Affordable Housing Resource Center

LIHTC Equity Market Moving Forward Cautiously in Light of COVID-19 Pandemic

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The coronavirus pandemic, or COVID-19, is having a huge impact on global health and the economy.

At this time, opinions from low-income housing tax credit (LIHTC) investors and syndicators present a wide range of viewpoints that are layered with uncertainty. Cautious optimism and uncertainty about the affordable rental housing investment market seem to be the starting point in the path of next steps, which will be informed by data.

"Our foot is off the gas a bit, but not on the brake," said Vihar Sheth, director of business development for equity at U.S. Bancorp Community Development Corporation (USBCDC). "We are closing transactions at the price and terms we originally offered and continuing to look at new opportunities with added scrutiny on the financial strength of our partners. No one is running for the hills at this point."

"We are not seeing a slowdown from investors," said David Salzman, president at Richman Real Estate Investments Inc. "Our pipeline is bigger than it was this time last year. Investor demand has remained steady."

"Our investors are honoring their commitments and we are closing deals at the original pricing and terms," said Scott Hoekman, president and CEO of Enterprise Housing Credit Investment LLC. "We are seeing additional scrutiny of sponsors and underwriting."

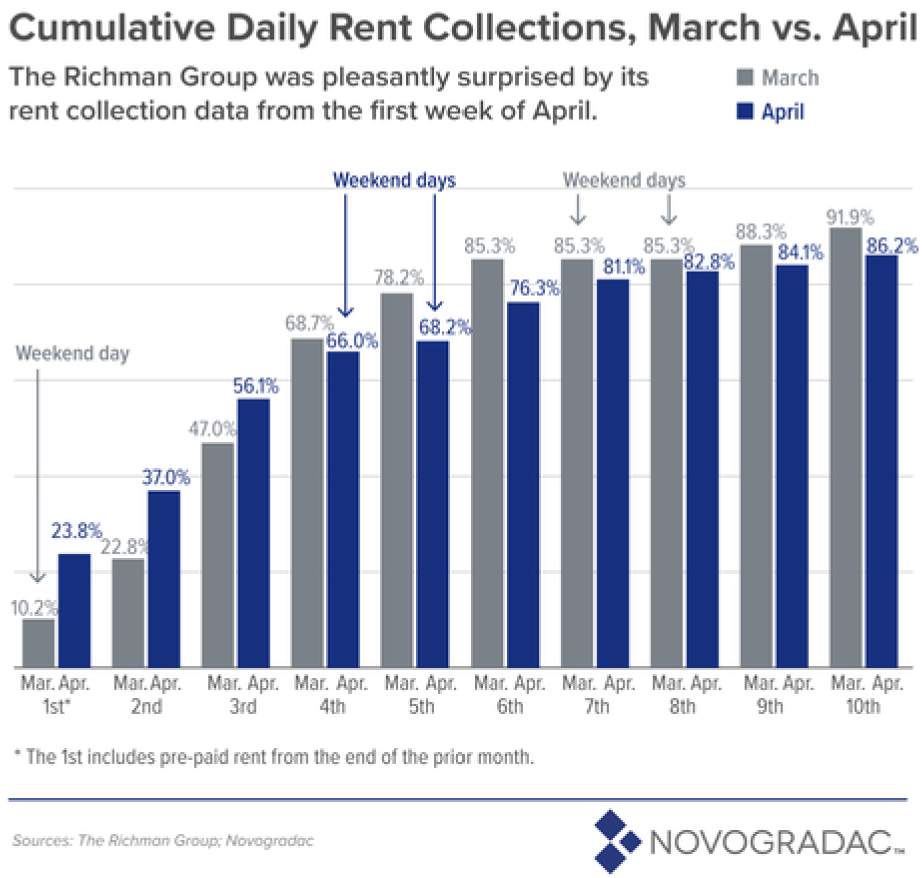
Using Data to Inform Uncertainty

"This is a new type of uncertainty. Though we don't necessarily know when we will come out of this, we're taking steps to evaluate the current impact and planning for long-term solutions," said Josh Levy, managing director and head of production of the Affordable Tax Credit group at Berkadia.

One approach to address investors' uncertainty may be to examine the underlying economics of the investments. For example, The Richman Group is using data mining to inform its investors and other market participants about portfolio performance, which indicates that things are more hopeful than originally anticipated.

Richman accumulated recent data on a managed portfolio of approximately 15,000 affordable rental housing units across 110 properties.

"It's still early but so far we are pleasantly surprised by the results of April rent collections. We had feared a much larger decline," said Brian Myers, president of Richman Asset Management Inc. "As of April 10, 86.2 percent of rents were paid. By comparison, over the same period in March, which we consider a normal month, we collected 91.8 percent of rents. We thought there would be a larger drop off, but our data doesn't support that." Myers noted that rent collection rates are virtually unchanged at the portfolio's senior properties.



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"Rent collections are not down as much as we were expecting," said Levy. "Will this trend continue into May? I don't know. The CARES Act will offer relief to a majority of residents this month. It's critical that property managers work with tenants to help them access relief programs that are available now and in the months to come."

Myers noted that if the effects of the pandemic last a few more months, affordable rental housing properties should still be able to operate. "Because properties have retained cash and funded operating reserves, most of our syndication portfolio can absorb a material drop in collections," said Myers. "In an extreme example, we stressed tested the portfolio and concluded that 78 percent of the properties could absorb a 50 percent decline in rental collections and still sustain operations for four-plus months by utilizing only the cash and reserves currently held at the lower-tier."

However, some members of the affordable housing community fear more challenges will likely arise in the months ahead.

"May could be worse than April since people likely paid April rents with March paychecks," said Sheth. "It could be a harder choice next month between buying food and paying rent or utilities."

Comparing Recent Crises

Affordable housing practitioners are saying the economic impact from COVID-19 has been different from the Great Recession.

"The only thing it tells us is it should be wise not to prognosticate," said Sheth. "This is so much different from the Great Recession. There is no crystal ball for this."

"The industry experienced a similar economic crisis in 2009," said Salzman. "Although in 2020, we are seeing a different type of macro-economic event, for the LIHTC market this may be similar to 2009. In 2009, we saw an increase in occupancies as incomes dropped and unemployment increased."

"In October 2008, almost all investors at the time exited the market. That resulted in a dramatic change in yield. I don't see that happening here," said Anil Advani, executive vice president of originations and finance at WNC & Associates. "It's tough to predict the future, but things have a different feel in a major way compared to 2008-2009. The economy has been hit hard, but the difference is in 2008-2009 it was a systemic failure of the financial industry, which took years to recover. Most forecasts we are seeing is that, while the disruption from COVID-19 will likely be severe, it will be much shorter lived, and we could be back to normalcy in less than a year."

"In 2009, there was a very profound exit," said Hoekman. "It was a total contraction of the market led by the government-sponsored enterprises pulling out. All of a sudden, 40 percent of the market was gone—that was catastrophic. We don't see that happening now."

LIHTC Equity Forecast

Before COVID-19, Sheth was seeing a slight reduction in LIHTC equity pricing. He said that trend will slowly continue through the COVID-19 pandemic. "What we paid 94 cents per credit for in January would likely go for 91 cents now," said Sheth. "Last recession was a 10 cent haircut. This time, it's a slow drip down. Tax credit equity pricing is still in the 90s in most deals, but at the low end."

Levy said economic investors in the LIHTC market are looking for yields between 6.5 and 7 percent, whenever possible. Conversely, he said LIHTC investments in California are seeing yields at 4.75 percent versus 4.25 percent before the COVID-19 pandemic. "Closing everyone's current 2020 pipeline still gives them a great year," said Levy.

LIHTC Transactions are Closing during the Pandemic

Levy said Berkadia is successfully fulfilling its signed letters of intent. "The quality and feasibility of new deals is paramount at this time," said Levy. "Berkadia and its investors are moving prudently with respect to new deals, balancing the needs of our developer clients, potential residents and the current uncertainty in the market. Investors want more clarity and a regular working economic environment in order to better understand how to successfully navigate the market. Until then, we will close the transactions we have and continue to assess new opportunities. In the past three weeks, we were able to successfully close $45.3 million of LIHTC equity."

Hoekman said Enterprise has a robust pipeline and deals continue to close. However, he said one deal type that will get more scrutiny than others is rehabilitation projects with residents—particularly seniors—living in-place. "The concern is how to carry out that rehab in a way that's safe for residents and workers," said Hoekman.

Advani was proud that WNC recently closed a national LIHTC fund with seven investors and $128.5 million in equity. "We were able to close a fund in the heart of the COVID-19 pandemic," said Advani. "We were able to keep the same terms, pricing and yield."

Moving forward, WNC is looking to close a California LIHTC fund in the coming weeks with the original terms. Next, it will look to close a national fund this summer. "Economic investors are telling us they are committed to moving forward," said Advani. "The bigger question is what type of properties will it include and how will the properties be underwritten."

How will the Affordable Housing Community Continue to Move Forward?

"It remains to be seen how much pricing will change, and to what deals that change might apply," said Hoekman. He noted that a related concern is how Community Reinvestment Act reform may affect the market.

"Everyone is itching to get the economy started again," said Advani. "How does that impact us?"

"We are hoping for some level of return by summer," said Sheth. "But if things get significantly worse, we could get a slower recovery and demand could go down."

"I'm hearing there are [some] syndicators taking a pause in the market. I understand that," said Advani. "If you are smart about what you do and trust the developers you work with, I'm confident the industry can find a way to continue to do business."

Novogradac will continue to monitor and report on LIHTC investors' and syndicators' perspectives. To participate, contact Blair Kincer.

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