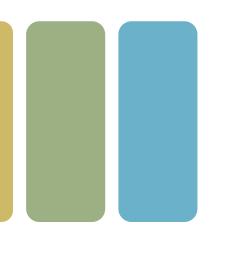
CONFIDENTIAL DRAFT FOR INTERNAL REVIEW



ישראל בונה Israel Builds: A Public / Private Partnership to Finance Affordable Housing

Workshop

May 26, 2014

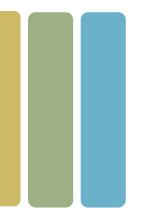
Workshop Agenda

- The Current State of Affairs in Israel
- 2. Harlem Project Rental Housing Development Case Study
- 3. Mechanisms of Affordable Rental Development
- 4. Israeli Rental Project: Creating a Rental Market in Israel
- Bridging the Gap:
- 6. Next Steps



Goals for Workshop

How to induce government and lenders to provide the financing tools that will spur development of rental housing in Israel.



Session 1:

The Current State of Affairs in Israel



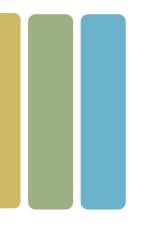
The Current State of Affairs in Israel **Financial Institutions**

- The establishment of Economic and Social Change committee,
 Aug 2011.
- The amendment to the Income Tax Act (Exemption from Taxes to Provident Funds on Income from Rental Fees Relating to Long Term Residential Rentals), July 2012.
- The Regulations on Supervision of Financial Services (Provident Funds) (Investment Regulations for Financial Institutions), July 2012.
- The Provisions of the Commissioner of the Capital Market-Investment Regulations for financial institutions (investment in partnership/corporation and managing real estate), Aug 2013.



The Current State of Affairs in Israel Marketing, Planning and Building Acts

- Israel Lands Council Resolution No. 1248- marketing of long-term rental housing, March 2012. (amended following decision no. 1291, October 2013).
- The recommendations of the "90 Days Team", Oct 2013.
- The Amendment to the Planning and Construction Law, March 2014.
- The amendment to the Israel Lands Authority Law, March 2014.



Session 2:

Harlem Rental Project: A Case Study Doing Well by Doing Good



Harlem Rental Project: Introduction and Context

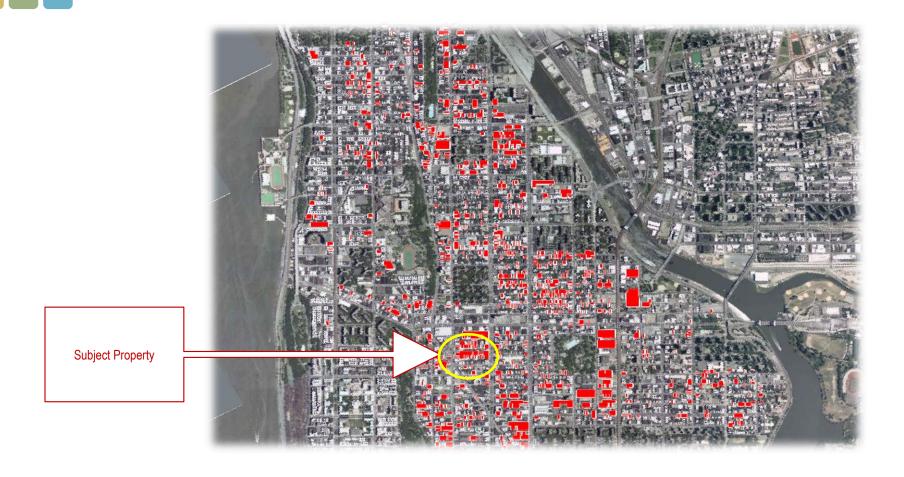
- A highly developed rental housing industry in the US
- A wide spectrum of target markets:
 - High-end luxury rentals
 - Middle class rentals
 - Low-income, subsidized rentals
 - Special needs
- Profitable to developers, property managers and lending institutions.
- Provides mobility and flexibility to the overall housing market
- Spurs the redevelopment of a blighted area.



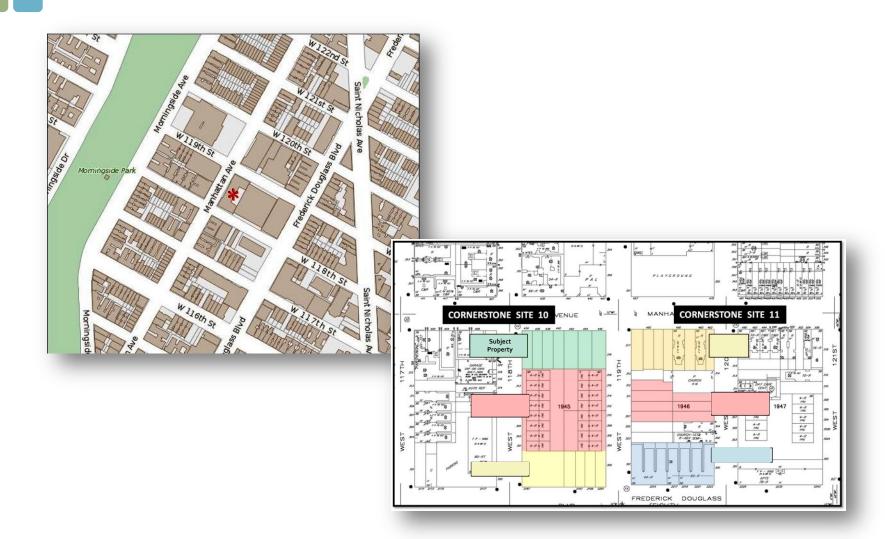
Why look at a rental project in Harlem?

- Similarities to Israel:
 - Tight housing market in New York City
 - Developers will not build rental housing on a large scale because rental levels are insufficient to support land and development costs.
 - Lots of government-owned land (formerly, anyway)
- Differences from Israel:
 - Stakeholders with extensive rental experience.
 - Government tools to make rental projects profitable to developers and lenders.

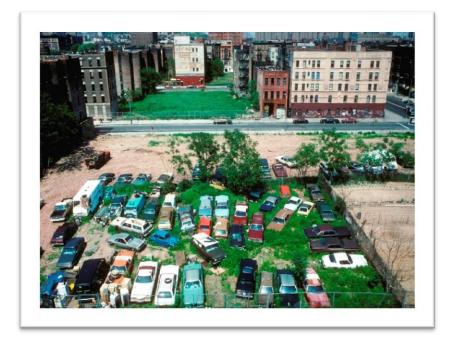
City-Owned Property in Upper Manhattan (1987)



The Location

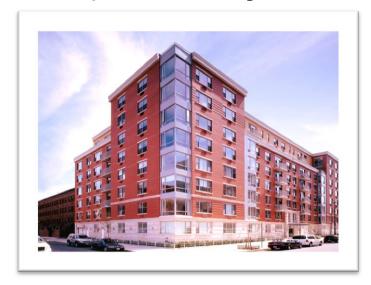


Site 10 Before and During Construction





Completed Project Photos

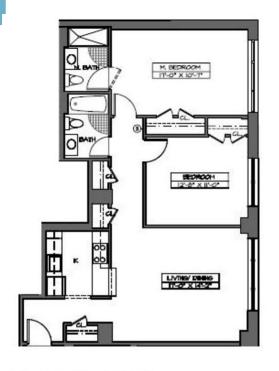






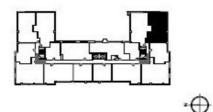


A Mixed-Income Project



APT. 2D-6D (2 BEDROOM)

1/8*=1'-0*



Units

Total Units:	122	
Market Rate Units:	10	No program requirements
Middle-Income Units:	87	@ 80% to 250% median income
Low-Income Units:	25	@ 40% and 50% median income
By Tenant Income		

By Unit Size

Total Units:	122
2 Bedroom:	72
1 Bedroom:	28
Studio:	22

		Middle				
Unit Distribution (#)	Market Rate	Income	Low Income	Super's Unit	Total	%
Studio	2	16	5	-	23	19%
1 BR	2	21	6	-	29	24%
2 BR	6	50	14	1	71	58%
Total Units	10	87	25	1	123	100%

Total "Affordable" Units

		Middle		
Rent	Market Rate	Income	Low Income	Super's Unit
Studio	\$1,350	\$1,045	\$489	
1 BR	\$1,750	\$1,395	\$529	
2 BR	\$2,400	\$1,810	\$635	\$0
Distribution by Affordability	8%	71%	20%	1%

		Middle			
Gross Rental Income	Market Rate	Income	Low Income	Super's Unit	Total
Studio	32,400	200,640	29,340	-	262,380
1 BR	42,000	351,540	38,088	-	431,628
2 BR	172,800	1,086,000	106,680	-	1,365,480
Total	247,200	1,638,180	174,108	-	2,059,488

		Monthly	Annual
Other Income	Number	Fee	Revenue
Parking Space	33	180	71,280
Laundry	123	10	14,760
(Reserved)			-
Total			86,040

Gross Annual Revenue 2,145,528

Harlem Rental Project: Development Budget

Development Budget		Total	Per Unit
Acquisition	\$13,000 per Unit	1,592,500	13,000
Hard Costs			
Construction Costs	\$160,000 per Unit	19,600,000	160,000
Construction Contingency	5% of Hard Costs	980,000	8,000
Total Hard Costs		20,580,000	168,000
Soft Costs			
Pre-Construction Fees:			
Borrower's Legal Fees		145,000	1,184
Lender's Legal Fees		45,000	367
Accounting		10,000	82
Architect Fees	\$6,400 per Unit	784,000	6,400
Bank's Engineer		15,000	122
Appraisal		7,500	61
Test Borings		18,000	147
Survey		10,000	82
Environmental Analysis		10,000	82
Consultants		75,000	612
Financing Fees:			
Bank Comittment Fees	1% of LC	136,917	1,118
Housing Agency Fee	0.75% of 1st Mortgage	128,360	1,048
Credit Enhancement Fee	1% for 30 months	427,865	3,493
Bond Issuance Fees	2% of 1st Mortgage	256,719	2,096
Tax Exemption Fee	0.40%	11,140	91
Capitalized Construction Interest		1,029,767	8,406
Interest Rate Cap	1% of 1st Mortgage	171,146	1,397
Taxes and Insurance:			
Real Estate Taxes / Water & Sewer		20,000	163
Utilities		19,200	157
Title Insurance	0.90% of 1st & 2nd Mortgages	191,832	1,566
Liability Insurance		160,000	1,306
Marketing and Lease-up		125,000	1,020
Soft Cost Subtotal		2,677,946	21,861
Soft Cost Contingency	4%	107,118	874
Total Soft Costs		2,785,064	22,735
Developer Fee	10%	2,495,756	20,374
Total Development Cost		27,453,321	224,109

Harlem Rental Project: Operating Expenses

Operating Expenses		Total	Per Unit	Per Room
Supplies		17,514	143	42
Heating		91,740	749	220
Gas & Electricity		20,850	170	50
Cooking Gas		13,230	108	32
Repairs		39,813	325	95
Legal and Accounting	_	13,843	113	33
Painting	•	16,680	136	40
Maintenance Staff Salaries		64,680	528	155
Elevator Maintenance	\$4,000 per Elevator	8,000	65	19
Management Fee	5% of EGI	101,913	832	244
Water & Sewer		52,125	426	125
Fire and Liability Insurance		61,250	500	147
Doorman / Security		103,023	841	247
Replacement Reserve		15,925	130	38
Total Expenses Before Taxes and Debt	Service	620,584	5,066	1,488
Real Estate Taxes		11,000	90	26
Building Reserve		30,750	251	74
Total Expenses After Taxes and Debt So	ervice	662,334	5,407	1,588

Harlem Rental Project: Operating Proforma

Operating Proforma		Year 1	Year 2	Year 3	Year 8	Year 9	Year 10
Revenue							
Gross Rental Revenue	2%	2,059,488	2,100,678	2,142,691	2,365,704	2,413,018	2,461,279
Other Gross Revenue	2%	86,040	87,761	89,516	98,833	100,810	102,826
Vacancy Allowance	5%	(107,276)	(109,422)	(111,610)	(123,227)	(125,691)	(128,205)
Effective Gross Income (EGI)		2,038,252	2,079,017	2,120,597	2,341,310	2,388,137	2,435,899
Operating Expenses	3%	620,584	639,202	658,378	763,240	786,137	809,721
Real Estate Taxes	2%	11,000	11,220	11,444	12,636	12,888	13,146
Building Reserve		30,750	30,750	30,750	30,750	30,750	30,750
Total Expenses		662,334	681,172	700,572	806,626	829,776	853,617
Net Operating Income		1,375,918	1,397,845	1,420,025	1,534,685	1,558,361	1,582,282
Net Available for Debt Service	115%	1,196,450	1,196,450	1,196,450	1,196,450	1,196,450	1,196,450
Net Cash Flow		179,468	201,395	223,575	338,235	361,911	385,832



Harlem Rental Project: Sources and Uses of Funds

Sources and Uses	Total	Per Unit	%
Sources			
Agency First Mortgage	17,114,616	139,711	62%
Agency Second Mortgage	4,200,000	34,286	15%
Cash Equity	6,138,705	50,112	22%
Total Sources	27,453,321	224,109	100%
Uses			
Acquisition	1,592,500	13,000	6%
Hard Costs	20,580,000	168,000	75%
Soft Costs	2,785,064	22,735	10%
Developer Fee	2,495,756	20,374	9%
Total Sources	27,453,321	224,109	100%

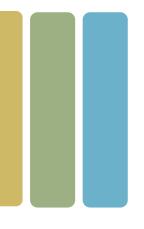
Harlem Rental Project: Developer Returns

Developer Returns		Year -1	Year 0	Year 1	Year 2	Year 3	Year 8	Year 9	Year 10
Equity		(6,138,705)							
Builder's Overhead and Profit	#######################################		1,960,000						
Developer Fee			2,495,756						
Management Fee Profit	5% of EGI			20,383	20,790	21,206	23,413	23,881	24,359
Net Cash Flow		_		179,468	201,395	223,575	338,235	361,911	385,832
Total (Pre-Tax Basis)		(6,138,705)	4,455,756	199,850	222,185	244,781	361,648	385,792	410,191
Tax Benefits from Tax Credit				230,000	230,000	230,000	230,000	230,000	230,000
Total (After Tax)		(6,138,705)	4,455,756	429,850	452,185	474,781	591,648	615,792	640,191
Cash on Cash Return (Pre-Tax	Basis)			11.87%	13.20%	14.54%	21.49%	22.92%	24.37%
IRR (Pre-Tax Basis)	6.58%								
Cash on Cash Return (After-Ta	ax Basis)			25.54%	26.87%	28.21%	35.16%	36.59%	38.04%
IRR (After-Tax Basis)	14.66%								

Summary of Subsidy from Government

- Land contributed for free (Value at Time: \$30 per developable foot)
- First mortgage debt at preferable rate and terms (Bond-Financed)
- Subordinate debt at 1% interest only. (City funds)

- After 30 years, government gets:
 - First mortgage repaid with interest
 - Second Mortgage repaid with interest
 - Community development impacts
 - Economic multipliers



Session 3:

Mechanisms to Stimulate Rental Housing Development

Sources of Debt / Equity for Rental Housing in the US

Commercial banks

Institutional investors

REITs

Bank consortia

Community development finance institutions

Municipal bonds

Governmentsponsored agencies

Developer Equity

Third-Party Private Equity

Sale of tax credits

Philanthropic grants

Public Policy Benefits of a Robust Rental Market

Serves Underserved Market Segments

- Allows adults to save money toward a purchase.
- Financial relief for parents of young married couples.
- Better permanent housing option for low-income households.

Part of a Community Development Strategy

- Enhances property values and improves quality of life.
- Diverse housing options close to job centers lowers commute times and transportation costs, reduces traffic congestion and improves air quality.

Broad Economic Stimulus

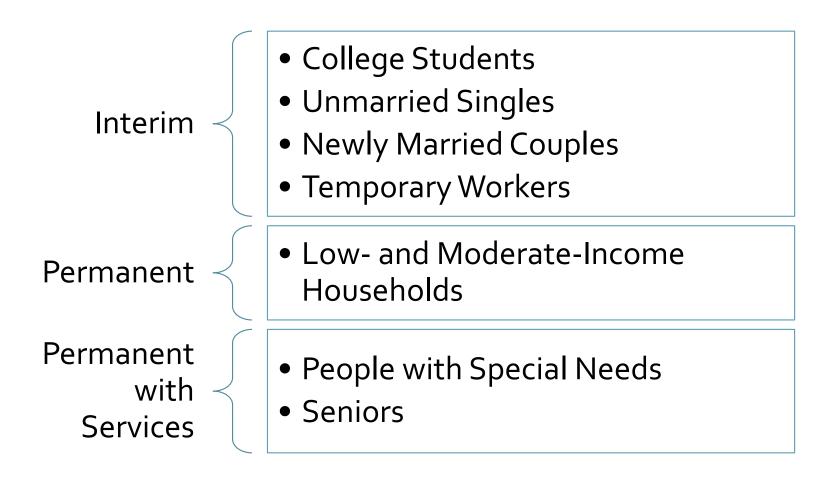
- Higher savings rates and more discretionary capital expenditures on local goods and services.
- Stimulates construction, development and property management employment.
- Countercyclical benefits of government subsidies in housing construction.

Other Public Policy Goals

- Labor mobility
- Stem brain drain
- Reduce social unrest



Close to 30% of Israeli Households Currently Live in Rental Housing





Government Incentives to Stimulate the Rental Housing Market

Reduced Land Costs

Sale or lease of Government-Owned Land

Zoning - Higher density development in exchange for affordability

Lower Capital Costs

Tax Exempt Bond Debt (Below Market Debt)

Soft Subordinate Debt from Government

Direct Capital Subsidies

Inexpensive Equity through Tax Credits

Credit Support and Insurance

Operating Support

Tax Abatements and Exemptions

Rent Subsidies for Low-Income Tenants

Multifamily Rental Development Roles and Rewards

Developers

- Develop
- Construct
- Own
- Property Management
- Asset Management

Financial Institutions

- Provide Construction Financing
- Provide Permanent Financing
- Provide Credit Enhancement / Guarantees

Government

- Impose Regulatory
 Agreements / Enforcement
 Mechanisms
- Provide Land
- Provide Capital Subsidies
- Provide Operating Subsidies
- Provide Tax Incentives

Developer Rewards

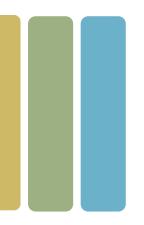
- Builder's Profit
- Developer Fees
- Management Fees
- Cash Flow
- Sale or Refinancing Proceeds

Financial Institution Rewards

- Fees
- Interest Spread
- Reputation

Government Rewards

- Achieve Housing Goals
- Catalytic investment in neighborhoods
- Long-term return on public capital
- Commercial stimulus
- Workforce retention



Session 4:

Creating a Multifamily Rental Market in Israel



Prototype Project Overview

- Location: Redevelopment Site in a City.
- Land acquired from private owner.
- Proposed project: 120 units.
- Units priced at market. At this location, market is roughly analogous to what a middle income household can afford.

120 **New Rental Units** Middle (Reserved) **Market Rate** (Reserved) Super's Unit Total Rent Income Studio \$0 \$0 \$0 \$0 \$0 0% 1 BR \$0 \$800 \$0 \$0 \$0 **62**% 2 BR \$0 \$1,000 \$0 \$0 \$0 35% 3 BR \$0 \$0 \$1,200 \$0 \$0 3% Distribution by Affordability 0% 100% 0% 0% 1% 100%

		Middle		Very Low		
Unit Distribution (#)	Market Rate	Income	Low Income	Income	Super's Unit	Total
Studio	-	-	-	-	-	-
1 BR	-	74	-	-	-	74
2 BR	-	42	-	-	1	42
3 BR	-	4	-	-	-	4
Total Units	-	120	-	-	1	120

		Middle		Very Low		
Gross Rental Income	Market Rate	Income	Low Income	Income	Super's Unit	Total
Studio	-	-	-	-	-	-
1 BR	-	710,400	-	-	-	710,400
2 BR	-	504,000	-	-	-	504,000
3 BR	-	57,600	-	-	1	57,601
Total	- '	1,272,000	-	-	-	1,272,001

		Monthly	Annual
Other Income	Number	Fee	Revenue
Parking Space	0	0	-
Laundry	120	10	14,400
(Reserved)			-
Total		<u> </u>	14,400

Gross Annual Revenue 1,286,401



Prototype Project: Development Budget

Average Apartment Size	80	square meters
Acquisition Price	\$800	per meter

Development Budget		Total	Per Unit
Acquisition	\$65,000	\$7,800,000	\$65,000
Hard Costs			
Construction Costs	\$135,000 per Unit	\$16,200,000	\$135,000
Construction Contingency	5% of Hard Costs	\$810,000	\$6,750
Total Hard Costs		\$17,010,000	\$141,750
Soft Costs			
	200/ - []	ĆE 402 000	Ć42 F2F
Soft Cost Subtotal	30% of Hard Costs	\$5,103,000	\$42,525
Soft Cost Contingency	5%	\$255,150	\$2,126
Total Soft Costs		\$5,358,150	\$44,651
Developer Fee	0%	\$0 [*]	\$0
Total Development Cost		\$30,168,150	\$251,401

Prototype Project: Operating Expenses

Operating Expenses		Total	Per Unit	Per Room
Supplies		19,700	164	50
Heating and Electricity (Paid by Tenant))	-	-	-
Electricity (Common Areas)		7,880	66	20
Cooking Gas (Paid by Tenant)		-	-	-
Repairs		18,000	150	46
Legal and Accounting	_	12,000	100	30
Painting (Common Areas)	*	11,820	99	30
Maintenance Staff Salaries		12,000	100	30
Elevator Maintenance	\$2,500 per Elevator	5,000	42	13
Management Fee	3% of EGI	36,662	306	93
Fire and Liability Insurance		24,000	200	61
Doorman		-	-	-
Replacement Reserve		30,000	250	76
Total Expenses Before Taxes and Debt	177,062	1,476	449	
Real Estate Taxes (Paid by Tenants)		-	-	-
Total Expenses After Taxes and Debt Se	ervice	177,062	1,476	449

Prototype Project: Operating Proforma

Operating Proforma		Year 1	Year 2	Year 3	Year 8	Year 9	Year 10
Revenue							
Gross Rental Revenue	2%	1,272,001	1,297,441	1,323,390	1,461,129	1,490,352	1,520,159
Other Gross Revenue	2%	14,400	14,688	14,982	16,541	16,872	17,209
Vacancy Allowance	5%	(64,320)	(65,606)	(66,919)	(73,884)	(75,361)	(76,868)
Effective Gross Income (EGI)		1,222,081	1,246,523	1,271,453	1,403,787	1,431,863	1,460,500
Operating Expenses	3%	177,062	182,374	187,846	217,764	224,297	231,026
Real Estate Taxes	2%	-	-	-	-	-	-
Total Expenses		177,062	182,374	187,846	217,764	224,297	231,026
Net Operating Income		1,045,019	1,064,148	1,083,607	1,186,022	1,207,565	1,229,474
First Mortgage Debt Service *	120%	870,849	870,849	870,849	870,849	870,849	870,849
Net Cash Flow	<u> </u>	174,170	193,299	212,759	315,174	336,716	358,625

^{* 20} yr, 5% Debt Constant

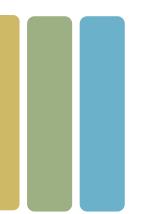
Prototype Project: Developer Returns

Developer Returns		Year -1	Year 0	Year 1	Year 2	Year 3	Year 8	Year 9	Year 10
Equity		(19,315,449)							
Builder's Profit and Overhead	10% of Hard Costs		1,620,000						
Management Fee Profit	3% of EGI			7,332	7,479	7,629	8,423	8,591	8,763
Net Cash Flow				174,170	193,299	212,759	315,174	336,716	358,625
Total		(19,315,449)	1,620,000	181,502	200,779	220,387	323,596	345,308	367,388
Cash on Cash Return				1.0%	1.1%	1.2%	1.8%	2.0%	2.1%
IRR	-20.71%								

Prototype Project: Sources and Uses

Israel Project	Total	Per Unit	%
Sources			
First Mortgage	10,852,701	90,439	36%
Second Mortgage	-	-	0%
Cash Equity	19,315,449	160,962	64%
Total Sources	30,168,150	251,401	100%
Uses			
Acquisition	7,800,000	65,000	26%
Hard Costs	17,010,000	141,750	56%
Soft Costs	5,358,150	44,651	18%
Developer Fee	-	-	0%
Total Uses	30,168,150	251,401	100%
IRR	-20.71%		
Cash on Cash Return	1.03%		

Harlem Project	Total	Per Unit	%
Sources			
Agency First Mortgage	17,111,138	139,683	62%
Agency Second Mortgage	4,200,000	34,286	15%
Cash Equity	6,141,675	50,136	22%
Total Sources	27,452,813	224,105	100%
Uses			
Acquisition	1,592,500	13,000	6%
Hard Costs	20,580,000	168,000	75%
Soft Costs	2,784,603	22,731	10%
Developer Fee	2,495,710	20,373	9%
Total Sources	27,452,813	224,105	100%
IRR	6.58%		
Cash on Cash Return	11.87%		



Session 5:

Bridging the Gap



How to Fill the Gap?

- Reduce the Cost of Land
- Modify the Capital Structure of First Mortgage Debt
 - Cost
 - Duration
 - Loan to Value
- Provide Subordinate Debt

Israel Bond Concept

Expand State of Israel Bond Program

Create an 'Affordable Housing Fund'

Provide the necessary 'gap' financing.

Provide subordinate capital and/or loan guarantees equal to 25% -35% of total development costs.

A \$200 million Fund could stimulate the development of 3,000 – 4,000 units of affordable rental housing.

Israel Bonds Timeline

1950 - 1951 1966 1980 1980 - 1993 - 1992 2012:

- The inaugural issue exceeded \$52 million.
- Funded immigrant absorption and infrastructure.
- Secondary Engage Diaspora Jewry.
- Expanded bond sales to 35% of Israel's special development budget.
- Proceeds funded industrial and agricultural projects.

- Bond sales continued to increase
- Six-Day War, bond sales > \$250 million
- Yom Kippur War, bond sales > \$500 million.
- Major source of external net borrowings by Israel.
- During the Persian Gulf War, bond sales > \$1 billion threshold.

• Annual bond

sales exceeded

\$1 billion.Viewed as a true financial

investment

 Increased bond sales to pension funds.



Development Corporation for Israel

- "Israel Bonds" is the generic name of Development Corporation for Israel (DCI).
- DCI is a registered broker-dealer.
- Israel Bonds are sold in the United States as well as in Canada, Latin America and Europe
- On October 31, 2011, Izzy (Israel) Tapoohi became president and CEO of DCI/Israel Bonds.

Other Terms

Rates

- Rates change two times per month based on prevailing Treasury bond-rates, plus a spread.
- Rates for floating rate bonds are equal to the 6month LIBOR rate.

Default and Transferability

- Israel has never defaulted in the payment of principal or interest
- The bonds are not freely transferable.

Investment Rating

- Israel bonds are not formally rated but several rating international rating agencies have assigned investment grade ratings.
- Standard & Poor's: A/A
- Moody's Investors
 Service : A1
- Fitch Ratings: 'A,'



Who Invests in Israel Bonds?

- Members of the diaspora Jewish community who wanted to help Israel.
- The investor base became increasingly widespread.
- Investment that both helps Israel and is a useful means of portfolio diversification.
- Investors include more than 1,700 labor unions, over 1,800 foundations, and numerous government, financial institutions and private investors.

How are Israel Bonds Used?

- Capital designated by Israel's Finance Ministry for economic development projects:
 - The National Water Carrier
 - The Dead Sea Works
 - Port development and expansion in Ashdod, Haifa, and Eilat
 - The Hadera power plant
 - Ben-Gurion Airport expansion;
 - Extending Israel's rail network;
 - Improving the national highway system; and
 - Desalination plants.
- Israel bonds expected to help fund development of the Negev desert, and industrial parks in the Galilee.



Establishment of a Public/Private Lending Institution

- In cooperation with the Finance Ministry and Israeli private sector lending institutions, we proposed to capitalize a new public/private lending entity.
- Bond proceeds and private financing will be used to underwrite and lend needed funds into affordable rental housing production.
- Philanthropic funds could be used to help capitalize the establishment of such an entity.
- Deploy this public/private lending partnership to 'jumpstart' a rental housing industry by 'proving the market' through the development of pilot projects.



Possible Lending Institution Models

Within Government

A specialized government entity tasked with coordinating public and private resources to develop, regulate and maintain affordable housing

NGO

A nongovernment organization that serves in an intermediary role between government and the private sector in assembling financing and provides technical assistance to affordable housing developers.

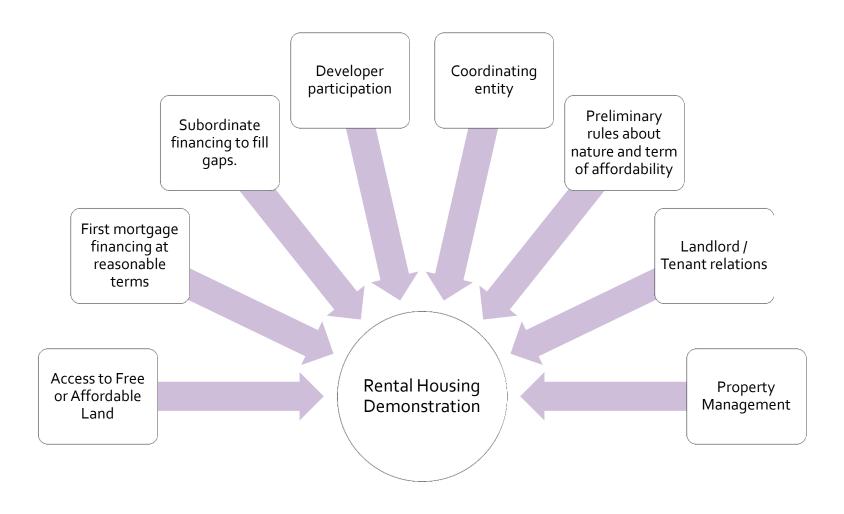
Lender Consortium Model

Consortium of banks with the technical expertise to underwrite affordable housing transactions.
Coordinates the assembly of resources and provides technical assistance to developers.

Private Model

Lending
institutions create
a special
affordable
housing finance
office with
specialized
expertise to
underwrite and
service affordable
housing loans.

Elements for a Rental Housing Demonstration Project



Initial Activities Underway



• Introduce concept with key North American leaders and representatives involved in the sales and marketing of State of Israel Bonds.

Prepare Financial Models to Identify Gaps • Use actual pipeline deals

• Determine optimum mix of financing resources needed to jumpstart a self-sustaining finance system.

Explore Creation of a Public/Private Lending Institution

- Determine the feasibility and organizational structure for creating institution.
- The institution would leverages both Israel Bonds and private financing to underwrite this 'first generation' of affordable rental housing in the State of Israel
- Over time, the institution would develop and implement a range of financing tools and programs that would substantially expand the development of quality affordable housing opportunities across Israel.

Explore Establishment of a Demonstration Program Meet with key representatives from Israeli private financing institutions, Israel Finance Ministry, and other relevant government and non-governmental institutions to determine the feasibility of establishing a 'Demonstration Program' financed by this public/private partnership.