

# ABD OZONE FUND EXECUTIVE SUMMARY

*Affordable By Design*





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**Riaz Capital is an experienced and vertically integrated developer, owner and operator of small format housing that pursues tax-optimized investment strategies.** Operating in the Bay Area since 1977, Riaz Capital’s principals have built deep market knowledge, civic relationships, and the Micro-Studios strategy brick-by-brick over decades, profitably developing housing that anyone earning area median income can proudly call home. Today, the Riaz Capital team includes over 60 talented professionals across core competencies in development, construction, property management, finance & capital markets to exercise control and speed of execution through every stage of the project cycle. Recognizing the generational opportunity to eliminate future tax liabilities, Riaz Capital offers Opportunity Zone compliance for those investors who wish to allocate tax-optimized capital gains.

**Micro-Studios produce a 16% investor IRR and return 60% of invested capital within 4 years with conservative rent growth and leverage assumptions.** The investment will produce an average cash-on-cash yield of 12.0% on invested capital, and all distributions through the period of the hold will be tax-free based on the current regulatory context. Opportunity Zone tax benefits make an investment in the ABD Ozone Fund the equivalent of a 3.9x equity multiple. Importantly, the strategy is risk-averse, with a buffer of 30% or more in rent decline while still covering debt service.

Return Summary	IRR	Equity Multiple	Average Cash on Cash
Return as a %	16%	2.6x	12%
Cash Return	n/a	\$2.6M	\$117K

Tax Adjusted Return Summary	IRR	Equity Multiple	Average Cash on Cash
Return as a %	25%	3.9x	24.4%
Cash Return	n/a	\$3.9M	\$243K

**Micro-Studios represent a pure play investment at a time when traditional mixed-use multifamily buildings have significant risk factors, both in their exposure to luxury multifamily and due to the ground-floor retail for which there was minimal demand pre-Covid and for which there is virtually zero demand post-Covid.** Offerings such as Bridge, Related, or Starwood that provide the same Opportunity Zone tax treatment are funds of funds, which partner with local developers to develop a mix of asset classes. Because this structure adds a layer of fee and promote, investors first sacrifice yield for a tax strategy, settling for a single-digit IRR that nearly washes out the tax benefit. Additionally, these diversified fund structures split investment capital across retail, office, and even hospitality assets in addition to multifamily – and even in multifamily projects often include mixed-use such as ground floor retail spaces. The micro-studio strategy, on the other hand, focuses capital and risk exclusively in multifamily, exclusively in the low-risk workforce segment of the market.



**Long before the Covid-19 pandemic, the housing market spectacularly failed the Bay Area's single-income professionals.** Average rent in the Bay Area represents 40%+ of average income, compared to 25% nationally. Burdened by a functionally obsolete and car-centric zoning code, strict local land use controls, widespread NIMBYism, and skyrocketing construction costs, it has become nearly impossible over the past several years to produce housing below \$500K per dwelling unit – forcing developers to increase rents to generate a market return. As a result, in the Bay Area a paltry 10,000 units of middle-income housing (as measured by permit activity) were delivered over a decade of economic growth; this against a labor market that added over 375,000 middle-income jobs – a ratio of over 37 to 1. Paradoxically, middle-income represents a superlative customer demographic: we serve young professionals making \$50,000 - \$120,000 per year such as police officers, teachers, firefighters, healthcare workers, government employees, or nonprofit workers. We have found these incomes to be largely unperturbed by economic cycles and less vulnerable to the disruptions of remote work – because nurses can't spend the summer working from the Hamptons.

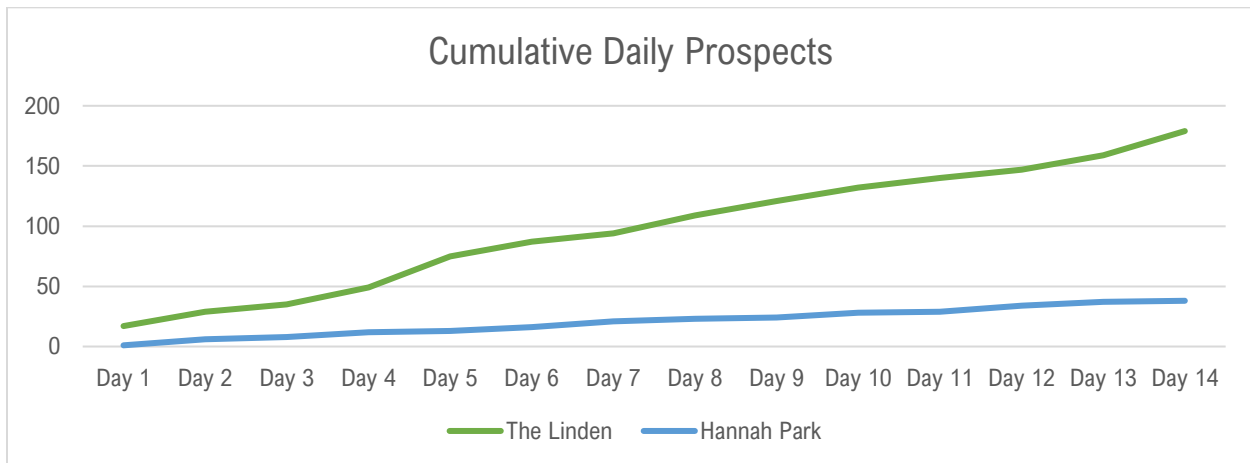
**The Bay Area and Oakland are beneficiaries of this market cycle.** As companies are faced with the decision to relocate from major cities, immediate secondary cities like Oakland will be the first to receive the expelled workforce. The micro-studio strategy has always considered its primary tenants to include nurses, municipal workers, and young professionals looking for more privacy for their dollar, and these exact demographics are most likely to end up in Oakland after any relocations. Amid the Shelter-in-Place experience, Oakland's attributes as a warmer, flatter neighbor to San Francisco have made it a much more welcoming place to spend time, and much more compatible with trendy bike transportation. Furthermore, the

macroeconomic trends of this particular crisis have been generally positive for the Bay Area. Many of the region’s largest employers are the tech giants that have propped up the stock market, and the Bay’s position as the preeminent innovation capital of the world is unlikely to change no matter the outcome of this economic cycle.

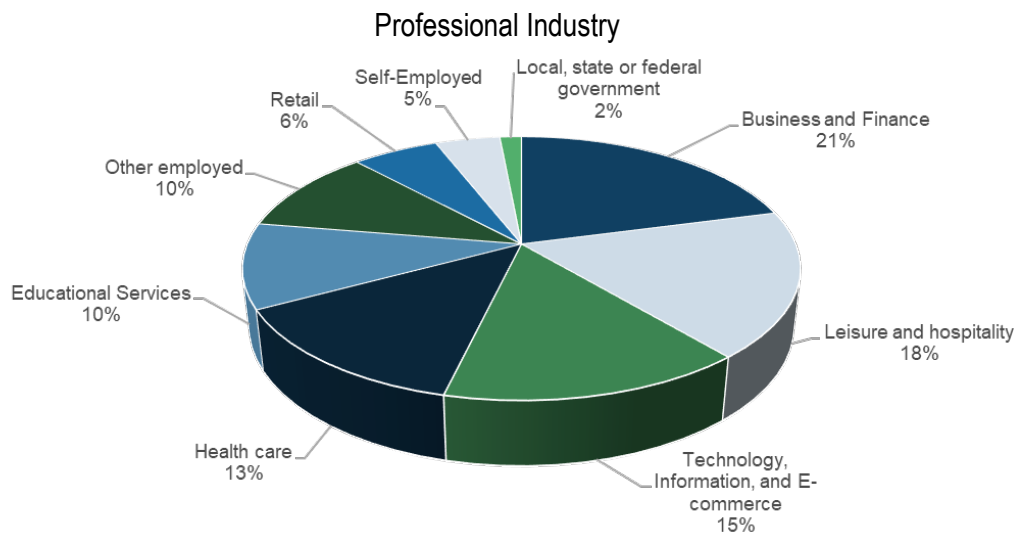
**Oakland does suffer some disadvantages relative to San Francisco, however, they are diminishing over time and less of a concern to our target customer.** Our strategy focuses on serving the pre-parent professional, a single-income person who is not personally concerned with the quality of Oakland schools. And although Oakland had a reputation for crime and disruptive protests in the past, it has in recent decades become a safe and prosperous city at the core of the Bay, with a majority-female population and a fast-growing median income. Amid recent protests and civil disturbance, San Francisco suffered far more property damage than did Oakland.

**Investors must consider not only location, but also the price point of an asset – in a down market, assets serving the entry-level price point significantly outperform the higher end of the market.** At our price point urban single-income professionals must otherwise live with roommates (sacrificing privacy), commute from distant but more affordable suburban areas (sacrificing time), or choose aging, rent-controlled housing stock (sacrificing quality). Particularly for basic needs like housing, entry-level products that respect their residents capture downsizing market share at times when luxury condo products struggle to be seen as anything other than a frivolous expense. Historical data bears out this thesis: even in the worst economic downcycles in the Bay Area’s history, the workforce sector typically sees only a ~4% drop in rents (versus 30%+ for luxury). Our current crisis proves to be no exception – we have seen a ~2 percentage-point decrease in economic occupancy across our portfolio, compared to “core” assets in San Francisco that have seen 10-20% declines.

**The Micro-Studio easily outperforms the competitive market in leasing and market interest.** We began pre-leasing The Linden – our latest micro-studio project – on September 1st. While Hannah Park and The Linden are only 1.1 miles apart and include the same design standards and interior finishes, we observe a significant difference in leasing traffic between the 2 properties. Over the first 14 days we received over 4 times more leads at The Linden, as represented in the chart below. The building achieved 70% leased during pre-leasing, far outperforming the projected 33%. We hit fully stabilized within 30 days of opening the building.



**Our target demographic is price sensitive, but stable.** Offering a product that our tenants can lease individually at a price within reach is the key factor that leases up The Linden and other micro-studio projects faster than any other new construction property in the area. And our resulting residents are more diversely employed than the tenants of luxury properties in expensive downtown markets, creating a steadier revenue base. Whereas luxury properties in the Bay Area have high concentrations in tech and finance occupations, our tenant base includes a much larger proportion of sectors, particularly healthcare, education, and government. Across our portfolio, of the last 100 leases, no professional sector exceeded 21% representation. In our most recent project, residents can qualify for our units at an income of only \$65,000 per year, whereas applicants to competing alternatives would require incomes above \$95,000. Additionally, if you compare the all-in cost of a traditional building versus living in our semi-furnished micro-studios, someone living in a competing building would need to earn as much as \$105,000. That income differential represents hundreds of thousands of Bay Area residents with stable, non-tech jobs who are priced out of competing properties and looking for a welcoming place to call home. In our most recent micro-studio project, despite only needing an average qualifying income of \$65,000, the average income was \$75,000 and the average age was 33.



**Micro-Studios are a market solution that produce housing at \$230K per occupant by aggressively attacking every element of the cost structure.** Riaz Capital has spent a decade building different projects in the workforce housing space and learning what works for this market and this resident. We’ve synthesized that experience into five clear value-creation principles that set micro-studios apart. (1) We achieve hidden density through higher occupant dwelling ratio. By using the latest regulatory tools for building housing in the Bay Area as well as our own innovative designs, we make room for more occupants on each plot of land. (2) We don’t build unnecessary space (e.g. parking, circulation, elevation). (3) We don’t pay unnecessary municipal, utility, and permit fees. (4) We use a predictable administrative entitlement process. We have a target 24-34 month timeline from Acquisition to Stabilization, depending on the size of the building. And (5) we build transit and bike-oriented projects to reduce the need for parking. Micro-studios’ carefully crafted pricing strategy produces a meaningful spread to competitive products, requiring 60% income growth to move up-market (e.g. traditional studio) or a substantial sacrifice in privacy, proximity, desirability, or functionality

to move to more cost-effective options (e.g. roommates, long commutes, poorly maintained properties, single-room occupancies, or living with family).

**We achieve our competitive advantage through an affordable price, stylish product, and fast deployment cycle.** Micro-Studios are priced at \$1,675 per month, which is 62% less expensive than new traditional studios in Oakland which rent at an average \$2,712 per month. We believe our interior, exterior, and operational design elements can inspire surprise and delight in urban single-income professionals which holds a distinct advantage in an otherwise commoditized market. And our fast deployment cycle creates high velocity of capital which can give us 60% return of capital by year 4.

**Our product helps solve the housing crisis affecting the Bay Area’s missing middle by developing urban workforce housing that is affordable, convenient, and stylish.** We have two designs: one for low-density zonings and another for higher-density urban centers. The Micro-Studio Townhouse features five micro-studios with a shared full kitchen and dining area that qualifies as a single legal dwelling unit. The Townhouse reduces impact & utility fees by 80%, with a simple wood-frame construction that is fast, repeatable, and lower cost than traditional (i.e. podium) multi-family. The Micro-Studio Mid-Rise is a 4-story garden style apartment building consisting of a mix of studios and 2 to 4 bedrooms leveraging the micro-studio concept with ensuite bathrooms, kitchenette and sitting area. It will leverage the density bonus to reduce parking and open space and increase the allowed number of units.

**The Micro-Studio offers the same eye-catching design and attention to detail as our higher-end projects, at a price point that respects our residents.**



**Future projects will provide greater privacy and deploy higher concentrations of capital through the Micro-Studio Mid-Rise design.** They will also be more suited to the desirable locations closer to the urban center.



**This fund is the next step in Riaz Capital’s corporate development, and the go-forward strategy focus of the firm.** During this most recent economic cycle Riaz Capital has invested \$76M in the acquisition or development of real estate which today carries a market / projected value of \$190M, equating to \$114M in value creation. Our completed investments average a 36.5% investor-level IRR and 2.78x Equity Multiple. Our firm has performed over 160 different residential and multifamily projects. We have focused our capital strategy into a fund structure in order to allow our development activities to benefit from the scale and infrastructure of a single capitalization. As a result, we achieve the value-creating benefits of small projects at the scale of an institutional development platform.

**With a Biden presidency – and thus tax policy – on the horizon, and with a market offering few cash-flowing investment opportunities, we expect investors over the next 6-12 months to show increased demand for assets and structures which enable the reduction, deferral, and elimination of their tax liabilities.** In this rebalancing, investors will look to find tax-optimized fixed-income alternatives, and multifamily real estate is a clear choice to meet those needs.<sup>1</sup> Although within multifamily, many observers note the drop in luxury rents during this period in core markets like San Francisco and Manhattan, such observations often miss the fact that entry level rents have held up significantly better, especially in primary suburban markets.

**The backbone of the U.S. economy, the urban workforce has been systematically underhoused through years of housing policy designed to prioritize cars and families, and today constitutes the largest and most defensible market opportunity in the built environment.** The Micro-Studio is a comprehensive, customer-centric strategy to build urban workforce housing at scale, at rents within reach of the urban workforce, and at market returns. As the world adapts to the Covid-19 pandemic, the micro-studio thesis only grows stronger.

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<sup>1</sup> For further discussion of the benefits of real estate investing to optimize tax planning, please see our full article on the Riaz Capital website at [www.riazcapital.com](http://www.riazcapital.com).

Please read on for a summary of key sensitivity analyses

**Rent Sensitivity at Construction**

The combination of the micro-studio strategy’s \$1,675 per month rent assumption (which represents a \$125+ discount from market-validated direct competitors) and **conservative use of leverage means that rents could drop to \$1,080 per month (a 36% drop from underwriting and an over 40% drop from current market rents) and micro-studio projects can still service construction debt at the riskiest juncture of the project cycle** (please see the below sensitivity table). In other words, a micro-studio project would not be at risk of handing the keys to a lender until market rents declined by over 40% or double the worst recession the region has historically experienced and 5x what the Company has experienced in its own portfolio.

RENT SENSITIVITY ANALYSIS (at Construction)						
Weighted Average Rents	\$1,080	\$1,475	\$1,575	\$1,675	\$1,775	\$1,875
<b>Return Metrics (Investor):</b>						
IRR	8%	8%	10%	16%	20%	23%
EM	1.7x	1.7x	1.9x	2.6x	3.2x	3.8x
Average Cash-on-Cash (Years 0-9)	5%	5%	7%	12%	15%	19%
<b>Stabilized Cash Flow (Year 5):</b>						
Cash-on-Cash (Invested Capital)	0%	0%	4%	7%	10%	14%
Cash-on-Cash (Risk Capital)	0%	1%	8%	17%	28%	42%
<b>Tax Adjusted Returns:</b>						
IRR	13%	14%	17%	25%	31%	36%
EM	2.3x	2.3x	2.7x	3.9x	5.0x	6.2x
<b>Debt Metrics:</b>						
DSCR	1.00	1.62	1.78	1.94	2.10	2.25
LTV (at 5.00 Cap)	90%	55%	50%	46%	43%	40%

**Rent Sensitivity at Stabilization**

**Even after refinancing into a slightly higher LTV permanent loan (but after the key risks – entitlement, construction, and lease-up – have passed) a micro-studio project is still able to service its debt at rents of \$1,180 per month (or a 35% decline from current market).**

RENT SENSITIVITY ANALYSIS (at Refinance with cash-out, loan fixed at \$1,675 level)						
Weighted Average Rents	\$1,180 (Breakeven)	\$1,275	\$1,475	\$1,675	\$1,875	\$2,075
<b>Return Metrics (Investor):</b>						
IRR	8%	8%	10%	16%	20%	23%
EM	1.7x	1.7x	1.9x	2.6x	3.2x	3.8x
Average Cash-on-Cash (Years 0-9)	5%	5%	7%	12%	15%	19%
<b>Stabilized Cash Flow (Year 5):</b>						
Cash-on-Cash (Invested Capital)	0%	0%	4%	7%	10%	14%
Cash-on-Cash (Risk Capital)	0%	1%	8%	17%	28%	42%
<b>Tax Adjusted Returns:</b>						
IRR	13%	14%	17%	25%	31%	36%
EM	2.3x	2.3x	2.7x	3.9x	5.0x	6.2x
<b>Debt Metrics:</b>						
DSCR (IO)	1.00	1.13	1.40	1.68	1.95	2.23
LTV (at 5.00 Exit Cap)	99%	87%	70%	59%	51%	45%



**Cost and Interest Rate Assumptions**

And recent scenario analysis shows potential for outperformance of our base expectations. When we reset our cost and interest rate assumptions to the current environment, even with only a 5% drop in construction/development cost and an interest rate conservatively underwritten to 3.5%, we could actually achieve a higher IRR of 20.07%.

		Total Costs / Suite					
		15% Lower 179,000	10% Lower 189,000	5% Lower 199,000	Base Case 209,000	5% Higher 219,000	10% Higher 229,000
Interest Rate	3.00%	25.97%	23.47%	20.93%	18.56%	16.50%	14.71%
	3.50%	25.10%	22.57%	20.07%	17.76%	15.87%	14.25%
	4.00%	24.25%	21.69%	19.25%	17.10%	15.34%	13.44%
	4.50%	23.43%	20.84%	18.52%	16.52%	14.50%	12.66%
	5.00%	22.60%	20.05%	17.93%	15.65%	13.70%	11.94%
	5.50%	21.76%	19.43%	17.03%	14.82%	12.94%	11.25%