Appendix D: Development Feasibility Assessment

Five to Nine Consulting

A collaboration between Main Street Oregon City (MSOC) & Five to Nine Consulting, a student group from Portland State University

Cover Photo: Fourth and Main Project, Hillsboro, OR

Contents

Concept for the city-owned vacant site at 10th and Main, from the Oregon City Development Opportunities Study

Context

Introduction

The feasibility of various kinds of development in Oregon City - commercial, residential, office - has been explored through several studies, with the support of Metro and other organizations. Site-specific studies have looked at rehabilitating the historic Multnomah Lodge and Busch buildings for housing and analyzed the feasibility of commercial and office development on the city-owned 10th and Main property. However, as of this writing, very little new construction or reconstruction has occurred in downtown Oregon City.

Methodology

This analysis looks at the potential market for residential housing downtown, including what kind of housing is preferable to potential future residents, and the willingness to pay for housing based on existing studies and an online survey conducted by Five to Nine Consulting in April 2013. We review existing market comparables - that is, the current per-square-foot rents for multi-family housing in or near Oregon City. We also look at the potential difference in rents between downtown multi-family housing and suburban multi-family housing to examine whether downtown housing achieves lower or higher rents. Finally, we review the financial feasibility of two hypothetical developments through pro forma analyses. We use different funding and financing assumptions, including the addition of public funding and land donations, to see how the gap between making a project "pencil out" or not pencil out can be closed.

Previous Market Analysis

To date, several studies have analyzed the development potential of properties in downtown Oregon City, including the Multnomah Lodge and Busch Building adaptive reuse case studies (2011) and the Downtown Oregon City Development Opportunity Study (2010). However, no study has provided an in-depth look at the residential market.

A 2009 Downtown Oregon City Market Analysis and Business Development Strategy conducted by Marketek focused on retail. The study noted that about 1,500 businesses employing 14,000 people operate within a two-mile radius of downtown Oregon City. Of these, the largest share work in services (35%) and retail trade (25%), with government (15%), construction (7%), and manufacturing (7%) jobs making up the next largest share.

With respect to residential opportunities, the Marketek study surveyed 239 respondents about living in downtown Oregon City, and found that 47% expressed an interest in living downtown. Of these, most would like to own townhomes, lofts, or units in mixed-use buildings. There is a preference for two bedroom units, and the top desired amenities include a parking garage, natural light/windows, in-unit washers/dryers, and patios or balconies.

The 2010 Development Opportunity Study noted that future target residential markets for downtown include both single and two-person households. The study also proposed that studio apartments and senior housing represent key opportunities for housing in downtown Oregon City.

A 2012 adaptive reuse case study for the Multnomah Lodge building observed that the apartment stock in Oregon City can be generally characterized as low quality, wood frame walk-ups constructed from the 60s-80s. The authors noted a conspicuous absence of historic apartment infrastructure for rent in the city (with the exception of a few on the bluff), and argued that converting existing historic buildings into residential spaces would create a unique and desirable commodity in downtown.

Though the studies above begin to describe and theorize about people's preferences for living in downtown Oregon City, there is little hard data on the subject. The following section looks at our recent survey results in an effort to paint a clearer picture of who might be interested in living in downtown Oregon City.

Survey Results

Five to Nine Consulting conducted an online survey to assess people's attitudes about downtown Oregon City. Results from 300 respondents show that about 40% of respondents are willing to consider living in downtown Oregon City. A little more than a third are definitely willing to consider living downtown, while the rest might consider it depending on a variety of factors.

Factors Contributing to Interest in Living Downtown

Respondents who indicated that their willingness to consider living downtown was dependent on certain factors were asked to identify these factors. Top factors included the availability and type of residential units downtown, respondent age or presence of children in the household (with most expressing an interest in living downtown once they retired or their children left the house), cost of housing, availability of services downtown, improved nightlife and cultural/entertainment opportunities, and better transportation access to Portland (Figure 1). The departure of the courthouse and existing bars were also listed as a condition by several respondents. Interestingly, parking availability was not one of the leading criteria.

Respondents aged 26-35 were the most likely to be interested in living downtown

Housing Preferences

Condominiums and townhomes were the most preferred housing types (consistent with the Marketek study findings) among people willing to live downtown, but many respondents expressed interest in apartments as well (Figure 2). Although single family houses are prohibited downtown by current code regulations, almost 40% of respondents who are willing to live downtown also expressed interest in living in a house.

Demographics & Housing Preferences

Figure 1

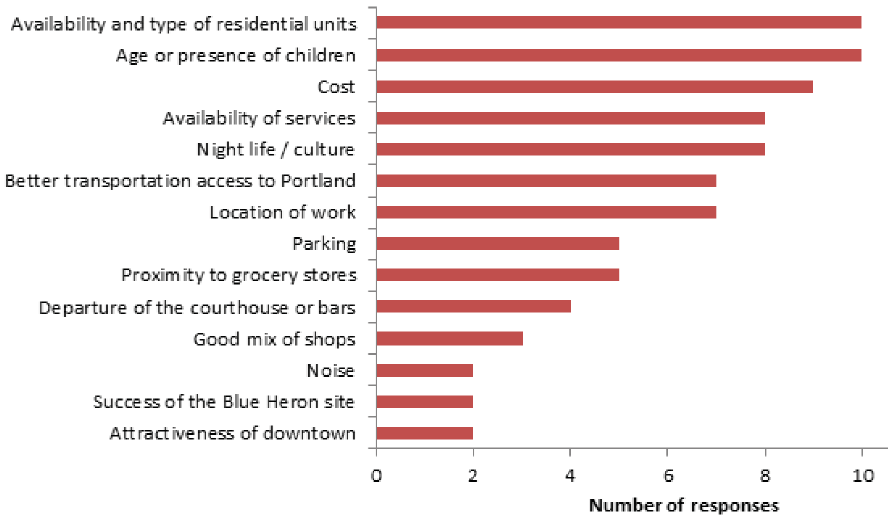
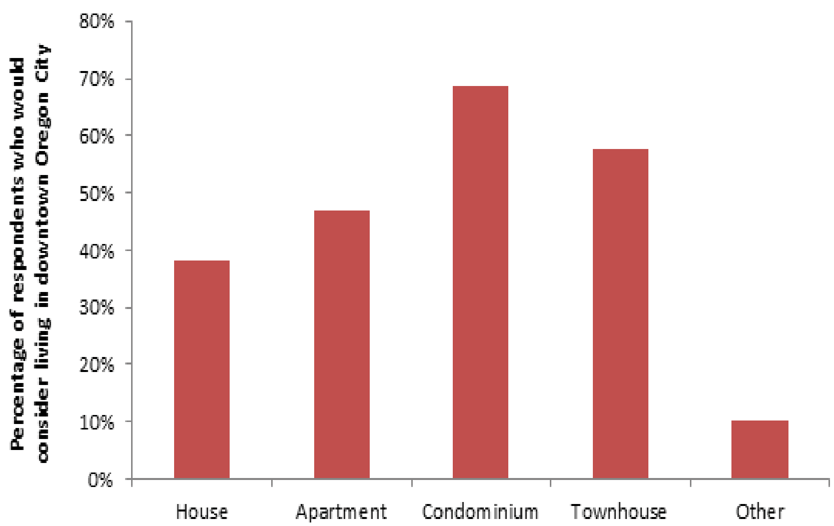


Figure 2



Demographics of Respondents Interested in Living Downtown

- The demographics of respondents who expressed some level of interest in living in downtown Oregon City were compared to those who expressed no interest. The results are far from conclusive and show a roughly even split between these two groups for most demographic factors. However, some interesting differences appeared. For example:

- Respondents aged 26-35 were the most likely to be interested in living downtown. The two age groups comprising the 45-65 year olds showed a relatively high level of interest as well, with over 40% willing to consider living downtown (Figure 3).

- Respondents who pay between $1 and $599 for household rent or mortgage were the most likely to consider living downtown, while those paying between $1,000 and $1,500 were the next most likely (Figure 4).

- As might be expected, people who pay nothing (presumably, those who have paid off their mortgage or live with parents) are much less likely to be interested in moving downtown (Figure 4).

- Approximately 7% of respondents who expressed interest in living downtown said they would be willing to pay more than they currently pay to live in downtown Oregon City, while around 50% would be willing to pay the same as they currently pay.

- Respondents with household incomes under $20,000, between $40,000 and $60,000 and above $100,000 showed a greater willingness to consider living in downtown Oregon City than other income groups (Figure 5).

- There was a slightly greater willingness among current renters to consider living downtown than among people who own their homes (Figure 6).

Figure 3

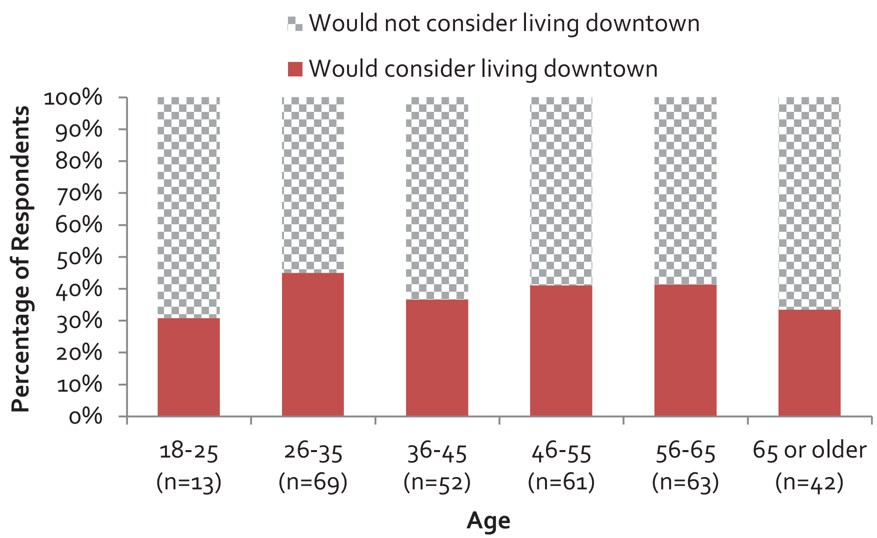


Figure 5

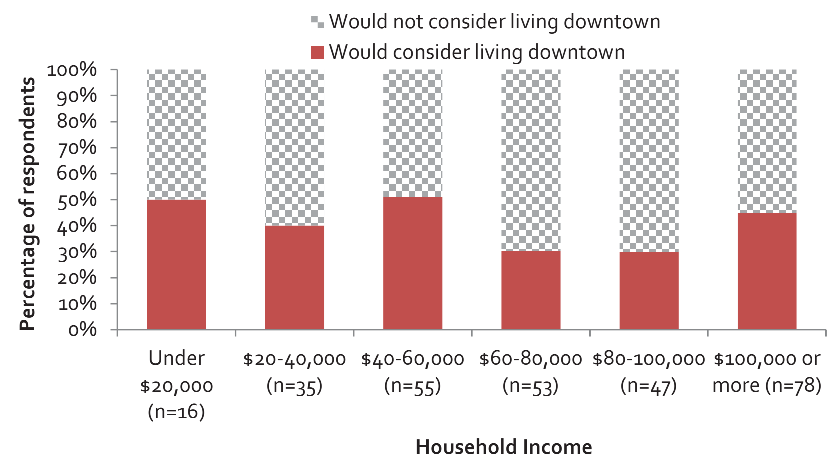


Figure 4

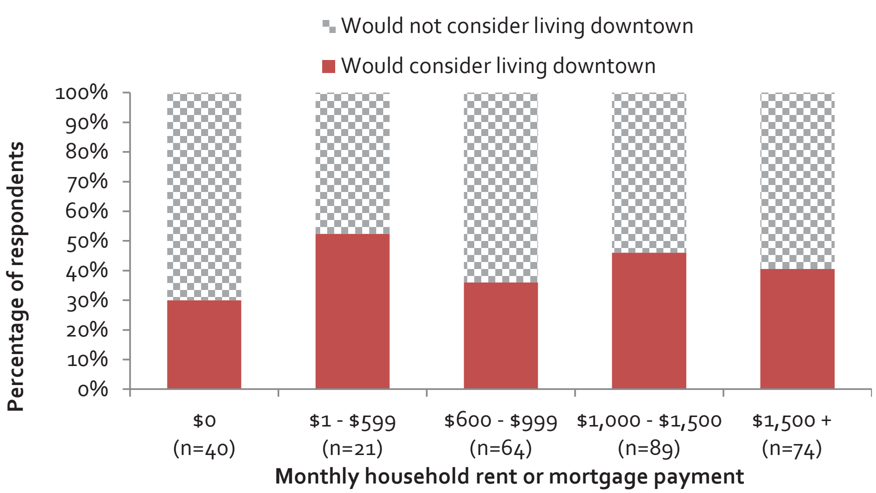
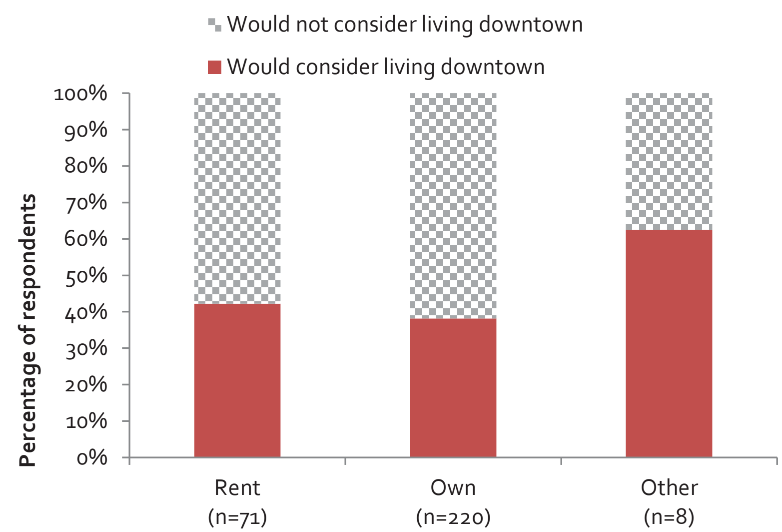


Figure 6



Demographics & Housing Preferences

Demographic Profile of Oregon City Area

Data from the 2005-2009 American Community Survey and 2010 Census were combined to produce a demographic profile of Oregon City and all census tracts within a 2 mile radius, including portions of West Linn, Gladstone, and rural areas to the south and east of Oregon City.

The resulting profile shows a predominantly white, older population with moderate income levels. Closer examination of income shows higher incomes are concentrated in western tracts encompassing the city of West Linn. Almost three quarters of households are owner-occupied, and two thirds do not have children under the age of 18.

Employment is concentrated in the business/financial, professional, sales, and administration sectors. This information conflicts with the employment profile contained in the Marketek study, which showed employment concentrated in services and retail trade (25%), followed by government, construction, and manufacturing. This reason for this is unclear, but is likely due to differences in geography or job classification.

Total Population	120,092
Age	
Under 18	24.1%
18-24	7.4%
25-34	10.8%
35-44	13.7%
45-54	15.9%
55-64	14.6%
Over 65	13.4%
Race/Ethnicity	
White	90.6%
Black	0.7%
Native American	0.8%
Asian	2.3%
Hawaiian or Pacific Islander	0.2%
Other	2.2%
Two or more races	3.1%
Hispanic	6.5%
Households	46,044
With children under 18	33.8%
Without children under 18	66.2%
Average* Median Household Income	$65,036
Average* Median Rent	$949
Average* Median Homeowner Costs for owners with a mortgage	$1,891
Owner Occupied	73.0%
Renter Occupied	27.0%

Employment	
Business, Management, Finance	17.0%
Professional	19.6%
Health Services	1.9%
Protective Services	1.7%
Food Service	3.8%
Maintenance	2.8%
Care	3.7%
Sales	12.4%
Administration	16.8%
Farm, Fishing, Forestry	0.5%
Construction	9.3%
Manufacturing	5.4%
Transportation Services	5.2%
Primary Means of Transportation to Work	
Motor Vehicle	84.0%
Public Transit	3.0%
Bicycle	0.4%
Walk	2.3%
Other	0.5%
Work at Home	7.3%
Commute Time	
0 minutes (work at home)	7.3%
10 minutes	12.0%
10-19 minutes	23.8%
20-29 minutes	21.2%
30-39 minutes	18.9%
40-59 minutes	10.3%
60-89 minutes	2.9%
More than 90 minutes	1.2%

Source: Author's analysis of 2005-2009 ACS and 2010 Census data. Median values for each census tract were averaged

Discussion

Our results confirm what we have heard during focus groups and interviews: the target age groups for downtown living are younger people and those nearing retirement. In this case, the youngest age group surveyed (18-25 year olds) was noticeably less interested in living in downtown Oregon City than other groups, but 26-35 year olds were the most likely. This could reflect a desire for very young people to move to more urbanized areas like Portland in search of jobs and entertainment rather than stay in Oregon City. Slightly older age groups who have experienced urban living but have jobs near Oregon City may be more interested in a quieter, but up-and-coming urban location.

Older households without children also seem to be a likely market for downtown Oregon City. 46-65 year olds were interested in living downtown and comprise the largest share of population in the area around Oregon City. Survey results indicated that the presence of children in a household was a major barrier to living downtown and that many people were more willing to consider living downtown after retirement. This reflects the generational shift in attitudes about retirement, as retiring "baby boomers" return to smaller housing units in urban neighborhoods.

Although 26-35 year olds were slightly more interested in living downtown than 46-65 year olds, the younger age group represents only 10% of the population within two miles of Oregon City, while 45-64 year olds make up over 30% of the population. Recently, downtown has had some success in attracting creative businesses with younger employees, but it is unclear whether a large enough market exists in downtown for housing aimed at young people - and whether they could afford downtown housing rents. Residential marketing strategies should be designed with both age groups in mind, but the opportunity to cater to a "creative boomer community" is intriguing given the large presence of boomers in the area. Oregon City could present a perfect compromise for retiring people in surrounding suburban areas like West Linn, Lake Oswego, and Milwaukie, seeking to downsize and move into a walkable neighborhood but unwilling to move too far from friends and family or live in the "big city."

Survey results show that the age group that comprises the largest share of population in the area around Oregon City (46-65 year olds) were interested in living downtown

Households making more than $100,000 per year and households paying between $1,000 and $1,500 per month for housing showed a higher than average willingness to live downtown, suggesting that regardless of age, it may be possible to attract wealthy people and charge premium rents for attractive housing in downtown Oregon City. At the same time, the highest level of interest in downtown living came from households making $40,000 to $60,000 per year and from households paying between $1 and $599 per month for housing. Thus, it seems there may be a market for affordable housing (artist studios have been suggested as a pioneer housing type) as well as high end housing such as condos with river views. Perhaps the most interesting trend from our survey is that the middle ranges in terms of age and income are less interested in living downtown. For those who are interested in living downtown, it is clear that finding the right housing type for their needs will be one of the most important factors in their decision.

The highest level of interest in downtown living came from households making $40,000-$60,000 per year and from households paying $1-$599 per month for housing

Current Multi-Family Market

Potential Residential Rental Market

With survey results indicating substantial interest in housing in downtown Oregon City, we looked to residential rental rates in neighboring cities to determine what the potential residential rental market might be in Oregon City. There are currently five apartments located in downtown. The mixed-use building is located at 1408 Washington Street and currently commands rents of $0.87 per square foot per month. However, this small sample size is hardly representative of what the residential market could bear.

We looked up residential rental costs for cities throughout the Portland metropolitan region via HotPads.com. Our findings indicate that the median rent for an apartment or condo in Oregon City is $890 per month, which is also the average rental rate for a 2-bedroom unit in Oregon City (Figure 7). Oregon City median rental prices ranged from $685 for a studio to $1650 for a 4-bedroom. As we anticipated, Oregon City's rents were considerably lower than those of Portland (with a median rental cost of $1,270 compared to Oregon City's $890). However, Oregon City's median rent was higher than its neighboring cities of Milwaukie ($815) and Canby ($775). Not surprisingly, Oregon City's median rents were also far lower than those of nearby affluent suburbs of West Linn ($1,200) and Lake Oswego ($1,150).

We then searched for available multi-family rentals in cities near Oregon City via Zillow.com. We compiled a database of 170 available units in Canby, Gladstone, Happy Valley, Lake Oswego, Oak Grove, Oatfield, Oregon City, Tigard, Tualatin, West Linn, and Wilsonville. However, we decided to exclude Canby, Happy Valley, Oak Grove, and Oatfield because of small sample sizes. On the date we compiled our database there were no multi-family units for rent in Aurora, St. Paul, Dundee, Hubbard, Woodburn, Beaver Creak, Estacada, Boring, or Sandy. Our database includes city, number of bedrooms, square footage, and price. Units that did not include all of these factors in the listing were not included. Single-family homes were not included because downtown Oregon City's zoning does not allow detached dwellings except for accessory dwelling units.

In our database we also included whether or not the unit was located downtown or outside downtown. Unfortunately, we did not have enough units available for rent in each downtown to calculate a meaningful differential between downtown and not downtown rentals for all of the cities. Based on our back-

Figure 7

Current Housing Rental Rates in Portland Metropolitan Region (4/18/13)

City	Median	Studio	1 Bed	2 Bed	3 Bed	4 Bed
Portland, OR	$1,270	$845	$1,356	$1,250	$1,395	$1,895
West Linn, OR	$1,200	$450	$800	$1,172	$1,550	$2,800
Hillsboro, OR	$1,150	$885	$867	$1,112	$1,365	$1,695
Lake Oswego, OR	$1,150	$875	$955	$1,170	$1,499	$2,995
Beaverton, OR	$1,000	$724	$825	$950	$1,200	$1,750
Wilsonville, OR	$994	$840	$904	$1,095	$1,262	$1,855
Troutdale, OR	$977	$1,495	$630	$810	$1,195	$1,450
Sunnyside, OR	$925	$1,300	$775	$937	$1,200	$1,582
Tualitin, OR	$919	$719	$864	$995	$1,222	$1,995
Gladstone, OR	$900	$1,250	$785	$875	$1,120	$1,400
Tigard, OR	$900	$643	$762	$885	$1,295	$2,195
Oregon City, OR	$890	$685	$750	$890	$1,380	$1,650
Vancouver, WA	$880	$695	$750	$865	$1,150	$1,695
Gresham, OR	$825	$695	$675	$775	$1,195	$1,695
Milwaukie, OR	$815	$625	$750	$845	$1,150	$1,600
McMinnville, OR	$795	$450	$605	$725	$1,200	$1,295
Canby, OR	$775	$900	$600	$775	$1,160	$1,500

Source: Hot Pads website (hotpads.com)

of-the-envelope calculations, it appears that downtown units in Lake Oswego are renting for approximately $0.20 more per square foot than those outside downtown while units in downtown Milwaukie are renting for approximately $0.12 less than those outside downtown.

We then calculated the price per square foot of each unit and found the median cost per square foot for each unit type for each city (Figure 8). Cost per square foot rental rates in our sampled cities ranged from $0.65 per square foot for a 1200 square foot 2-bedroom in Milwaukie to $2.50 per square foot for a 1000 square foot studio apartment in Lake Oswego. The median cost per square foot was $1.06 and the average cost per square foot was $1.09.

We found that Oregon City multi-family rentals were listed at median prices of $1.22 per square foot for 1-bedrooms, $1.02 for 2-bedrooms, and $1.05 for 3-bedrooms, for a total median for all unit-types of $1.05. This median square foot cost was higher than that of Gladstone at $0.85 per square foot, Tigard at $0.99, and Tualatin at $1.00. It was slightly lower than Milwaukie at $1.08 and considerably lower than Lake Oswego at $1.40. It was also slightly lower than the median square foot cost reported in a recent survey conducted by Multi-Family Northwest, which listed Oregon City's median cost per square foot for residential at $0.98 per square foot and the Portland Metro's median cost per square foot at $1.04. The Multi-Family Northwest study was cited in an Oregonian article by Elliot Njus, entitled "Apartment market grows tighter, but rent increases slow," dated 4/17/13.

Oregon City multi-family rentals were listed at median prices (all unit-types) of $1.05 per square foot

Our theory for the discrepancy between the median price per square foot we calculated and the price calculated by Multi-Family Northwest is that the units currently available may be smaller on average than the units already rented. Cities with large suburban areas such as Oregon City have larger homes on average than the dense, urban areas of Portland's central city. There are more large detached rentals in the suburbs and they draw a lower cost per square foot than studio and 1-bedroom apartments, so it may be that the lower rent per square foot on large units pulls the median down.

Additionally, when we look instead at average cost per square foot rather than median cost per square foot we find that Oregon City is commanding an average of $1.10 per square foot, which is on par with Milwaukie ($1.09), West Linn ($1.11), and Wilsonville ($1.15), and higher than Tualatin ($1.01) and Tigard ($1.04). Lake Oswego's cost per square foot is considerably higher with an average of $1.43 per square foot and Gladstone's is considerably lower at $0.86. We understand that medians are used by the real estate industry, but the median price per square foot for all multi-family units in Oregon City includes many units that are larger than downtown apartments would likely be. Average rental rates in Oregon City are higher than the median rental rates, indicating that the rental market for small units in Oregon City may be healthier than it initially appears.

Studio and 1-bedroom units often claim higher rents than 2-bedroom units. Our survey respondents preferred one and two bedroom units (particularly if downsizing once their children left the household), so providing small units would likely not only meet the needs of our target market better than larger units, but would also command higher rents per square foot and be more likely to pencil out.

Figure 8

	Median Cost / Square Foot (4/23/13)				
	Studio	1 Bed	2 Bed	3 Bed	Total
Lake Oswego	$2.00	$1.39	$1.32	N/A	$1.40
West Linn	N/A	$1.31	$1.02	$1.16	$1.17
Wilsonville	$1.51	$1.17	$1.07	$1.31	$1.15
Milwaukie	$1.37	$1.04	$1.05	N/A	$1.08
Oregon City	N/A	$1.22	$1.02	$1.05	$1.05
Tualatin	$1.38	$1.17	$0.96	$0.95	$1.00
Tigard	$1.32	$1.07	$0.94	$1.05	$0.99
Gladstone	N/A	$0.91	$0.82	$0.87	$0.85

Source: Zillow.com

Figure 9

	Average Cost / Square Foot (4/23/13)				
	Studio	1 Bed	2 Bed	3 Bed	Total
Lake Oswego	$2.00	$1.40	$1.35	N/A	$1.43
Wilsonville	$1.51	$1.16	$1.08	$1.23	$1.15
West Linn	N/A	$1.31	$1.02	$1.06	$1.11
Oregon City	N/A	$1.22	$1.02	$1.05	$1.10
Milwuakie	$1.34	$1.06	$0.96	N/A	$1.09
Tigard	$1.38	$1.11	$0.95	$1.02	$1.04
Tualatin	$1.38	$1.16	$0.97	$0.92	$1.01
Gladstone	N/A	$0.91	$0.83	$0.87	$0.86

Source: Zillow.com

Current Multi-Family Market

Realtor Confirmation

We vetted our findings with local real estate agents. One of the realtors confirmed that $1.24 per square foot is a decent estimate for Oregon City rentals. He also stated that, in his experience, Oregon City commands higher rents than Milwaukie, despite Milwaukie's closer proximity to Portland. He indicated that Oregon City's historic character is a contributing factor, but its convenient location also increases Oregon City's marketability compared to some other Portland suburbs.

As the Multi-Family Northwest article notes, Portland's rental market is very tight, with vacancy rates around 3-4% for the metro area. According to the article, Oregon City's vacancy rate is 3.7%. Realtors stated that clients sometimes ask about loft apartments or condominiums in downtown Oregon City and are disappointed to discover there are just a handful of units. One of the realtors said that he would live in downtown Oregon City himself if high-quality housing were available in the historic core.

Although our urban-suburban differential calculation was rough, it was in-line with realtors estimates that people would pay 10-15% less for downtown units initially. One realtor pointed out that rents in Portland's Pearl District were low initially and that the area was occupied primarily by artists and other "creatives." Once the residential market took off, rents increased considerably. Another realtor explained that there are not yet enough businesses and amenities for people to pay a premium for living in downtown Oregon City, especially if they must contend with train noise and long-term parking challenges. The realtor believed this would eventually shift as more amenities become available and if a rail quiet zone is enacted. He suggested that people would likely be willing to ignore the inconveniences if a developer was able to construct residential units that captured views of Willamette Falls. He also suggested that shared parking would probably be a viable option for providing parking for residential uses since so much of the parking in downtown is used during the business day by the county courthouse and supporting services and is not in demand at night.

> Oregon City's vacancy rate is 3.7%

When asked why there are so few housing options available in Downtown Oregon City if there is a demand for it, one of the realtors stated that the System Development Charges (SDCs) are too high for development to pencil out. He indicated that a reduction would be beneficial to kick-start the housing market downtown, even if it was only available for a limited period of time or for the first project or two. Train noise was also stated as a concern, so a quiet zone would go a long way towards increasing marketability.

The realtors indicated that they believe the first project should be a high-quality, market rate development, rather than affordable housing. They suggested including amenities such as a gym and a pool to increase the marketability of the units. They noted that the target market would likely be young single professionals, young couples, and baby boomers, which lines up with the findings of our survey. They also indicated that residents of Lake Oswego and West Linn might choose to move to downtown Oregon City as rents increase in those cities.

The realtors recommended that the first project be rentals rather than condominiums since buyers will be as hesitant as developers to invest initially. One of the realtors suggested constructing the first residential project in downtown Oregon City as condominiums (with a double-wall construction) but renting them initially. If the rental market proves feasible buyers will begin requesting condos and the units could then be sold rather than rented. He also noted that condominium associations would have Home Owners Association fees. It might be possible to structure the fees in such a way that a small percentage of these fees are used to slowly reimburse Oregon City for the revenue that would be lost initially by reducing SDC fees or writing down property values.

Several cities that we studied for our Case Studies report found that a pioneering developer can prove the market for housing downtown by investing in properties when no other developers are willing to take on the risk. Once he or she is successful, other property owners and developers often follow suit. One of the realtors with whom we spoke suggested that the marketing campaign for downtown living in Oregon City could be explicit about recruiting

> Realtors stated that clients sometimes ask about loft apartments or condominiums in downtown Oregon City and are disappointed to discover there are just a handful of units

pioneer residents. She noted that this would be particularly clever in Oregon City because of its history as the first city in the Oregon Territory and the end of the Oregon Trail. She noted that Oregon City's charm, character, and rich history could be drawn on in the marketing campaign for downtown housing. In discussion with development professionals, we developed two proposals, each using different assumptions, to analyze how market-rate residential development could "pencil out" in downtown Oregon City. This hypothetical analysis is highly dependent on the many financial variables that go into a speculative development project. Our conclusions are based on one particular financial model, but allow analysis of how the financial feasibility of a project can be improved based on different assumptions.

We analyze financial feasibility in terms of return on total cost (RTC) and return on total equity (RTE). These two measures are typically used in the development community to make a high-level determination of whether a project may be worth pursuing further. Generally, development professionals and investors seek RTC in excess of 9% and RTE in excess of 10%. While other considerations are also key to determining whether a speculative development project moves forward - cash equity required, financing terms, relative risk, etc. - these serve as good proxies for development feasibility: the higher the RTC and RTE, the more likely the project is to pencil out. Detailed pro formas can be found at the end of this report.

10th & Main Site

The vacant 10th and Main site, owned by the City of Oregon City, presents an excellent opportunity for new, small-scale development. Our program scenario for this site is significantly different from that proposed in the Development Opportunity Study, which primarily consisted of office and retail uses. We developed the following program as a starting point to evaluate financial feasibility:

- Three story building, footprint approximately 4,900 square feet
- Surface parking, 16 parking stalls total
- 4,900 square feet of ground floor retail
- 16 apartments, a blend of studios and one bedrooms, in the top two stories

The following financial assumptions, based on input from local development professionals, were used to assess feasibility:

- $1.25 per square foot per month in residential rent
- $15.00 per square foot per year in commercial rent
- 8% market capitalization rate
- 70% loan-to-value ratio for construction loan; 50% developer fee deferral
- 10% vacancy factor

Two different financing scenarios were developed. The first assumed no public assistance with the project and hard construction costs of $120 per square foot, based on input from local development professionals and the RSMeans online cost estimating tool (http://www.rsmeans.com/calculator/index.asp?specialUser=FSONL). The second scenario assumed that land costs would be $0, system development charges would be waived, and the state's vertical housing tax credit program implemented. These assumptions significantly reduce the "soft" costs of development. Project construction costs savings were also assumed, due to potential improvement grants available from the Urban Renewal Commission, at a reduction of $10 per square foot.

An RTC of 5.4% and RTE of 5.0% result under the first scenario (Figure 10). These rates of return are far below what would be considered feasible by developers or investors. However, the second scenario results in a significantly more feasible project due to reduced costs. With this scenario, an RTC of 7.2% and RTE of 8.7% result, which is much closer to financial feasibility in the speculative development market.

Public financial incentive tools - property write-downs, fee reductions, and tax credits - can reduce costs to the point where development is more likely to pencil out

Financial Feasibility Analysis

Multnomah Lodge (707 Main Street)

The Lodge building is one of the iconic historic buildings in downtown Oregon City. In conversations with developers, community members, and many others, this building was repeatedly mentioned as a good candidate for adaptive reuse of several floors. This property was analyzed by Metro as part of the Multnomah Lodge Adaptive Reuse Case Study in 2011. The study ultimately concludes that residential adaptive reuse of the building is financially infeasible, based on the following assumptions:

- General renovation of the building to include 11 office units, 2 retail spaces, and 13 apartments of varying sizes for a total leasable square footage of 19,320 feet. No parking improvements were assumed.
- $1.25 per square foot in residential rent
- 9% market capitalization rate
- Permanent loan financing rate of 6%, 25 year term, 10 year maturity
- 70% loan-to-value ratio for construction loan financing
- 13% vacancy factor
- Net operating costs equal to 50% of revenue
- No analysis of soft costs

With these assumptions, and a total project cost in excess of $4,000,000, the project as presented would not have made financial sense. Instead of the full program, we analyzed the costs and income associated with a scaled-down version of this program with our model, with the following assumptions:

- General renovation to include 13 one-bedroom apartments
- $1.25 per square foot per month in rent
- 8% market capitalization rate
- Same construction and permanent loan financing assumptions as the Adaptive Reuse Study
- 10% vacancy factor
- Soft costs included (the adaptive reuse study did not include soft costs), though no developer fee and reduced system development charges and other soft costs normally associated with new development
- Less conservative net operating costs equal to approximately 33% of year one net operating income (the Adaptive Reuse Study used 50%)

These assumptions are a blend of those made in the adaptive reuse study and our own based on the advice of development professionals. The most significant difference between Metro's case study and our analysis is the site program (13 apartments, as opposed to residential, retail, and office uses) and construction costs. For our purposes, general building shell, core improvements, and apartment construction costs were considered, excluding voluntary seismic upgrades and facade improvements contemplated under the Adaptive Reuse Study. This yields approximate total project costs (all soft and hard costs) of $141 per square foot.

Applying our model results in an RTC and RTE of 8.3% and 7.9%, respectively. If project costs could be reduced through tax credits, fee reductions, or other means, the financial feasibility of the project would increase greatly (Figure 11).

Discussion

There are many variables in estimating whether a speculative development project will "pencil out." The general assumptions made above for these two very different projects illustrate several fundamental financial challenges for residential development in Oregon City.

First, it is clear that residential rents of $1.25 per square foot do not generate enough income to make downtown residential projects feasible, given costs. Additionally, these rents are speculative, as there are few existing market comparables to determine the range of potential rents in downtown Oregon City. Because of the lack of market comparables, and perceived risk, private lenders are unlikely to give favorable financing terms to development of this type.

However, public assistance can help make projects financially feasible. The public financial participation tools listed above are all readily available to Oregon City. These tools can reduce costs to the point where development is more likely to pencil out. It is very likely, based on this analysis and similar studies done in Oregon City, that public financial incentives of some kind will be required in order to generate significant developer interest in downtown development.

Figure 10

10th and Main - New Construction	Scenario 1	Scenario 2
	Assumes no public financial incentives. Market-rate mixed-use development.	Assumes public financial incentives, including SDC waivers, land write-down, cost reductions through urban renewal grants, and tax credits.
Project facts		
Site Area (sq ft)	9,970	9,970
No. surface parking spots	16	16
Gross square footage	15,900	15,900
Number of stories	3	3
Number of residential units	16	16
Residential square footage	9,800	9,800
Rent (per sq ft per month)	$1.25	$1.25
Commercial square footage	4900	4900
Rent (per sq ft per year)	$15.00	$15.00
Costs		
Land cost (per sq ft)	$15.00	$15.00
Hard construction costs (per sq ft)	$137.00	$126.00
Soft costs (per sq ft)	$52.00	$36.00
Total project cost:	$3,157,845	$2,566,169
Results		
Return on Total Cost	5.40%	7.20%
Return on Total Equity	7.20%	8.70%

Figure 11

Multnomah Lodge - Adaptive Re-use	Scenario
	Assumes no seismic upgrades and only those improvements necessary for reconfiguring the building space for apartments. No SDCs included; developer fee also assumed to be waived.
Project facts	
Site Area (sq ft)	N/A
No. surface parking spots	None
Gross square footage	10,250
Number of stories	2
Number of residential units	13
Residential square footage	9,750
Rent (per sq ft per month)	$1.25
Commercial square footage	0
Rent (per sq ft per year)	N/A
Costs	
Land cost (per sq ft)	N/A
Hard construction costs (per sq ft)	$110.00
Soft costs (per sq ft)	$32.00
Total project cost:	$1,450,802
Results	
Return on Total Cost	7.90%
Return on Total Equity	8.30%

10th & Main Pro Formas

Without Public Assistance

10th and Main Property

Density (du/acre) **70**

16 surface parking stalls

Proforma results	
year one cash flow	**$76,658**
Construction loan	**$1,710,091**
Cash equity required	**$1,274,440**
Return on Total Cost	**5.4%**
Return on Equity	**5.0%**
Cash on cash 10 year IRR	**7.2%**

PROJECT FACTS:					
Site Area			sq.ft	**9,970**	
Number of stories				**3**	
Studio	7	500	sq.ft	**3,500**	
One bedroom	9	700	sq.ft	**6,300**	
				0	
				0	
				0	
				0	
				0	
Total residential	16			**9,800**	
Retail space	1	4,900	sq.ft	**4,900**	
interior common area sq.ft.				**1200**	
Gross area	17			**15,900**	
FAR				1.59	
Net Leasable					
Studio	7	500	sq.ft	**3,500**	625.00
One bedroom	9	700	sq.ft	**6,300**	875.00
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
Net Leasable Residential	**16**			**9,800**	
decks	2	150	sq.ft. total	**150**	
Retail space	1	4,900	sq.ft	**4,900**	
Net Leasable Retail	**1**			**4,900**	
Total leasable				**14,700**	
GROSS BUILDING AREA				**15,900**	
TOTAL NET LEASABLE				**14,700**	
Overall Efficiency				92%	

CONSTRUCTION LOAN CALCULATION		
Interest Rate		5.50%
Const term (Months)		7
Rental term (months)		3
Construction Loan, max of term loan		**$1,710,091**
Const. Loan, % of cost	**75%**	**$2,346,667**
Const. loan, min of term loan or 70% of cost		**1,612,921**
Loan-to-Cost		**51.08%**
Loan-to-Value		**70%**
Const. Period Drawdown Factor		55%
construction period interest		$30,176
rental period interest		$27,789
Interest		**$57,965**

PERMANENT FINANCING ASSUMPTIONS	**DCR**	**LTV**
Loan Amount	**$2,166,160**	**$1,483,088**
Perm. Interest Rate	**4.75%**	**4.75%**
Term (Years)	**30**	**30**
Debt-Coverage Ratio	**1.25**	
Stabilized NOI	**$169,496**	**$ 169,496**
CAP Rate		**8.0%**
Project Value		**$2,118,697**
Loan-to-Value		**70%**
Supportable Mort, min of DCR or LTV		**$1,483,088**
Supportable Loan Primary Debt Service		($92,838)
DCR		**1.83**
Value per Net Square Foot		**$133**

With Public Assistance

10th and Main Property

Density (du/acre) **70**

16 surface parking stalls

Proforma results	
year one cash flow	**$76,658**
Construction loan	**$1,710,091**
Cash equity required	**$1,274,440**
Return on Total Cost	**5.4%**
Return on Equity	**5.0%**
Cash on cash 10 year IRR	**7.2%**

PROJECT FACTS:					
Site Area			sq.ft	**9,970**	
Number of stories				**3**	
Studio	7	500	sq.ft	**3,500**	
One bedroom	9	700	sq.ft	**6,300**	
				0	
				0	
				0	
				0	
				0	
Total residential	16			**9,800**	
Retail space	1	4,900	sq.ft	**4,900**	
interior common area sq.ft.				**1200**	
Gross area	17			**15,900**	
FAR				1.59	
Net Leasable					
Studio	7	500	sq.ft	**3,500**	625.00
One bedroom	9	700	sq.ft	**6,300**	875.00
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
0		-	sq.ft	**0**	
Net Leasable Residential	**16**			**9,800**	
decks	2	150	sq.ft. total	**150**	
Retail space	1	4,900	sq.ft	**4,900**	
Net Leasable Retail	**1**			**4,900**	
Total leasable				**14,700**	
GROSS BUILDING AREA				**15,900**	
TOTAL NET LEASABLE				**14,700**	
Overall Efficiency				92%	

CONSTRUCTION LOAN CALCULATION		
Interest Rate		5.50%
Const term (Months)		7
Rental term (months)		3
Construction Loan, max of term loan		**$1,710,091**
Const. Loan, % of cost	**75%**	**$2,346,667**
Const. loan, min of term loan or 70% of cost		**1,612,921**
Loan-to-Cost		**51.08%**
Loan-to-Value		**70%**
Const. Period Drawdown Factor		55%
construction period interest		$30,176
rental period interest		$27,789
Interest		**$57,965**

PERMANENT FINANCING ASSUMPTIONS		
	DCR	**LTV**
Loan Amount	**$2,166,160**	**$1,483,088**
Perm. Interest Rate	**4.75%**	**4.75%**
Term (Years)	**30**	**30**
Debt-Coverage Ratio	**1.25**	
Stabilized NOI	**$169,496**	**$ 169,496**
CAP Rate		**8.0%**
Project Value		**$2,118,697**
Loan-to-Value		**70%**
Supportable Mort, min of DCR or LTV		**$1,483,088**
Supportable Loan Primary Debt Service		($92,838)
DCR		**1.83**
Value per Net Square Foot		**$133**

Multnomah Lodge Pro Forma

Multnomah Lodge

Proforma results	
year one cash flow	**$37,111**
Construction loan	**$1,710,091**
Cash equity required	**$446,972**
Return on Total Cost	**7.9%**
Return on Equity	**8.3%**
Cash on cash 10 year IRR	**11.2%**

PROJECT FACTS:				
Site Area			sq.ft	**10,000**
Number of stories				**4**
One bedroom	13	750	sq.ft	**9,750**
				0
				0
				0
				0
				0
Total residential	13			**9,750**
Retail space	0		sq.ft	**0**
interior common area sq.ft.				**500**
Gross area	13			**10,250**
FAR				1.03
Net Leasable				
0		-	sq.ft	**0**
One bedroom	13	750	sq.ft	**9,750**
0		-	sq.ft	**0**
0		-	sq.ft	**0**
0		-	sq.ft	**0**
0		-	sq.ft	**0**
0		-	sq.ft	**0**
Net Leasable Residential	**13**			**9,750**
decks	2	150	sq.ft. total	**150**
Retail space	0	-	sq.ft	**0**
Net Leasable Retail	**0**			**0**
Total leasable				**9,750**
GROSS BUILDING AREA				**10,250**
TOTAL NET LEASABLE				**9,750**
Overall Efficiency				95%

CONSTRUCTION LOAN CALCULATION		
Interest Rate		5.50%
Const term (Months)		7
Rental term (months)		3
Construction Loan, max of term loan		**$1,710,091**
Const. Loan, % of cost	**75%**	**$1,068,739**
Const. loan, min of term loan or 75% of cost		**1,003,830**
Loan-to-Cost		**69.19%**
Loan-to-Value		**70%**
Const. Period Drawdown Factor		55%
construction period interest		$30,176
rental period interest		$27,789
Interest		**$57,965**

PERMANENT FINANCING ASSUMPTIONS		
	DCR	**LTV**
Loan Amount	**$1,187,057**	**$1,003,830**
Perm. Interest Rate	**6.00%**	**6.00%**
Term (Years)	**25**	**25**
Debt-Coverage Ratio	**1.25**	
Stabilized NOI	**$114,723**	**$ 114,723**
CAP Rate		**8.0%**
Project Value		**$1,434,043**
Loan-to-Value		**70%**
Supportable Mort, min of DCR or LTV		**$1,003,830**
Supportable Loan Primary Debt Service		($77,612)
DCR		**1.48**
Value per Net Square Foot		**$140**