Waterville Industrial

Bailard Real Estate Fund

ACQUISITION DATE
December 14, 2022

LOCATION
San Diego, CA
(San Diego MSA)

PROPERTY TYPE
Industrial

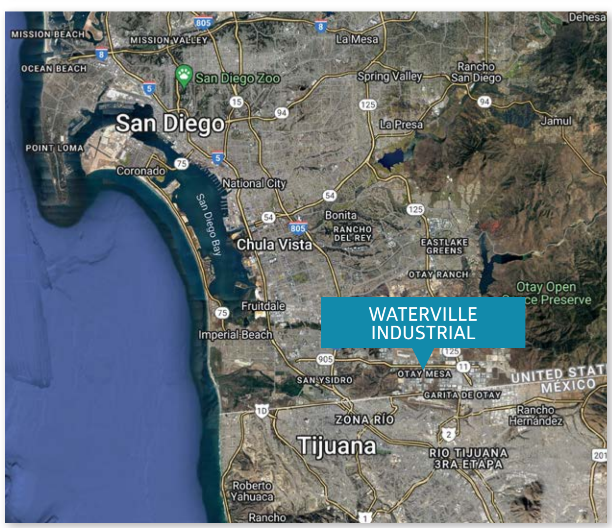
YEAR BUILT
1996

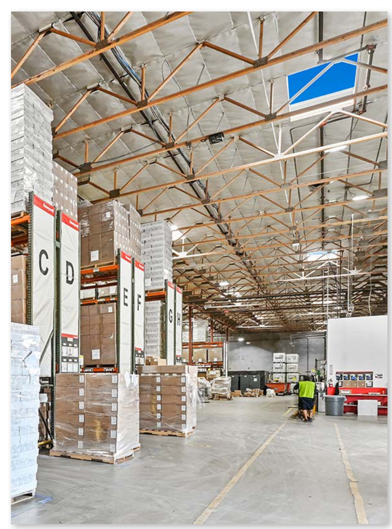
SIZE
101,435 square feet (SF)

PARKING
114 spaces
9 dock high / 2 drive-in

OCCUPANCY
100% leased

PURCHASE PRICE
$15.25 million





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Waterville Industrial
San Diego, CA

THE PROPERTY

Waterville Industrial (the "Property") is a single free-standing industrial and manufacturing property, totaling 101,435 square feet situated on six acres of land located at 7828 Waterville Road in San Diego, California. The Property's seller, Honeywell International Inc., occupies the building for the use of its Safety Products division, manufacturing low pressure foam earplugs. Honeywell leased back the entire facility through March 31, 2025 (~27 months). Following the expiration of the lease, Honeywell will vacate the Property, at which time the Fund will renovate and re-lease it. Waterville Industrial is strategically located in Otay Mesa, one of San Diego's premier industrial nodes due to its proximity to the Mexico-United States border.

The Property represents a rare value-add opportunity: a high-quality, functional, and well-located asset with substantial appreciation potential from renovation and re-leasing but with an immediate income stream from the leaseback to Honeywell.

THE OPPORTUNITY

Purchase a Well-Located Property with Outstanding Economic Driver Potential – The Property is in Otay Mesa, a fundamentally-strong industrial submarket of San Diego due its proximity to the Otay Mesa Land Port of Entry to Mexico. With more than $56 billion in trade on an annual basis, Otay Mesa has become California's largest commercial land border port and one of the busiest commercial land border crossings in the United States. Otay Mesa is home to more than 4,400 companies, most of which are large corporate warehousing, distribution, and manufacturing users whose businesses work within the United States-Mexico supply chain. The Property benefits from its access to California State Route-905, an east-west freeway that reaches the Otay Mesa border crossing into Mexico within a three mile-drive time.

A Rare Value-Add Investment – The Property was acquired under market conditions that included economic uncertainty, a volatile stock market, and rising interest rates, which rapidly shrunk the size of the pool of potential investors. Normally, an industrial investment such as Waterville would have had a highly competitive bidding process resulting in elevated pricing and compressed yields. The sidelining of capital resulted in a less competitive bidding process, allowing the Fund to purchase the Property at a price that will not only allow appropriate returns for a value-add investment but also reduce the risk due to the low-cost basis relative to replacement cost in Otay Mesa.

Partner with a Reputable Developer/Operator – The Fund partnered with Murphy Development Company ("MDC"), a San Diego-based operator and developer with over 40 years of experience in the San Diego market. Since its establishment, MDC has master planned and developed projects throughout San Diego County. Partnering with MDC enhances the probability of a successful outcome, and it will result in more deal flow in San Diego as they plan to continue to share new investment and development opportunities.

IDENTIFIED RISKS

Renovation Costs – As with all value-add investment, there are risks associated with doing a substantial renovation project stemming from cost overruns, timing, and other factors. However, these risks are mitigated through partnering with an experienced developer and operator in MDC that has built strong relationships with local municipalities and construction companies in the Otay Mesa area that provide comfort for the Fund that MDC will be able to execute the renovation plan within budget and the underwritten timeline. In addition, the Property's initial low basis at $153/SF provides additional cushion. The underwritten renovation budget also includes a 25% (of hard costs) contingency.

Future Lease-Up – As noted earlier, the Property will be fully vacant in April 2025, following the expiration of the Honeywell lease. The lease-up opportunity provides upside potential, but also adds risk. The Fund has done a deep investigation of the market and competitive set. User demand for industrial properties in Otay Mesa continues to outpace new supply. In addition, the Otay Mesa submarket is largely built-out with limited available land for new development. Given the tightness of the market, the Fund is confident that the Property will lease-up within the underwritten downtime and at the projected rents.

Clear Height – The Property was built in 1996 with a 24 to 26-foot clear heights. Recent generation industrial buildings have clear heights that are 30 feet or higher, which is consistent with what many users demand in the market. While the Property's clear height is still considered competitive and functional, there is a risk that the pool of tenants looking at the building will be shallower due to the lower clear height. The Fund investigated the market to determine the significance of this risk to the investment and believes it will be low. The clear height is more than adequate for most users, especially manufacturers that typically do not need racking, which requires higher clear heights.

THE INVESTMENT

The total purchase price, inclusive of closing costs, was $15.5 million ($153/SF), equating to a 4.4% year-one return-on-investment. The Fund's value-add business plan projects to increase the basis to $20.5 million ($211/SF). Once leased, the investment is projected to provide the Fund a stabilized return-on-cost of 7.4%. The Property was acquired unlevered. The Fund will own 85% interest with MDC owning the remaining 15%.

PROJECTED RETURNS*

Projected four-year unlevered IRR of 13.0% and a 1.5x equity multiple net to the Fund.

** Projected Returns are hypothetical in nature. There can be no assurance that this investment will achieve such projected returns. Please see important disclosures regarding these hypothetical returns at the end of this document. IRR and Equity Multiple represent the investment's projected returns, net of joint venture partner fees and investment-level leverage. As such, Fund-level fees and expenses are not included in the calculations.*

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