1. Conditions

The assessment of credit quality (risk assessment) for a project begins with a macroeconomic evaluation (the industry that it is in) and then assess the local market of the business, i.e. local market demand. Understanding economic Conditions are critical in determining the viability of a project. This is because economic conditions affect different industries – differently. For example, the Homebuilding Industry was severely and negatively impacted during the recent recession. Conversely, the Pharmaceutical Industry was only slightly impacted.

Understanding the industry that a project is in is a very important factor in assessing overall project risk. Below is an industry risk assessment table that was created using generally accepted U.S. Rating Agency industry data. It shows how the state of the economy impacts different industries.

Many of the business in the highly affected and moderately affected industries noted to the right have seen significant contraction during the current recession. That has further impacted the broad economy as their declining need for office space, equipment and services which in turn has affected other businesses.

<table>
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<tr>
<th>How Industries are Affected by Economic Change</th>
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<td><strong>HIGHLY</strong></td>
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<td>Technology</td>
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<td>Broadcast &amp; Pub.</td>
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<td><strong>SLIGHTLY</strong></td>
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<td>Branded Consumer Products</td>
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Let’s look at the Health Care Industry as an example, because it’s an industry that most would agree is in a growth mode. It’s generally agreed that the need for drugs, medical devices, health-care facilities, etc. will grow, based upon predictable population growth. While the industry might be strong, there are local markets that have declining populations or an abundance of health care facilities. As a result, the prudent EB-5 investor will need to not only assess the broad industry but also the local market demand for a facility or business.

For example, assessing the local market opportunity for a new Assisted Living Facility (“ALF”) is fairly straightforward. If the occupancy of the competing facilities is above 93%, then the market need for a new ALF is considered - strong. Conversely, assessing the market opportunity for a new manufactured product or technology is much more challenging, even if it is in a growth industry. However (there is always a “however” in Credit Analysis), a financier needs to also assess the possibility of the local market...
becoming overbuilt. This happened in many local markets with health care facilities.

There is an old saying, “a rising tide lifts all boats”. Therefore, a project in a stable or growth industry with strong and verifiable local market demand can truly benefit from the “rising tide.”

**Lender’s Commentary:** As a commercial real estate lender for over 20 years and having financed over $5 billion (USD), we do not consider funding the new construction of a project without first evaluating a third party market study that would assess the demand of all competing projects. In the case of health care – possibly a nursing facility, we will need to see a market study that compares the new project against the local competing facilities. If the local market shows that the average occupancy of the competing facilities is less than 93%, then we will not fund the project, because of a possible risk of failure. Building the project and creating an oversupply in a market will usually result in price erosion, negatively affecting revenues and profitability.

However, if all the competing facilities are old and “tired”, we might consider financing the project with the expectation of attracting occupants of the “tired & older” facilities. This decision starts the subjective underwriting assessment and considers all the factors of the project. All financiers (and EB-5 investors too) need to know that there is a strong market demand for a project. That should be based upon a solid third party market study.

Additionally, we look carefully at the source of the business’s revenues. If the revenues are from a governmental agency that has promised payments on some measurable criteria, then the risk assessment of the business achieving its revenue objectives can be much clearer. If the business has to go out and create its customer base from scratch, that’s an entirely different matter. As a result, Publicly Funded - Privately Managed businesses can show a much more predictable revenue stream than Privately Funded – Privately Managed businesses.

**EB-5 Investor guidance:** Be sure to evaluate the future economic trends for the industry and the immediate local market demand for the EB-5 project. You should understand the current need for the project because that will likely affect the projects short term success and directly impact the job creation timeframe. Further, evaluate future industry trends to help you assess whether it’s likely that you will be able to get your EB-5 investment back in the timeframe that you expect.

**Bottom line:** the EB-5 investor should carefully review the market study and appraisal for the project - prior to making a final investment determination.