October 29, 2021

Ms. Cherisse Vickers, Executive Director
City of Newburgh IDA
City Hall, Third Floor
83 Broadway
Newburgh, NY 12550

Via email: IDADirector@cityofnewburgh-ny.gov

**RE: TEST OF REASONABLENESS FINDINGS – NEWBURGH HOTEL
FSH NEWBURGH HOTEL, LLC AND GRAND STREET NEWBURGH PROPERTY CO, LLC**

Dear Cher:

The City of Newburgh Industrial Development Agency (the "IDA") is considering providing assistance to a real estate development project in the City of Newburgh (the "City") as proposed by FSH Newburgh Hotel LLC and Grand Street Newburgh Property Co, LLC (the "Developer"). The Developer is proposing to construct a mixed-use project that includes a hotel, event center, spa, and dining facility (the "Project"). The IDA engaged MRB Group to provide certain advisement and analysis including the completion of a cost-benefit analysis (CBA) of the Project that conforms to the requirements of Section 859-a(5) of General Municipal Law and the completion of a "reasonableness test" of the assistance being requested by the Developer.

The CBA has been delivered under separate cover and this letter serves to summarize our analysis and findings.

Scope of Analysis

To conduct this test of reasonableness, the IDA required the Developer to submit to MRB Group a pro forma financial analysis of the Project. MRB Group analyzed the Developer's submitted information and requested level of assistance. We compared the assumptions used in that pro forma analysis against other sources. As necessary, we adjusted the pro forma assumptions and calculated a new anticipated return or range of returns.

The analysis focused on two key outputs: (1) whether the Project would meet bank financing conditions, such as meeting minimum Debt Service Coverage Ratios (DSCR), and (2) whether the Project's pre-tax cash flow internal rate of return (IRR) would be in excess of normal returns for the area and project type. We benchmarked the projected IRR against returns listed in RealtyRates.com's most recent "Investor Survey" to determine reasonableness.

Discussion

MRB Group requested certain pro forma financial projections and the Developer provided two spreadsheets:

- The first detailing the project's overall budget, the construction budget, employment counts, stabilized operating revenues, and projected EBITDA (Earnings Before Interest Taxes Depreciation and Amortization, an indicator of operating cash flow), and
- The second detailing the capital structure of the deal, financing terms and conditions, and a profit-and-loss summary.

MRB Group reviewed the above, asked for and received certain clarifications, and participated in two phone consultations with the Developer. To preserve confidentiality, we do not disclose the exact figures provided by the Developer and the discussions therein. However, we do note that our analysis and conversations with the Developer included the following assumptions and projections used by the Developer: the Average Daily Rate (ADR), Revenue per Available Room (RevPAR), occupancy rate, cost-of-goods-sold (COGS), financing terms and conditions, such as interest rate, term, loan-to-value, debt-service-coverage-ratio, etc. We also discussed and reviewed the financial incentives requested by the Developer, including the proposed PILOT terms and financial assistance the Developer would be receiving through other sources.

We benchmarked the assumptions used by the Developer against several sources, including the afore-mentioned RealtyRate.com "Investor Survey" and Costar's hospitality-related market information on ADR, RevPAR and occupancy rate. The "Investor Survey" provided the following data regarding the market's "Equity Dividend Rates": rates ranged from a minimum of 7.83% to a maximum of 18.11% with an average of 12.46%.[1] It also listed the current cap rate for such properties at 9.44%.

Using these assumptions and after making certain adjustments, we modeled the return-on-equity of the project by estimating cash flows to/from the equity investor(s) with a hypothetical exit in year 5. The exit price was estimated using the terminal year EBITDA and the cap rate described above, from which we subtracted out the remaining debt principal outstanding and presumed costs of sale. This provided a simplified Internal Rate-of-Return (IRR) that is equivalent to the above Equity Dividend Rate. We then recommended an adjustment to the Developer's proposed PILOT exemption schedule, which the Developer agreed to and formalized by submitting a revision to its IDA application, such amendment dated October 19, 2021.

[1] Source: RealtyRates.com Investor Survey Q3 2021 for "Full Service Lodging" properties.

Summary of Findings

We find that the Applicant's requested assistance, including the sales tax exemption, the mortgage recording tax exemption and the PILOT abatement schedule, as amended, provides the Developer a reasonable, risk-adjusted return and the Project's DSCR is adequate for financing purposes.

Thank you for this opportunity to assist the Newburgh IDA.

Sincerely,

R. Michael N'dolo
Director of Economic Development