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THE INVESTOR HUB

The Case for Affordable Housing

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While the case for affordable housing has been strong for many years, it particularly holds true in the current economic environment.

Factors that generated steadily increasing investor interest among buyers of affordable housing properties over the last decade are expected to remain in place into the foreseeable future, despite COVID-19 and other headwinds confronting our economy.

institutional sources and by a CAGR of 41.7% from private capital sources.[1] These figures illustrate the evolution of the affordable housing asset class during the period. As markets adjust to COVID-19 risks, investor appetite for lower risk investment classes such as affordable housing is expected to continue to increase.

HISTORICAL PROGRAM SUCCESS

The LIHTC program, historically creating or rehabilitating approximately 75,000 units per year, is by far the most successful affordable housing production program ever.[2] Without a better solution, this program, along with Section 8 HUD programs, seem destined to be part the affordable housing landscape into the future and could potentially be expanded.

CONSISTENT NEED

Supply/demand imbalance in affordable housing stock is forecasted to persist into the foreseeable future. Trends in income inequality, real wage growth for affordable renters, and societal shifts toward renting vs. owning all increase affordable housing demand. At the same time, the stock of affordable units and workforce housing has been largely unchanged since the Great Financial Crisis—we are simply not building enough new product relative to the need. In absolute rental dollar terms, the number of units renting for less than $800/unit has dropped by four million since 2011.[4] There are currently 58 units at 50% AMI available for every 100 households in need.[5]

SOLID FUNDAMENTALS

Operations at affordable properties are more stable than market rate properties, resulting in solid, reliable cash flows, and compelling returns on a risk-adjusted basis. During the peak of the Great Financial Crisis, market-rate multifamily vacancy was 10.7% while LIHTC vacancy was 3.7%.[6] Physical occupancy for properties financed with LIHTCs are in the 96%-97% range historically with median vacancy at approximately 2.2%. A key demand driver is the rent differential between LIHTC and comparable market rate units, with LIHTC rents are approximately 22% below average market rents nationally, and much higher in higher cost markets.[8] The spread between LIHTC rents and market rate rents has grown steadily since the last recession and will provide even greater occupancy support in the current downturn.

EXCEPTIONAL DEBT ENVIRONMENT

Financing is favorable for affordable housing assets and is readily available for most borrowers, despite COVID-19. Agency lending continues to provide borrower liquidity for refinancing and purchase transactions. Record low interest rates, multi-year interest only periods, low 1.20-1.25 DSC ratios and 80% LTV terms are available for qualified borrowers. The social benefits of affordable housing are likely to provide preferred terms from government sponsored lenders into the future. In September 2019, FHFA increased their commitment to mission driven affordable housing by revising multifamily loan caps for Freddie Mac and Fannie Mae and increasing their affordable mandates to 37.5%.[10]

VALUE-ADD OPPORTUNITIES

Value-add investment opportunities will continue due to the aging of properties and the misalignment of interests that can exist in LIHTC partnerships, creating management improvement upside. Management improvement upside for LIHTC

Many believe that social impact investments, such as investing in affordable housing, inherently comes with lower financial returns. We argue that on a risk-adjusted basis, this is simply not the case. At a time when investors continue to navigate what investing in ESG means to them, affordable housing will help any investment strategy align financial return with impact, and those with patient capital can benefit greatly from its long-term stability. We anticipate the trend in ESG impact investing will continue to drive more capital to affordable housing.

During a time when the daily news causes us to focus on the short term, it is great to remind ourselves that the drivers of the affordable housing marketplace remain strong. While affordable housing property operations will be affected by the current downturn, the more insular nature of cash flows will allow it to recover more quickly than other asset classes.

[1] *Real Capital Analytics, Subsidized Multifamily Acquisition Capital Flows*

[2] *CohnReznick Housing Tax Credit Investments and Operational Performance, November 2019.*

[4] *JCHS tabulations of US Census Bureau, American Community Survey 1-Year Estimates. 2011-2017*

[5] *NLIHC – The Gap: A shortage of Affordable Homes, March 2019*

[6] *U.S. Census Bureau, CohnReznick.*

[8] *CBRE Affordable Housing Brief, April 2018.*

[10] *Federal Housing Finance Agency Press Release, September 2019.*

[11] *Ibid #2*

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