Commercial Real Estate

Evaluation of Holding, Refinancing or Sale/Investment in APFC Managed Funds

July 30, 2020

Trust
Alaska Mental Health Trust Authority
25 YEARS

Questions Addressed

- Should the Trust sell the Commercial Real Estate assets and reinvest in financial assets managed by the APFC?
- If the assets are held, is the current financing optimal, or are there alternatives that can improve cash flow for Trust benefit?
- Are there legislative, legal or financial risks that outweigh the benefits of the financing options?

Overview of Properties' Value, Financing and Leasing Status

$MM

Cordova (2011)
(TLO)

Current Value:	$4.100
Debt:	$0

100% occupied, includes TLO

Commercial (2013)
(Cummins)

Current Value:	$2.870
Debt:	$1.010
Rate:	3.94%
Prepay Penalty:	None

100% occupied with anticipated lease renewal

Rulon (2013)
(IRS)

Current Value:	$20.100
Debt:	$6.556
Rate:	4.20%
Prepay Penalty:	None

100% occupied with long-term, strong-credit, single-tenant lease

Israel (2014)
(WA)

Current Value:	$18.860
Debt:	$6.809
Rate:	4.35%
Prepay Penalty:	$0.506

WA purchase option at 98% of appraisal. Current lease negotiations expected to set a reference rate for 2023 renewal

Ridgepoint (2015)
(Promontory Point, TX-DOT)

Current Value:	$15.500
Debt:	$9.408
Rate:	4.69%
Prepay Penalty:	$1.158

100% occupied. DOT backfilling upcoming vacancy

San Pedro (2015)
(North Park, Marriott)

Current Value:	$13.500
Debt:	$6.628
Rate:	5.20%
Prepay Penalty:	$0.197

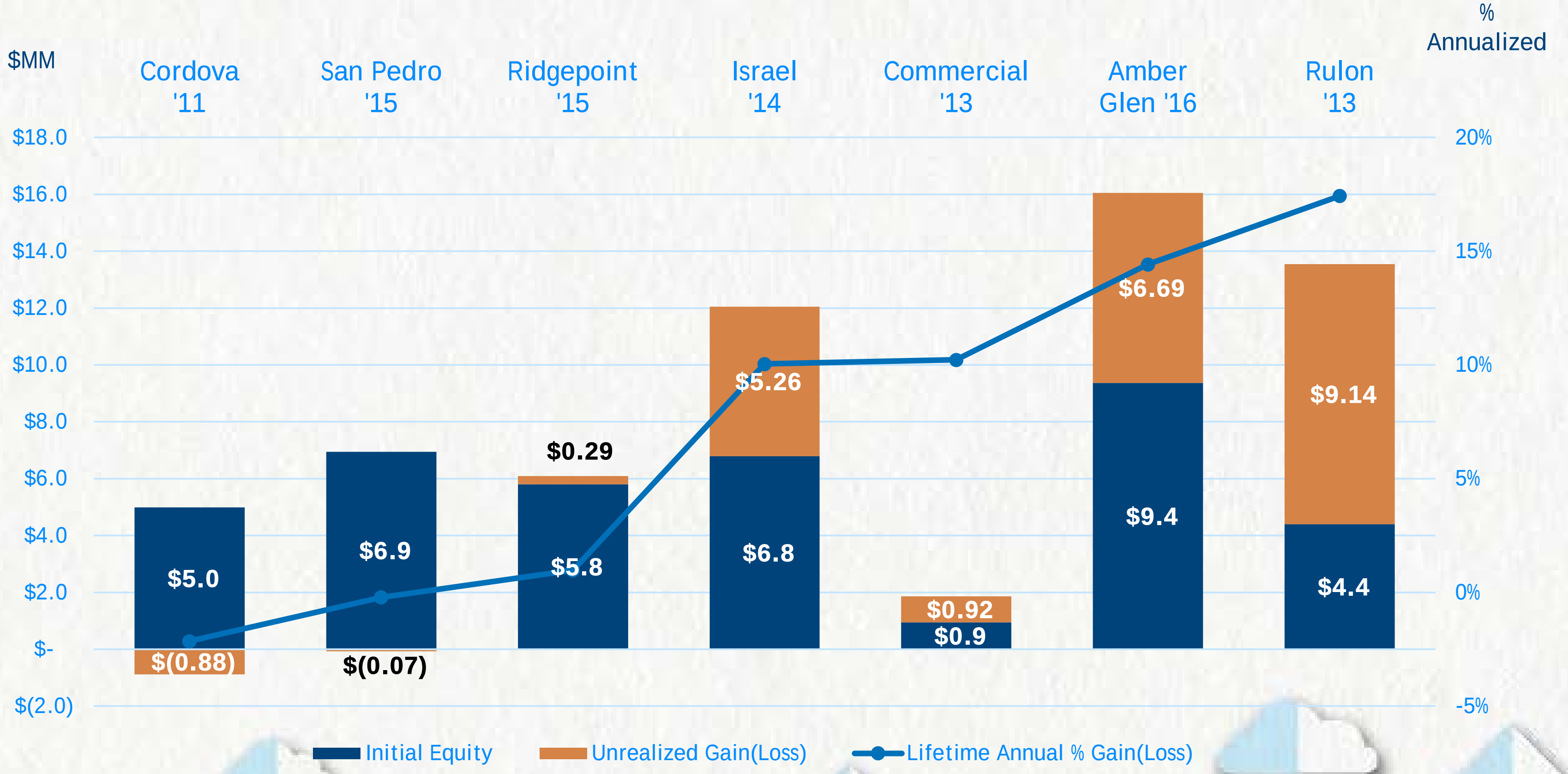
Active leasing showings to fill vacancies, including potential October vacancy

Amber Glen (2016)
(Amber Oaks, Xerox)

Current Value:	$27.644
Debt:	$11.592
Rate:	4.25%
Prepay Penalty:	$1.573

Active leasing showings to fill vacancies.

CRE assets have generated a 7% average annual unrealized gain since purchase



FY20 Value: $102.6MM
Debt: $42.0MM
Trust Equity: $60.6MM

Rulon, Amberglen, Commercial and Israel show strength.
San Pedro and Ridgepoint are expected to strengthen with new leases.

Since 2016, CRE's Performance for the Trust: $1.6MM average annual distribution 12% average realized and unrealized gains

2016-2020

Average Distribution of $1.6MM is below $2.6MM purchase prediction

Strong average year-over-year returns

- ➢ 3% Average Realized Return
- ➢ 9% Average Unrealized Return
- ➢ 12% Total

Note: Status Quo forecast excluding scheduled balloon payments

Since inception, CRE and APFC average returns are comparable, with CRE slightly outpacing APFC

FY20 CRE returns are anticipated to outperform both APFC total fund and real estate's anticipated returns.

TLO's 5-year forecast anticipates more aggressive performance than APFC.

Commercial Real Estate Portfolio and APFC Performance

Annual Average Return Since CRE Inception, FY 2020 Estimate and Forecast

	2012-2019 Average	FY 2020 Estimate	Average 5-yr Forecast
CRE Portfolio			
Operating Return	1.8%	1.7%	6.2%
Unrealized Gain (Loss)	7.0%	5.8%	3.0%
Total CRE Return	**8.8%**	**7.5%**	**9.2%**
APFC			
Fund Total	**7.80%**	**0.0%**	**7.0%**
Real Estate	**7.79%**	**0.8%**	

Source: FY20 estimate: APFC 5/31/20 1-year returns; CRE: 6/30/20 reports. Forecast source: APFC – Callan FY20 10-year forecast; CRE – TLO 5-year forecast

Refinancing Options

Decisions are driven by holding strategy, cash need, and required return

Trust
Alaska Mental Health Trust Authority

Evaluation using four scenarios

Scenarios

- Status Quo
  - Six existing amortizing mortgages
- Interest-Only Portfolio Refinancing
  - Finance portfolio of seven CRE assets
- Partial Interest-Only Refinancing
  - Three assets refinanced, three maintain amortizing mortgages
- Sale of CRE assets, APFC investment management of proceeds

Assumptions

- Loans
  - 3.7% refinance interest rate
  - New financing must generate 3% or more over status quo in present value
- Sale/Invest
  - Assets sell at 6/20 valuation
  - 7% long-term APFC return
- Evaluation: 17 years
- Transactions: January 2021

Option 1: Status Quo

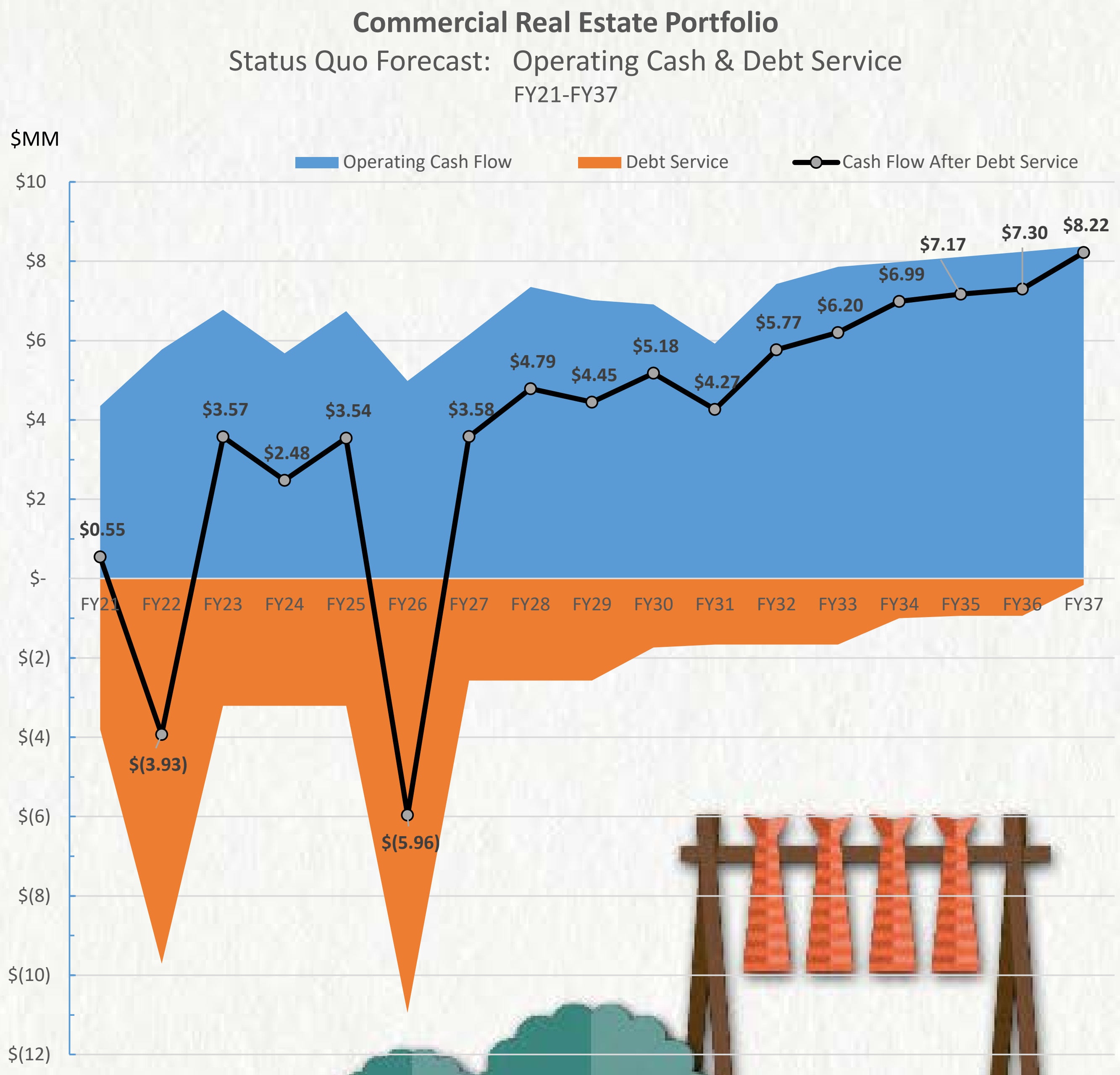
CRE need estimated cash infusion of $3.93MM in FY22 and $5.96MM in FY26

- ➢Mortgage balloon payments:

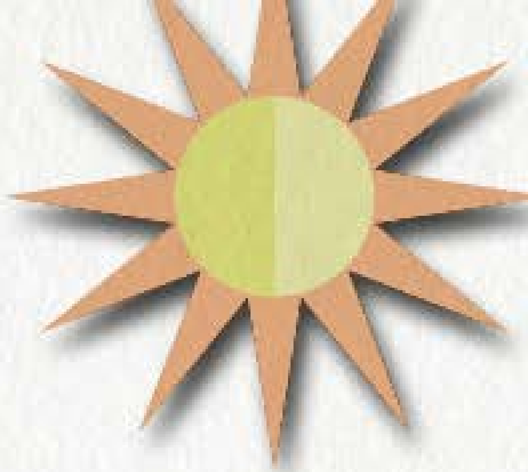
  FY22 $ 6.3MM   San Pedro

  FY26 $ 8.4MM   Ridgepoint

- ➢Israel worst case cash support needed: $1.7MM for FY22 and FY23



Option 1: Status Quo Requires Action



Alternatives

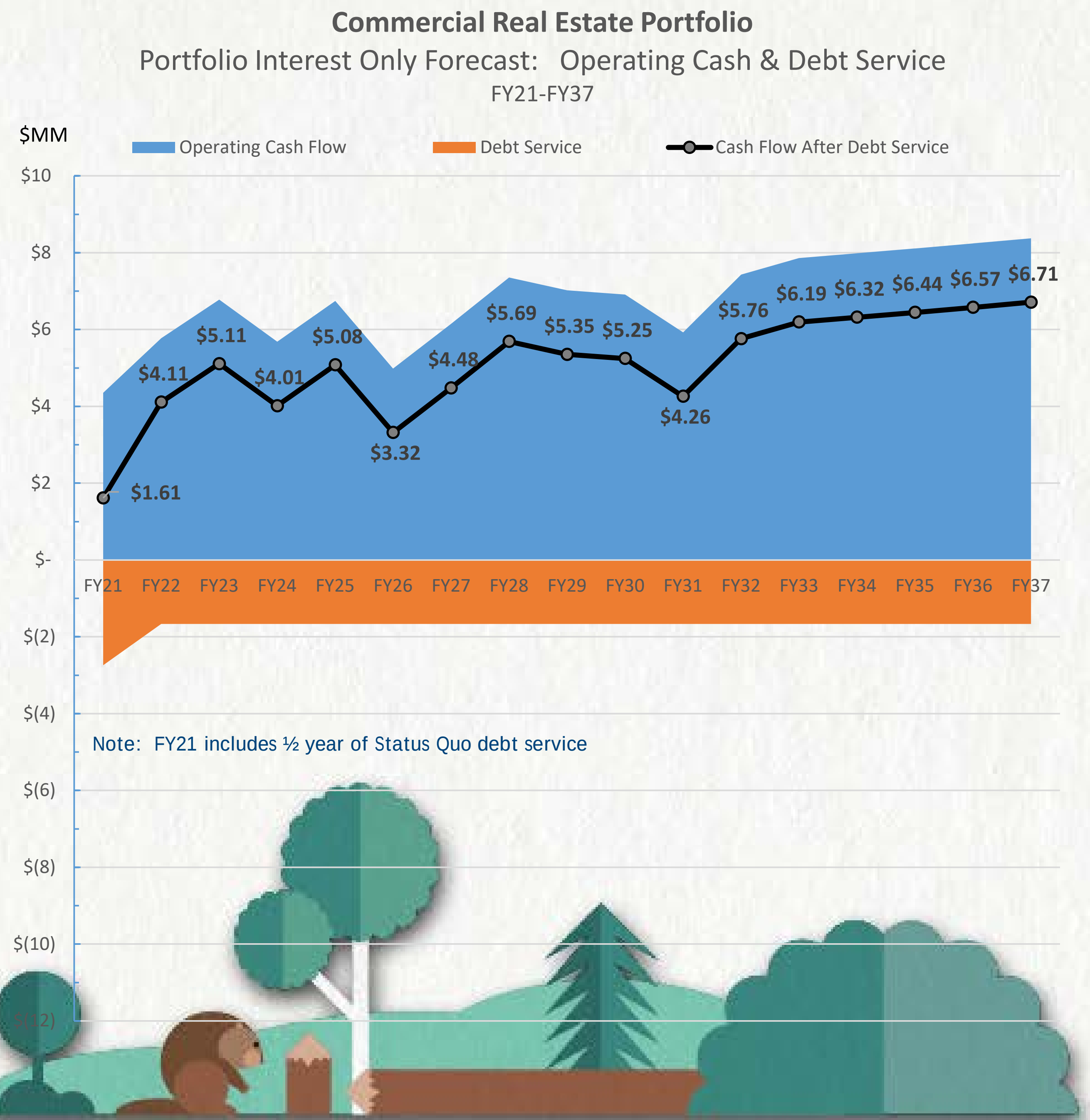
- Draw from existing cash
- Obtain new cash

Considerations

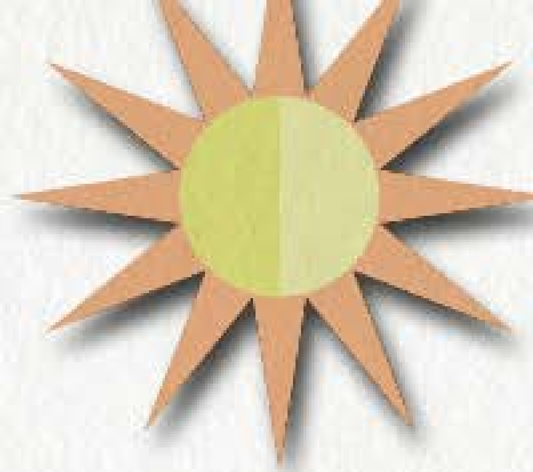
- Need for Trust Budget Reserves for beneficiary benefit
- Asset values in uncertain commercial real estate market
- Allowable use of proceeds

Option 2: Interest Only Portfolio Refinance

- Roll assets into Special Purpose Vehicle (SPV), financing $45.05MM portfolio
- Estimated interest payments: $1.7MM per year
- $45.05MM principal to be repaid ultimately



Option 2: I/O Portfolio Refinance is Favorable to Status Quo



Alternatives

- Long-term holding
- Medium to long-term holding with asset sales and reinvestment in Trust funds managed by APFC

Considerations

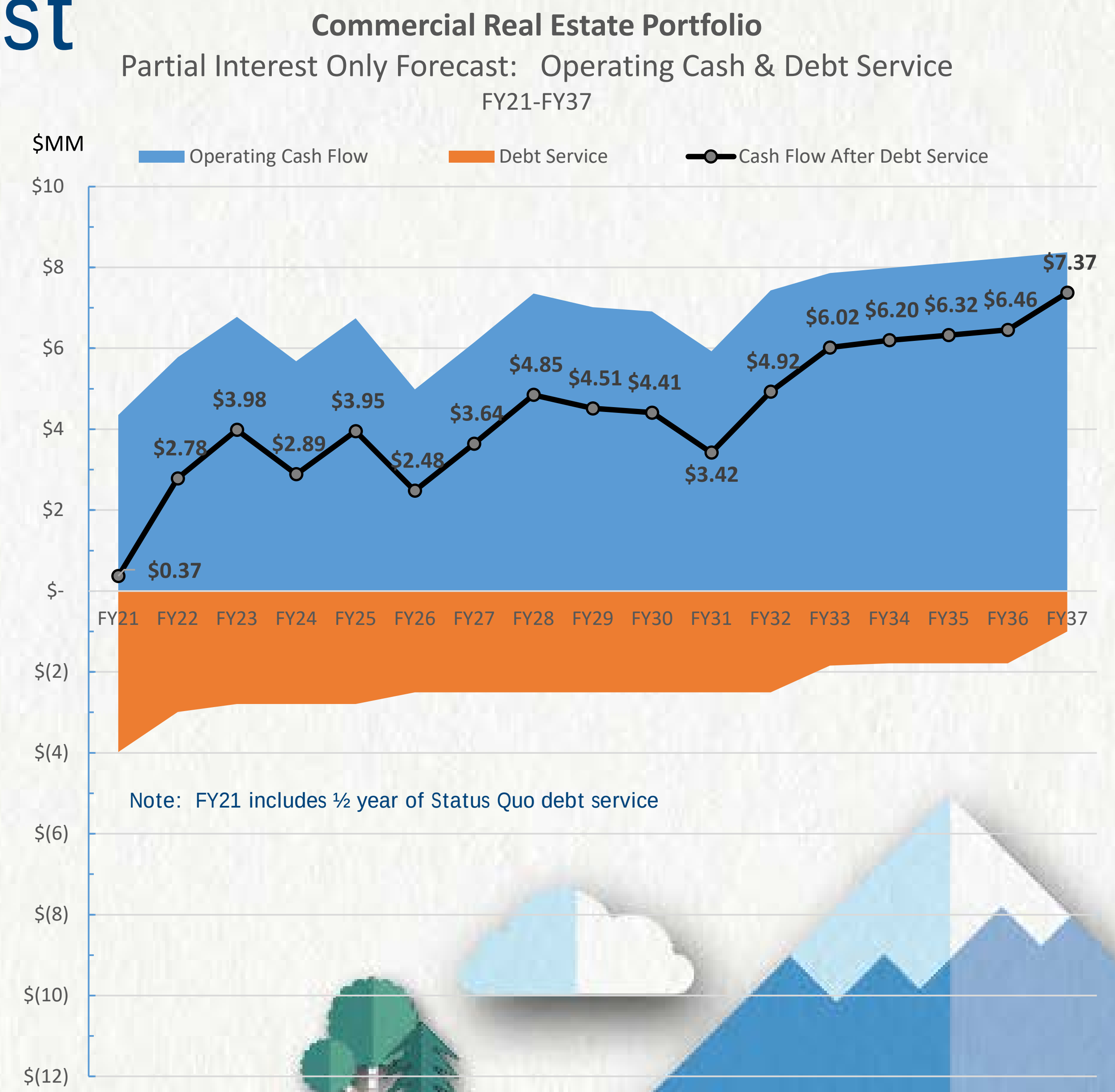
- Potential to reduce loan prepayment penalties and secure lower interest rate
- Financing terms with substitution or liquidation rights
- Long term benefit of hold v sell/invest

Pros

- LLC liability protections are retained in SPV
- Ability of new financing to generate 3% or more long-term cash benefit over status quo
- Flexible cash flow management at Trust level, not asset level

Option 3: Partial Interest Only Refinance

- ➢Refinance three properties as cash needs occur within individual LLC structures
- ➢Projected interest payments decline from 3.7MM in FY21 to $1.1MM in FY37
- ➢Ultimately $21.49MM principal to be repaid



Option 3: Partial Interest Only Refinance is Favorable to Status Quo

Alternatives

- Long-term holding
- Asset sales at maturity and investment of net proceeds

Considerations

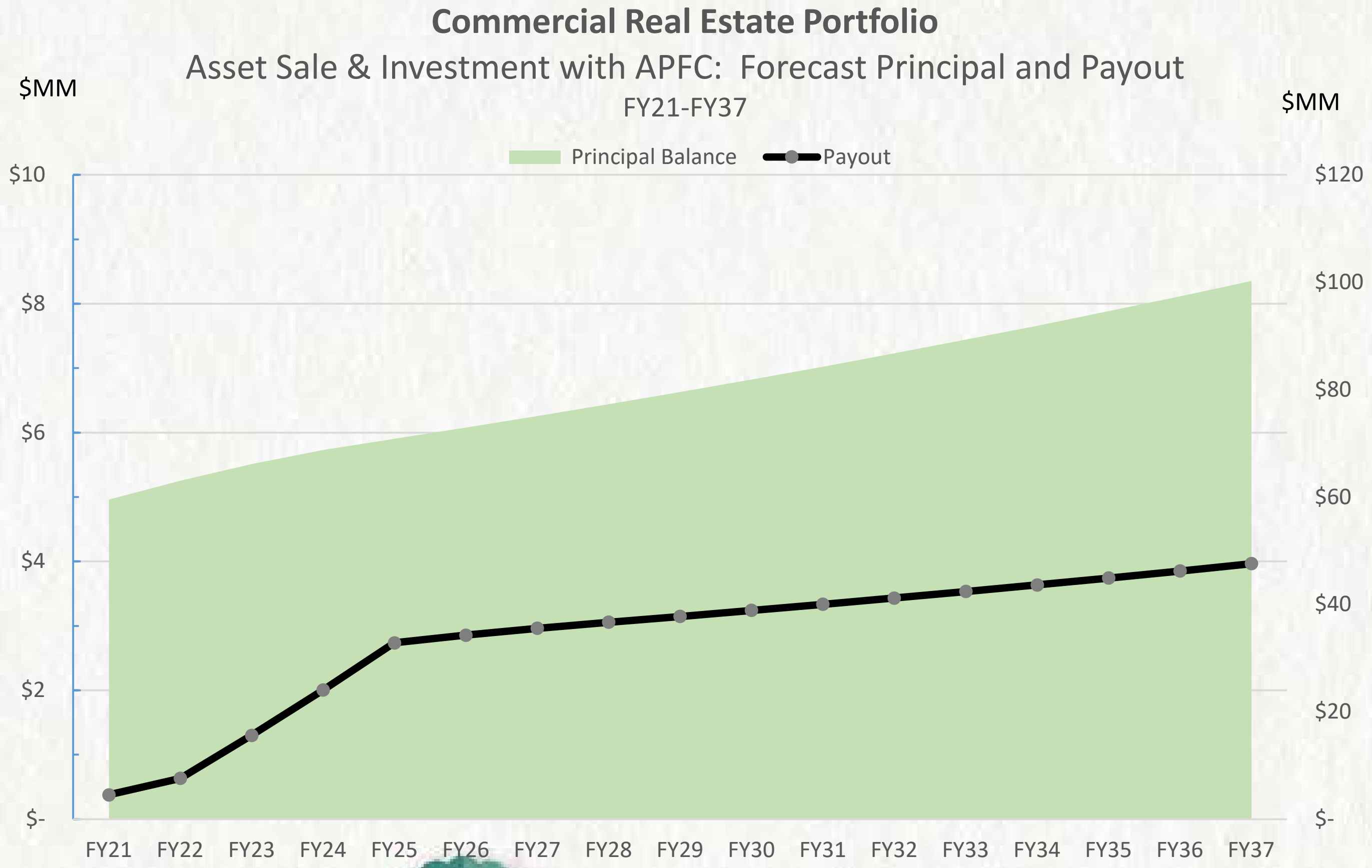
- Cash management at Asset or Trust level
- Long term benefit of hold v sell/invest

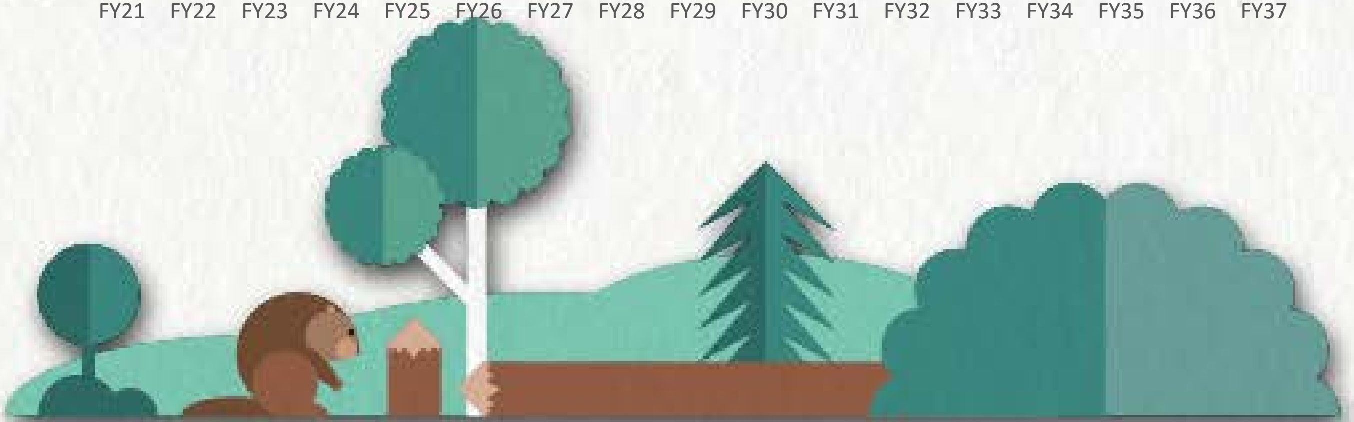
Pros

- Avoidance of $2.9MM prepayment fees with portfolio refinance
- Ability of new financings to generate 3% or more long-term cash benefit over status quo

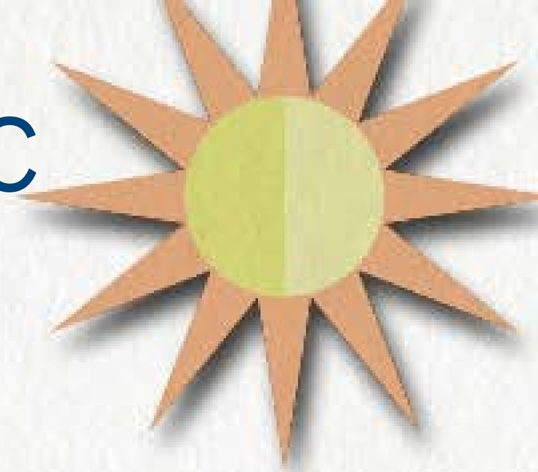
Option 4: Asset Sale and Investment in APFC Managed Fund

- ➢Sell assets at market values, netting est. $57.5MM
- ➢Invest in APFC managed fund, earning forecast average 7%
- ➢Draw 4.25% of rolling prior 4 year average





Option 4: Sale and Investment in APFC Managed Fund



Alternatives

- Sell all assets in near term and invest
- Strategically time asset sales and investment

Considerations

- Ability to forecast both near and long-term with uncertainty in investment assets

Cash flow after debt service of options have large differences near-term

Commercial Real Estate Portfolio Forecast Distributions	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
Fiscal Year	**FY21**	**FY22**	**FY23**	**FY24**	**FY25**	**FY26**
Operational Baseline: Cash Flow Before Debt Service	$ 4,350,983	$ 5,776,309	$ 6,776,730	$ 5,680,093	$ 6,744,960	$ 4,983,548
Income Generated Under Alternate Financing Scenarios:						
Option 1: Maintain Status Quo (No Refinancing)	$679,743	($3,953,378)	$3,362,798	$2,482,206	$3,370,617	($5,859,791)
Option 2: Refinance Assets as a Portfolio	$1,899,309	$4,239,564	$5,138,342	$4,305,621	$5,189,841	$3,724,430
Option 3: Refinancing As Needed	$930,598	$2,958,143	$4,012,158	$3,179,437	$4,063,657	$2,872,898
Option 4: Sale & APFC Investment	$378,320	$632,219	$1,301,818	$2,004,290	$2,734,464	$2,854,297

- Medium-term, CRE cash to Trust begins to converge under hold strategies
- Longer term, cash from Status Quo and Partial ReFi exceed Interest Only

AMPS requires valuation based on today's value of future cash flows

Estimated Present Value Cash Flow generated over 17-year horizon:

- **Status Quo** **$28.4MM**
  Range: $5.5MM to $36.8MM
- **Interest Only Portfolio** **$46.2MM**
  Range: $23.5MM to $54.6MM
- **Partial Interest Only** **$38.1MM**
  Range: $15.5MM to $46.5MM
- **Sale/Invest in APFC** **$24.3MM**
  Range: $24.2MM to $24.3MM

Considerations

- Expected market rates: APFC returns, financing and CRE returns
- Near term cash generation
- Current and long-term beneficiary benefit
- Impact of strategic asset sales and APFC investment on overall returns
- Specific financing requirements' pros and cons

Discussion

Trust
Alaska Mental Health
Trust Authority