



THE AFFORDABLE HOUSING ASSET CLASS

ULI HOUSING OPPORTUNITY CONFERENCE FEBRUARY 5, 2019



Urban Land
Institute

Terwilliger Center for Housing

RCLCO
REAL ESTATE ADVISORS

Executive Summary

Affordable Housing -- What is it?

- Housing (rental in this case) affordable to households earning less than 60% of median income
- Approximately half of the nation's 20.4M units of multifamily housing should be classified as "affordable"
- Half of the affordable housing is subsidized, by a wide variety of public policies/subsidies
- Half of our affordable housing is "naturally-occurring," non-subsidized but in many places at risk of being improved to unaffordable
- Affordable housing is meaningfully driven by for-profit entities, with over half of owners, managers, and developers being for-profit.

Executive Summary Cont.

Affordable Housing – How does it perform as an investment?

- The asset class performance is strong -- especially in downturns -- driven primarily by its stability of income.
- Interest/appeal correctly driven by (1) consistently high occupancies (2) low turnover, and (3) lower and slower growing operating and capital expenses.
- Result -- Per-square-foot revenues and NOIs that are comparable to, if not higher than those at market-rate properties.
- Dramatic growth in transaction volume driven by influx of institutional capital
- Result -- Cap rates for subsidized assets have compressed to be on par with conventional properties, though volatility remains high.

Executive Summary Cont.

What is the outlook for demand of affordable rental housing?

- Affordability of housing broadly under threat from value add investing and new development unusually focused on high cost locations
- Regularly expiring subsidy contracts will naturally constrain the supply of subsidized affordable housing.
- Historical and projected trends in housing costs and wage stagnation indicate a persistent and pervasive need for affordable housing

I. Size and Scope

Affordable Rental Housing Supply

Key Players

Transactions

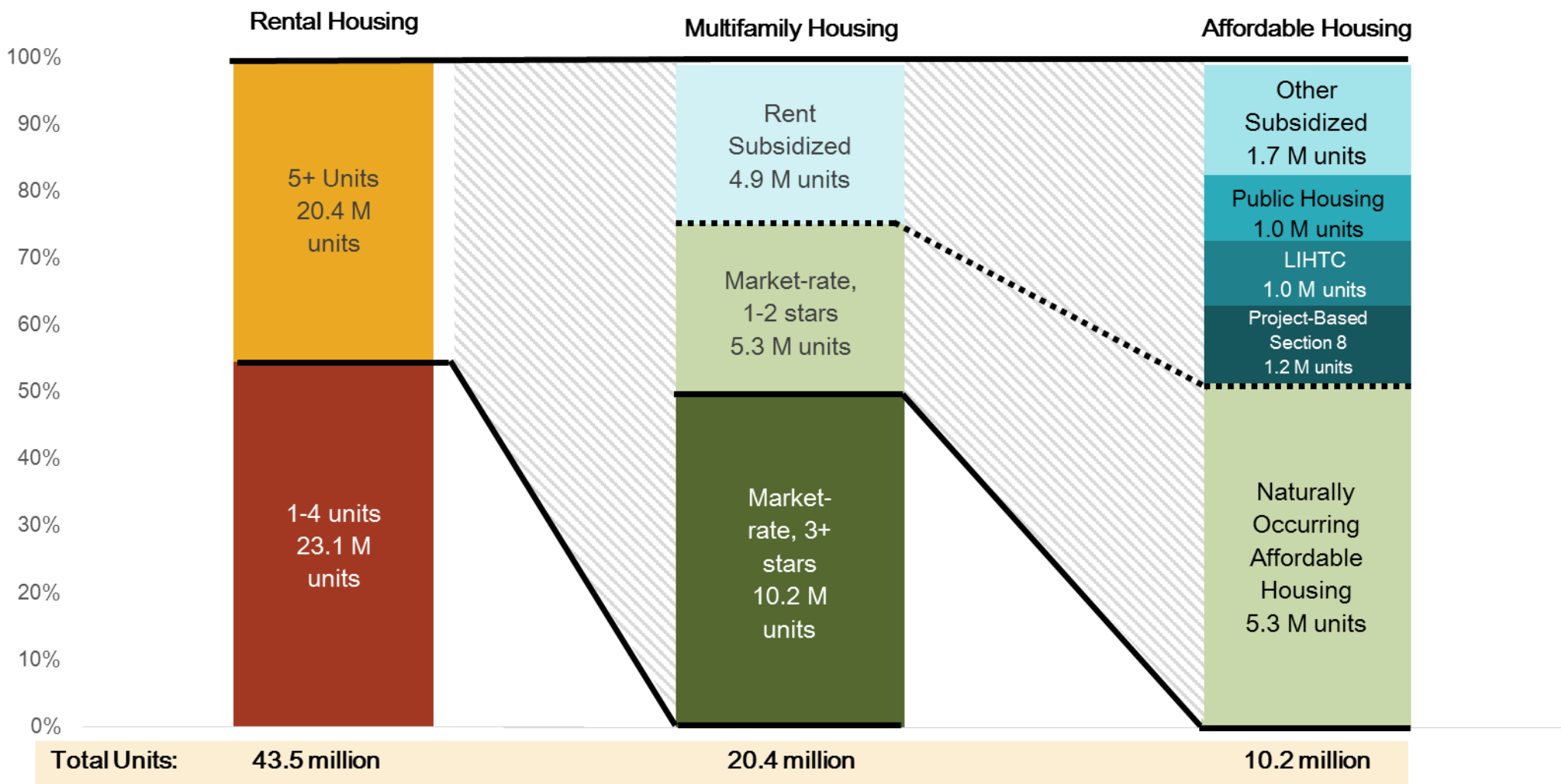
Size and segmentation of rental housing

About 25% of rental housing is affordable multifamily

More than half of the rental housing stock is small-format, with 1 to 4 units.

50% of multifamily (5+) units are “affordable,” with or without subsidies.

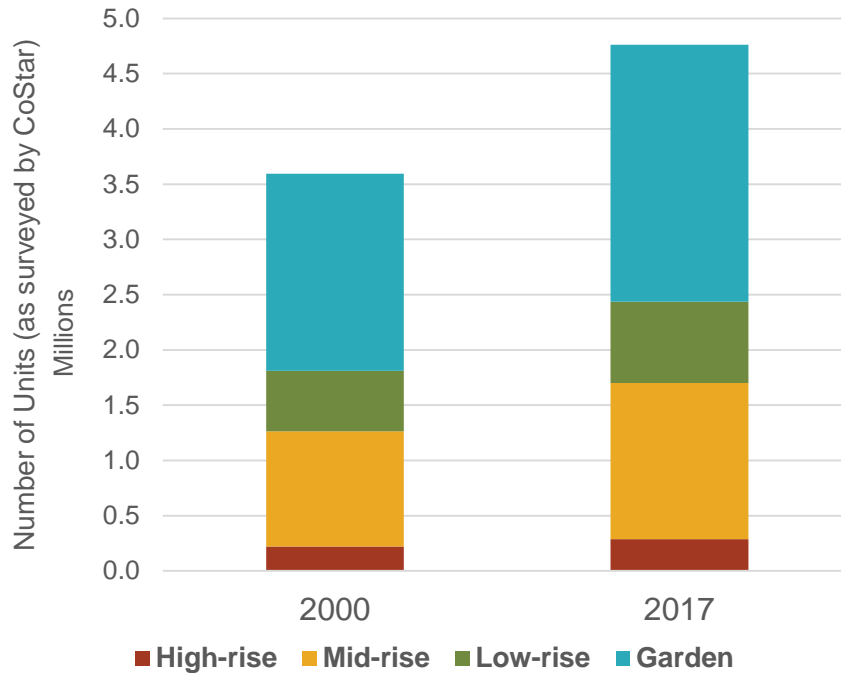
48% of “affordable” housing receives government subsidies.



Affordable buildings: low-density, older

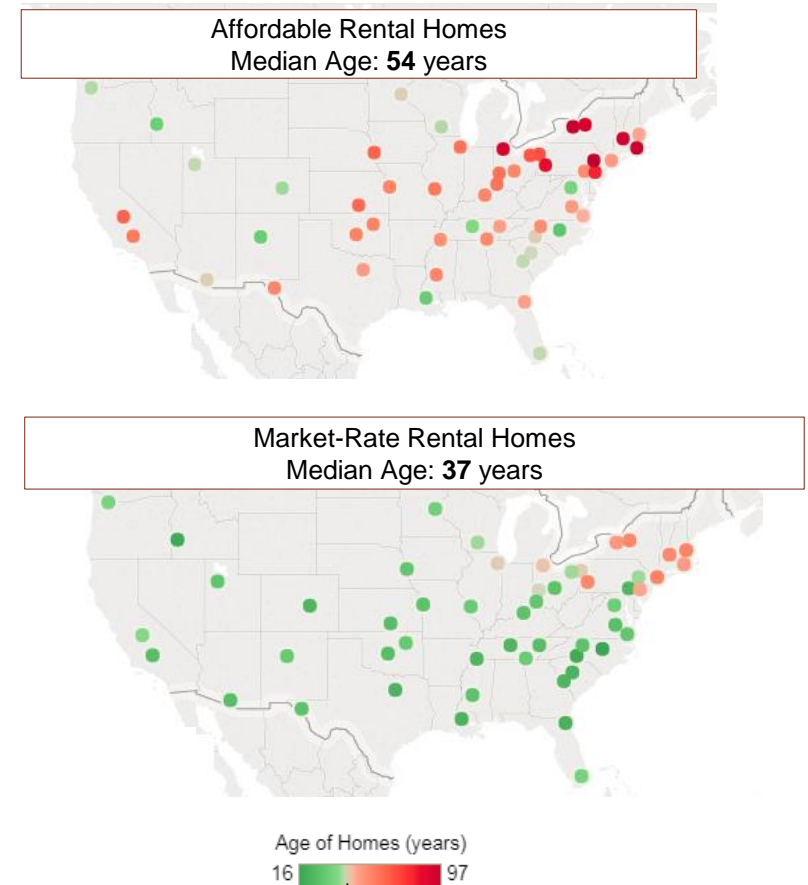
Reflects lower construction costs and depreciation

Distribution of Units in Subsidized Affordable Buildings, by Building Type 2000 – 2017



- Highrise** 15+ stories, 1 or more buildings
- Midrise** 4-14 stories, 1 or more buildings
- Low-rise** 1-3 stories, 1-3 buildings
- Garden** 1-3 stories, 4 or more buildings

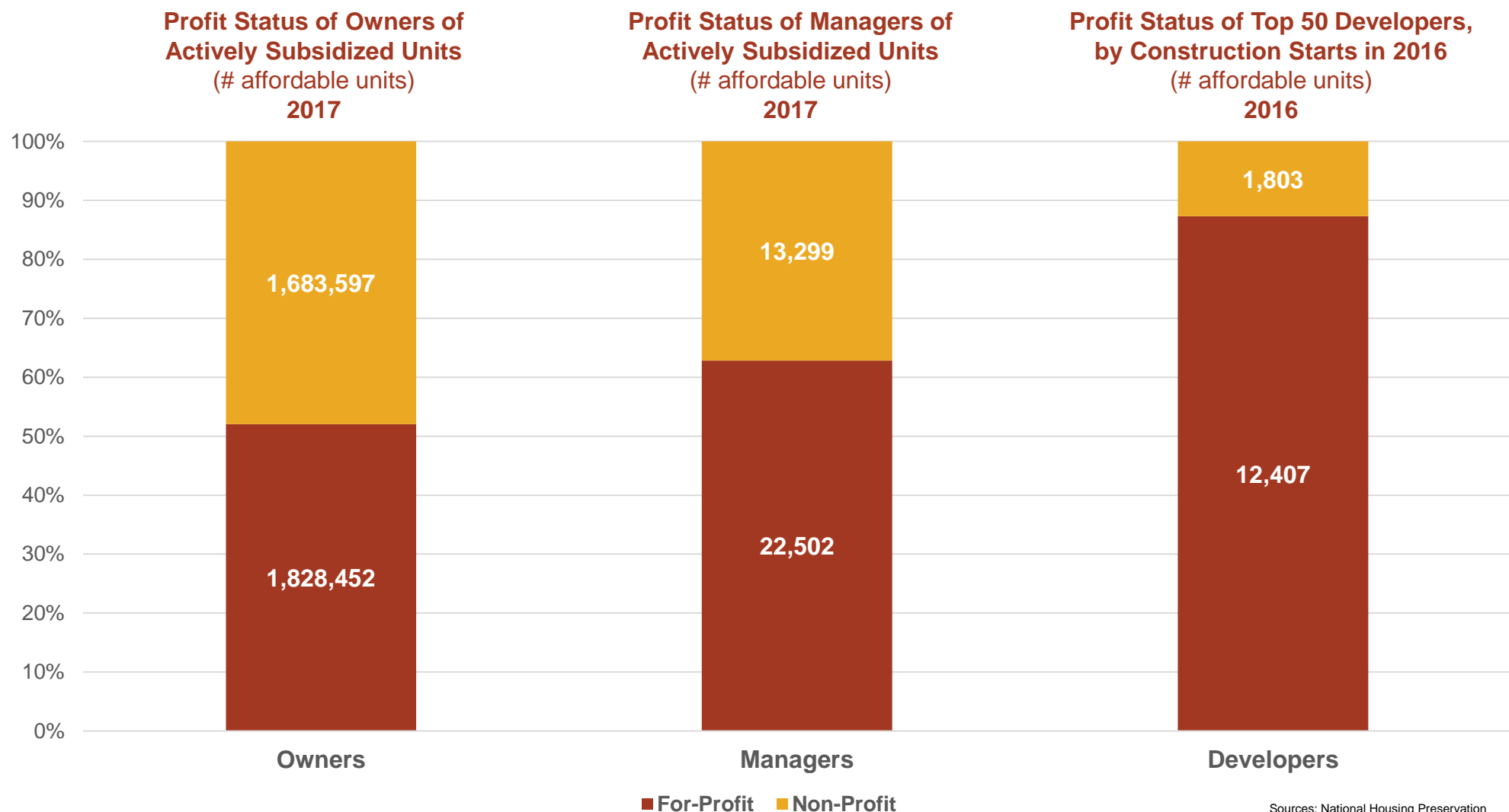
Median Age of Affordable and Market-Rate Rental Homes 2017



Based on Zillow research. Units surveyed include both multifamily and single-family. "Median Age" stated is the weighted mean of the median age across 100 largest metros.

Most affordable housing players are for-profit

Across ownership, management, and development roles



Sources: National Housing Preservation Database; Affordable Housing Finance; RCLCO

Key players mostly developer/owners

Otherwise, institutional—whose holdings have a higher PPU

Top 50 U.S. Investors in Subsidized Housing (by number of units held) Data Through 2017

Rank	Company	Units	Projects
1	The Michaels Organization	42,359	364
2	Dominium	27,989	208
3	Millennia Companies	22,998	211
4	Mercy Housing	22,635	327
5	Volunteers of America	20,088	497
6	National Church Residences	18,348	269
7	GHC Housing Partners	17,673	159
8	Southport Financial Services	17,433	188
9	Beacon Communities	15,774	146
10	Jonathan Rose Cos.	14,095	92
11	Herman & Kittle Properties	14,052	147
12	Retirement Housing Foundation	14,004	160
13	The NRP Group	13,294	119
14	The Cornerstone Group	13,898	63
15	Winn Companies	13,664	101
16	McCormack Baron Salazar	13,658	123
17	LIHC Investment Group	13,255	61
18	Omni NY	13,255	61
19	Conifer Realty	13,158	217
20	Gene B. Glick Co.	12,429	91
21	Capital Realty Group	12,403	86
22	Pennrose	12,331	190
23	Highridge Costa Cos.	12,184	117
24	American Community Developers	12,154	91
25	L-M Development Partners	11,929	87

Rank	Company	Units	Projects
26	Bridge Housing Corp.	11,352	105
27	USA Properties Fund	10,996	87
28	Ledic Realty Co.	10,886	77
29	Woda Cooper Cos.	10,866	286
30	Vitus	10,436	107
31	The Pacific Cos.	10,213	167
32	The Community Builders	10,155	136
33	The Hallmark Cos.	10,151	264
34	Related California	9,635	82
35	Silver Street Development Corp	9,620	66
36	Preservation of Affordable Housing	9,162	77
37	The Nurock Cos.	8,985	32
38	Eden Housing	8,716	130
39	Wallick Communities	8,192	112
40	Security Properties	7,915	57
41	Jamboree Housing Corp	7,536	84
42	LDG Development	7,503	74
43	Standard Communities	7,412	32
44	Midpen Housing Corp	7,275	104
45	The Reliant Groupz	7,258	52
46	LHP Capital	7,128	54
47	Avanath Capital Management	6,964	62
48	TM Associates	6,927	167
49	Enterprise Homes	6,889	68
50	The Arker Cos.	6,676	48

Sources: Affordable Housing Finance; RCLCO

Transactions in institutional capital

Growth in volume reflects both acceptance and appetite

**Institutional Investor* Subsidized Housing Transaction Volume
by Total Value of Acquisitions and Sales 2001 – 2017**



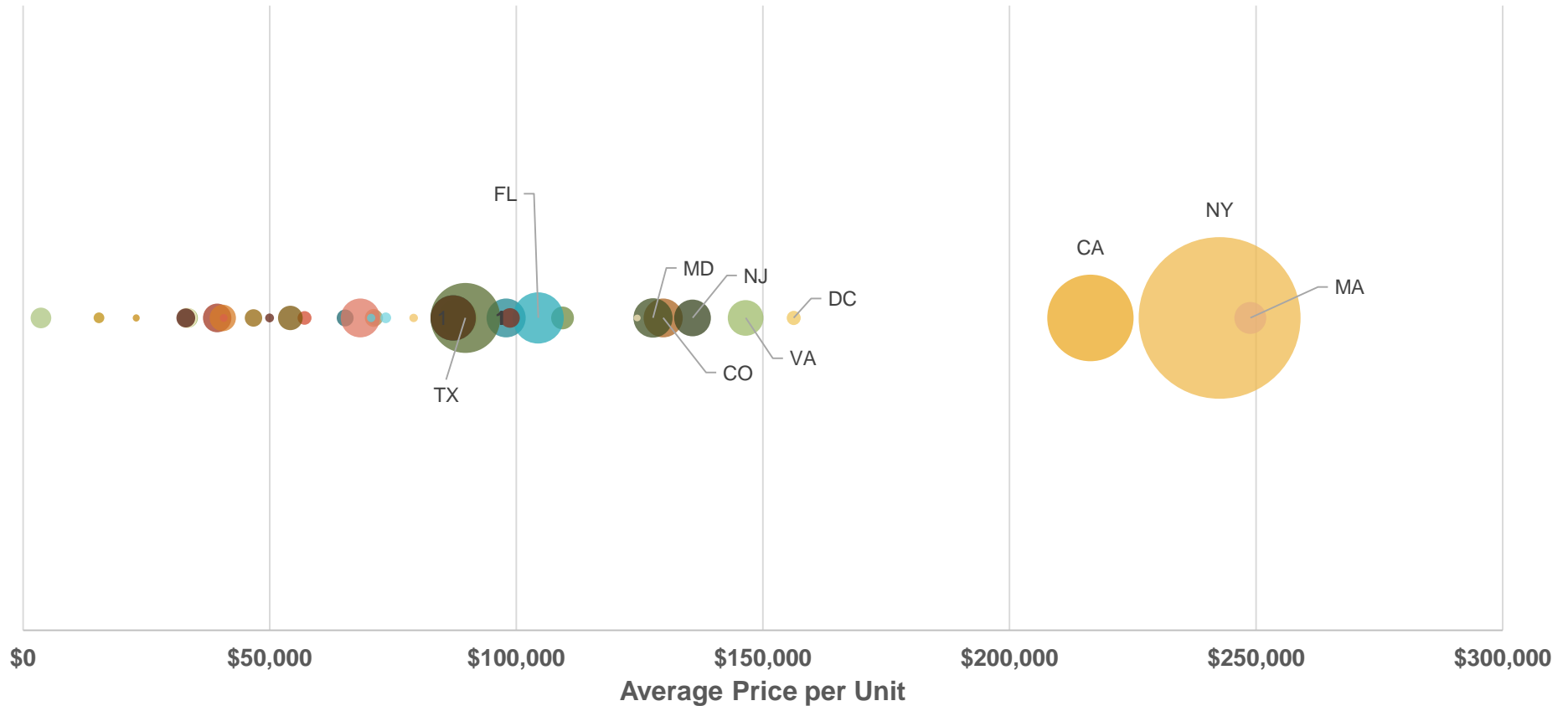
*Note: RCA defines "Institutional Investors" to include equity funds, pension funds, insurance companies, banks, investment managers, sovereign wealth funds, open-ended funds, and other financial services firms.

Sources: Real Capital Analytics; RCLCO

Acquisitions by institutional capital

Have favored large, high-cost, and/or fast-growing states

Subsidized Apartment Units Acquired and Price Per Unit Paid, By State 2000 – 2017



Note: Size of bubble represents *number* of units within any fully or partially subsidized properties that were acquired.

Sources: Real Capital Analytics; RCLCO

II. Performance Real Markets: Operations

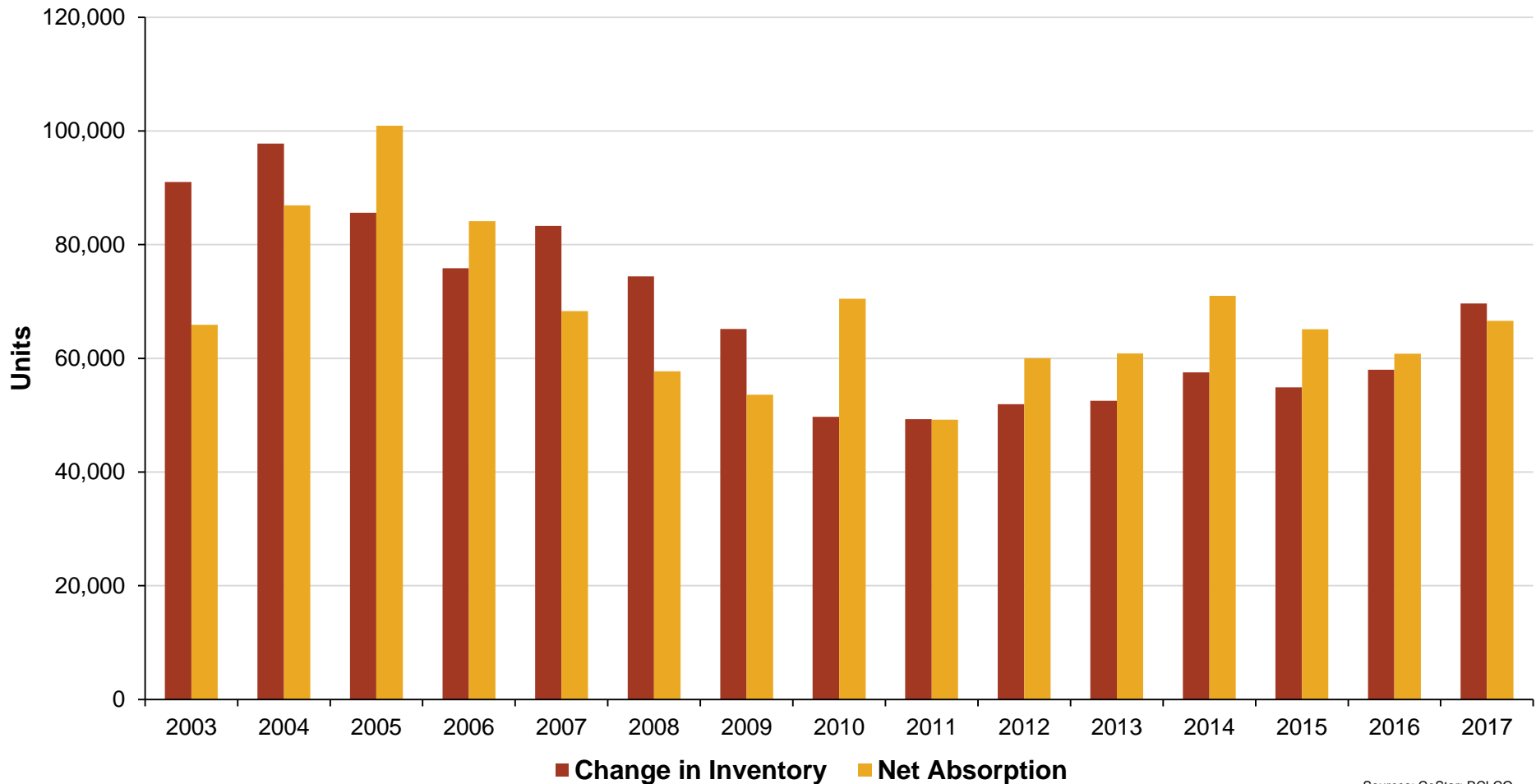
Real Markets: Operations

Capital Markets: Pricing

Absorption has outpaced new deliveries

In seven of the eight years since the great recession

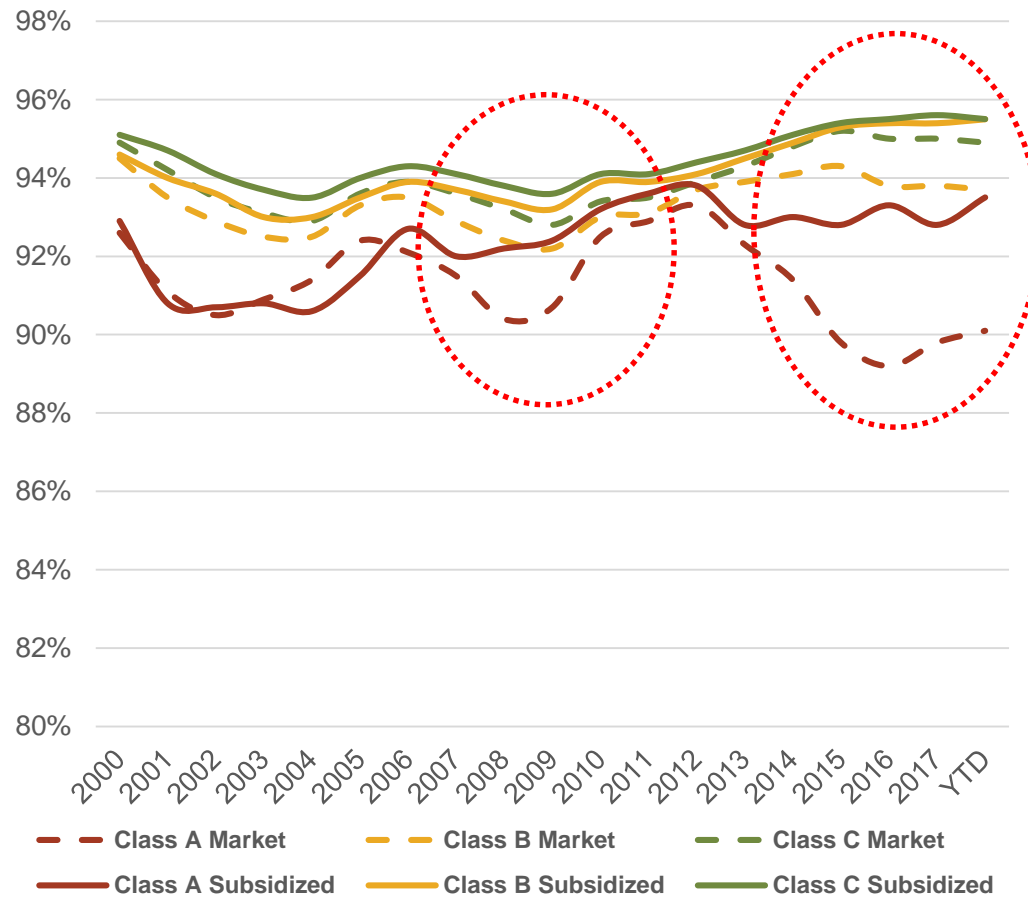
Deliveries and Absorption of All Subsidized Affordable Housing, U.S. 2003 – 2017



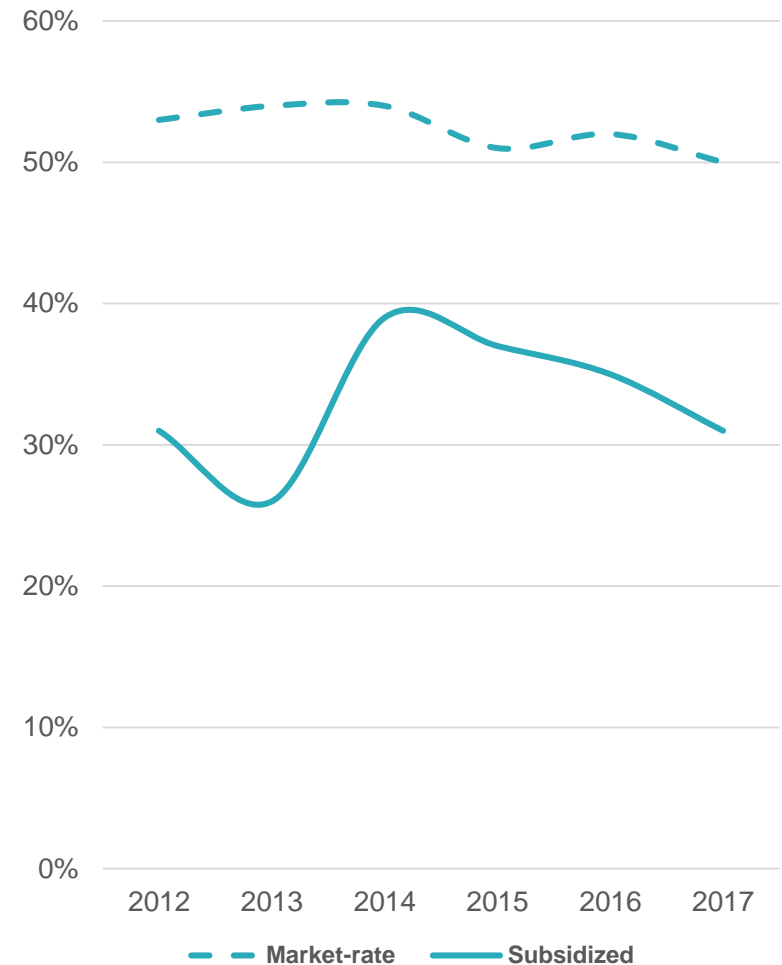
Occupancy advantage over market-rate

Subsidized: persistently higher occupancies & lower turnover

Average Occupancy Rate of Market-Rate vs. Subsidized Properties, by Class 2000 – 2017



Tenant Turnover Rate at Individually-Metered Market-rate and Subsidized Properties 2012 - 2017

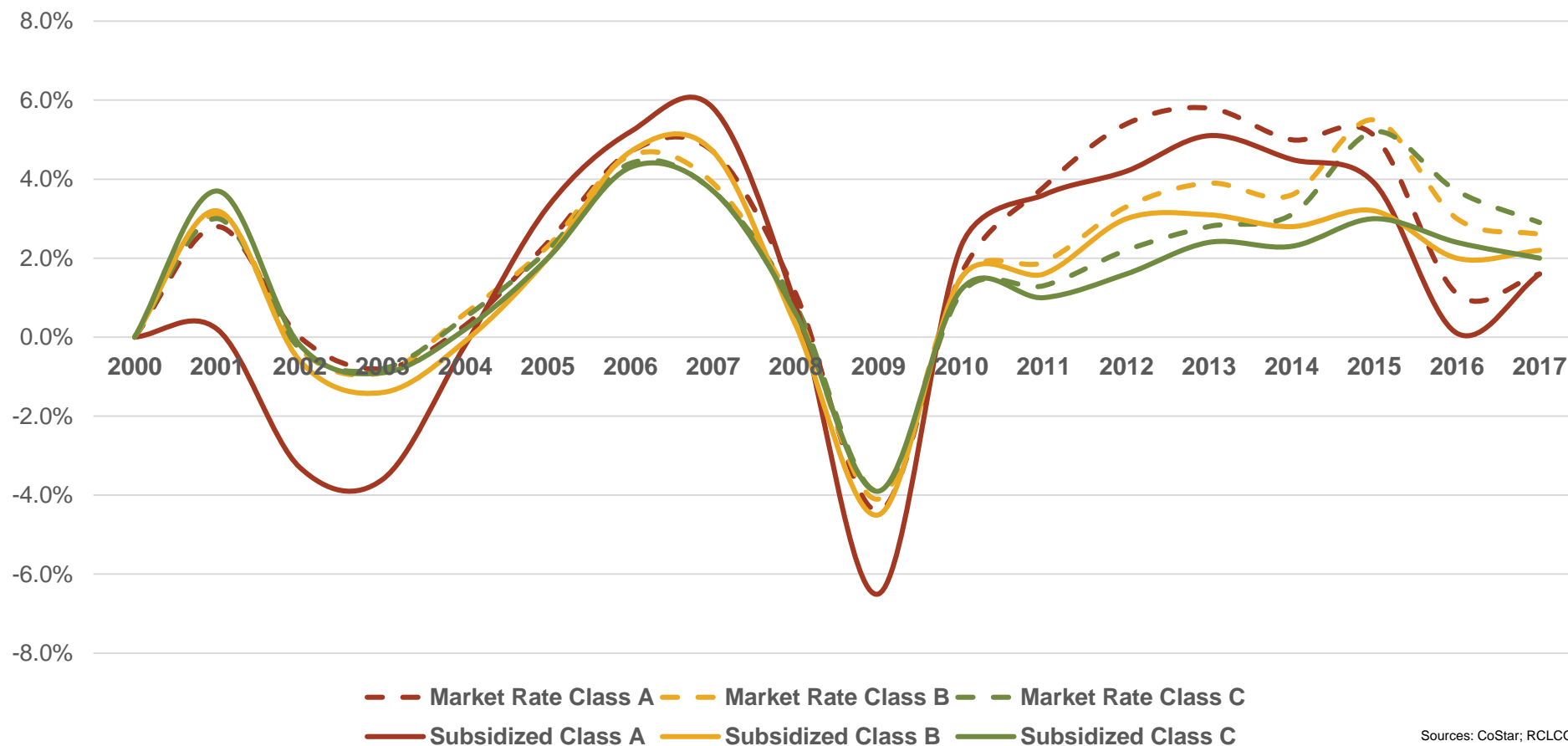


Sources: CoStar; National Apartment Association Income and Expenses Report; RCLCO

Rent growth lower, but still positive

As is expected of low-income, rent-restricted units

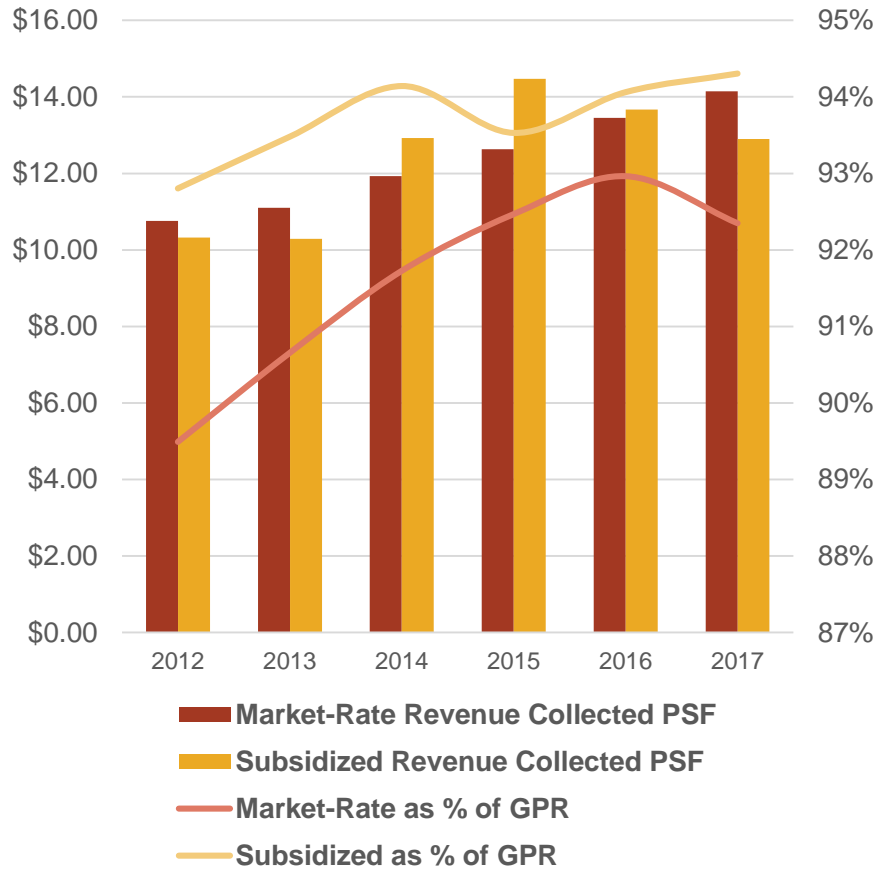
Rental Growth Rate of Market-rate and Subsidized Affordable Housing, by Class 2000 – 2017



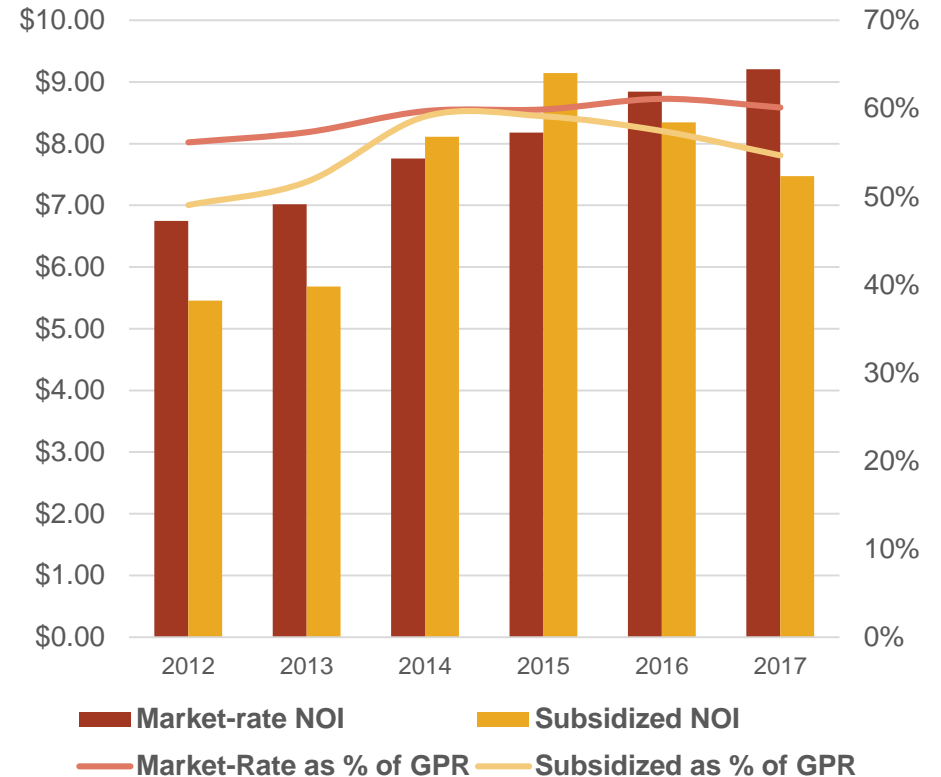
Per-square-foot revenues and NOI similar

And revenue as a *share* of the gross potential is much higher

PSF Revenues and Revenues as a % of Gross Potential Revenue at Market-Rate and Subsidized Properties 2012 – 2017



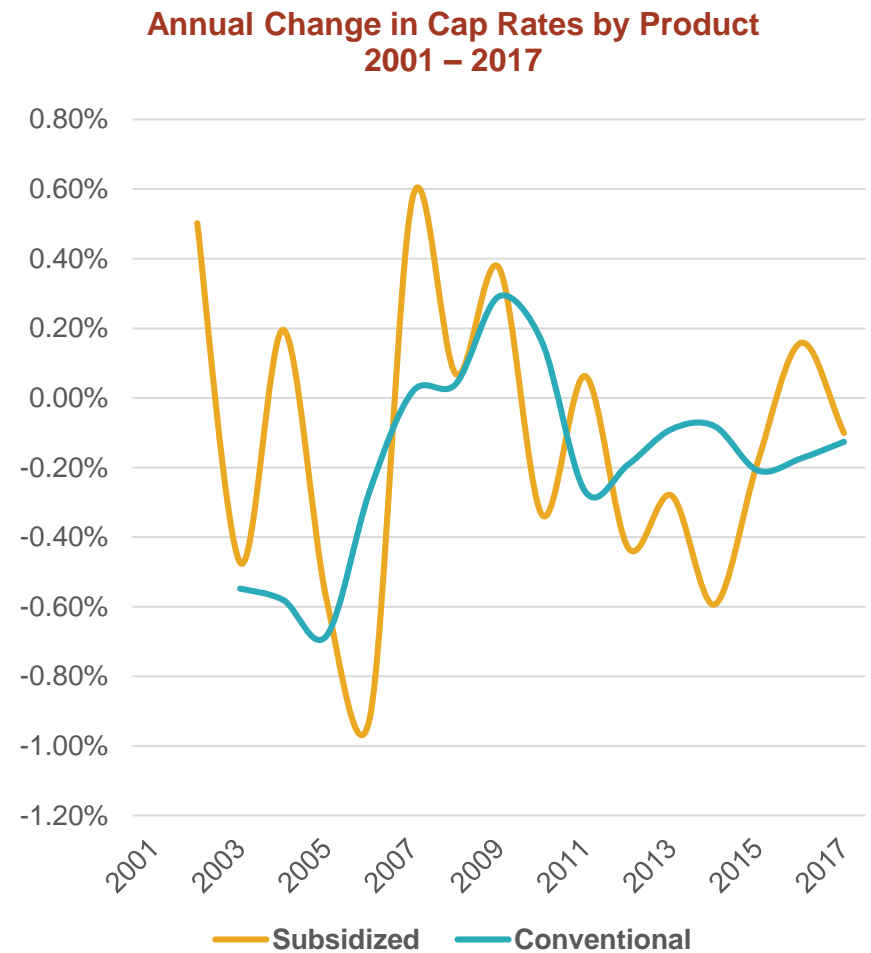
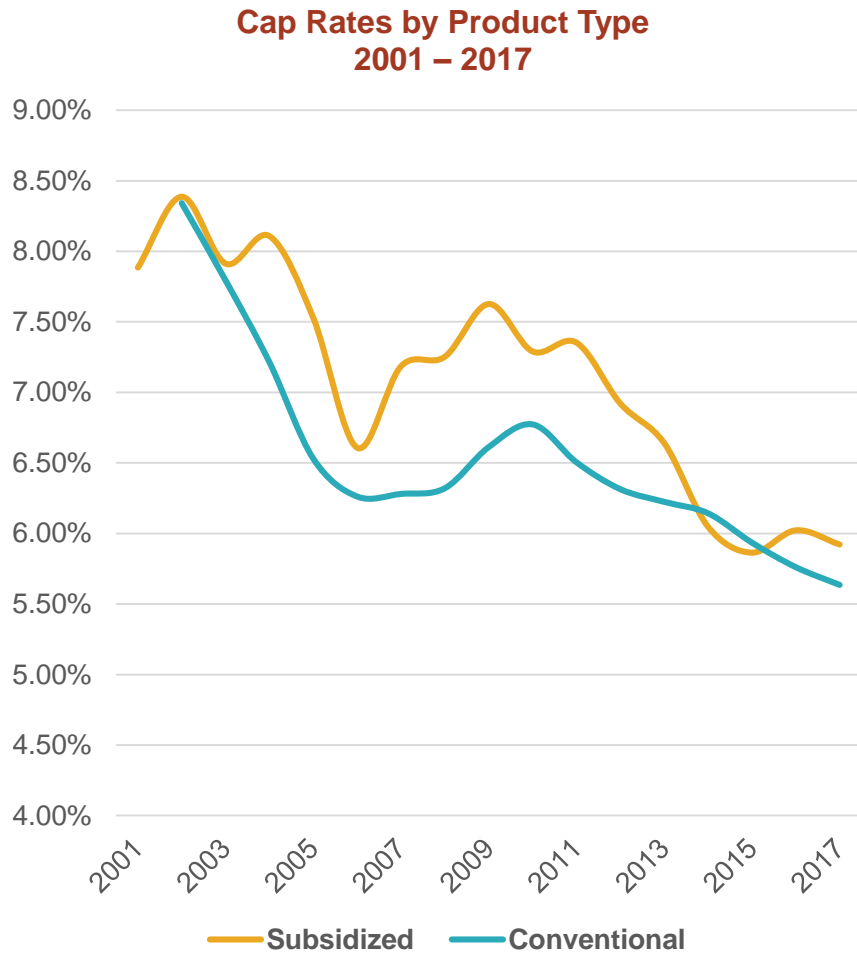
PSF NOI as % of Gross Potential Revenue of Market-rate and Subsidized Housing 2012 – 2017



Sources: National Apartment Association Income and Expenses Report; RCLCO

Cap rate spread has tightened

Cap rate volatility still higher (due to smaller sample)



Sources: Real Capital Analytics; RCLCO

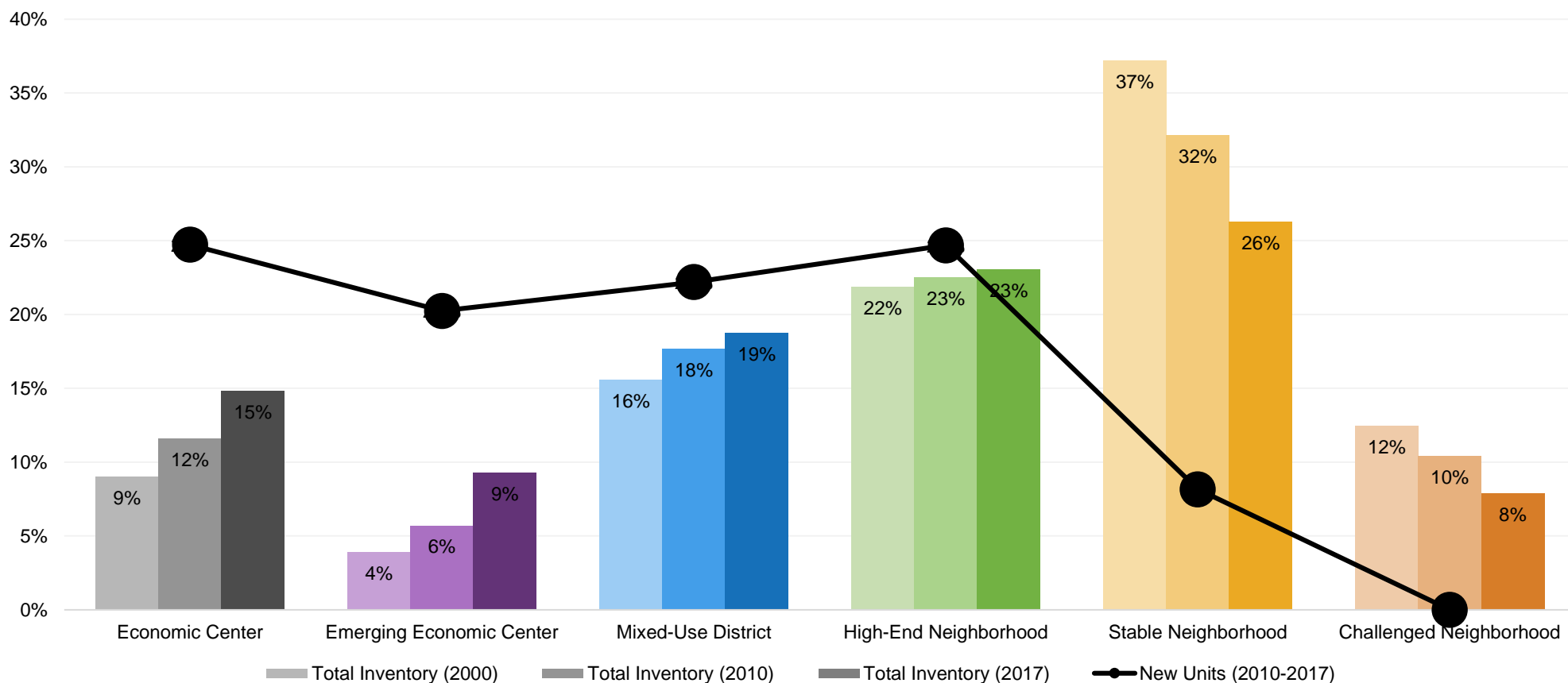
III. Fundamental Drivers

Eroding Supply
Growing Demand

Changing dynamics of rental housing more broadly

Housing being added disproportionately in high cost locations

Distribution of New and Total Rental Apartment Inventory by Urban Neighborhood Type, 2000-2017; Top 50 MSAs

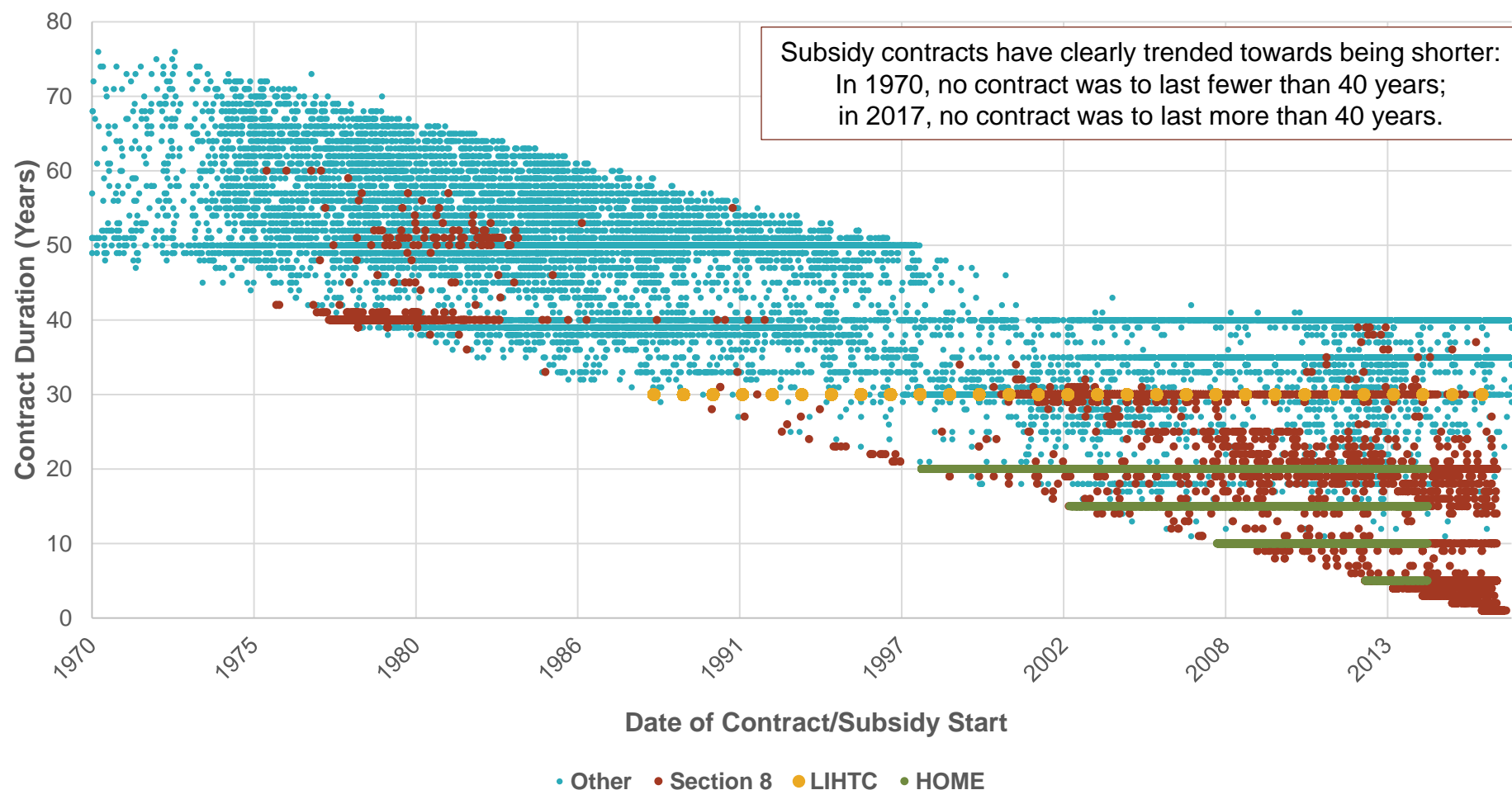


Sources: RCLCO; Axiometrics

Lifespan of subsidies has become shorter

Impending rate of subsidy expiration will be unprecedented

Duration of Housing Subsidy Contracts Over Time 1970 – 2017

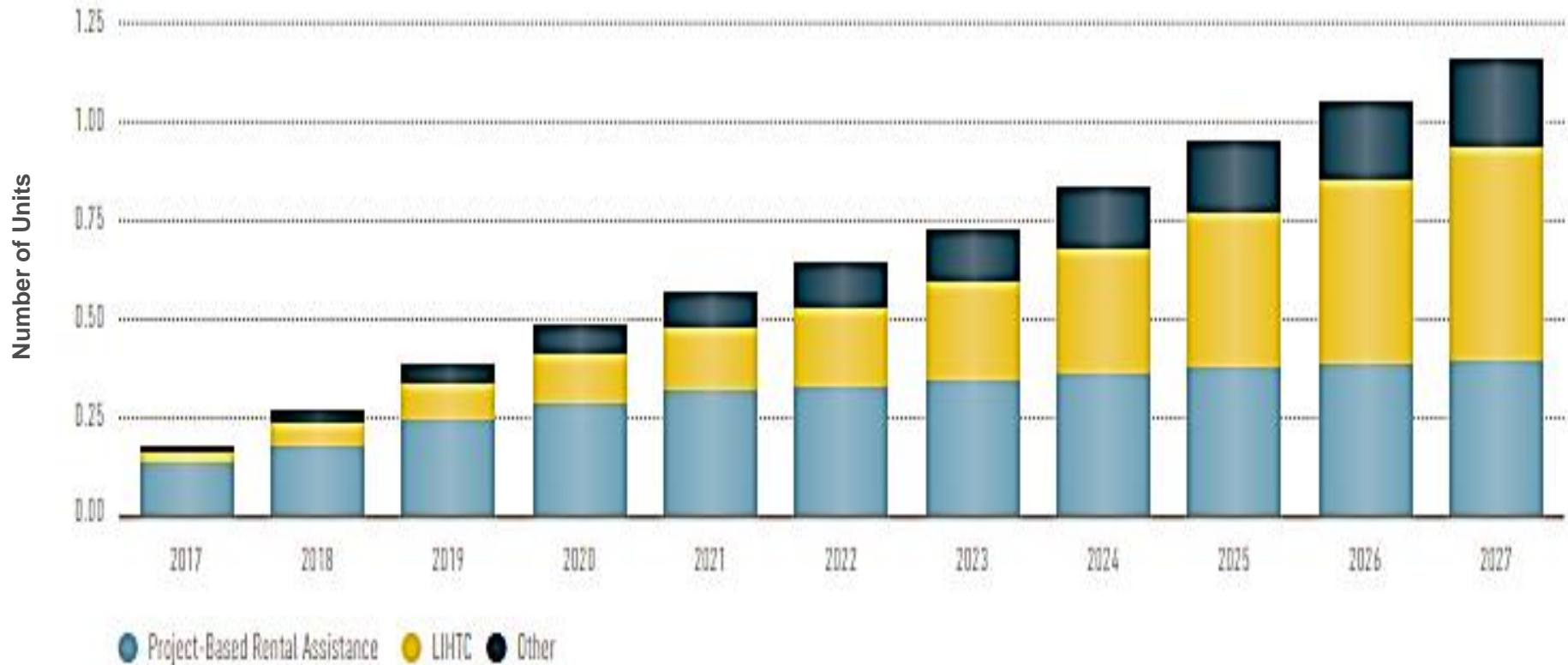


Sources: National Housing Preservation Database; RCLCO

Existing supply is eroding

Units funded by tax credits set to expire most rapidly

Cumulative Units with Expiring Affordability Periods (Millions) 2017 – 2027

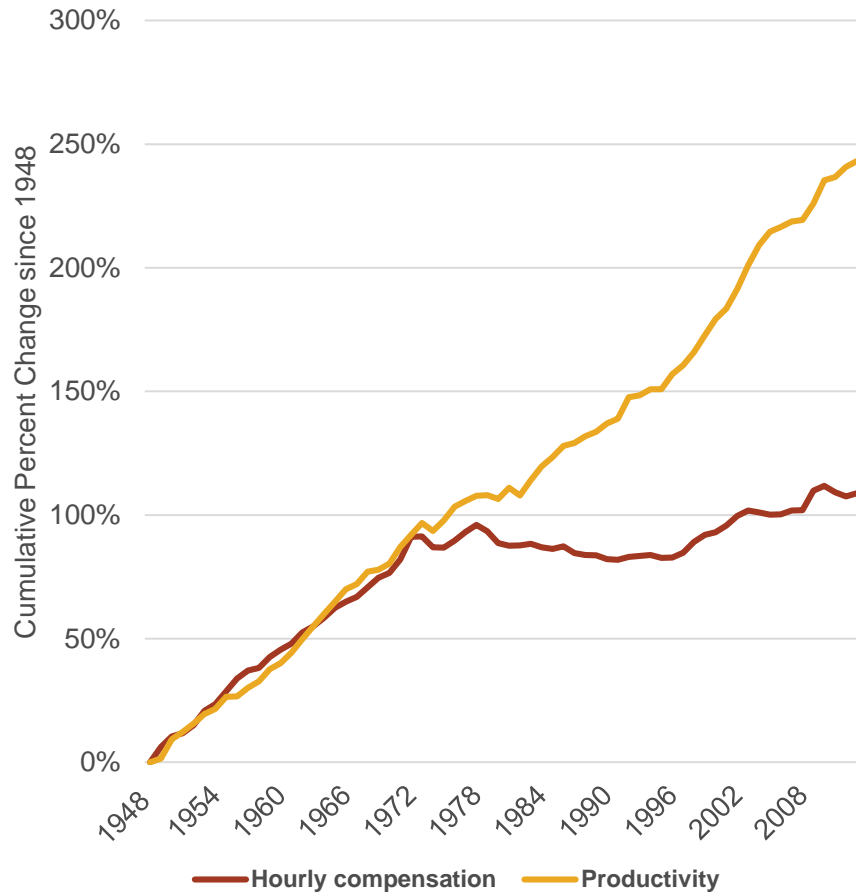


Source: Joint Center for Housing Studies 2017 tabulation of National Housing Preservation Database data, as of January 1, 2017.

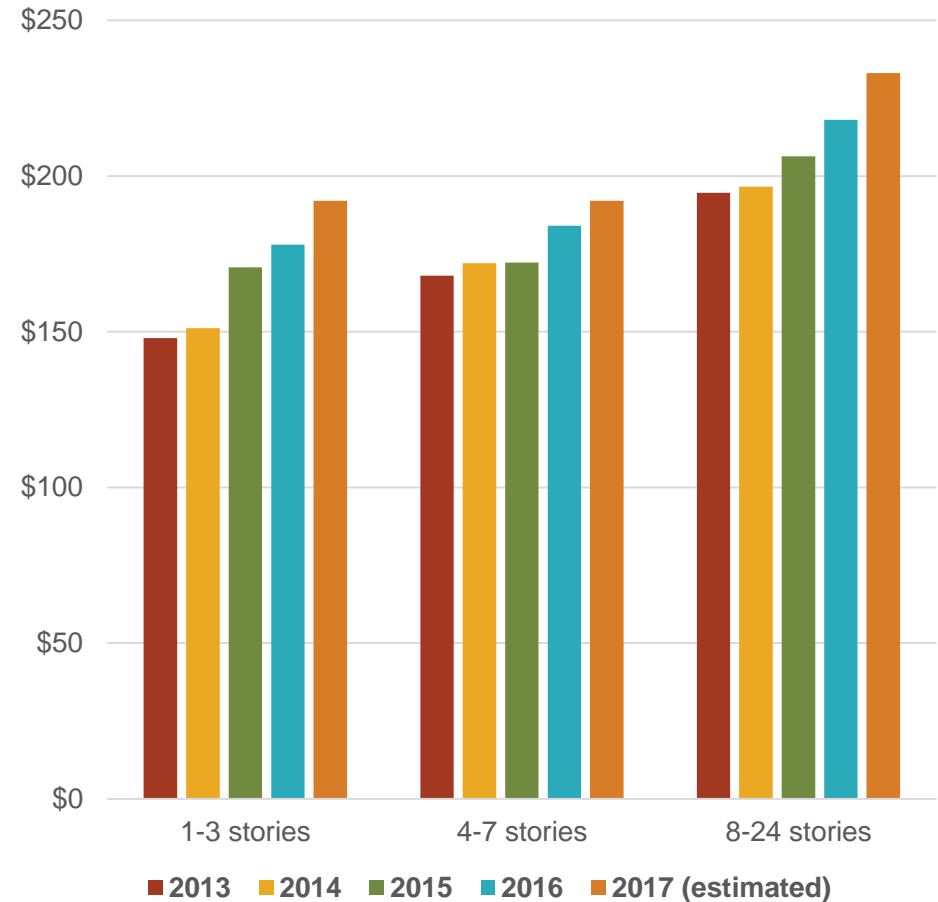
Hourly wages have stagnated

Meanwhile, development costs rising – pushing rents

Percentage Increase in Labor Productivity
and Hourly Wages 1948 – 2013



Development Costs PSF for Building Type
2013 – 2017 (estimate)

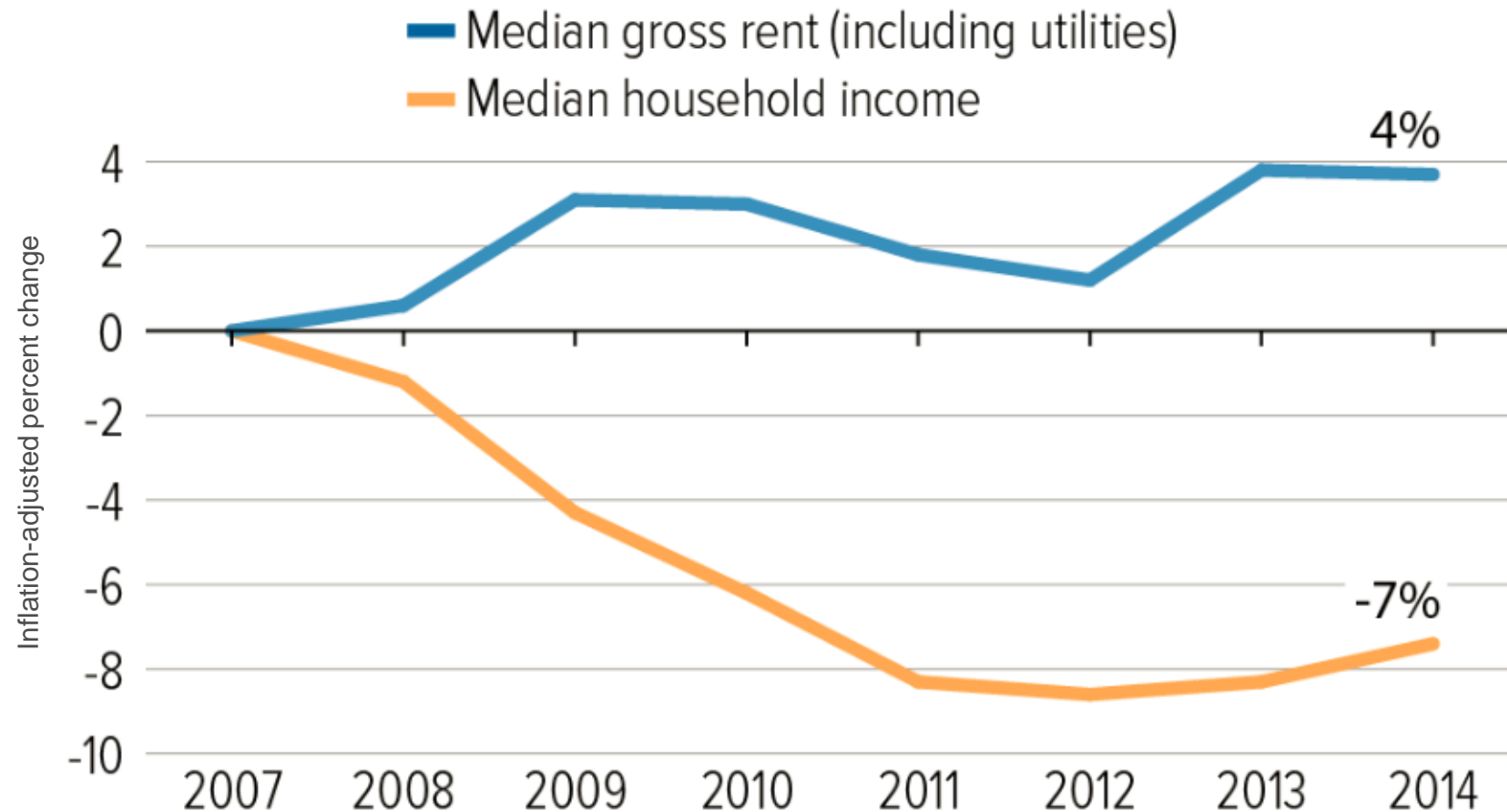


Sources: Bureau of Labor Statistics; Fannie Mae account of RSMeans data; RCLCO

Gross rents outpace household incomes

Reflecting costs of development and wage stagnation

Percent Change in Median Gross Rent and Median Household Income 2007 - 2014

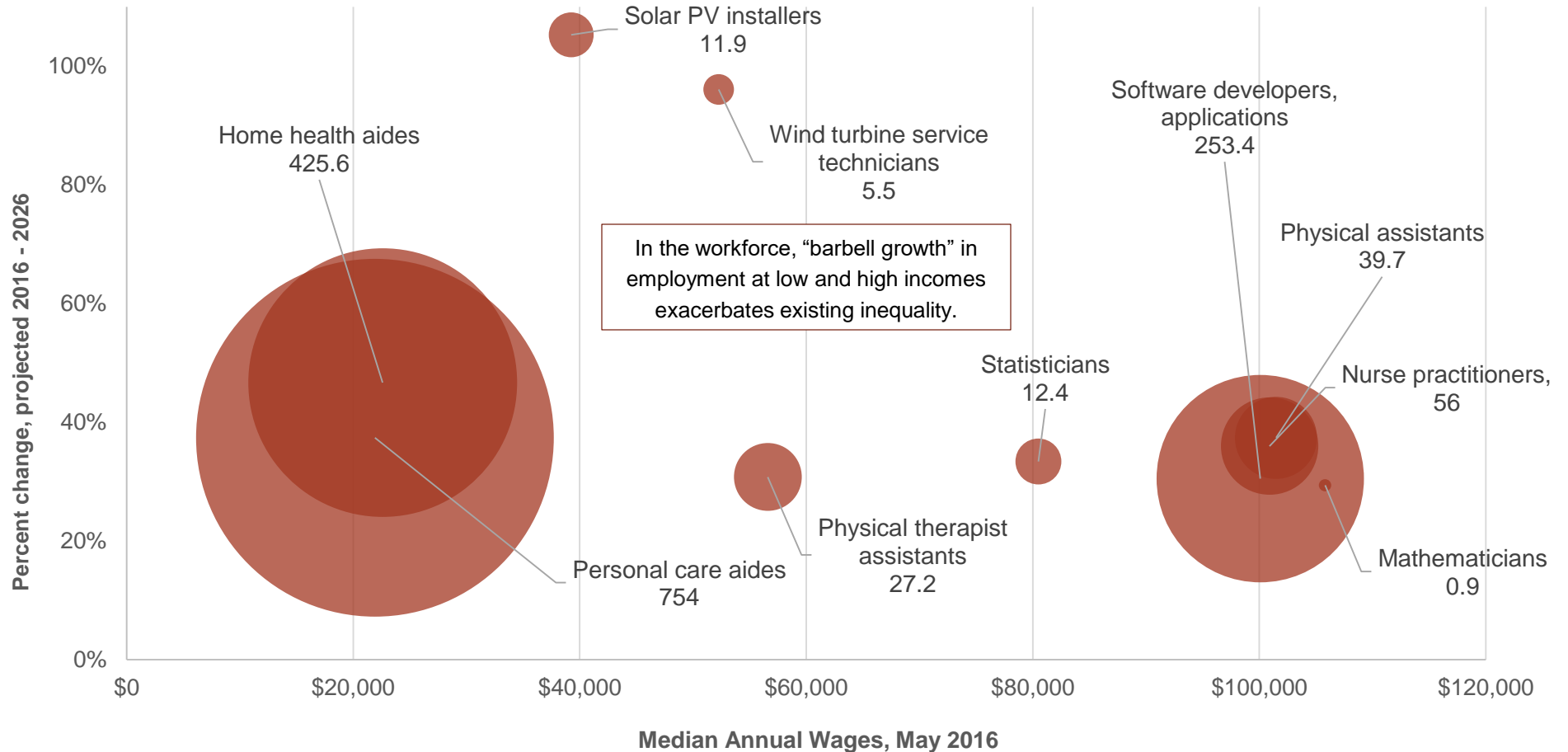


Source: Center on Budget and Policy Priorities analysis of Census ACS data

Most new demand from low-income renters

Fastest-growing jobs over next decade earn ~\$22,000

Ten Fastest-Growing Occupations (Occupation, Number of New Employees in Thousands) 2016 – 2026



Sources: Bureau of Labor Statistics; RCLCO

Report prepared by RCLCO
For
Urban Land Institute
Terwilliger Center for Housing