Special Sidebar Q&A:

AFFORDABLE AS AN INVESTMENT

REAL ESTATE FORUM: AFFORDABLE HOUSING IS A SECTOR THAT HAS HISTORICALLY BEEN UNDERSERVED BY INSTITUTIONAL CAPITAL. HOW HAS THIS SECTOR EVOLVED, AND WHAT MAKES IT AN ATTRACTIVE INVESTMENT NICHE/ASSET CLASS FOR INVESTORS?

DOUG WESTFALL, SVP, NorthMarq Capital: Over the past five to 10 years, the affordable housing industry has greatly matured, with institutional (private capital) much more plentiful than when the tax credit program was just getting started. The availability of capital now exceeds the opportunities to invest, creating intense competition among lenders and equity investors. The challenge is finding soft funds to fill the gap between the cost of providing and maintaining affordable housing and the amount of capital the housing can support and provide a reasonable return for investors; the more affordable the housing the greater the gap.

LAURA BAILEY, SVP of Community Finance, Capital One: Historically the question of affordable housing was seen as something the federal government addressed through the Section 8 Program. Once the Low Income Housing Tax Credit program started to become increasingly familiar to investors, they began to see the benefits of the program, which are truly win-win. In addition, the ability to support development of affordable housing options, while also utilizing economic and tax incentives, attracts not only institutional investors, but also quality, housing developers.

ALBERTO MILO JR., EVP and Principal, Related Urban Development Group: Affordable housing is still not a huge draw for institutional capital due to the relatively small returns and extensive regulatory requirements. Involvement from major banks is mostly CRA driven; however, municipalities like Miami Dade County and the City of Miami are working to create programs and incentives meant to generate additional interest.

JOHN WILLIAMS, President and CIO, Avanath Capital Management: Several factors make affordable housing an attractive asset class for investors. First, there is a limited supply and a virtually unlimited demand for affordable and workforce housing throughout the US, and especially in coastal markets. These fundamentals create a natural opportunity for investors to leverage this demand to maximize occupancies and generate strong cash flow. Second, there's a tremendous opportunity to generate not only financial returns but also social benefits. Many institutional investors are shifting their focus toward Corporate Social Responsibility investment platforms that positively impact communities, while also generating risk-adjusted returns.

FORUM: WHICH MARKETS ARE YOU TARGETING FOR AFFORDABLE AND WORKFORCE HOUSING INVESTMENTS IN 2017 AND BEYOND?

WESTFALL: Due to the CRA needs of national and regional banks the competition for deals in major markets is intense with most deals funded by banks that offer tax credit equity, construction loans and permanent debt all in the same package. Companies such as NorthMarq Capital, which represent a sources for permanent debt but don't offer construction debt and tax credit equity at competitive pricing, are challenged to compete in the secondary and tertiary markets.

BAILEY: 2017 will be an exciting year for us. We are growing the part of our business that targets affordable and workforce housing investments, while addressing new challenges. Our core markets, which follow our bank's strongest markets, are New York, the Mid-Atlantic, and the Gulf Coast. We are also looking for new opportunities in Boston, Chicago, Miami, San Francisco, and Los Angeles.

WILLIAMS: The top markets for affordable and workforce housing investments mirror the top markets for any product, whether it's market-rate multifamily, office, or retail. We target markets with strong employment growth, a wide availability of mass transit options, and a high quality of life. We also concentrate on markets with strong school districts, primarily because many of the families that live in our affordable housing communities like to be in close proximity to excellent schools for their children. Further, we invest in areas where rent growth considerably outpaces income growth, and where there's a 25% to 30% difference between market rate and affordable rents.

MILO: There is a huge demand for this kind of development through all major urban centers in the country. Related Urban is focused on urban infill markets throughout the State of Florida, with emphasis on Miami Dade County, Southeast Florida and Southwest Florida.

FORUM: THERE'S BEEN A LOT OF TALK ABOUT DEVELOPING NEW AFFORDABLE PROJECTS TO ACCOMMODATE DEMAND. WHAT'S YOUR POSITION ON NEW CONSTRUCTION VS. REHABILITATION?

MILO: It really depends on the functionality of the structure(s) relative to the site. The merits of each property must be analyzed independently. If the existing structure(s) are not underutilized and are consistent with the area's zoning and master plan, then we strongly support the rehabilitation and preservation of the property. We're always looking for ways to create more value for our public partners, more efficiently utilizing public funds, and thus create additional affordable housing.

WILLIAMS: Given the high costs of new construction and limited government subsidies through the LIHTC program, the redevelopment of existing affordable housing is a much more viable and cost-effective alternative to new construction. By acquiring and repositioning existing affordable housing, we can deliver a high quality, affordable product at a huge discount to new development in a shorter period of time. Typically, the development cycle requires five to seven years to bring a new project on line. We can acquire an existing property and transform it within a year to 18 months. As a result, we can make a more immediate impact on neighborhoods, and preserve affordable housing today in areas where it is most needed. ◆

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