January 11, 2024

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 V2
IV NEWBURGH SOUTH LOGISTICS CENTER 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 IV Newburgh South Logistics Center LLC (the "Developer"). The proposed project is located at 700 South Street in the City of Newburgh (the "Site") and includes the construction of a 416,320 square foot speculative industrial building on 49.5 acres of land (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 and Test of Reasonableness analysis were delivered to the IDA on December 21, 2023. Subsequently, the Developer made a number of adjustments to its IDA application for assistance, such changes potentially having a material impact on the Test of Reasonableness findings. On January 3, 2024, the IDA directed MRB Group to update its CBA and Test of Reasonableness. The revised CBA has been delivered under separate cover and this letter serves to update our summary of the analysis and findings of the reasonableness test.

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 "Investor Survey" to determine reasonableness.

Discussion

MRB Group requested certain pro forma financial projections, which the Developer provided in spreadsheet format (the "Projections"). The Projections included comprehensive details on the Project's:

- Sources of capital, including financing terms and conditions.
- Construction budget, including hard, soft, carrying and other costs.
- Operating revenues and expenses, including proposed PILOT terms.
- Cash flows, debt service requirements and owner returns.

For the original analysis dated December 21, 2023, MRB Group reviewed the above, asked for and received certain clarifications, and participated in several phone consultations with the Developer. As noted above, the Developer has since revised certain portions of its application for assistance, including material changes to its requested PILOT abatement schedule, such changes impacting the Test of Reasonableness.

Following the IDA's request on January 3, 2024 to update the analysis, MRB Group analyzed the revised pro forma financials from the Developer, updated to account for the change in the requested PILOT abatement schedule. To preserve confidentiality, we do not disclose the exact figures provided by the Developer and the discussions therein. However, we took the information and assumptions contained within the Projections, as revised, and benchmarked them against market data. The table below shows some of the benchmark reference values we used to evaluate the revised Projections, such benchmarks provided by RealtyRates.com.

Reference Values for Pro Forma Analysis

Metric	Min	Max	Average
Interest Rate - Construction	9.50%	15.45%	12.51%
Interest Rate - Permanent - All Industrial	5.25%	9.95%	7.34%
Interest Rate - Permanent - Distribution Only	5.25%	7.45%	6.35%
Debt Service Coverage Ratio*	1.10	2.05	1.45
Loan-to-Value Ratio*	50%	80%	70%
Amortization*	15	40	25
Equity Dividend Rate**	6.66%	13.91%	9.92%
Discount Rate	9.69%	15.33%	12.59%
Capitalization Rate	n/a	n/a	9.35%

*Metric with respect to permanent financing. **See note in narrative.
Source: RealtyRates.com's "Investor Survey" 4th Quarter 2023.

In previous analyses done for the IDA, MRB Group used the Equity Dividend Rate (see definitions below) as a benchmark for the Developer's return on investment. For consistency's sake, we have retained this line in the reference values table. However, due to the speculative nature of this Project, the more appropriate benchmark in this case would be the discount rate.

The definitions of the terms used in the table can be found below.

- Amortization: Years required at the specified interest rate to pay off the entire mortgage, including principal and interest, with a level payment.
- Capitalization Rate: The rate of return on a real estate investment property based on the net income that the property is expected to generate.
- Debt Service Coverage Ratio (DSCR): Ratio of annual mortgage payment, including interest and principal, to total net operating income (NOI, defined below).
- Discount Rate: An annual competitive rate of return on total invested capital necessary to compensate the investor for the risks inherent in a particular investment. A yield rate used to convert future payments or receipts into present value.
- Equity Dividend: The dollar return to the equity component: Net Operating income - Debt Service = Equity Dividend.
- Equity Dividend Rate: Rate of return to the equity component: NOI - Debt Service = Equity Dividend / Equity Investment = Equity Dividend Rate.
- Loan-to-Value Ratio: The amount borrowed divided by the appraised value of the property, expressed as a percentage.
- Net Operating Income (NOI): Income net of all operating costs including vacancy and collection loss but not including debt service.[1]

The table below shows the comparison of the Developer's revised Projections to the benchmark reference values from above:

[1] Definitions provided by RealtyRates.com and Investopedia.com

Comparison of Developer Assumptions to Reference Values

Metric	Developer Assumption is:
Interest Rate - Construction	Just below range
Interest Rate - Permanent - All Industrial	Within range
Interest Rate - Permanent - Distribution Only	Within range
Debt Service Coverage Ratio*	n/a
Loan-to-Value Ratio*	Within range
Amortization*	n/a
Equity Dividend Rate	Within range
Discount Rate	Just below range
Capitalization Rate	Under average

*Metric with respect to permanent financing.

Source: RealtyRates.com's "Investor Survey" 4th Quarter 2023.

The Capitalization Rate[2] is used in financial analysis to estimate the future "exit price" of the Developer from the Project upon sale which, according to the Projections, would occur in year 10. The lower the Capitalization Rate, the higher the assumed sale price. Therefore, the Developer's lower assumption for this metric potentially overstates their exit price and therefore potentially overstates the Developer's return. Because of this, we are comfortable keeping the assumption as-is.

The Developer's assumed construction interest rate is slightly below the reference range, which, like the capitalization rate, potentially overstates the Developer's return. Because of this, we are comfortable keeping the assumption as-is.

Because the loan is modeled as interest-only, the debt service coverage ratio figure would not be comparable to the reference range. Likewise, there is no amortization period. And, as noted above, the equity dividend rate is not the appropriate comparison metric. Instead, the discount rate is a more appropriate metric to use to measure the Developer's presumed return against the benchmarks.

We also examined a number of other factors used in the Projections, including the assumed:

- Rental prices for the presumed tenants, and escalation rate thereof,
- Operating expenses, and escalation rate thereof,
- Hard, soft and other costs in the construction budget.

Operating expenses, escalation factors and the construction budget all appear to be consistent with similar projects. The presumed rental rates in the Projections are at the high end of the market. We are comfortable with this assumption, since this would have the impact of potentially overstating the Developer's return.

[2] RealtyRates.com does not provide a range for the Capitalization Rate, only an average.

Consistent with the Developer's revised application to the IDA, we used the estimated PILOT payments as shown to the right. Using these assumptions, and the pro forma model received from the Developer, we modeled the levered internal rate of return (IRR) of the project by estimating cash flows to/from the Developer. As noted above, the Developer is assuming an exit price in year 10 that is estimated using the terminal year NOI and the capitalization rate described above, from which is subtracted out the remaining debt principal outstanding and presumed costs of sale. This provides a simplified Internal Rate-of-Return (IRR). We compared this IRR to the benchmark reference rate shown above for the Discount Rate. We find that the Developer's return is just below the reference range.

Proposed PILOT Schedule

Year	PILOT Payment
Year 1	$226,691
Year 2	$231,224
Year 3	$513,108
Year 4	$523,370
Year 5	$706,913
Year 6	$838,744
Year 7	$975,564
Year 8	$1,117,522
Year 9	$1,264,768
Year 10	$1,417,456
TOTAL	$7,815,360

Source: Applicant

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 financials appear to be adequate for financing purposes.

Thank you for this opportunity to assist the Newburgh IDA.

Sincerely,

R. Michael N'dolo
Director of Economic Development