

T00A99
Maryland Economic Development Corporation

Executive Summary

The Maryland Economic Development Corporation (MEDCO) is an instrumentality of the State of Maryland created to serve as a statewide economic development engine. MEDCO has real estate development capabilities and bond issuance powers.

Financial Statement Data

Maryland Economic Development Corporation Financial Statement
Fiscal 2018-2020
(\$ in Thousands)

	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>Change</u> <u>2019-2020</u>
Total Assets	\$533,089	\$539,020	\$596,701	\$57,681
Total Liabilities	771,939	808,900	898,097	89,197
Net Assets (Deficit)	-\$238,849	-\$269,880	-\$301,396	-\$31,516
Operating Revenues				
Operating Facilities	\$133,844	\$139,830	\$112,632	-\$27,198
Other	3,990	2,262	2,558	296
Total Operating Revenues	\$137,833	\$142,091	\$115,189	-\$26,902
Operating Expenses				
Operating Facilities	\$90,463	\$96,866	\$84,217	-\$12,649
Depreciation/Amortization	29,769	30,824	26,215	-4,609
Administrative and Other	2,030	2,097	2,227	130
Total Operating Expenses	\$122,262	\$129,787	\$112,659	-\$17,128
Net Operating Income	\$15,571	\$12,304	\$2,530	-\$9,774
Net Non-operating Income	-\$29,326	-\$43,335	-\$34,046	\$9,289
Change in Net Position	-\$13,756	-\$31,031	-\$31,516	-\$485
Net Position, Beginning of Year	-225,094	-238,849	-269,880	-31,031
Net Position, End of Year	-\$238,849	-\$269,880	-\$301,396	-\$31,516

Note: Numbers may not sum due to rounding.

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Analysis of the FY 2022 Maryland Executive Budget, 2021

Key Observations

- MEDCO’s income from operating projects (\$115.2 million) continued to exceed expenses (\$112.7 million) in fiscal 2020, although by a smaller margin than in past years.
- Many of MEDCO’s student housing projects experienced revenue reductions as universities transitioned to delivering a majority of their courses remotely during the COVID-19 pandemic. MEDCO reached agreements with several of the institutions to release students from their leases or licensing agreements upon request and provide credits for future semesters.
- The Chesapeake Bay Conference Center remains a nonperforming project and suffered further setbacks due to pandemic-related closures and capacity limits. The Baltimore City Garages project operated by MEDCO was placed in “watch” status in August 2020, and two of MEDCO’s conduit projects are also in “watch” status.

Operating Budget Recommended Actions

1. Nonbudgeted.

T00A99
Maryland Economic Development Corporation

Operating Budget Analysis

Program Description

The Maryland Economic Development Corporation (MEDCO) is a nonbudgeted entity that allows the State to own or develop property for economic development purposes. MEDCO was created in 1984 with the mission to help expand, modernize, and retain existing Maryland businesses and to attract new businesses to the State. The stated legislative purpose of the corporation is to (1) relieve the conditions of unemployment; (2) encourage increased business activity and commerce and a balanced economy; (3) assist in the retention and attraction of new business activity; (4) promote economic development; and (5) generally promote the present and prospective health, happiness, safety, right of employment, and general welfare of State residents.

MEDCO purchases or develops property that is leased to others under favorable terms. MEDCO also makes direct loans to companies throughout the State to maintain or develop facilities, and it often serves as the conduit for loans administered by the Department of Commerce (Commerce). MEDCO issues bonds to raise funds for its loans. The bond debt consists primarily of revenue bonds and notes payable to government agencies, such as Commerce. The debt represents nonrecourse obligations because MEDCO is not liable to bondholders and lenders in the event of a project or borrower default. Each project must have self-supporting revenues, and no projects are cross-collateralized. As a result, MEDCO's debt is not debt of the State, and there is no implied State guaranty or State obligation to protect bondholders from losses.

MEDCO has been involved in 317 projects through fiscal 2020. Of these, MEDCO currently owns and operates 15 as operating facilities, meaning that the corporation is involved in management decisions and has a hand in ensuring successful daily operations. For most other projects, MEDCO generally serves as an arms-length financing entity.

The corporation is governed by statute under Sections 10-101 through 10-132 of the Economic Development Article. A 12-member board of directors oversees and approves actions pertaining to the corporation's affairs and appoints the executive director. The Secretary of Commerce and the Secretary of Transportation serve as *ex-officio* voting members. MEDCO's activities complement the marketing and financing programs of Commerce. MEDCO currently has 11 full-time employees.

Overall Financial Position

Operating Revenues Continue to Exceed Operating Expenses but with Smaller Margin

MEDCO operated 15 facilities in fiscal 2020, and the revenues from those facilities contribute to the corporation's bottom line. In fiscal 2020, operating revenues (\$115.2 million) decreased by 19%

T00A99 – Maryland Economic Development Corporation

from fiscal 2019 but continued to exceed operating expenses (\$112.7 million). However, the corporation experienced a net income deficit, and as such, the corporation's equity position declined. With the exception of fiscal 2017 when MEDCO sold a property, this has been the case for at least the last decade of operations. Noncash expenses, such as depreciation, and non-operating items, such as interest expense, cause the net income and net asset deficits.

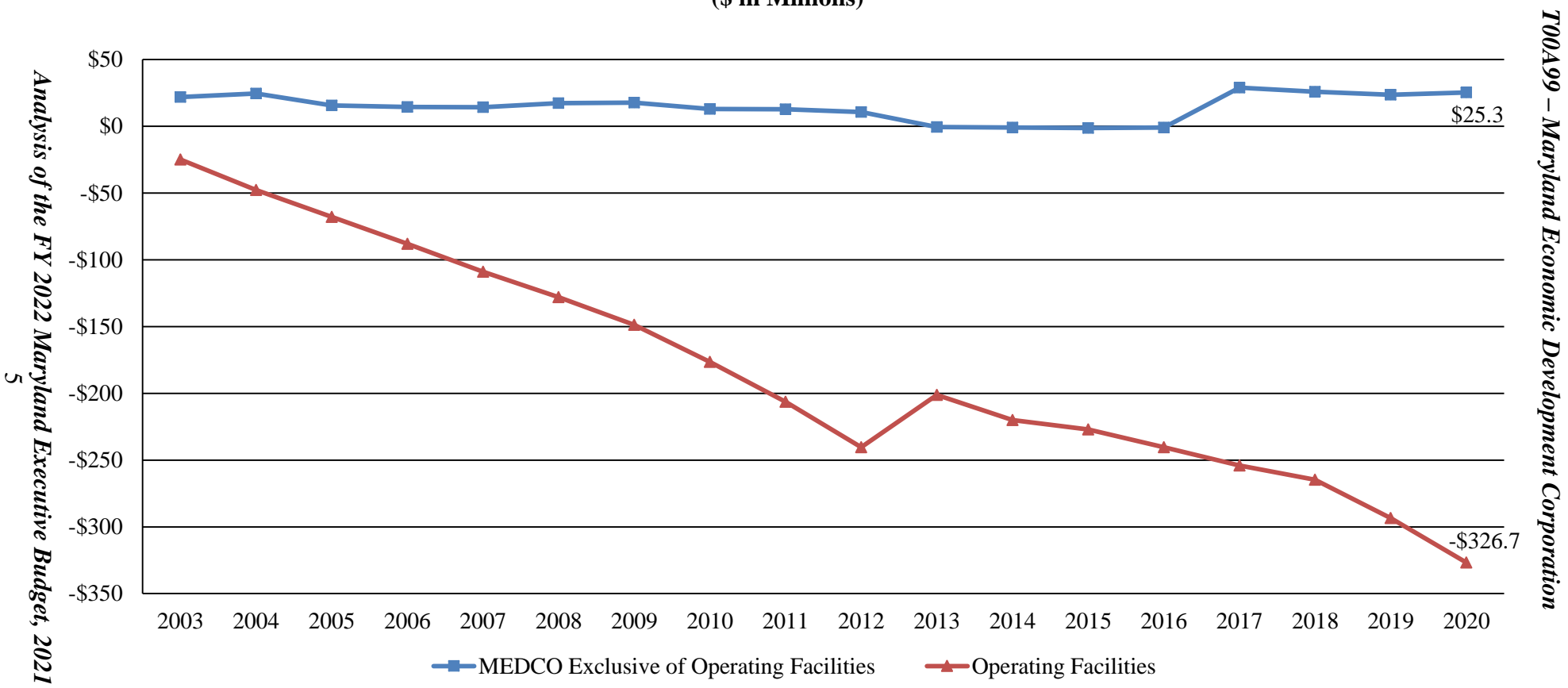
The corporation reports that a growing net asset deficit is not a significant concern as long as operating revenues exceed cash operating expenses. MEDCO notes that net losses and net asset deficits are not uncommon for real estate companies. With these companies, the market value of the assets generally exceeds the book value, and MEDCO reports that real estate investors look at market value or, more specifically, cash flow coverage rather than book value. Accordingly, the MEDCO operating position (operating revenues exceeding expenses) continues to be positive, although by a significantly smaller margin than in previous years: net operating income for fiscal 2020 totaled only \$2.5 million compared to \$12.3 million in fiscal 2019 and \$15.6 million in fiscal 2018.

MEDCO added a student housing project at Bowie State University (BSU) in fiscal 2020, bringing the number of student housing projects operated by MEDCO to 11. MEDCO refers to this new project as the Bowie Mixed Use project, and the project is in addition to the Christa McAuliffe Student Housing project that MEDCO has operated at BSU since 2004. The new project will include approximately 557 beds as well as retail space, classrooms, and an entrepreneurship center. Construction began in February 2020 and is expected to be completed in summer 2021 with a planned opening for the fall 2021 semester.

MEDCO Net Assets in a Negative Position

Historically, MEDCO has been involved in two types of projects: (1) operating projects – where MEDCO is involved in management decisions and has a hand in ensuring successful daily operations; and (2) conduit projects – where MEDCO generally serves only as an arms-length financing entity. **Exhibit 1** shows both the net assets of MEDCO facilities that it operates and those facilities it does not operate. The net assets are comprised primarily of the value of the properties offset by outstanding debt or capital lease obligations. The large negative net assets of the operating projects are due to the cumulative effect of year-over-year income deficits.

Exhibit 1
MEDCO Net Assets, Operating and Non-operating
Fiscal 2003-2020
(\$ in Millions)



Analysis of the FY 2022 Maryland Executive Budget, 2021

T00A99 – Maryland Economic Development Corporation

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

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The net asset deficit began to grow dramatically in fiscal 2003 when MEDCO greatly expanded its operating facility portfolio, including the Chesapeake Bay Conference Center (CBCC) and several university housing projects. The net asset deficit is largely the result of adding new operating real estate projects. MEDCO operating projects often have net income deficits as explained above; with the addition of each project, a net income deficit is added to the accounts, which in turn adds to the overall net asset deficit. Conversely, the removal of an operating project (Rocky Gap in fiscal 2013) improves the net asset deficit position. The removal of the National Cybersecurity Center of Excellence in fiscal 2019, however, added to the overall deficit due to the project's positive net assets prior to its disposition.

MEDCO's involvement in conduit projects, which it does not operate, also impacts the corporation's position as facilities are added to the portfolio or debt is retired. The corporation sold the Human Genome Sciences building in fiscal 2017 that resulted in a noncash gain in net assets of \$28.3 million. The recognized gain is the result of the early debt retirement offset by the depreciated book value of the property. Primarily due to that sale, MEDCO remained in a positive net position (\$25.3 million) exclusive of operating facilities in fiscal 2020.

Operating Facilities Financial Position

Net Assets Weighed Down by CBCC

Exhibit 2 shows the increases and decreases in MEDCO net assets by project. Operating facilities' net assets decreased by \$33.2 million in fiscal 2020. As discussed earlier, the decline is not uncommon. This is primarily due to a decline of \$22.2 million at CBCC, discussed further in the analysis. MEDCO disposed of the National Cybersecurity Center of Excellence and the Rockville Innovation Center projects in fiscal 2019.

Exhibit 2
MEDCO Increase/Decrease in Net Assets by Project
Fiscal 2018-2020

University Student Housing	<u>2018</u>	<u>2019</u>	<u>2020</u>	Total Net Assets (Deficit) at End of 2020
Morgan State University	-\$150,755	\$223,025	\$487,218	-\$6,360,620
Bowie State University	224,630	101,485	321,716	-3,698,635
Bowie Mixed Use Project	n/a	n/a	-1,051,721	-1,051,721
Frostburg State University	259,619	29,994	303,797	-3,398,405
Salisbury University	416,773	824,614	1,033,343	-1,263,269
Towson University	-2,038,270	104,130	-383,956	-7,336,625
Capitol Technology University	2,715,688	158,898	-279,793	2,594,793
University of Maryland, Baltimore Campus	178,834	338,938	-88,600	-10,825,914
University of Maryland Baltimore County	784,125	1,012,443	-81,360	200,671
University of Maryland, College Park Campus Housing	1,869,503	741,681	-1,232,181	-28,211,518
University Village at Sheppard Pratt	464,040	177,206	-875,474	-9,949,757
Subtotal	\$4,724,187	\$3,712,414	-\$1,847,011	-\$69,301,000
Other Facilities				
Chesapeake Bay Conference Center (Hyatt Cambridge)	-\$15,588,241	-\$15,853,598	-\$22,176,174	-\$247,498,793
National Cybersecurity Center of Excellence	-469,005	-14,268,597	n/a	n/a
Rockville Innovation Center	-508,787	2,033,960	n/a	n/a
Metro Centre	-669,142	-584,291	-504,458	-7,254,820
University of Maryland, College Park Campus Energy	1,920,617	-2,711,654	-8,152,549	15,633
Baltimore City Garages	n/a	-1,386,848	-515,175	-1,902,023
Subtotal	-\$15,314,558	-\$32,771,028	-\$31,348,356	-\$256,640,003
Subtotal Operating Facilities	-\$10,590,371	-\$29,058,614	-\$33,195,367	-\$325,941,003
MEDCO Exclusive of Operating Facilities	-\$3,022,934	-\$2,280,354	\$1,742,525	\$25,345,975
Elimination (Accounting Adjustment)	-\$142,238	\$307,816	-\$63,329	-\$801,417
Grand Total	-\$13,755,543	-\$31,031,152	-\$31,516,171	-\$301,396,445

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

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MEDCO has explained that it is not unusual for its real estate projects to show deficits, and it cautions that in the case of university housing, deficits are essentially guaranteed. There is a provision in the bond issuances that specifies that excess cash goes back to the university as additional rent or a ground lease rather than into the projects' equity. MEDCO reports that university housing bond issuances are usually structured this way.

Operating Facilities' Net Income Decreased Significantly Due to Pandemic

Exhibit 3 shows MEDCO operating income and loss by MEDCO-operated projects. This data indicates where projects are bringing in enough revenues to cover annual operating expenses. Operating facilities' net income decreased significantly to \$1.0 million in fiscal 2020 compared to \$11.5 million in fiscal 2019. Three projects posted losses in fiscal 2020.

Exhibit 3
MEDCO Operating Income/Loss by Project
Fiscal 2018-2020

University Student Housing	<u>2018</u>	<u>2019</u>	<u>2020</u>
Morgan State University	\$1,093,107	\$1,303,066	\$1,600,000
Bowie State University	883,617	748,576	903,521
Frostburg State University	840,273	585,000	808,431
Salisbury University	1,232,414	1,574,430	1,738,173
Towson University	2,556,957	2,854,797	1,250,869
Capitol Technology University	n/a	-162,022	190,101
University of Maryland, Baltimore Campus	1,275,948	1,400,131	863,569
University of Maryland Baltimore County	1,366,713	1,539,591	382,075
University of Maryland, College Park Campus Housing	6,442,069	5,137,587	3,069,571
University Village at Sheppard Pratt	1,364,033	1,115,547	-46,396
Subtotal	\$17,055,131	\$16,096,703	\$10,759,914
Other Facilities			
Chesapeake Bay Conference Center (Hyatt Cambridge)	-\$5,410,647	-\$5,555,977	-\$12,002,978
National Cybersecurity Center of Excellence	-959,088	-155,324	n/a
Rockville Innovation Center	-803,632	-94,607	n/a
Metro Centre	693,883	720,594	806,108
University of Maryland, College Park Campus Energy	3,219,327	-2,209,219	-922,421
Baltimore City Garages	n/a	2,678,022	2,371,919
Subtotal	-\$3,260,157	-\$4,616,511	-\$9,747,372
Subtotal Operating Facilities	\$13,794,974	\$11,480,192	\$1,012,542
MEDCO Exclusive of Operating Facilities	\$1,917,933	\$824,084	\$1,581,113
Elimination (Accounting Adjustment)	-\$142,238	-\$17	-\$63,329
Grand Total	\$15,570,669	\$12,304,259	\$2,530,326

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

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The COVID-19 pandemic and resulting business and school closures have significantly impacted revenues for many of MEDCO’s projects, especially the student housing facilities that make up the majority of MEDCO-operated projects. It is worth noting that the data in Exhibit 3 includes revenues and expenses through the end of June 2020 and therefore only partially reflects the impact of the pandemic. Student housing projects are discussed further below.

Many of MEDCO’s projects temporarily suspended operations or reduced capacity from March to June 2020. While the continued impacts of COVID-19 are still uncertain, MEDCO believes that all projects other than the CBCC project will be able to meet their operating needs and make required principal and interest payments in fiscal 2021, although some may need to use their reserve funds to make full debt service payments.

As it has been since 2014, the CBCC project remains a “nonperforming” project. This designation was made after the June 2014 debt service payment was only partially made. CBCC is located in Dorchester County and houses a hotel, golf course, and conference facilities. Revenues were further reduced due to the pandemic–related closure of the facility in March and the limited capacity following reopening of the hotel in June. Normally, the CBCC generates most of its revenues in the spring and summer. Investors have extended a short-term forbearance agreement through the end of June 2021 and have allowed reserve funds to be used to support daily operational costs.

The Baltimore City Garages project operated by MEDCO entered “watch” status in July 2020 when Standard & Poor’s downgraded the ratings on several series of bonds for the project to BB-, which is not an investment grade rating. Parking customers in Baltimore City decreased significantly due to pandemic-related closures. MEDCO noted that revenues increased slightly when certain sectors of the economy reopened, but MEDCO expects the recovery to be slow and does not anticipate meeting the required coverage ratios for the project in fiscal 2021. MEDCO has retained a parking consultant and meet regularly with the manager to monitor project performance.

MEDCO’s Purple Line conduit project was classified as “watch” in August 2020 when Purple Line Transit Partners gave notice of its intent to terminate its agreement with the State. MEDCO continues to provide financial and consulting services to the Maryland Department of Transportation to support the project. Another conduit project that was classified as “watch” in fiscal 2019 (929 North Wolfe Street in Baltimore City) remained in watch status but had improved performance in fiscal 2020. The bondholders approached MEDCO regarding restructuring the bonds. However, MEDCO advises that restructuring at this time would be difficult due to the economic climate surrounding the pandemic.

Student Housing

In March 2020, the University System of Maryland and Morgan State University transitioned from in-person to remote learning for the remainder of the spring semester, and MEDCO worked with the institutions to issue refunds to students living in MEDCO-operated housing projects. For the fall 2020 semester, institutions delivered a majority of their courses remotely, and as a result some students living in MEDCO housing projects chose not to return to their campuses and requested refunds from MEDCO. The terms of the leases or licensing agreements vary by facility, as do the agreements

reached between MEDCO and the universities. **Exhibit 4** summarizes the status of each housing project that experienced significant issues during the pandemic. The fiscal 2022 allowance includes a \$1 million deficiency appropriation for the University System of Maryland Office in fiscal 2021 to compensate MEDCO for losses incurred as a result of releasing students.

Exhibit 4
Status of Housing Project Agreements Between MEDCO and Universities

University

Status of MEDCO-operated Housing

Morgan State University

Contracts were deferred for students that wanted to be released, and the university made payments to MEDCO for the released students of \$118,000 for spring and summer 2020 and \$1.2 million for fall 2020. An additional payment is expected for the spring 2021 semester.

Towson University

MEDCO and the university reached an agreement in December 2020 to reduce capacity in student housing facilities operated by MEDCO. MEDCO will release certain students from their licenses and issue credits for both fall 2020 and spring 2021 if requested, and any partial payments made by students will be credited for a future semester. MEDCO and the university will split the estimated operating shortfall of \$2.3 million.

University of Maryland, Baltimore Campus

The university executed residence agreements that allowed students to be released from their contracts; the university provided payments to MEDCO for the released students of \$277,000 for spring 2020 and \$924,000 for fall 2020. An additional payment will be made in January 2021 for the spring 2021 semester.

University of Maryland Baltimore County

Students had the right to cancel their contracts up until moving into housing; occupancy in the fall semester was low as a result.

University of Maryland, College Park

MEDCO and the university reached an agreement in December 2020 whereby MEDCO will release certain students from their licenses and issue credits for both fall 2020 and spring 2021 if requested, and any partial payments made by students will be credited for a future semester. The estimated operating shortfall is \$6.2 million, with the university contributing up to \$3.3 million through the deferral of expenses and fees, and MEDCO contributing the remainder.

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation; University of Maryland, Baltimore Campus; Towson University

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Due to the revenue impacts of low occupancy during the pandemic, several of MEDCO’s student housing projects were classified in “watch” status: University of Maryland, College Park; University of Maryland, Baltimore County; University of Maryland, Baltimore; Salisbury University; Towson University; and Bowie State University. Salisbury University was later removed from “watch” status in September 2020. Each of the projects classified as “watch,” with the exception of Salisbury University and Bowie State University, failed to meet the required debt coverage ratio of 1.20 as of the last day of the fiscal year, and MEDCO has retained a management consultant for these projects, as required.

Exhibit 5 shows the debt coverage ratio at the end of the last three fiscal years, the maximum debt service, and outstanding balance at the end of fiscal 2020 for each housing project, as well as the occupancy rates for October 2020. MEDCO anticipates that as long as occupancy for the spring 2021 semester is the same or better than for fall 2020, the student housing projects will be able to fund operating expenses and meet all debt service obligations for fiscal 2021. MEDCO also expects that the projects will recover quickly once occupancy levels can return to pre-pandemic levels.

Exhibit 5
Status of Student Housing Project Debt
(\$ in Millions)

<u>Project</u>	<u>Debt Coverage Ratio¹</u>			<u>Maximum Debt Service Payments</u>	<u>Outstanding Balance June 2020</u>	<u>Occupancy Rate October 2020</u>	
	<u>Fiscal 2018</u>	<u>Fiscal 2019</u>	<u>Fiscal 2020</u>			<u>Contracted</u>	<u>Actual</u>
Bowie State University	1.55	1.58	1.33	\$1.4	\$13.5	86.5%	70.0%
Frostburg State University	1.51	1.57	1.38	1.2	11.8	81.8%	81.3%
Capitol Technology University	n/a	1.78	1.66	0.9	13.9	65.0%	65.0%
Morgan State University	1.59	1.56	1.68	2.4	25.6	82.0%	50.9%
Salisbury University	2.00	2.16	1.49	2.2	18.7	97.3%	94.9%
Towson University	1.59	1.59	1.06	3.5	39.5	89.0%	56.0%
University of Maryland, Baltimore Campus	1.31	1.39	1.16	1.9	23.9	54.3%	54.3%
University of Maryland Baltimore County	1.66	1.79	1.05	1.2	16.7	53.6%	53.6%
University of Maryland, College Park Campus	1.76	1.76	1.14	10.1	118.3	90.0%	78.0%
University Village at Sheppard Pratt	2.91	2.91	2.27	1.6	17.0	66.8%	66.8%

¹ Debt coverage ratio is the ratio of net operating income to debt service payments. The required coverage ratio is 1.2.

Source: Maryland Economic Development Corporation

Operating Budget Recommended Actions

1. Nonbudgeted.