KT URBAN

March 28, 2019

Jacky Morales-Ferrand
Director, Housing Department
City of San Jose
200 E Santa Clara Street
San Jose, CA 95113

Dear Jacky,

I am currently the CFO for KT Urban. I have been a Chief Financial Officer for the past 16 years for several real estate companies including a publicly traded company (NYSE: UCP) based in San Jose, which completed an IPO in 2013 and raised approximately $200 MM in construction financing, as well as over $275 MM of other debt and equity proceeds in the capital markets. Prior to my experience in the real estate industry, I spent many years working at international banks such as BNP and Deutsche Bank that provided various forms of financing for several technology companies here in the Bay Area (Sun Microsystems, 3Com, Informix, Sybase) totaling some $2 billion.

I understand that you are considering matters pertaining to the City San Jose's Ellis Act Ordinance and its re-control provisions impact on the ability of projects to obtain equity and construction financing in the capital markets. I would like to, respectfully, offer a few observations for your consideration:

1. ***Rent controlled projects increase risk*** as rent controlled projects recover more slowly from market downturns. In Table 1 of the David Paul Rosen & Associates report, the market rents for that sampling of projects declined 8.7% in 2009 and it took over 2 years for the market to recover. If a 5% rent cap were in place, it would have taken the markets rents nearly 4 years to recover. The capital markets (institutional investors and the debt market) study long term cycles carefully and the reduced ability to recover from inevitable market downturns increases risk. Projects with higher risk require higher returns which, in turn, reduces the number of viable projects and investors while at the same time increasing the need for equity investment as higher risk projects are not able to borrow as much.

2. ***Rent controlled projects are less valuable***, of course, because of reduced revenue and cash flow. Again, using the Dave Paul Rosen data and applying the 5% cap, the 11-year average annual rent growth would have been less than 2.5%. Separate but in addition to the risk issue discussed above, less valuable projects attract fewer investors and require

more equity as the borrowing capacity of the project is reduced. If we factor in reduced annual growth rate and the increased risk and apply this data to a large multifamily project we are currently working on located in San Jose, we estimate the pretax profit of the project would be reduced by approximately $50 MM.

3. From a capital markets standpoint, ***addressing the housing crisis in the Bay Area requires large scale institutional investors and debt***. For the reasons cited above, institutional investors will shy away from and in some cases be precluded, as a matter of policy, from investing projects that have rent control or other limitations.

4. Over $30 billion was invested in US in value-add multifamily projects in 2018. In this category of investment ***private equity and debt funds specifically target under-utilized, neglected or under-performing urban, infill properties with the primary goal of redeveloping the property at higher densities and increasing rents at above market rates***. By definition, this type of significant investment, while usually being welcomed in the community, would be significantly diminished under the proposed Ellis Act ordinance.

5. ***It is widely understood by economists that rent control often results in having the opposite effect than intended***. In a recent study from Stanford University on this topic, which I am sure you are aware, the authors concluded that rent control reduces housing supply and drives up rent.

Having lived my whole life in the Bay Area, most of which living or working in Santa Clara Valley, I am very excited to see the development of Downtown San Jose over the past 10+ years. Downtown San Jose is emerging as the social and cultural hub of Silicon Valley. Very significant large-scale investment seems to be on the near-term horizon, but the Ellis Act's re-control provision will discourage investment activity. I am very hopeful that the City of San Jose will continue to work hard to encourage this continued investment.

Sincerely,

William J. La Herran
Chief Financial Officer
KT Urban