71</sup>

### **Site Planning**

Any new construction or major renovation will require design review and approval by the City of Santa Cruz Planning Commission. The goal of the review will be to promote designs that are “in harmony with its natural setting.” Criteria include minimizing the impact of grading and development on the topography and natural features, such as bluffs; preserving ocean views and other vistas; and ensuring that building design, scale and landscaping are “compatible with the character of the area.”<sup>72</sup>

The City requires a minimum of 60% of square footage of mixed use development (excluding parking) be residential in Front Street area. Further, any riverfront development would have to allow pedestrian and solar access to the river.<sup>73</sup>

Other notable site requirements mandated by the City include:

- Maintaining the ten-foot setback area between any new development and the adjacent river levee trail. The setback area should be filled to be the same elevation as the

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<sup>71</sup> Sheldon Wiseman Commercial Real Estate, [www.sheldonwiseman.com](http://www.sheldonwiseman.com), (April 2012).

<sup>72</sup> Santa Cruz, *San Lorenzo Restoration Plan*, 32.

<sup>73</sup> Santa Cruz, *Downtown Recovery Plan*, 30.



levee trail and should incorporate outdoor public seating or visually accessible green space, using native trees.<sup>74</sup>

- Ensuring that any parcel consolidation strategy provides public access from the Front Street sidewalk to the river levee trail.<sup>75</sup>
- Encouraging pedestrian traffic through creative “inviting” design and incorporating water features, gardens, paving, and stairways to the river levee into the design.<sup>76</sup>
- Avoiding large expanses of parking, and attempting to “green” parking areas by using native trees.<sup>77</sup>
- Preserving views from both taller downtown buildings to the River and from the River trail to distant mountains and ridges.<sup>78</sup>
- Preserving views along the Front Street area to Beach Hill (a local historic feature).<sup>79</sup>
- Running all new utility lines underground.<sup>80</sup>
- Preserving existing wild vegetation “to the maximum extent possible” and maintaining the integrity of wildlife habitat.<sup>81</sup>

Parking requirements must also be addressed, with a residential development requiring one parking space per bedroom. In addition, the City requires minimum bicycle parking spaces for all new construction of at least one space per unit for multifamily residential.<sup>82</sup>

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<sup>74</sup> Ibid, 51.

<sup>75</sup> Ibid.

<sup>76</sup> Ibid.

<sup>77</sup> Ibid.

<sup>78</sup> Ibid.

<sup>79</sup> Ibid.

<sup>80</sup> City of Santa Cruz, *Municipal Ordinance, Community Design*, 24.12 “Underground Utilities.”

<sup>81</sup> City of Santa Cruz, *Municipal Ordinance, Community Design*, 24.14 “Wildlife Habitats and Plant Communities.”

<sup>82</sup> City of Santa Cruz, *Municipal Ordinance, Community Design*, 24.12 “Bike Parking Requirements.”

## **Building Design**

Santa Cruz has adopted the California Uniform Building Codes (UBC) to stipulate construction requirements for all new construction and renovations.<sup>83</sup>

### **Aesthetic Requirements**

The City's design guidelines for downtown encourages the use of specific building materials for a building's façade, to include the use of natural wood, brick and stone and avoiding overuse of concrete and stucco.<sup>84</sup> There is no mention of glass, but a glass curtain shell would be out of character with surrounding buildings and would likely meet objections from the City.

### **Seismic Requirements**

California is known for its seismic activity, and Santa Cruz is located just 10 miles west of the San Andreas fault. The city experienced significant damage in the 1989 Loma Prieta earthquake (34 commercial buildings had to be demolished as result).<sup>85</sup> Older masonry structures will have been retrofitted in accordance with the Uniform Code for the Abatement of Dangerous Buildings to mitigate earthquake risk; however, any alterations or renovation of an existing structure will require a review of its design and may require upgrades to the latest seismic engineering codes.<sup>86</sup> Any new construction requires a site-specific

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<sup>83</sup> Santa Cruz, *General Plan*, 122.

<sup>84</sup> *Ibid.*

<sup>85</sup> *Ibid.*, 114.

<sup>86</sup> *Ibid.*, 122.

investigation by a qualified professional to assess the potential for seismic impact and recommend methods to mitigate the risk.<sup>87</sup>

## **Flood Risk**

The Front St area had once been designated as an A-11 Federal Emergency Management Agency (FEMA) flood plain, which required new construction to meet FEMA flood elevation/proofing requirements. However, in 2001, the Army Corps of Engineers, in partnership with the City, completed a \$21 million flood control and environmental restoration project along the San Lorenzo River. The project improved levees and instituted other flood control measures to meet 100-year FEMA flood protection standards. This upgrade eliminated the flood plain designation for the parts of the CBD adjacent to the river, eliminated flood mitigation measures for new construction, as well as the requirement for flood insurance. The project allowed for more flexible and economically viable development along the river.<sup>88</sup>

## **Sustainability**

The Santa Cruz Green Building Program specifies environmentally-friendly criteria for new construction projects. Minimum standards must be met in order to receive a building permit, and exceeding the minimum standards can result in accelerated building permit processing and recognition from the City.<sup>89</sup> The Planning Department follows the U.S. Green Building Council Leadership in Energy and Environmental Design (LEED) point system for commercial developments, and compliance is measured and enforced through

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<sup>87</sup> City of Santa Cruz, *Municipal Ordinance, Community Design*, 24.14 "Seismic Hazards."

<sup>88</sup> City of Santa Cruz, *San Lorenzo River Flood Control & Environmental Restoration Project*, <http://www.cityofsantacruz.com/index.aspx?page=1033>.

<sup>89</sup> City of Santa Cruz, *Municipal Ordinance, Community Design*, 24.15 "Green Building Regulations."

building inspections. It is possible to earn up to 75 points in the LEED program under the following categories:

- Sustainable Sites
- Water Efficiency
- Energy & Atmosphere
- Materials & Resources
- Indoor Environmental Quality
- Innovation & Design Process

A minimum of 7 points are required to qualify for a building permit, 33 points qualify for accelerated building permit approval, and 40 points or more earns a Green Building Award from the City.<sup>90</sup> (See Appendix G for full list of point by point LEED criteria)

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<sup>90</sup> City of Santa Cruz, *Green Building Program: Standards for Compliance*, June, 2005.



Figure 21: Bachenheimer Building (Source: Equity Residential)

### Proposed Design

Conceptually, the 408 Front St project would be similar in design to the Bachenheimer Building, a mixed use development in Berkeley, CA, another university town with similar demographics to Santa Cruz.

The design would entail full demolition of the existing structure, excavating for two levels of below ground parking to accommodate the 48 parking spots (one

**Table 4. Parcel Information**

Parcel Size	9,583
FAR by Right	5.5
Max By-Right Density	52,707
Lot Coverage Ratio	90%
Max Foot Print	8,625
Number of Stories	4
<b>Total Building Size</b>	<b>34,499</b>

**Table 5. Space Calculations**

FAR to Gross Ratio	97%
Gross Square Feet	33,464
Gross to Rentable	91%
<b>Rentable Square Feet</b>	<b>30,452</b>
Parking Spots Needed	48
Space per Spot	400
<b>Area needed for parking</b>	<b>19,200</b>

per bedroom) required by code, and constructing a four story, mixed-use building that meets the City's design requirements.<sup>91</sup> The parcel's 5.5 FAR would allow for a maximum development of 52,706 sf gross; however, the .22 acre lot size and zoning ordinance restrictions of 50 ft/4-story height limitation and a 90% maximum lot coverage ratio, limits the maximum development to 33,464 sf gross.<sup>92</sup> To account for common, structural, and mechanical spaces, a 91% gross to net space ratio is applied, resulting in 30,452 square feet of rentable space.

The first story would provide 7,614 sf net of retail space with access from both Front St and the San Lorenzo River Walk. This would be available for a single tenant, but more likely would be subdivided into three stores of just over 2,500 sf as the surrounding retail stores are predominately smaller boutique shops and restaurants. Parking for retail customers would be at ground level in the adjoining parking lot, available street parking, or a public city parking lot located just 200 feet south of the building at the corner of Front St and Laurel.

Stories two through four would provide 22,848 square feet net of residential space. Each floor would be subdivided into eight, 2-bedroom/2-bath apartments, 24 units in all. Units would average 952 square feet of rentable space each.

Although office space was considered a possible use for the second story as a way for to provide additional market diversification, higher vacancy rates (currently 14.3% vs 2.6%) and lower comparable rents (\$22 vs. \$25 per sf annually) proved residential use to be significantly more profitable in the Santa Cruz market.

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<sup>91</sup> City of Santa Cruz Municipal Code, 24.12.240 *Community Design*.

<sup>92</sup> City of Santa Cruz Municipal Code, 24.10.2850 *Design Standards*.

## Construction Budget (Preliminary)

The preliminary construction budget is based on median costs as quoted in *RSMeans Building Construction Cost Data, 2011* and adjusted by a “project size modifier”<sup>93</sup> and the city cost index for Santa Cruz<sup>94</sup> as recommended by the reference guide. Figures include all site preparation and excavation, finishes, and General Contractor overhead and profit. Architectural fees are calculated separately and include structural, mechanical, and electrical engineering fees.<sup>95</sup> An allowance of 20% is provided for other soft costs, such as due diligence, city fees and exactions, construction contingencies, and marketing. The cost of land is excluded from the construction estimates.<sup>96</sup> Altogether, the construction costs come to approximately \$7 million. Combining acquisition and construction, total development costs come to \$8.26 million.

**Table 6. Construction Budget**

CONSTRUCTION COST ESTIMATE								
Story	Description	Unit of Measure	Median Cost per Unit	Project Size Modifier	City Cost Modifier	Adjusted Cost per Unit	# Units (CF/SF)	Total Cost
n/a	Demolition of Existing Structure	Cubic Foot	\$0.33	1.1	1.138	\$0.41	58000	\$23,959
B2	Parking Garage	Square Foot	\$50.50	1.1	1.139	\$63.27	9600	\$607,406
B1	Parking Garage	Square Foot	\$50.50	1.1	1.139	\$63.27	9600	\$607,406
1	Retail Stores	Square Foot	\$83.50	0.975	1.139	\$92.73	8625	\$799,786
2 thru 4	Apartments Mid Rise (4 to 7 story)	Square Foot	\$107.00	1.1	1.139	\$134.06	25875	\$3,468,810
							Subtotal Construction Costs	\$5,483,408
							Architectural Fees @ 7%:	\$383,839
							Other Soft Costs @ 20%:	\$1,096,682
							<b>Total Construction Costs:</b>	<b>\$6,963,929</b>

<sup>93</sup> RSMeans, *Building Construction Cost Data, 2011*, 824.

<sup>94</sup> RSMeans, *Building Construction Cost Data, 2011*, 706.

<sup>95</sup> RSMeans, *Building Construction Cost Data, 2011*, 750.

<sup>96</sup> RSMeans, *Building Construction Cost Data, 2011*, 816.

*Table 7. Baseline Project Costs*

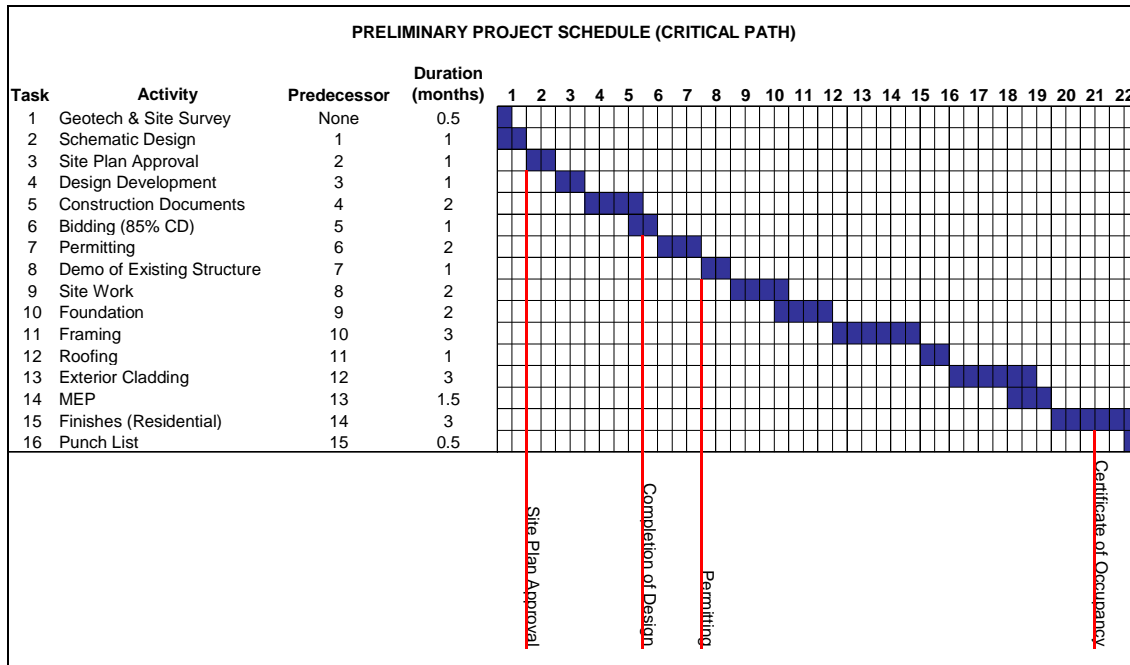
<b>Acquisition Information</b>	
Land Cost (based on avg sales psf)	\$ 1,160,000
Closing Cost as %	5.00%
Closing Cost	\$ 58,000
Brokerage Fees as %	1.50%
Brokerage Fees	\$ 17,400
Lease Termination (5%)	\$ 58,000
<b>Total Acquisition Costs</b>	<b>\$ 1,293,400</b>
<b>Construction and Design Costs</b>	
Total Hard Cost	\$ 5,483,408
Total Soft Cost	\$ 1,480,520
Soft Costs % of Hard Costs	27%
<b>Total Construction Cost</b>	<b>\$ 6,963,929</b>
<b>Total Cost of Project</b>	<b>\$ 8,257,329</b>



## Preliminary Construction Schedule (Critical Path)

Once the subject property is acquired, design and construction is estimated to take 22 months with Certificate of Occupancy in 20.5 months based on the schedule below.

**Table 8. Project Schedule**



In summary, design and construction would cost approximately \$7 million and take Bogard Construction, Inc. 22 months to complete. Sheldon Wiseman Commercial Real Estate would commence marketing and pre-leasing space once the final design is approved by the City and construction begins. After completion, leasing and ongoing property management would be continued by Sheldon Wiseman.

## **Financial Analysis**

### **Assumptions and Risks**

The financial analysis below presumes the following hold true through the life of the project:

- Project approval and ongoing support from Santa Cruz community and leaders.
- Continued economic recovery. If the current economic recovery falters, market conditions could deteriorate. Assumptions and projections used in the Pro Forma, such as demand for space, rental rates and terms, vacancy rates, absorption rates, and interest rates could prove inaccurate and risk the project's viability.
- No unexpected expenses beyond those budgeted for contingencies. Although the construction cost estimate includes contingency funds for unforeseen expenses, if a major issue arises that was missed in the due diligence phase of the project, development costs could exceed the budget, resulting in lower returns.
- Timely completion of construction. Although the project timetable and construction schedule includes flex time to accommodate unforeseen delays, any extended interruptions that push completion back would have a negative effect on expected returns.
- Obtaining financing at the proposed structure and rates. Prevailing rates are used for Loan to Values (LTVs), note rates, and Debt Service Coverage (DSC) throughout the pro forma calculations; however, a tightening of credit could raise the cost of capital with a negative impact on expected returns.

### **Financing Structure**

The project will be financed with a mini-perm loan at 70% LTV with a four year term, which should allow enough time to have the building fully leased before being reappraised and refinanced with a permanent loan. This would require an initial investment of \$2.5

million, plus additional capital infusions of \$400 thousand for years 1 and 2, and \$260 thousand in year 3, for a total equity requirement of \$3.5 million. However, in year 4, when the project becomes cash flow positive and the mini-perm construction loan is refinanced into a permanent loan, \$1.5 million will be returned to investors (cash out) while maintaining a 75% LTV.

**Table 9. Financing Assumptions**

ASSUMPTION		RATIONALE
<b>Mini Perm Loan</b>	Value (replacement)	\$ 8,257,329
	Prime Rate	3.25%
	Spread	1.50%
	Note Rate	4.75%
	Term	4 yrs
	LTV	0.7
	Owner Equity	\$ 2,477,199
	Construction Loan	\$ 5,780,130
	DS Payment	\$ 274,556
		Interest Only
<b>Permanent Financing</b>	Cap Rate	6.50%
	Value	\$ 9,785,288
	LTV	0.75
	Owner Equity	\$ 2,446,322
	Closing Costs	2.50%
	Target DSC	1.2
	Prime Rate	3.25%
	Spread	2.00%
	Note Rate	5.25%
	Amortization Term	30
Loan Amt	\$ 7,338,966	
DS Payment	\$ 486,313	
	Actual DSC = 1.39	

## Absorption Rates

Although some of the space would likely be pre-leased, in order to provide a conservative financial analysis, average absorption rates are applied from the Certificate of Occupancy milestone date and no pre-leasing is presumed.

### Retail Property Days on Market - Lease Trends

Median Days on Market Retail for Lease Santa Cruz-Watsonville, CA

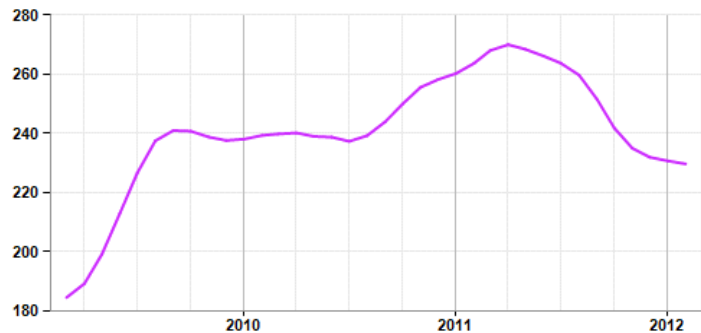


Figure 22: Retail Lease Days on Market (Source: Loopnet)

Absorption rates would differ for each space type. The residential units should rent quickly, with 100% occupancy expected within 8 months of completion. The retail space will be the bigger challenge to lease as absorption rates are lower. However, the river walk access provides a unique amenity in the market, and with the line of sight from Pacific Ave, stores should have no problem attracting shoppers. Full occupancy should be achievable within 15 months of completion.

## Vacancy Rates

To be conservative, the pro forma analysis uses higher than current vacancy rates in its calculations. For retail space, a vacancy rate of 4.5% (the 5-year average) is used vs. the current rate of 3.6%. For residential space, 3.5% is used, which is above the current rate of 2.6% and above the reported 3% average. However, if economic conditions continue to improve, actual vacancy rates in both categories should drop.

**Table 10. Vacancy Rate Assumptions**

ASSUMPTION		RATIONALE
Vacancy Retail	4.50%	5-yr avg per Loopnet
Vacancy Residential	3.50%	Conservative estimate (currently 2.6%)
Weighted Avg Vacancy	3.75%	Based on space allocation to tenant type

**Lease Structures**

Analysis of recent comparables and properties currently available shows that retail space should rent at \$33 per sf per year, NNN, and the apartment units are expected to lease for \$2,000 per unit per month gross.

The following lease structures are used for the projections:

805 Pacific	\$24.38
903 Pacific	\$18.00
1125 Pacific	\$33.00
1315 Pacific	\$33.00
1367 Pacific	\$42.00
110 Cooper	\$39.00
123 Locust	\$27.00
<b>Median</b>	<b>\$33.00</b>

Retail: 15-years NNN at \$33 psf, with 5-year options and 3% annual escalations (vs. current growth of 5%).

A percentage of gross sales may also be negotiated, but is excluded from the financial analysis to provide conservative projections.

Residential: 1-year master leases (i.e. not subdivided for roommates) averaging \$2,000 per unit per month. In actuality, there may be rent differentials among units based on location and whether they have street-side

views or river and park views. Rents would be adjusted to market levels annually at lease renewal. Month-to-month extensions may be allowed for a premium.

A lease renewal probability factor of 75% is used to project leasing and improvement costs.

**Table 12. Rent Rate Assumptions**

ASSUMPTION			RATIONALE
Target Rents	Retail psf \$	33.00	Market range is \$12-\$36; Median for comps = \$33 Based on avg \$2000/month per unit; market range=\$1050-\$2500
	Apartments psf \$	25.21	

**Reserves**

For financial stability, project reserves to pay for future tenant improvements, leasing commissions, and capital expenditures are based on averaging a 15-year projection, adjusted for inflation. The following assumptions are used to calculate reserve funding requirements as part of the Net Operating Income (NOI) calculations.

**Table 13. Reserves Assumptions**

	ASSUMPTION		RATIONALE
	New Tenant	Renewal	
Tenant Improvements (Residential Only)	\$ 2.00	\$ -	Based on 15 yr Rent Roll Projection
Leasing Comm (Retail)	5.00%	2.50%	Based on 15 yr Rent Roll Projection
Leasing Comm (Residential)	6.00%	0.00%	Renewals covered under Prop Mgt
CapEx	\$ 0.25		Estimate

## Projected Income

The Rent Roll below shows the tenant space and income allocations, pro rated for the first year of tenancy based on the applicable absorption rate. The Rent Schedule shows projected income based on the rent growth assumptions of 3% for retail space and 5% for residential space. The Rollover Schedule projects annual square feet rollover based on the 75% lease renewal probability to calculate the reserves required to cover future lease commissions and tenant improvement expenditures. It conservatively assumes 30 days on market to secure new residential tenant and 230 days on market to secure a new retail tenant.<sup>97</sup> Note that the vacancy rates are not applied here, but are applied in the NOI calculations.

**Table 14. Rent Roll**

Tenant	SF	Use Allocation	Rate (PSF)	Base Yr Rent	Income Allocation	Lease Start	Lease End	Term (yrs)	Escalation	Pro Rata First Yr
Retail 1	2,538		\$ 33.00	\$ 83,754		3/1/2015	2/28/2030	15	3.0%	75.00%
Retail 2	2,538		\$ 33.00	\$ 83,754		3/1/2015	2/28/2030	15	3.0%	75.00%
Retail 3	2,538		\$ 33.00	\$ 83,754		3/1/2015	2/28/2030	15	3.0%	75.00%
<b>Subtotal Retail</b>	<b>7,614</b>	<b>25%</b>		<b>\$ 251,262</b>	<b>30%</b>					<b>75.00%</b>
Apartment 1	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 2	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 3	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 4	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 5	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 6	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 7	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 8	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 9	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 10	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 11	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 12	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 13	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 14	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 15	952		\$ 25.21	\$ 24,000		8/1/2014	8/1/2015	1	5.0%	33.30%
Apartment 16	952		\$ 25.21	\$ 24,000		8/1/2014	8/2/2015	1	5.0%	33.30%
Apartment 17	952		\$ 25.21	\$ 24,000		8/1/2014	8/3/2015	1	5.0%	33.30%
Apartment 18	952		\$ 25.21	\$ 24,000		8/1/2014	8/4/2015	1	5.0%	33.30%
Apartment 19	952		\$ 25.21	\$ 24,000		8/1/2014	8/5/2015	1	5.0%	33.30%
Apartment 20	952		\$ 25.21	\$ 24,000		8/1/2014	8/6/2015	1	5.0%	33.30%
Apartment 21	952		\$ 25.21	\$ 24,000		8/1/2014	8/7/2015	1	5.0%	33.30%
Apartment 22	952		\$ 25.21	\$ 24,000		8/1/2014	8/8/2015	1	5.0%	33.30%
Apartment 23	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
Apartment 24	952		\$ 25.21	\$ 24,000		8/1/2014	7/31/2015	1	5.0%	33.30%
<b>Subtotal Residential</b>	<b>22,848</b>	<b>75%</b>		<b>\$ 576,000</b>	<b>70%</b>					<b>33.30%</b>
<b>Total</b>	<b>30,462</b>	<b>100%</b>	<b>\$ 27.16</b>	<b>\$ 827,262</b>	<b>100%</b>					

<sup>97</sup> Loopnet

**Table 15. Rent Schedule**

Year:	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Retail 1	\$ -	\$ 62,816	\$ 86,267	\$ 88,855	\$ 91,520	\$ 94,266	\$ 97,094	\$ 100,007	\$ 103,007	\$ 106,097	\$ 109,280
Retail 2	\$ -	\$ 62,816	\$ 86,267	\$ 88,855	\$ 91,520	\$ 94,266	\$ 97,094	\$ 100,007	\$ 103,007	\$ 106,097	\$ 109,280
Retail 3	\$ -	\$ 62,816	\$ 86,267	\$ 88,855	\$ 91,520	\$ 94,266	\$ 97,094	\$ 100,007	\$ 103,007	\$ 106,097	\$ 109,280
<b>Subtotal Retail</b>	<b>\$ -</b>	<b>\$ 188,447</b>	<b>\$ 258,800</b>	<b>\$ 266,564</b>	<b>\$ 274,561</b>	<b>\$ 282,798</b>	<b>\$ 291,282</b>	<b>\$ 300,020</b>	<b>\$ 309,021</b>	<b>\$ 318,291</b>	<b>\$ 327,840</b>
Apartment 1	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 2	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 3	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 4	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 5	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 6	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 7	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 8	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 9	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 10	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 11	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 12	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 13	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 14	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 15	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 16	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 17	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 18	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 19	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 20	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 21	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 22	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 23	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
Apartment 24	\$ 7,992	\$ 25,200	\$ 26,460	\$ 27,783	\$ 29,172	\$ 30,631	\$ 32,162	\$ 33,770	\$ 35,459	\$ 37,232	\$ 39,093
<b>Apartment Residential</b>	<b>\$ 191,808</b>	<b>\$ 604,800</b>	<b>\$ 635,040</b>	<b>\$ 666,792</b>	<b>\$ 700,132</b>	<b>\$ 735,138</b>	<b>\$ 771,895</b>	<b>\$ 810,490</b>	<b>\$ 851,014</b>	<b>\$ 893,565</b>	<b>\$ 938,243</b>
<b>Total</b>	<b>\$ 191,808</b>	<b>\$ 793,247</b>	<b>\$ 893,840</b>	<b>\$ 933,356</b>	<b>\$ 974,692</b>	<b>\$ 1,017,936</b>	<b>\$ 1,063,177</b>	<b>\$ 1,110,510</b>	<b>\$ 1,160,035</b>	<b>\$ 1,211,856</b>	<b>\$ 1,266,083</b>
Growth		313.56%	12.68%	4.42%	4.43%	4.44%	4.44%	4.45%	4.46%	4.47%	4.47%



**Table 16. Rollover Schedule (sf)**

	Year:	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Retail 1												
Retail 2								7,614				
Retail 3												
	<b>Subtotal Retail</b>	0	0	0	0	0	0	7614	0	0	0	0
Apartment 1			952	952	952	952	952	952	952	952	952	952
Apartment 2			952	952	952	952	952	952	952	952	952	952
Apartment 3			952	952	952	952	952	952	952	952	952	952
Apartment 4			952	952	952	952	952	952	952	952	952	952
Apartment 5			952	952	952	952	952	952	952	952	952	952
Apartment 6			952	952	952	952	952	952	952	952	952	952
Apartment 7			952	952	952	952	952	952	952	952	952	952
Apartment 8			952	952	952	952	952	952	952	952	952	952
Apartment 9			952	952	952	952	952	952	952	952	952	952
Apartment 10			952	952	952	952	952	952	952	952	952	952
Apartment 11			952	952	952	952	952	952	952	952	952	952
Apartment 12			952	952	952	952	952	952	952	952	952	952
Apartment 13			952	952	952	952	952	952	952	952	952	952
Apartment 14			952	952	952	952	952	952	952	952	952	952
Apartment 15			952	952	952	952	952	952	952	952	952	952
Apartment 16			952	952	952	952	952	952	952	952	952	952
Apartment 17			952	952	952	952	952	952	952	952	952	952
Apartment 18			952	952	952	952	952	952	952	952	952	952
Apartment 19			952	952	952	952	952	952	952	952	952	952
Apartment 20			952	952	952	952	952	952	952	952	952	952
Apartment 21			952	952	952	952	952	952	952	952	952	952
Apartment 22			952	952	952	952	952	952	952	952	952	952
Apartment 23			952	952	952	952	952	952	952	952	952	952
Apartment 24			952	952	952	952	952	952	952	952	952	952
	<b>Subtotal Residential</b>	0	22848	22848	22848	22848	22848	22848	22848	22848	22848	22848
<b>Total SF Rolling</b>		0	22848	22848	22848	22848	22848	38076	22848	22848	22848	22848
Renewal Probability			75.00%									
Tenant Improvements (Residential)	\$	-	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424	\$ 11,424
Leasing Commissions (Retail)	\$	-	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 9,103	\$ -	\$ -	\$ -	\$ -
Leasing Commissions (Residential)	\$	-	\$ 9,072	\$ 9,526	\$ 10,002	\$ 10,502	\$ 11,027	\$ 11,578	\$ 12,157	\$ 12,765	\$ 13,403	\$ 14,074
	<b>Subtotal LC</b>	\$ -	\$ 9,072	\$ 9,526	\$ 10,002	\$ 10,502	\$ 11,027	\$ 20,681	\$ 12,157	\$ 12,765	\$ 13,403	\$ 14,074
	<b>Total Projected Costs (baseline \$)</b>	\$ -	\$ 20,496	\$ 20,950	\$ 21,426	\$ 21,926	\$ 22,451	\$ 32,105	\$ 23,581	\$ 24,189	\$ 24,827	\$ 25,498
Reserve Balance Accum (baseline \$)	\$	26,577	\$ 32,658	\$ 38,285	\$ 43,436	\$ 48,087	\$ 52,212	\$ 46,684	\$ 49,680	\$ 52,067	\$ 53,817	\$ 54,896
Annual Avg TI psf (baseline \$)	\$		0.38									
Annual Avg LC psf (baseline \$)	\$		0.50									

## Discounted Cash Flow Analysis

Once gross rental income and required reserves were calculated, the following conservative assumptions were used to project NOI and Internal Rate of Return (IRR) for this project:

**Table 17. Discounted Cash Flow (DCF) Assumptions**

	ASSUMPTION		RATIONALE
<b>Income</b>	% Rent Growth (Retail)	3.00%	Conservative projection/current growth rate = 5%
	% Rent Growth (Residential)	5.00%	Projected 6-12% per Commercial Prop Exec/capped at CPI projection
	Vacancy Retail	4.50%	5-yr avg for market per Loopnet
	Vacancy Residential	3.50%	Conservative estimate per Soto interview (currently 2.6%)
	Terminal Cap Rate	6.50%	8-yr high per Cassidy Tuley
	Selling Costs	3.00%	Estimate
	Discount Rate	12.00%	WAAC = 8.94% + risk premium
<b>Operating Expenses</b>		PSF	
	Taxes \$	3.03	Per Santa Cruz prop tax rate
	Insurance \$	0.20	Estimate
	G&A \$	0.50	Estimate
	Utilities \$	0.12	per Pacifica offer
	Security \$	0.10	Estimate
	Grounds/Trash \$	0.25	Estimate
	<u>Total \$</u>	<u>4.20</u>	
	Management	5.00%	Local rate per Ataki interview
	Annual Exp. Growth	5.00%	Projected CPI per MIP Model
Annual Tax Growth	2.00%	Capped by CA Prop 13	

From these assumptions and projections, a 10-year DCF calculation is made for 408 Front St. The abbreviated DCF below results in the project having a NPV of \$780,582 and an IRR of 14.98%. The NPV provides a margin of error of almost \$800 thousand for the project to be viable at a 12% discount rate. (See Appendix H for full DCF calculation).

**Table 18. Discounted Cash Flow (DCF) Calculations (abbreviated)**

		408 Front St 10yr DCF							
		Construction		Absorption					
Year		2012	2013	2014	2015	2016	2023	2024	
<b>Rental Income</b>	Retail	N/A	N/A	\$ -	\$ 188,447	\$ 258,800	\$ 318,291	\$ 327,840	
	Residential	N/A	N/A	\$ 191,808	\$ 604,800	\$ 635,040	\$ 893,565	\$ 938,243	
Total		N/A	N/A	\$ 191,808	\$ 793,247	\$ 893,840	\$ 1,211,856	\$ 1,266,083	
Reimbursements (Retail) @	25%			vacant	75% occupied	100% occupied			
NNN	Taxes	\$ 3.03	N/A	N/A	\$ -	\$ 18,372	\$ 24,986	\$ 28,701	\$ 29,275
	Insurance	\$ 0.20	N/A	N/A	\$ -	\$ 587	\$ 1,851	\$ 2,605	\$ 2,735
	G&A	\$ 0.50	N/A	N/A	\$ -	\$ 1,468	\$ 4,627	\$ 6,511	\$ 6,837
	Utilities	\$ 0.12	N/A	N/A	\$ -	\$ 352	\$ 1,111	\$ 1,563	\$ 1,641
	Security	\$ 0.10	N/A	N/A	\$ -	\$ 294	\$ 925	\$ 1,302	\$ 1,367
	Grounds/Trash	\$ 0.25	N/A	N/A	\$ -	\$ 734	\$ 2,314	\$ 3,256	\$ 3,418
Reimbursements (Residential) @	75%	N/A	N/A	\$ 335	\$ 1,058	\$ 1,111	\$ 1,563	\$ 1,641	
Tenant pays utilities									
	Potential Gross Income (PGI)	N/A	N/A	\$ 192,143	\$ 816,110	\$ 930,764	\$ 1,257,356	\$ 1,312,997	
	Vacancy (Wt Avg)	3.75%	N/A	N/A	\$ -	\$ -	\$ 34,904	\$ 47,151	\$ 49,237
	EGI	N/A	N/A	\$ 192,143	\$ 816,110	\$ 895,861	\$ 1,210,205	\$ 1,263,760	
<b>Expenses</b>	Taxes	\$ 92,350	\$ 94,197	\$ 96,081	\$ 98,003	\$ 99,963	\$ 114,826	\$ 117,122	
	Insurance	\$ 6,092	\$ 6,397	\$ 6,717	\$ 7,053	\$ 7,405	\$ 10,420	\$ 10,941	
	G&A	\$ 15,231	\$ 15,993	\$ 16,792	\$ 17,632	\$ 18,513	\$ 26,050	\$ 27,353	
	Utilities	\$ 3,655	\$ 3,838	\$ 4,030	\$ 4,232	\$ 4,443	\$ 6,252	\$ 6,565	
	Security	\$ 3,046	\$ 3,199	\$ 3,358	\$ 3,526	\$ 3,703	\$ 5,210	\$ 5,471	
	Grounds/Trash	\$ 7,616	\$ 7,996	\$ 8,396	\$ 8,816	\$ 9,257	\$ 13,025	\$ 13,676	
	5.00% Management	N/A	N/A	\$ 9,607	\$ 40,806	\$ 44,793	\$ 60,510	\$ 63,188	
Total OpEx		\$ 127,991	\$ 131,620	\$ 144,982	\$ 180,066	\$ 188,077	\$ 236,293	\$ 244,315	
OpEx Ratio		N/A	N/A	75.45%	22.06%	20.99%	19.53%	19.33%	
<b>Reserves</b>	NOI	\$ (127,991)	\$ (131,620)	\$ 47,162	\$ 636,044	\$ 707,784	\$ 973,912	\$ 1,019,444	
	TI	N/A	N/A	\$ 11,424	\$ 11,995	\$ 12,595	\$ 17,722		
	LC	N/A	N/A	\$ 11,424	\$ 11,938	\$ 12,475	\$ 16,977		
	CapEx	N/A	N/A	\$ 7,616	\$ 7,996	\$ 8,396	\$ 11,814		
	Total Reserves	N/A	N/A	\$ 30,464	\$ 31,930	\$ 33,466	\$ 46,514		
CFfDS		\$ (127,991)	\$ (131,620)	\$ 16,698	\$ 604,114	\$ 674,317	\$ 927,398		
DS Payment		\$ 274,556	\$ 274,556	\$ 274,556	\$ 486,313	\$ 486,313	\$ 486,313		
CFaDS		\$ (402,547)	\$ (406,176)	\$ (257,858)	\$ 117,802	\$ 188,005	\$ 441,086		
Refi Cash Out						\$ 1,558,836			
Refi Closing Costs						\$ (183,474)			
Terminal Value								\$ 15,683,758	
Selling Costs								\$ 470,513	
Perm Loan Repayment								\$ 6,014,156	
Gain on Sale								\$ 9,199,088	
<b>Cash Flow</b>		\$ (2,477,199)	\$ (402,547)	\$ (406,176)	\$ (257,858)	\$ 1,493,164	\$ 188,005	\$ 9,640,174	
	IRR	14.98%							
	NPV	\$ 780,582							

## **Exit Strategies**

The 408 Front St project requires a commitment of at least 10 years to garner the projected returns. At that time, there are three possible exit strategies depending on market conditions at the time:

1. Sell the property outright: This is the exit strategy that is presumed in the Pro Forma. Once the property is fully leased and management optimized to maximize net income, assuming a favorable economic environment, the relatively low capitation (CAP) rates of the Santa Cruz market results in a potential gain on sale of over \$9 million, based on a conservative 6.5% terminal CAP rate (the 8-year high).
2. Continue to hold as a portfolio investment for a longer term: If economic conditions remain favorable, the scarcity of developable land in Santa Cruz will continue to apply upward pressure on demand and rental rates, possibly enough to exceed normal inflation rates and increase future returns. Depending on alternative investment opportunities (i.e. opportunity costs), holding on to the property may prove the best option. However, tax implications should also be considered as rental income exceeds depreciation expense, thereby increasing tax liability for the owners.
3. A combination strategy: Again, depending on the economic environment and opportunity costs at the time, a third possibility would be to subdivide the title to retain the retail portion of the building and sell the residential units as condominiums. This strategy may prove attractive if investors wish to hold a portion of the project for the long term, but free capital for other investment opportunities.

## **Conclusion**

The \$8.26 million 408 Front St project proves viable at a 12% discount rate based on conservative assumptions and well researched estimates. In addition, the \$800 thousand NPV gives a 9.4% margin of error for the analysis, making it an attractive investment in a promising market with growing demand and constrained supply.

## APPENDIX A

### Demographic Data for Santa Cruz

*Source: U.S. Census Bureau*

DP-1: Profile of General Population and Housing Characteristics: 2010		
2010 Demographic Profile Data		
Subject	Number	Percent
<b>SEX AND AGE</b>		
Total population	59,946	100.0
Under 5 years	2,358	3.9
5 to 9 years	2,276	3.8
10 to 14 years	2,153	3.6
15 to 19 years	7,504	12.5
20 to 24 years	11,354	18.9
25 to 29 years	4,416	7.4
30 to 34 years	3,717	6.2
35 to 39 years	3,465	5.8
40 to 44 years	3,435	5.7
45 to 49 years	3,461	5.8
50 to 54 years	3,742	6.2
55 to 59 years	3,822	6.4
60 to 64 years	2,958	4.9
65 to 69 years	1,721	2.9
70 to 74 years	1,132	1.9
75 to 79 years	833	1.4
80 to 84 years	750	1.3
85 years and over	849	1.4
Median age (years)	29.9	( X )
16 years and over	52,694	87.9
18 years and over	51,750	86.3
21 years and over	42,119	70.3
62 years and over	6,948	11.6
65 years and over	5,285	8.8
<b>RACE</b>		

Total population	59,946	100.0
One Race	56,544	94.3
White	44,661	74.5
Black or African American	1,071	1.8
American Indian and Alaska Native	440	0.7
Asian	4,591	7.7
Native Hawaiian and Other Pacific Islander	108	0.2
Some Other Race	5,673	9.5
Two or More Races	3,402	5.7
<b>HISPANIC OR LATINO</b>		
Total population	59,946	100.0
Hispanic or Latino (of any race)	11,624	19.4
Not Hispanic or Latino	48,322	80.6
<b>HOUSEHOLDS BY TYPE</b>		
Total households	21,657	100.0
Family households (families) [7]	10,005	46.2
With own children under 18 years	4,439	20.5
Husband-wife family	7,310	33.8
With own children under 18 years	3,005	13.9
Male householder, no wife present	862	4.0
With own children under 18 years	409	1.9
Female householder, no husband present	1,833	8.5
With own children under 18 years	1,025	4.7
Nonfamily households [7]	11,652	53.8
Householder living alone	6,773	31.3
Male	3,155	14.6
65 years and over	560	2.6
Female	3,618	16.7
65 years and over	1,302	6.0
Households with individuals under 18 years	4,817	22.2
Households with individuals 65 years and over	4,111	19.0
Average household size	2.39	( X )
Average family size [7]	2.92	( X )
<b>HOUSING OCCUPANCY</b>		
Total housing units	23,316	100.0
Occupied housing units	21,657	92.9
Vacant housing units	1,659	7.1

For rent	437	1.9
Rented, not occupied	74	0.3
For sale only	118	0.5
Sold, not occupied	43	0.2
For seasonal, recreational, or occasional use	692	3.0
All other vacants	295	1.3
Homeowner vacancy rate (percent) [8]	1.2	( X )
Rental vacancy rate (percent) [9]	3.4	( X )
<b>HOUSING TENURE</b>		
Occupied housing units	21,657	100.0
Owner-occupied housing units	9,375	43.3
Population in owner-occupied housing units	22,861	( X )
Average household size of owner-occupied units	2.44	( X )
Renter-occupied housing units	12,282	56.7
Population in renter-occupied housing units	28,796	( X )
Average household size of renter-occupied units	2.34	( X )
X Not applicable.		



## APPENDIX B

### Santa Cruz Employment Statistics by District

*Source: Gibbs Planning Group, Inc.*

Description	<i>West Zone</i>	<i>East Zone</i>	<i>Central Zone</i>	<i>Waterfront Zone</i>
	<i>Cabrillo Highway</i>	<i>Soquel Avenue</i>	<i>Pacific Avenue</i>	<i>Beach Street</i>
	<i>5 Minute(s) Drive Time 1</i>	<i>5 Minute(s) Drive Time 1</i>	<i>5 Minute(s) Drive Time 1</i>	<i>5 Minute(s) Drive Time 1</i>
<b>Total Employment</b>	32,987	37,779	33,621	28,523
<b>Executive and Professional</b>	11,245	12,664	11,432	9,602
Management	2,430	2,745	2,469	2,069
Sales and Marketing	3,651	4,070	3,719	3,080
Health-Legal-Social	1,991	2,489	2,061	1,782
Engineer-Science-Computer Professional	1,051	1,081	1,046	871
Educators	1,402	1,515	1,413	1,183
Journalists-Creative Professional	720	763	723	615
<b>Administration and Support</b>	8,769	10,143	8,903	7,489
Management Support	1,313	1,432	1,316	1,158
Admin-Clerical Support	6,240	7,169	6,340	5,305
Technical Support	1,216	1,542	1,247	1,025
<b>Service Personnel</b>	6,602	7,626	6,829	6,384
Health Care Personnel	378	707	416	341
Food and Beverage	4,065	4,441	4,229	4,054
Personal Services	1,428	1,685	1,451	1,324
Protective Services	731	793	733	665
<b>Trade and Labor</b>	6,372	7,346	6,456	5,048
Construction	837	1,003	828	586
Installation and Repair	2,013	2,428	2,047	1,749
Craft Production	490	511	480	313
Machine Operators	488	493	499	370
Assemblers	311	276	308	182
Transportation	900	1,018	942	800
Agriculture	496	621	494	398
Laborers	836	997	857	651

## APPENDIX C

### Local and State Plans Applicable to Development Efforts

*Source: Santa Cruz Planning Department*

In addition to the General Plan, the City has developed more detailed plans for specific areas within its jurisdiction. These include:

- Arana Gulch Master Plan, 2006
- Beach and South of Laurel Comprehensive Area Plan, 1998
- Downtown Recovery Plan, 1991 as amended through 2009
- Eastside Business Area Development Plan, 1996
- Mission Street Urban River Plan, 2003
- Santa Cruz Harbor Development Plan, 1992
- Seabright Area Plan, 1981
- Western Drive Master Plan, 1979

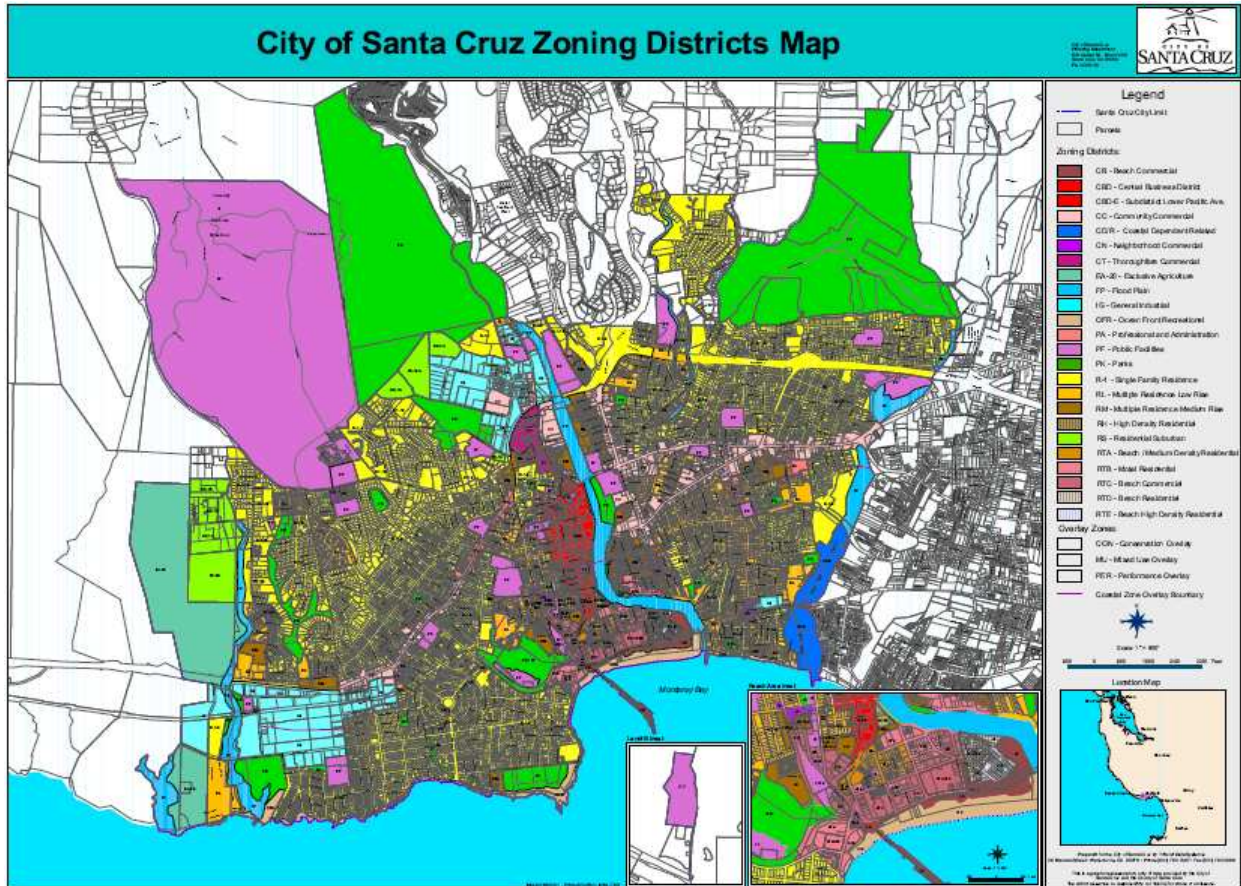
The State of California also has five land-use plans which affect areas in and around Santa Cruz:

- Lighthouse Field State Beach General Plan, 1984
- Natural Bridges State Beach Plan, 1988
- Twin Lakes State Beach General Plan, 1988
- UCSC Long Range Development Plan, 2006
- UCSC Marine Science Campus Coastal Long Range Development Plan, 2004

# APPENDIX D

## Zoning Map

Source: City of Santa Cruz Planning Department



## APPENDIX E

### Residential Rent Statistics

Source: University of California, Santa Cruz Housing Office



The banner features the University of California Santa Cruz logo on the left, followed by the text "UNIVERSITY OF CALIFORNIA SANTA CRUZ" and "Community Rentals" in large white font on a blue background. Below the banner is a navigation bar with links: Home, Search Rentals, Post a Rental, Online Services, Rental Resources, and FAQ's.

### Rental Costs Statistics

#### Rental Cost Statistics

January 1, 2011 - December 31, 2011

[Print statistics](#) (PDF) on Community Rentals letterhead

Rental Type	Rent Range	Listings	Average Rent
Room in Household*	\$400-950	645	\$697
Studios/Efficiencies	\$600-1150	244	\$852
1 BR House/Duplex	\$850-1500	46	\$1192
1 BR Apt/Condo	\$800-1578	143	\$1180
2 BR House/Duplex	\$1250-2500	120	\$1823
2 BR Apt/Condo	\$1050-2500	215	\$1715
3 BR House/Duplex	\$1800-3500	179	\$2565
3 BR Apt/Condo	\$1750-2950	60	\$2376
4 BR House/Duplex	\$2100-4200	70	\$3231
5-6 BR House/Duplex/Apartment	\$2990-5800	62	\$4260

Several variables will determine your monthly housing costs in the off-campus community

- Proximity to campus
- Age or condition of unit
- Size of room or unit
- Amenities included, e.g. utilities, Wi-Fi, gardener

\*These figures include both unfurnished and furnished rentals. They can include the cost of utilities, WiFi, private baths, allowing 2 people per room, special locations (e.g. oceanfront), housecleaner, and/or gardener.

We cannot confirm if these listings were rented at these prices.

You may access an abbreviated version of current listings for more specific price comparisons [here](#). Click on the **Post Your Rental Here** button. Then click on **View Rental List**. This list is grouped first by type of unit and then by number of bedrooms.

## APPENDIX F

### Commercial Real Estate (Retail) Sales Comparables From Central Business District

*Source: Loopnet*

<b>Date Sold</b>	<b>Address</b>	<b>Size (sf)</b>	<b>Price</b>	<b>Cost per sf</b>
April, 2009	815 Pacific Ave	15,000	\$2.25M	\$150
July, 2008	923 Pacific Ave	10,000	\$1.75M	\$175
March, 2006	907 Cedar St	7500	\$1.75M	\$233
March, 2006	216 Lincoln St	7500	\$1.75M	\$233
November, 2005	816 Pacific Ave	3000	\$925K	\$308

## APPENDIX G

### LEED Construction Green Building Checklist

*Source: City of Santa Cruz Planning Office*

LEED Criterion	Points Available for Building Dept Incentives
<b>A. Sustainable Sites</b>	
Erosion & Sediment Control	1
Site Selection	1
Urban Redevelopment/Development Density	1
Brownfield Redevelopment	1
Alternative Transportation – Public Transportation Access	1
Alternative Transportation– Bicycle Storage and Changing Rooms	1
Alternative Transportation—Alternative Fuel Vehicles	1
Alternative Transportation—Parking Capacity	1
Reduce Site Disturbance—Protect or Restore Open Space	1
Reduce Site Disturbance—Development Footprint	1
Stormwater Management—Rate and Quantity	1
Stormwater Management—Treatment	1
Heat Island Effect—Non-roof	1
Heat Island Effect—Roof	1
Light Pollution Reduction	1
Available Points	15
<b>B. Water Efficiency</b>	
Water Efficient Landscaping—Reduce by 50%	1
Water Efficient Landscaping—No Potable Use or No Irrigation	1
Innovative Wastewater Technologies	1
Water Use Reduction—20% Reduction	1
Water Use Reduction—30% Reduction	1
Available Points	5
<b>C. Energy &amp; Atmosphere</b>	
Fundamental Building System Commissioning	1
CFC Reduction in HVAC&R Equipments	1

Optimize Energy Performance	10
Renewable Energy—5%	1
Renewable Energy—10%	1
Renewable Energy—20%	1
Additional Commissioning	1
Ozone Depletion	1
Measurement & Verification	1
Green Power	1
Available Points	19
<b>D. Materials &amp; Resources</b>	
Storage and Collection of Recyclables	1
Building Reuse—Maintain 75% of Existing Shell	1
Building Reuse—Maintain 100% of Existing Shell	1
Building Reuse—Maintain 100% of Existing Shell and 50% Non-Shell	1
Construction Waste Management—Divert 50%	1
Construction Waste Management—Divert 100%	1
Resource Reuse—Specify 5%	1
Resource Reuse—Specify 10%	1
Recycled Content—Specify 5%	1
Recycled Content—Specify 10%	1
Recycled Content—Specify 20%	1
Local/Regional Materials—20% Manufactured Locally	1
Local/Regional Materials—20% Manufactured Locally + 50% Harvested Locally	1
Rapidly Renewable Materials	1
Certified Wood	1
Available Points	14
<b>E. Indoor Environmental Quality</b>	
Minimum IAQ Performance	1
Environmental Tobacco Smoke Control	1
Carbon Dioxide Monitoring	1
Ventilation Effectiveness	1
Construction IAQ Mgt Plan—During Construction	1
Construction IAQ Mgt Plan—Before Occupancy	1
Low-Emitting Materials—Adhesives & Sealants	1
Low-Emitting Materials—Paints	1
Low-Emitting Materials—Carpet	1

Low-Emitting Materials—Composite Wood	1
Indoor Chemical & Pollutant Source Control	1
Controllability of Systems—Perimeter	1
Controllability of Systems—Non-perimeter	1
Thermal Comfort—Comply with ASHRAE 55-1992	1
Thermal Comfort—Permanent Monitoring System	1
Daylight & Views—Daylight 75% of Spaces	1
Daylight & Views—Daylight 90% of Spaces	1
Available Points	17
<b>F. Innovation &amp; Design Process</b>	
Innovation in Design	1
Another Innovation in Design	1
Another Innovation in Design	1
Another Innovation in Design	1
LEED Accredited Professional	1
Available Points	5
<b>Total Available Points</b>	<b>75</b>

Source: City of Santa Cruz Green Building Program: Standards of Compliance, Appendix A



