City of San Leandro
Development Feasibility Review

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OUTLINE

- Background
- Development Feasibility
- Measuring Returns
- Market Conditions
- Review of Specific Projects Proposed in City
- Findings

DEVELOPMENT FEASIBILITY

- Developers typically elect to pursue a real estate development to generate a profit
  - Projects can generate profit when development value exceeds development cost
  - Typically rely on investors (equity) and lenders (debt) to fund most of development cost
- Investors and lenders will only fund projects that they expect to be successful and pay back their investment with interest / provide a return on investment
- If a development is not projected to generate a substantial enough profit, the developer will not be able to secure the funds necessary to construct it
- Generally, when interest rates go up, borrowing costs go up, and required investment returns go up

MEASURING RETURNS – THE CAPITALIZATION RATE & RETURN ON COST

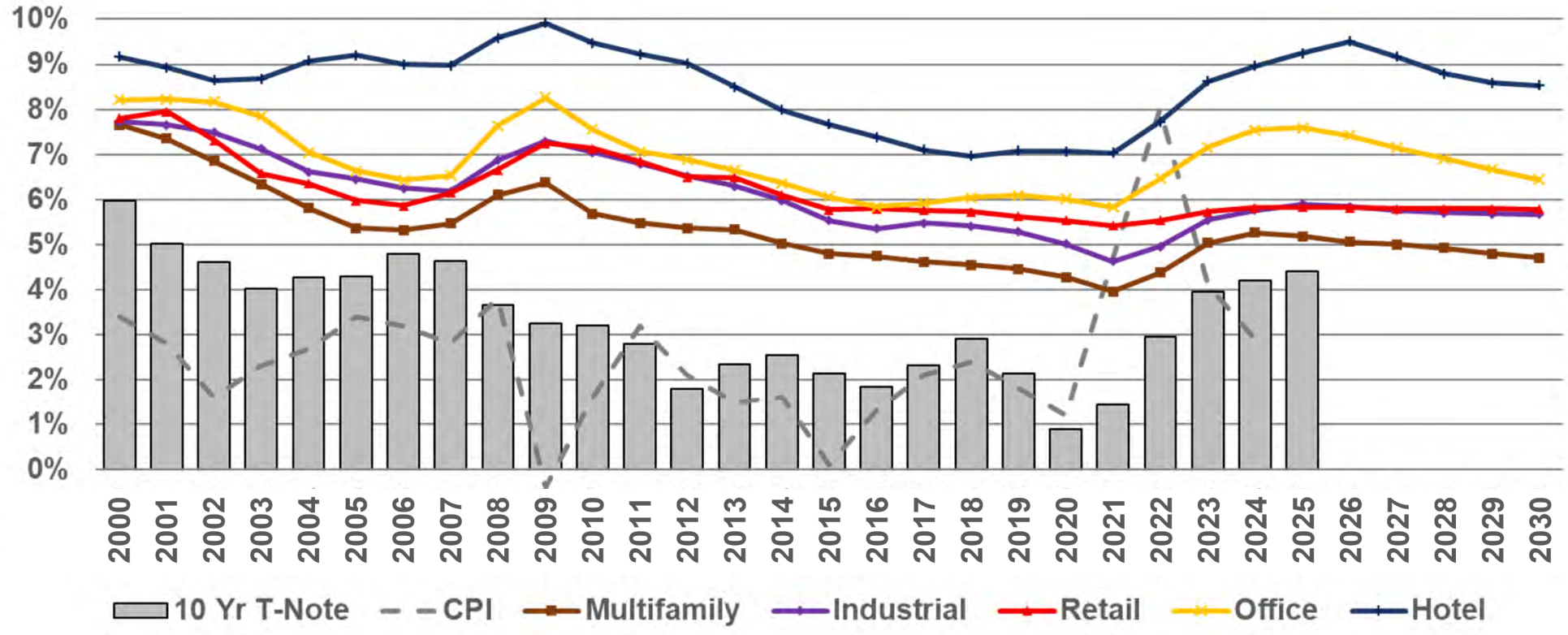
- A capitalization rate or "cap" rate is a common method of evaluating value of a development based on the revenue it generates
- The cap rate is a rate of return (%) that an investor receives for their investment

$$\text{Cap Rate} = \text{Cash Return} / \text{Value}$$

$$\text{Value} = \text{Cash Return} / \text{Market Cap Rate}$$

- New / ground up developments often evaluate feasibility based on a return on cost ("ROC") relative to value of a development at a given cap rate
- The return portion of ROC is how much profit a development yields as a percent of costs
- As an example, a development that is valued at $110 million (based on the cap rate) and costs $100 million to deliver would yield a 10% return on cost

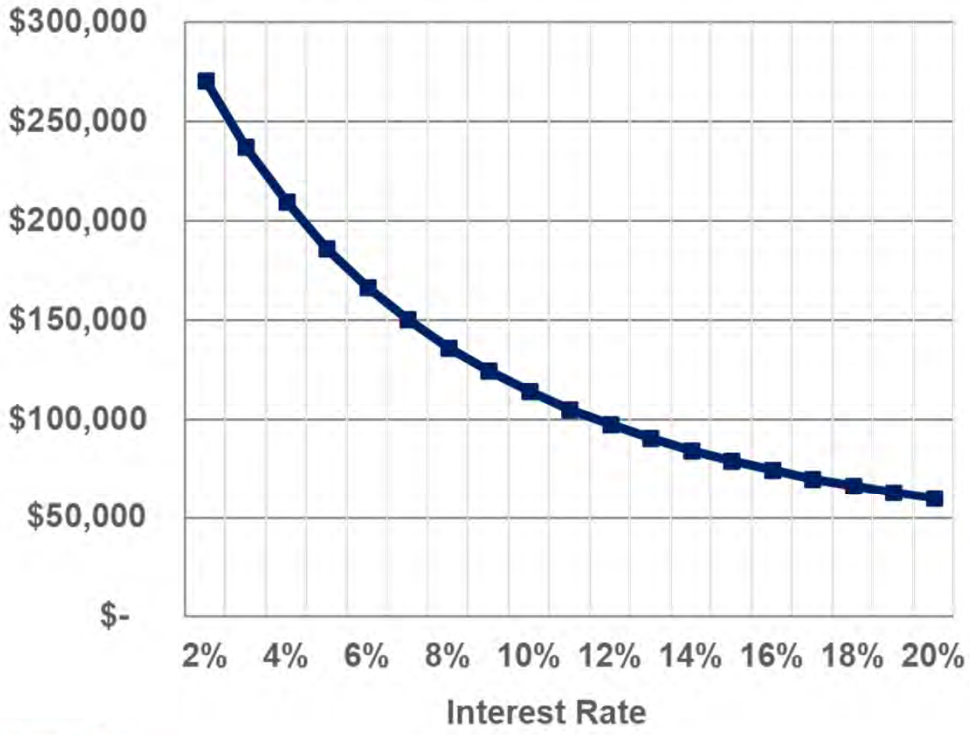
CAP RATE BY SEGMENT VS. 10 YEAR T-BILL (EAST BAY MARKET)



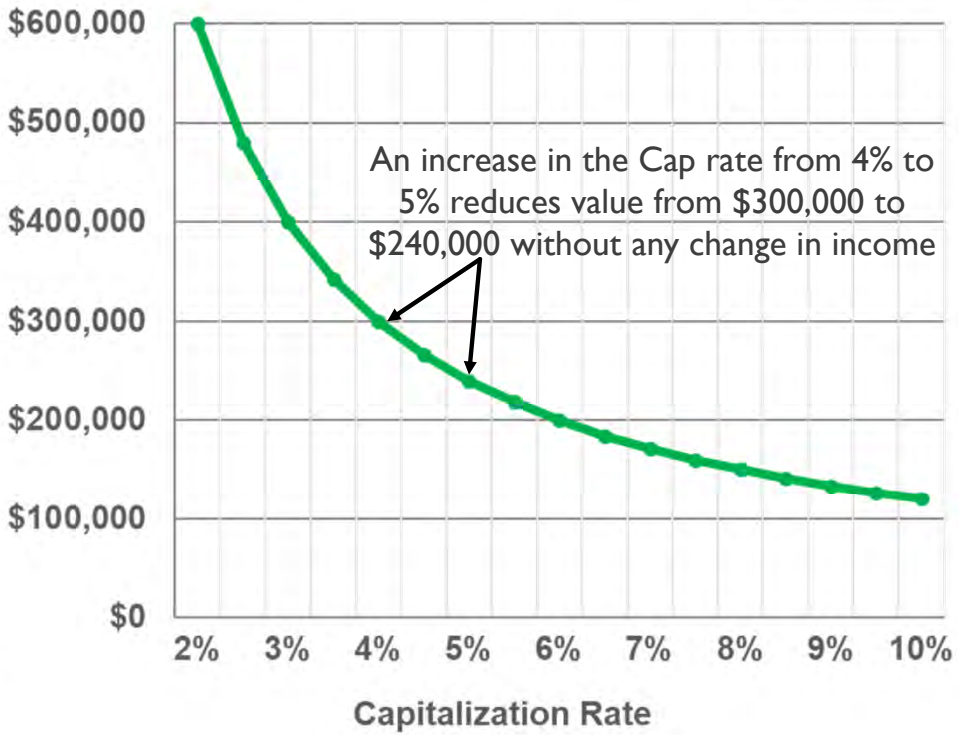
Source: Kosmont, CoStar 2025

IMPACT OF CHANGES IN INTEREST RATES & CAP RATES

Purchasing Power - $1,000 Per Month, 30 Yr Loan



Capitalized Value - $1,000 Per Month in Net Income



IMPACTS OF MARKET CONDITIONS TO VALUATION

- Increases in rent increase cash return = increased value
- Increases in vacancy reduce cash return = reduced value
- Increases in interest rates reduce cash return = reduced value
- Increases in cap rates reduce value, decreases in cap rates increase value
  - The value of a property with $1 MM in net income at a 4% cap = $25 MM
  - The same property at a 5% cap = $20 MM, a loss of $5 MM in value with no change in income
  - Increases in cap rates in the last few years have made many ground up projects financially infeasible

MARKET CONDITIONS - COSTAR MULTI-FAMILY SUBMARKETS

Proximate Markets Evaluated in Clusters

- San Leandro / San Lorenzo versus:
- East Oakland
- Hayward / Castro Valley / Union City
- Fremont / Newark
- Emeryville
- Downtown Oakland
- Alameda
- Walnut Creek / San Ramon
- Berkley
- Dublin / Pleasonton / Livermore

- Limited 4 & 5 Star (Quality) product in San Leandro makes it challenging to accurately compare rents
- Other markets seeing downward rent pressure as new inventory added and absorbed
- San Leandro projected to have slightly higher vacancy rates for 4 & 5 Star product than most peers

GENERAL MARKET CONDITIONS

- Ground up multi-family development has been constrained by shifts in capital markets over the last few years
- Absent increases in rents and/or decreases in vacancy, property values decrease as capitalization rates increase
- Increases in interest rates over the last few years have driven increases in capitalization rates and resulted in decreases in values for new (and existing) product
- Some general concerns in market about construction cost inflation and uncertainty
- Capital markets / lenders and investors remain on a conservative footing / hesitant to lend for ground-up development
- Projects that do achieve financing often required to have lower loan to value ratios, higher debt service coverage ratios, etc.

REVIEW OF SAMPLE PROJECTS PROPOSED IN CITY

- KR asked to review fundamentals for select projects that are entitled, but have yet to be developed:
  1. Maximus Project – 915 Antonio Street / 899 Alvarado St
  2. Town Hall Square – 1199 E. 14th Street
  3. 1388 Bancroft Ave
- Projects represent slightly different development approaches
- Projects have slightly different opportunities and constraints

SUMMARY OF SAMPLE PROJECTS

Project	Maximus	Town Hall Square	1388 Bancroft Ave
Land Area	5.74 Acres	1.20 Acrea	1.27 Acres
Building Stories	5	7	3
Gross Building Area	932,000 SF	280,000 SF	56,500 SF
Units	687	180	42
Avg SF / Unit & Efficiency	731 SF / 54%	944 SF / 61%	961 SF / 71%
DU / Acre	120	120	33
Parking Stalls	892 Subterranean	236 Subterranean	55 Surface
Parking Stalls / DU	1.3	1.3	1.3
Feasibility	Expect to require substantial improvement in market fundamentals	Expect to require moderate improvement in market fundamentals, Centro Callun stabilization	Expected to be financially feasible

FINDINGS

- The City is an attractive market for future development
- The market for new quality product in the City has yet to be fully proven out
- Newly completed Centro Callan may be a bellwether for future development in the near term
- City requirements of new development can have an impact on financial feasibility for projects that are *on the bubble*
  - Inclusionary housing, impact fees, development standards, etc.
- Even seemingly small changes in broad market conditions can have a big impact on financial feasibility
- Market fundamentals have been difficult for the last few years; the City could see some of the more feasible projects built out if broad market conditions improve
- Developing a ground up project is a difficult and risky proposition, especially in unproven markets; if the City desires to see new development it can help by working as a partner in facilitating projects

Thank You!