TEAM 12

QUARTET

LAND DEVELOPMENT

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REPORT HIGHLIGHTS

- **Recommendation:**
  - Continue land development business in Calgary
  - Partner with non local developer to raise equity funding
- Market expansion is too risky given management preferences and unfamiliarity with the market

GUIDING PRINCIPLES

- Market Fundamentals
- Risk Appetite of Management
- Management Expertise
- Strategic Direction

ALTERNATIVE 1 - STATUS QUO

- What? Sit on the sidelines
- Pros:
  - Aligns with shareholders low appetite for risk and future objectives
  - Allows Quartet to focus on core competency as a home builder
- Cons:
  - Current business model is not sustainable
  - Significant economic volatility in Calgary could cause land prices to spike when oil prices recover
  - Quartet’s existing land supply to be completely used in the next four years

ALTERNATIVE 2 - MARKET EXPANSION

- What? Expansion to Edmonton
- Results: Unlevered IRR: 12.1% Levered IRR 27.2%
- Pros:
  - Market fundamentals (i.e. employment and population growth) support demand for housing
  - Less competition
- Cons:
  - Lack of expertise in the local market
  - Lack of relationships with local regulatory bodies
  - Extra time commitment from management
  - Limited relationships with local trades

ALTERNATIVE 3 - CALGARY EXPANSION

- What? Land acquisition in Calgary
- Results: Unlevered IRR: 10.8% Levered IRR 26.4%
- Pros:
  - Long term demand for single family housing is strong
  - Tight land supply will continue to drive up prices
  - Local developers are seen more favourably by planning bodies and regulatory agencies
  - Can leverage local expertise and reputation
- Cons:
  - Market fundamentals may weaken in the near term due to economic uncertainty
  - Highly cyclical economic drivers (ie. commodities) increases volatility in the housing market
  - Proposed capital structure at 80% leverage may not be optimal given current debt ratio

FINANCIAL ANALYSIS

		Construction Phase							
		0	1	2	3	4	5	6	7
Land	$70,000,000	$70,000,000							
General	$44,000,000		$7,333,333	$7,333,333	$7,333,333	$7,333,333	$7,333,333	$7,333,333	
Servicing	$144,000,000		$24,000,000	$24,000,000	$24,000,000	$24,000,000	$24,000,000	$24,000,000	
Project Management	$16,000,000		$2,666,667	$2,666,667	$2,666,667	$2,666,667	$2,666,667	$2,666,667	
Marketing	$3,000,000		$-	$-	$-	$-	$1,500,000	$1,500,000	
DEVELOPMENT COST	$277,000,000	$70,000,000	$34,000,000	$34,000,000	$34,000,000	$34,000,000	$35,500,000	$35,500,000	$-
Sales Proceeds									$444,000,000
PROJECT CASH FLOW		$(70,000,000)	$(34,000,000)	$(34,000,000)	$(34,000,000)	$(34,000,000)	$(35,500,000)	$(35,500,000)	$444,000,000
Project IRR (unlevered)	10.8%								
Financing (Interest)	$8,000,000		$1,333,333	$1,333,333	$1,333,333	$1,333,333	$1,333,333	$1,333,333	
Equity	$45,000,000	$(45,000,000)							$212,000,000
PROJECT CASH FLOW		$(45,000,000)	$1,333,333	$1,333,333	$1,333,333	$1,333,333	$1,333,333	$1,333,333	$212,000,000
Levered IRR	26.4%								

Sensitivity	LOW: Number of Units	MID: Number of Units	HIGH: Number of Units
Single	1,320	600	600
Small	-	1,100	825
Stacked	600	1,000	1,500
Project IRR	**3.8%**	**10.8%**	**13.2%**
Levered IRR	**13.4%**	**26.4%**	**30.0%**

CAPITAL STRUCTURE

- Pros
  - Magnified IRR with increased leverage
  - Flexibility to diversify equity in other investments
  - Equity partners builds relationships and distributes risk
- Cons
  - Increased volatility with more leverage
  - Increased overall risk to the business

RECOMMENDATION

Land Acquisition in Calgary

- Partner with non local Developer to raise equity funding (Ie. McKee, Carlisle Group, ReidBuilt Homes)
- Remaining capital sourced from institutional investor
- Continue land development as an integrated firm is best in current market
- Market fundamentals anticipated to be strong
- Agreement with management objectives

IMPLEMENTATION

- Immediately
  - Due Diligence on Calgary acquisition
  - Source equity partner and institutional investor
- Year 1-5
  - Service land and prepare for lot sales to integrated builder
- Year 5+
  - Reassess Calgary market and available supply and demand, while considering changing management preferences