REALTY MENTORS
EXPERT ADVICE FOR COMMERCIAL REAL ESTATE INVESTING.

COMMERCIAL REAL ESTATE ANALYSIS REPORT

PROPERTY

Name	Sunset Apartments
Address	1800 Main Street, Hometown, USA
Property Type	Class C Apartments, Partially Section 8
# Units / SF	62 Units
Year Built / Renovated	1968 / NAP
Occupancy (Current)	97%
(Projected)	95%
Unit Mix / Top Tenants	• 1 BR/1 BA - 1 unit • 2 BR/1.5 BA - 23 units • 3 BR/2 BA - 38 units
Construction Type	2-story garden style; brick façade with pitched roofs
Parking	Surface parking lot (# of spaces not provided) **This is potentially an important piece of data**
Amenities	Pool, playground and pond mentioned **Very little detail provided**

DEAL TERMS

Sponsor	ABC Realty Group
Management	ABC Realty Group LLC; Self-managed
Dollars Being Raised	$1,450,000 in equity (See Sources & Uses Below)
Funding Purpose	Acquisition and renovation of the subject property
Value (Current)	$2,200,000 acquisition cost *(No appraisal provided)*
(Projected)	$5,089,837 projected sale price at the end of year 3
Investment To Value (Current)	100% (Debt & Preferred Equity) **100% because the Sponsor is not contributing any equity**
(Projected)	70% (Debt & Preferred Equity)
Equity Raise / Total Cost Basis	41%

Projected IRR	24% **Only meaningful if you trust the pro-forma projections**
Term or Exit Strategy	Sale of the subject property; projected at 3 years but subject to extension at sponsor's sole discretion **Not uncommon in crowdfunding for Sponsor to have this level of control but an institutional investor would require more control**
Rate / Return Schedule	10% preferred distributions per annum and 2% deferred until reversion of the Investment (unaccrued), cumulative and non-compounding ** This could be considered a reasonable/fair structure** • 100% of all Distributable Cash to each Investor, until such Investor receives the aggregate amount of the Investor's Capital Contribution • 100% of all Distributable Cash to each Investor until such Investor has received a total annual preferred return of 10% on unreturned Capital Contributions paid monthly, and 2% deferred (unaccrued) until time of sale 80% of all remaining Distributable Cash to the Investors ** This is a reasonable ratio**
Special Conditions	$51,316 cash flow reserve $118,191 rehab contingency
Fee Structure	• 3% property acquisition fee (% of purchase price) • 6% disposition fee (% of sale price) • 6% management fee [Self-Managed and no management agreement provided – fee extrapolated from pro-forma] (% of cash flow) ** At the high end of typical fees of 3%-6%** • 5% administration Fee (% of cash flow) ** This is a high fee when considering the Sponsor is already collecting management fees** • 8% Construction Management Fee; Paid quarterly (% of renovations) ** Higher than typical fees of around 6%** 20% of all cash distributions (To be paid out of excess cash generated over preferred investor return)
Sponsor Equity	None **We look for the Sponsor to have equity in the property, so that they are sharing in the risk**
Net Operating Income (Current) (Projected)	 $97,811 (As of YE 2016) $356,289 (Year 3 of operation)
Fixed Obligation Coverage Ratio	Year 1: 1.42x on debt – 0.41x with Investor Preferred Distributions Year 2: 1.82x on debt – 0.94x with Investor Preferred Distributions (Year 2 and still not projected to be cash flow positive) Year 3: 1.87x on debt – 1.30x with Investor Preferred Distributions

SOURCES & USES

USES				
Sunset Acquisition			$2,200,000	
Acquisition Costs			$155,688	
Renovation Expense			$1,013,731	
Cash Flow Reserves			$51,316	
Rehab Contingency			$118,191	
Total Cost Basis				$3,538,926
SOURCES				
Debt				
Senior Debt		65%	($1,430,000)	
Renovation Debt			($658,925)	
Total Debt				($2,088,925)
Equity				
	Acquisition	35%	($770,000)	
	Renovation	35%	($354,806)	
	Origination Fees (2pts)		($41,779)	
	Closing Costs		($113,909)	
	Cash Flow Reserves		($51,316)	
	Rehab Contingency		($118,191)	
Total Equity				($1,450,000)
Total Sources				($3,538,926)

Strengths:

Location:

Proximity to University and the associated University Health System

0.5 miles to retail/shopping/restaurant corridor at 1st Avenue and Main Street in addition to scattered shopping centers and big box stores in the local area

Occupancy:

97% occupancy pre-renovation

Market:

Per ALN Apartment Data, strong market occupancy of 96.2% as of April 2017 with a 0.2% increase over April 2016

Risks / Mitigants:

Section 8 Units:

The market can view a Section 8 property as stigmatized depending on the nature of the property. This can inhibit the Sponsor's ability to raise rents aggressively. In addition, some Section 8 tenants can be difficult to turn over depending on the nature of the Section 8 program. This can be mitigated with a better understanding of the subject program. There are typically specific rules and regulations for how a given property can be converted to market rate rents.

Sponsor Equity Contribution:

It appears that the Sponsor will not be contributing any capital towards the $1,450,000 necessary to fund the project equity requirement. If this is the case, the Sponsor essentially has no "skin in the game" and therefore does not share the same level of risk as the investors. This could be an indication that the Sponsor is more financially motivated to generate deals in volume to collect fees vs. taking a more thoughtful approach to selecting higher quality deals. In addition, the fee structure is very generous for the sponsor. The investor's returns are "preferred" but appear to remain subordinate to the 3% property acquisition fee, 6% disposition fee, 6% management fee, 5% administration fee and 8% construction management fee. If investors want to remove Sponsor as Manager of the Operating Agreement, they must pay a one-time buyout fee of $500,000. It is worth knowing if the Sponsor is personally guaranteeing the debt on the 1st mortgage. If the loan is personally guaranteed, the Sponsor will have at least some degree of risk if the entire investor raise is wiped out. Nothing is disclosed regarding the Sponsor's financial background, their ability to contribute capital to the Property or why they have chosen not to contribute any capital up front.

Age/Condition:

The property was constructed in 1968, and the OM states the property has had very little in the way of capital improvements since 2005 (~ $300,000). This is somewhat mitigated by the approximate $1MM in planned property renovations. With that said, there is no engineering report provided so there is no way of knowing how much maintenance is necessary at the Property. Further, there are no specifics provided for what is actually being done to rehab the units.

Aggressive rehab and lease up schedule:

Pro-forma includes only one month of downtime per unit. Two to three months would be more in line with standard unit rehab and re-leasing. In addition, projections call for only 14 months from acquisition to rehab all units and rent stabilization. 8% annual increases on stabilized rents may be an aggressive assumption. Consider the fact that early on, as units turn over, will new tenants be willing to pay a full market rate rent while surrounded by section 8 units? Even the 3 year disposition is a short turn-around for the property to reposition itself in the market, especially considering the possible poor current property condition and the Section 8 units currently in place. This is partially mitigated if the investor is willing to tolerate a longer hold period for the subject investment.

Sponsor Execution Risk:

No sort of resume or track record has been provided for the Sponsor. Has the Sponsor successfully completed similar projects in the past? For a rehab project of this nature, a prudent investor would want to see a track record to evidence that the Sponsor has the experience and expertise to execute the aggressive plan which has been laid out in the offering and pro-forma. Further, this Property is to be self-managed so no assistance is being procured to help with execution.

Real Estate Tax Risk:

There is very little provided regarding the local real estate taxes. In some jurisdictions, a sale of a property can trigger a re-assessment. We do not know the current assessed value. If taxes are increased, this directly impacts the bottom line cash flow the property generates.

Overall Thoughts and Recommendations:

In the opinion of Realty Mentors, there is not enough information and/or data being provided to determine this investment opportunity's merit. While it appears that the property should not have trouble operating at high occupancy now or in the future based on the market, there are a number of concerns that bring into question the ability to re-position the property and increase rents within this timeframe, including the unknowns regarding the Section 8 units, tight construction timelines, and the lack of adequate information about the sponsor's experience. Further, an investor should note that the Sponsor is not projected to generate enough cash to pay the preferred 10% return to investors until year 3 of the project.

There are no independent 3rd party reports, particularly an appraisal. In addition, the Sponsor does not provide an engineering report. This would very much help in understanding the Property's current condition and whether the Sponsor's rehab plan is sufficient.

In summary, based on available information, this is not a deal that Realty Mentors would view as favorable from a risk/return perspective. There are too many questions and concerns outstanding, and the financial structure of the deal appears to heavily favor the Sponsor.

Assumptions:

- All information provided by the sponsor is true and correct. There is no willful or inadvertent fraud being propagated.
- There are no zoning issues currently or associated with the planned renovations.
- The city/township has or will approve all plans for property renovations.
- All past due accounts and liens have been settled and real estate taxes are current.
- The Property does not have any environmental issues; thus, an environmental report is not needed.

Legal Disclosures:

- The work product contained herein is confidential. Its use shall be in accordance with the Client Services Agreement.
- Realty Mentors does not guarantee the future performance of this investment opportunity. All investment opportunities are subject to inherent risks, including but not limited to those outlined in the due diligence documents provided by the investment's sponsor.
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REALTY MENTORS
EXPERT ADVICE FOR COMMERCIAL REAL ESTATE INVESTING.

Phone: 412-263-3440

Email: contact@realtymentors.com