Affordable Housing Equity Market Update

January 14, 2021

Contents:

I. Summary
II. Outlook
III. Underwriting
IV. Income Averaging
V. Portfolio Composition
VI. Rent Collections
VII. Consolidated Appropriations Act, 2021 & COVID Relief
VIII. Implications for LIHTC & Affordable Housing
IX. LIHTC Pricing Outlook
X. Fund Level vs. Property Level Pricing Trends
XI. National Funds
XII. California Regional Funds
XIII. State LIHTC
XIV. Secondary Transactions
XV. Interest Rate Environment: 10-year U.S. Treasury & Corporate Bonds
XVI. Preservation & Workforce Housing Funds
XVII. CRA Reform & Modernization

Friends & Colleagues,

First and foremost, we hope this January finds you safe and healthy as the global pandemic drags on. The intent of this newsletter is to provide our investor and syndicator clients a market update with respect to low-income housing tax credit (LIHTC) funds, and to a lesser extent, preservation and workforce housing funds. New for this issue, we will use *italics* for text that has been carried forward from previous issues. This should make it easier for regular readers to quickly look for what's new while providing important context for readers new to the newsletter, or the industry.

As always, this update is a collaborative effort with our colleagues at Beacon Hill Capital. Together, Strategic Tax Credit Investments and Beacon Hill Capital represent nearly a dozen affordable housing syndicators of various sizes, including both for-profit and non-profit sponsors. Combined, our syndicator partners account for more than 50% of the syndicated LIHTC market. Broad market representation is the foundation of our information-based approach to the brokerage and advisory services we provide, and it is the basis of the commentary that follows.

For LIHTC funds, our primary focus is on multi-investor fund pricing, yields and trends. We also consider pricing across the entire market, including proprietary funds, guaranteed funds, secondary sales, and direct investor activity.

In the context of this newsletter, preservation funds (or naturally occurring affordable housing (NOAH), and workforce housing funds are non-tax advantaged multi-family real estate equity funds generally comprised of Class B and C properties or developments. Investments in these funds may qualify under Regulation H as public welfare investments (PWIs) by targeting low- to moderate-income households, which can help attract equity from CRA investors. These types of funds fall along a spectrum as to how oriented they are toward PWI criteria. In terms of portfolio composition, some include a component of new construction workforce housing while others do not.

This issue follows our July 2020 newsletter which, along with previous newsletters, are available on our website: StrategicTaxCreditInvestments.com

We hope you find this update informative and useful and we welcome your comments and perspective.

Summary

The LIHTC market was remarkably stable in 2020 despite the global pandemic. Looking ahead, an increase in the supply of credits and somewhat constrained investor demand indicates that yields will likely trend upward in the first half, though not dramatically.

As investor demand is still down slightly from pre-pandemic levels, yields available to the largest investors have continued to improve as syndicators compete for large, anchor investors. In California, yields have continued to trend up and may rise further with additional credit supply coming on-line as discussed below. Nationally, there will continue to be solid demand for transactions that underwrite well in a pandemic environment with little demand for those that do not. This continued application of higher underwriting standards, a so-called "flight to quality," should constrain the upward yield trend.

The "4% fix", with respect to tax-exempt bond financing, refers to the change from a floating rate calculation, recently in the low 3% range, to a permanent 4% fixed rate to determine the amount of credits associated with those transactions. The 4% fix was part of the year-end omnibus spending package and it has several implications for the industry. As a long-time policy goal of industry advocates, it will improve project feasibility, and create more affordable housing. It is also likely to lower average hard debt, and help to offset the diminished availability of soft money from state and local sources. However, the transition to the new fixed rate for eligible transactions will likely delay some fund closings early in the year as syndicators have to renegotiate some transactions and adjust portfolio compositions. **More broadly, the move to a 4% fixed rate will increase the total supply of tax credits going forward.** More on that below.

Outlook

While vaccines have brought hope for an end to the pandemic, **we believe that 2021 will look a lot like 2020. Many of the issues that the housing industry has been working through will continue to be underwriting and portfolio concerns in 2021.**

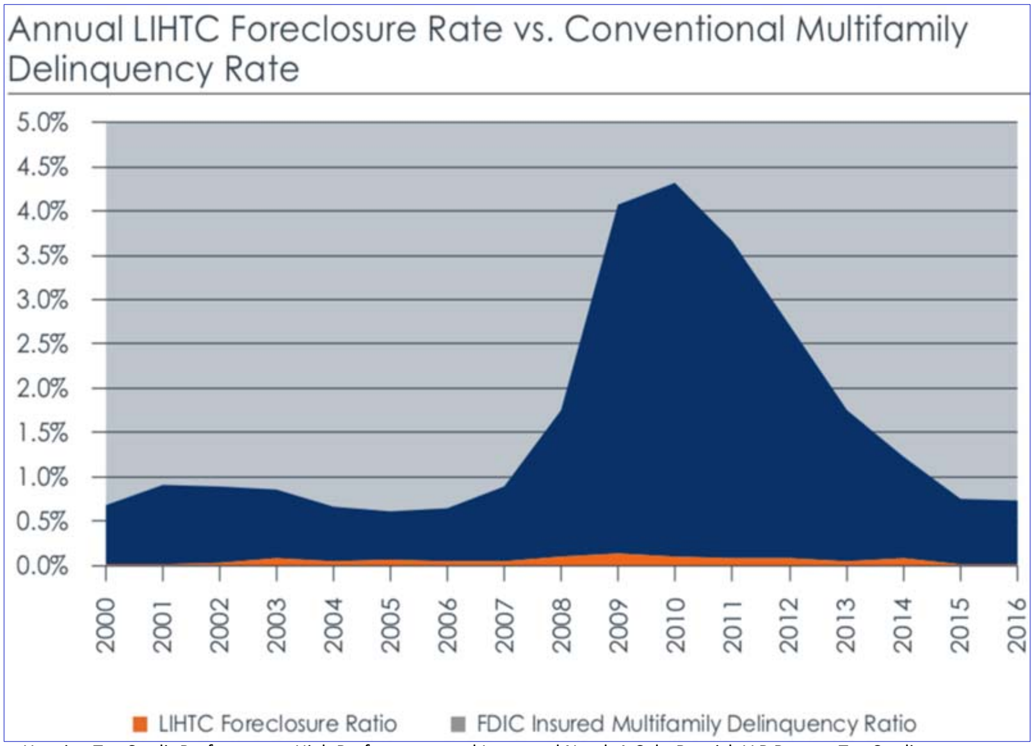
The good news is that we may currently be at the peak of the pandemic crisis and the economy will strengthen as the year goes on. We anticipate a strong and proactive response by the incoming Administration and Congress to getting the pandemic under control as well as providing economic stimulus which, in turn, should stimulate demand for tax credits.

Before the November election when there was talk of a potential Democrat "sweep", speculation of tax reform, specifically higher corporate tax rates, gained favor. As investments in LIHTC would be a hedge against increasing corporate tax rates, we saw a small shift in investor behavior on the margin. While the Democrats now have control of Congress by the narrowest of margins as a result of the Georgia run-off elections, some investors are beginning to consider the possibility of rising corporate tax rates again. For example, a sensitivity analysis on a national fund currently in the market resulted in the after-tax yield rising from 6.00% to 7.62%, when assuming a 28% tax rate

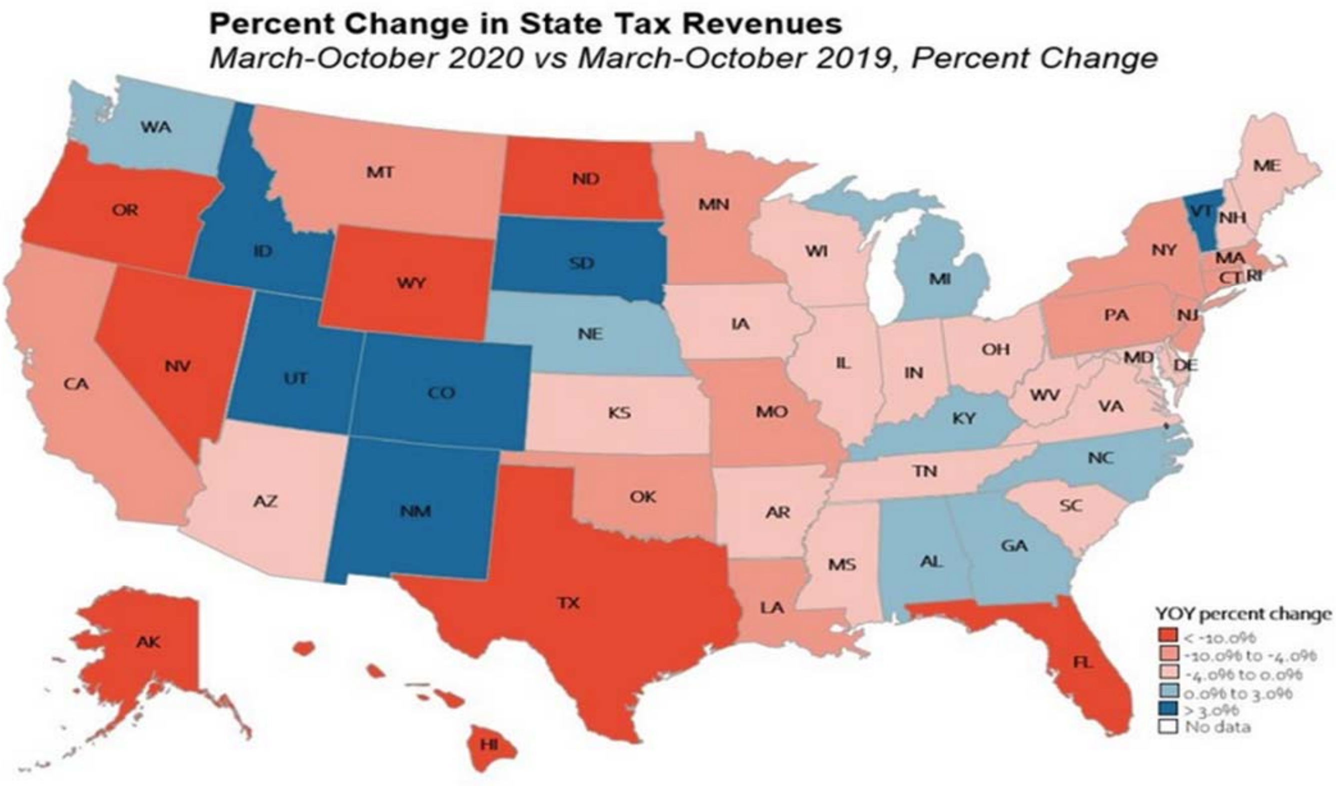
ESG (Environmental, Social and Governance) initiatives have increasingly become part of corporate culture and long-term strategy, and we believe that investments in affordable housing could become a core component of those initiatives. As a result, we view long-term demand trends as positive and anticipate demand for LIHTC investments to exceed pre-pandemic levels as the U.S. and world economy recovers in 2021 and beyond.

The affordable housing industry, and the market for LIHTC investments specifically, continues to demonstrate resiliency in times of economic distress. Affordable housing fundamentals remain strong with demand for quality affordable housing far exceeding supply nationally. For LIHTC properties in particular, the underlying assets have consistently performed well during economic downturns. Investor benefits based on tax credits and tax deductions, rather than cash flow and operations, remain relatively steady unless operational challenges persist for several years in a row. Having said that, the unprecedented fiscal stimulus by the federal government, including the most recent $900 billion, has at least temporarily blunted the impact that the massive increase in unemployment would otherwise have on property operations.

During 2020, many states forecasted drastic shortfalls in revenue due to the economic slowdown. As we pointed out in July, it is important to note that state and local governments often contribute to the financing of affordable housing at the project level, closing funding gaps with sources such as grants, TIF loans, real estate tax abatements, etc. Many states also have their own state level low income housing and historic preservation tax credit programs. While we hope any eventual impact to affordable housing resulting from state and local budget shortfalls will be limited, we will continue to monitor potential impacts to the LIHTC industry.



Housing Tax Credit Performance: High Performance and Increased Need. A CohnReznick LLP Report. Tax Credit Investment Services 2017: https://www.cohnreznick.com/insights/housing-tax-credit-monitor



Source: State Tax and Economic Review Project, State and Local Finance Initiative, Urban Institute.
https://www.urban.org/policy-centers/cross-center-initiatives/state-and-local-finance-initiative/projects/state-tax-and-economic-review/subscribe
Notes: For Nevada data is through September; for New Mexico data is through July; and for Wyomoing data is through June.

Underwriting

This data indicates that COVID-19 will continue to impact the economy and our industry. It follows that syndicators will have to continue to respond to the impact of the pandemic on the underwriting of new transactions and existing portfolios. As a result, it makes sense to recap the underwriting challenges we highlighted back in July.

As a result of the pandemic, all of our syndicator partners have adjusted their policies and procedures with respect to underwriting new transactions and reporting on existing portfolios. While there were instances of construction work stoppage in various parts of the country, all 50 states now designate the construction of affordable housing as "essential". As a result, new construction and rehabilitation of existing projects has not been as negatively impacted as initially feared. Some syndicators have added three months to all construction, lease-up and credit delivery schedules, whereas others are evaluating timelines on a transaction by transaction basis.

Syndicators continue to monitor and provide sensitivity analysis to investors on monthly rent collections in the context of existing budgets, continued HUD and USDA rental assistance payments and operating reserves. Area Median Income (AMI) projections have also become a concern. AMI governs maximum allowable LIHTC rents, and a prolonged recession could result in flat or negative AMI trends in some locations.

Income Averaging

A more recent underwriting focus for investors has been properties that elected income averaging, or the Average Income Test (AIT). AIT was established as a new minimum set-aside election for LIHTC projects by The Consolidated Appropriations Act of 2018, but only recently have started to be included in funds.

Historically, there were two main set-asides with respect to tenant income qualifications, commonly known as the 20-50 and 40-60 tests. The first, where at least 20% of the units in a development are set-aside for households with incomes at or below 50% of AMI, or the second, where at least 40% of the units have to be set aside for households with incomes at or below 60% of AMI.

AIT creates a third set-aside option which the developer or local general partner can elect where at least 40% of units are rent restricted. The units can be restricted to AMI levels between 20% to 80% of AMI in increments of 10%. The average AMI designation of all rent restricted units must be at or below 60% AMI. The intent of this new set-aside was to increase the qualifying household income range to increase the feasibility of some projects.

In the original two set-asides, if a unit falls out of compliance due to over income tenants but otherwise complies with the set-aside, the project is only at risk of losing the credits associated with the percentage of units that are out of compliance.

The current underwriting challenge for AIT stems from a recent notice of proposed rulemaking from the IRS which lead to concerns regarding potential recapture due to noncompliance. On October 30, 2020, the IRS released a ruling indicating that if an AIT project's average household income exceeds 60% of AMI based on the average of all qualified units, then the project runs the risk of **losing all credits** allocated to the project regardless of whether the test of 40% of the units averaging 60% AMI is met. While the IRS included provisions allowing developers to take mitigating actions and amend an AIT project that has fallen out of compliance, this 'cliff event' risk has also resulted in investor pushback and required syndicators to mitigate the risk with underwriting solutions.

LIHTC industry groups have looked very unfavorably on this latest ruling and have submitted comments to the IRS in an attempt to amend the ruling and restore what they see as the original intent of the AIT set-aside. We anticipate seeing increased scrutiny on AIT projects and will keep an eye on future developments in regards to the latest ruling.

Portfolio Composition

The pandemic has created some shifts in investor preferences with respect to fund portfolio composition, some of which are counter to historical trends.

For example, the focus on subsidy appropriation risk seems to have shifted to favor subsidized units as investors feel more comfortable with properties receiving government supported rental payments.

Small and rural markets, which have generally been impacted less by the virus, with some notable exceptions, have become more attractive to investors. Senior properties, characterized predominately by tenants on fixed incomes, have been posting slightly better rent collections. Conversely, the senior properties are both much more at risk to the Coronavirus and have a more sensitive population with respect to conducting rehabilitations with tenants in place.

Investor sentiment seems split with respect to new construction versus rehabilitations. On the one hand, new construction's longer timeline to completion might miss much of the impact of the pandemic. Whereas rehabilitations of existing properties face greater near-term construction challenges, but benefit from having qualified renters in place if the economic recovery is prolonged. As the pandemic wears on, investors are increasingly focused on deal terms at the property level, and in general, deal terms from the investor's perspective have improved. There is still solid demand for clean transactions that adhere closely to underwriting guidelines, but transactions with underwriting challenges are finding little traction.

Rent Collections

As more than ten million Americans remain unemployed relative to pre-pandemic levels, occupancy and rent collections will remain a focus until employment rebounds.

During 2020, across a range of syndicators, we consistently saw initial monthly rent collections range from 85-95% of historic averages and full month collections within a few percentage points compared to the same months in the prior year for both LIHTC and preservation/workforce housing. Again, with respect to LIHTC property operations specifically, investor benefits consisting of tax credits and tax losses are historically insulated from short-term changes in property operations.

Consolidated Appropriations Act, 2021 and COVID-19 Relief

The economic impact of the pandemic has been blunted by the largest ever U.S. government fiscal intervention, now totaling nearly $4 trillion. To put that number in context, the Marshall Plan, put in place to help Europe rebuild after WWII, was roughly the equivalent of $135 billion in today's dollars, and distributed over four years.

At the time of our July newsletter, additional fiscal stimulus seemed imminent, but took until the end of December for Congress to act and the President to sign legislation providing additional fiscal support. The resulting legislation includes $284 billion for the Paycheck Protection Program (PPP); $25B in rental assistance for households at or below 80% of AMI with priority given to households at 50% AMI or below, and for individuals who have been unemployed for 90 days or more. Ninety percent of the funds are for housing related financial costs including rent, utility payments, etc. Households can receive assistance for up to 12 months. The aid includes $600 in direct payments to households and $300 per week in enhanced unemployment assistance. These funds will be distributed by the U.S. Treasury to individual states based on their populations, but all states will receive a minimum of $200 million. States must deploy the funds by the end of September 2021, or they can be swept by the Treasury and redeployed. It is also important to note that local municipalities will have the ability to add additional requirements that may impact deployment.

Cities Esimated to Receive the Most Rental Assistance

City	Rental Assistance Estimate	City	Rental Assistance Estimate
New York, NY	$554,951,671	San Jose, CA	$68,017,203
Los Angeles, CA	$264,906,003	Austin, TX	$65,162,368
Chicago, IL	$179,328,177	Jacksonville, FL	$60,675,713
Houston, TX	$154,451,855	Fort Worth, TX	$60,547,786
Phoenix, AZ	$111,897,589	Columbus, OH	$59,813,415
Philadelphia, PA	$105,445,398	Charlotte, NC	$58,958,393
San Antonio, TX	$102,995,040	San Francisco, CA	$58,681,534
San Diego, CA	$94,780,619	Indianapolis, IN	$58,337,652
Dallas, TX	$89,436,799	Albuquerque, NM	$53,462,919
Anchorage, AK	$78,737,467	Seattle, WA	$50,169,430

Sources: NLIHC; U.S. Census; Novogradac

NOVOGRADAC®

Implications for LIHTC & Affordable Housing

The legislation included the permanent 4% fix mentioned earlier as well as $1.1 billion in additional credits for disaster areas. The 4% credit for tax exempt bond financed properties had previously been calculated on a floating rate basis and had been well below 4% for a very long-time. Recently, it has been in the low 3% range. The permanent change to a fixed 4% rate has been a long-time goal of the affordable housing industry to improve the feasibility of bond financed transactions and create more housing.

Given that tax-exempt bond transactions have accounted for roughly 40-45% of the annual housing credit market, a 30% increase in the amount of 4% credits (4% vs low 3s) results in an overall increase in supply of approximately 12-13%. Presumably, many projects that did not pencil with a low 3% credit rate may now work with the 4% floor. It remains to be seen if that supply increase will result in a corresponding decrease in pricing, as not all states have historically used all of their bond volume cap. Additional credits will also help make up for declines in other sources of state and local financing that have been drying up over the years, particularly in light of increased budgetary pressures during the pandemic.

In addition, the legislation included a one-month extension of the eviction moratorium through the end of January. While that allows much needed aid to reach households before the expiration, it also puts any extension of the deadline into the hands of the incoming Biden Administration.

Fund Level vs. Property Level Pricing Trends

It is estimated by a number of industry sources that the $25 billion in rental housing assistance may cover only about a third of the estimated back rent due nationally which has been estimated at up to $70 billion. While the economy and employment has rebounded to some extent, economic indicators have been deteriorating as the virus flares nationally and more states and localities adopt tighter restrictions.

It is also worth noting that he LIHTC industry has been lobbying for program changes, including the 4% credit fix, since tax reform went into effect in 2018, when the equity market decreased in size due to the value of losses generated in LIHTC equity investments decreasing following the corporate tax rate adjustment from 35% to 21%. In March of 2018, Congress provided some relief with the temporary increase in LIHTC allocation of 12.5% for 9% credits for 4 successive years, which is set to expire in 2021.

LIHTC Pricing Outlook

As always, we emphasize that there is a range in LIHTC yields across the market. Reasons for this include, but are not limited to, differences in portfolio composition, sponsor strength, load, the use of bridge financing as well as inefficiencies in the market.

In general, investors with CRA needs are less price-sensitive than non-CRA buyers. CRA pricing can apply to investors who require a CRA letter on individual transactions or groups of transactions depending upon their geographic location. As a result, there is often bifurcated pricing in the market.

While the influence the non-CRA component of the equity market has on lower-tier pricing (property level) is limited because it comprises only about 15-20% of the total market, this segment can move the market. When non-CRA investors pull back, fund sponsors who rely on non-CRA investor equity will typically cut fees and raise yields as necessary to obtain the investor equity needed to clear their funds. If this pricing pressure persists at the fund level, ultimately lower tier pricing will follow suit.

Our pricing summary focuses on three specific segments: multi-investor national funds; CRA versus non-CRA; and California regional funds. Below, we discuss the outlook for pricing during the first half of 2021.

Our pricing outlook for the next six months is based on both fund-level and property-level information from syndicators and investors. It is important to look at both because property-level and fund-level pricing do not always move in concert in the short-term. Historically, there has been a pricing lag of at least six months in the LIHTC market.

Tax credit pricing can be somewhat inelastic due to a number of factors including the long project lifecycle from conception to construction, and the protracted negotiations between syndicators and developers over terms and pricing. There is also a lag in feedback from investor demand to resulting adjustments in property-level negotiations with developers.

Federal credit pricing remained relatively stable in the second half of 2020 with a slight downward trend in pricing and slight upward trend in yields. As investors increasingly focused on pandemic-related underwriting concerns, there has been the aforementioned "flight to quality" which contributed to firming prices for the best transactions, while less desirable projects are receiving lower pricing.

To confirm whether fund-level pricing is in sync with property-level pricing trends, we conducted an informal survey of our syndicator partners. Based on the data we received, pricing at the property-level has been flat to down a penny or so from mid-year 2020, but a further decline in tax credit prices is forecasted due to increased supply and somewhat diminished demand from investors, particularly economic investors, in the first half of 2021.

National Funds

At this time, national funds seeking to attract economically motivated non-CRA equity are generally priced in the $0.93-$0.98 per credit range on a fully loaded basis with after-tax QIRRs in the 5.50-6.50% range. This is generally consistent with the pricing we reported in July. Yields for the largest, non-CRA investors have moved up slightly on the latest fund offerings as syndicators compete for the relatively limited number of investors who are willing to make the largest investments in a fund. We anticipate that yields will continue to trend upward in the first half of 2021 given the additional supply of credits (from the 4% fix and credits for disaster areas) and somewhat reduced investor demand at least through Q1. Forces that could temper this trend include increasing competition for the best transactions and investor expectations of an increase in corporate tax rates.

Pricing can fall outside of these ranges based on geographic location of properties, investment size and other special circumstances (e.g. a sponsor replacing a lost equity commitment). At the higher-end of the yield spectrum there are a number of economic investors that will make larger investments to secure premium yields within national multi-investor funds. There are also larger CRA-motivated banks that are making blended investments that mix both CRA selections at lower yields with non-CRA selections to achieve higher overall returns.

Outside mainstream LIHTC multi-investor funds, some investors who require higher returns are willing to invest in funds with higher risk profiles including mixed-income developments, assisted living properties and LIHTC transactions with higher leverage. Currently, we see opportunistic offerings ranging from 6.50% to 8.50% on an after-tax basis.

For CRA-motivated investors, the yield range has generally been between 4.00% for higher demand metropolitan statistical areas and counties to 5.50% for less competitive CRA markets. Overall, we expect this upward trend to continue. There are exceptions to this range as well with some funds offering yields to CRA investors above 5.50%, and even above 6.00%, depending upon the specific composition of the fund and the syndicator's investor base.

Conversely, the most competitive CRA areas (e.g. Bay Area, NYC five boroughs, Boston, Utah, etc.) could hold steady and may still have yields that dip into the 3% range for certain transactions.

One variable affecting the IRR and price per credit ranges above is the amount of bridge financing being utilized by the fund sponsor. In *general, fund bridging became more prevalent as interest rates have declined and arbitrage opportunities have increased. Most national funds assume at least some modest level of bridge financing to manage capital calls, and a number of syndicators use additional bridging to more effectively compete for product, enhance yield and manage investor capital contributions.*

For investors that are focused on the lowest price per credit and little or no bridging, some funds will offer an unbridged investment class option ("cash needs"), which results in a lower IRR.

Conversely, some syndicators offer bridged returns for investors focused on a higher IRR, which generally increases the gross price per credit. These options appeal to different investors based on their internal investment models. It should be noted that the use of bridging by syndicators varies depending on the spread between the cost of bridging and fund yields. It should also be noted that while pre-COVID interest rates were at a record low, some lenders have since increased those rates and required additional underwriting and internal approvals during the pandemic.

California Regional Funds

Due to California's large economy and population, it has always accounted for a relatively large percentage of the LIHTC market. California will also receive roughly $2.6B of the $25B of recently passed rental assistance.

Historically, syndicators have offered California regional funds for three primary reasons: the large number of California transaction, demand from the large number of banks located in the state and the historic disparity in pricing between California transactions and the national average.

Over the last few years, we have reported on the trend of rising yields for California regional funds due to continued increases in the supply of both federal and CA state credits combined with relatively steady demand. California LIHTC supply increased markedly in 2020 from its previous annual benchmark of roughly $2.5B. The CA Assembly Bill 101 and COVID relief bills added $500M of state tax credits and roughly $1.1B of federal credits for the 2020 allocation year for disaster relief from the 2018 wildfires. Additionally, CA received another $80M in disaster relief credits for the 2021 allocation year ($800M over 10 yrs) as a result of the COVID relief package signed in December of 2020. As a result, the combined 2021 California federal & state tax credit market has increased in size significantly since 2019.

As of July 2020, yields ranged from 4.00% IRR in the Bay Area, 4.25%-4.50% in LA/San Diego and 5.00% statewide. While projects in the Bay Area are still commanding premium pricing and fund level offerings remain in the 4.00%-4.50% range, yields have risen to 5.00% in Los Angeles and San Diego, and 5.50%-5.75% in smaller metro and rural areas with premium pricing for large investments ($25M+) at 6.25% and higher.

Now that the pricing differential between national and California regional funds has narrowed substantially, investors can expect to see an increasing amount of California product in national funds and potentially a decrease in the number of CA funds offered overall.

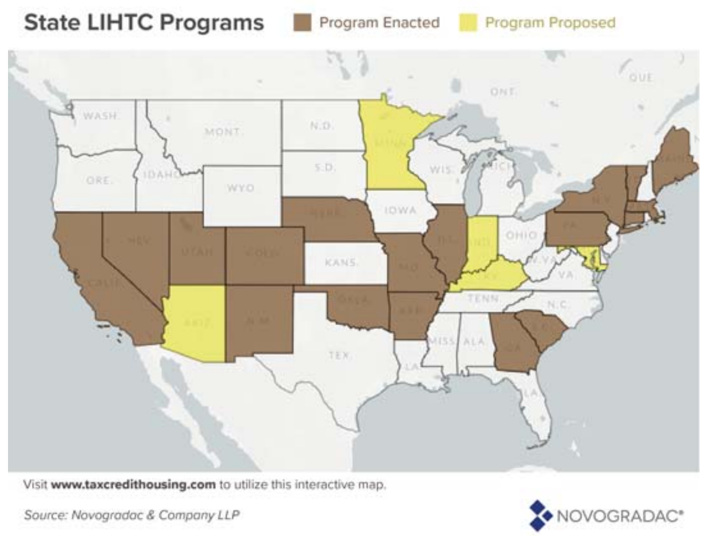
State LIHTC

Due to growing interest from investors in state LIHTC, we've included a summary reference of state LIHTC programs below. Pennsylvania, for example, enacted a state LIHTC program in 2020. Investors often focus on states where the state credit is bifurcatable (can be purchased separately or disproportionally allocated) from the federal credit. States with bifurcatable state LIHTC include: AR, CA, CO, CT, D.C., GA, HI, IL, MA, MO, NM, NY, OK, UT, and VT.

Novogradac & Company LLP is an excellent resource for affordable housing related questions and with their permission, we have reproduced their national map of state LIHTC programs here. States shown in brown have existing state LIHTC programs. States shown in yellow have proposed state LIHTC programs.

To see an outline highlighting the particulars of each state's program, follow this link:

https://www.novoco.com/resource-centers/affordable-housing-tax-credits/application-allocation/state-lihtc-program-descriptions,



Secondary Transactions

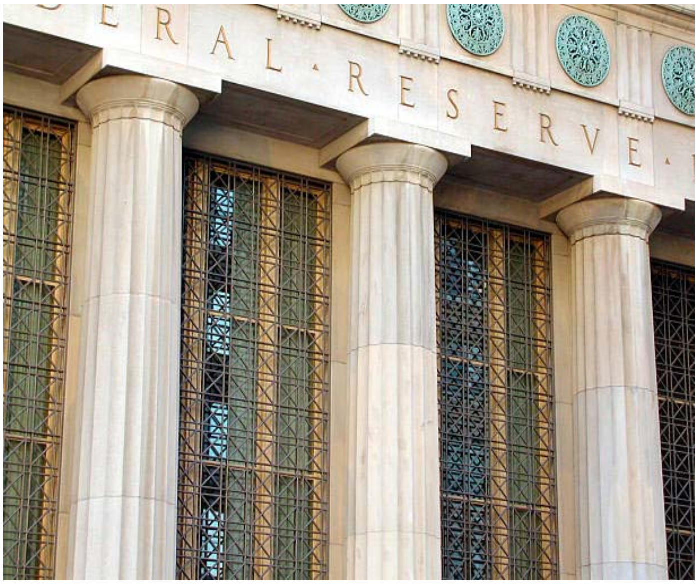
Secondary transaction volume in 2020 was roughly equal to 2019 volume. We were aware of six different sellers with total secondary transactions ranging somewhere between $900 million and $1.25 billion. At this level, secondaries comprise 5%-6% of the total LIHTC market. To our knowledge, all sellers and buyers were banks, and one seller and one buyer accounted for nearly 50% of the total in 2020.

Interest Rate Environment: 10-Year U.S. Treasury & Corporate Bonds

The Federal Reserve has been committed to doing whatever is necessary to support the economy during the pandemic. The response to COVID-19 has been historic. On January 6, 2021, the Federal Reserve's balance sheet was approaching $7.5 trillion[1]. The overnight federal funds rate remains at its record low range of 0.0%-0.25%, and the Federal Reserve has returned to a program of quantitative easing to promote low interest rates. All of this has helped buoy the stock market despite the pandemic's impact on the economy.

Due to the industry's size and specific characteristics, LIHTC yields do not correlate directly with Treasury yields. However, the U.S. 10-Year Treasury bond rate (10-year) remains a common and important reference point. The 10-year crested at 3.20% in Q4 2018 and at the time of our last newsletter in July, the 10-year was at 0.67%. Since the election, the 10-year has moved up as investors anticipate more inflationary pressure from fiscal spending and currently sits at 1.12%. Even with the recent increase in Treasury yields, the spread for LIHTC investments has remained quite favorable and has moved above the long-term historic average.

Over the past 15 years, the spread between LIHTC yields (non-CRA yields in national funds) and the 10-year yields (on an after-tax basis) has ranged widely from a low of approximately 135 bps in 2006 to a high of around 900 bps in 2010. The historic average has been approximately 420 bps. **Using a non-CRA 6.00% after-tax QIRR from the most recent round of closed multi-investor funds, that spread today is above historical norms at approximately 529 bps, a favorable spread not seen since 2010-2013**.



Over the years, a number of investors have indicated that BBB rated corporate bonds may be the best credit proxy for LIHTC investments. The spread between LIHTC yields has also trended favorably against BBB's. **Historically, LIHTC yields have been approximately 300 bps over BBB's** after-tax equivalent. Back in March of 2020, the BBB index spiked to around 5.50%, but after the Fed's actions stabilized market liquidity issues, BBB's returned to their downward trend. As of January 6th 2021, BBB's sit at 2.16%, **the resulting after tax equivalent spread to LIHTC has increased to 429 bps.**

Please see our attached exhibits for graphical representations of our yield data.

[1]https://www.federalreserve.gov/monetarypolicy/bst_recenttrends.htm

Preservation & Workforce Housing Funds

Preservation funds have generally mirrored the pricing and underwriting trends we've been discussing for the LIHTC market. That is to say, that pricing has improved and yields rose modestly over the past twelve months. There has been a similar flight to quality transactions and somewhat decreased investor demand. We expect returns and demand to follow the broader trends we have been discussing for 2021. Occupancy and rent collection trends have been similar as well.

Preservation funds constitute a segment of the multi-family market that is typically comprised of existing, older multi-family rental properties with rents at or below 80% of area median income (AMI) which may or may not have some form of government subsidy, and generally cater to renter households with incomes at or below 80% of median income.

Over the last five years, the number of these funds have proliferated and pricing and terms have started to coalesce. The fund sponsors range from those with stated missions to preserve affordable housing, to those that see value-add plays for older multi-family real estate with strong occupancy and cash flow history.

These funds have different investment models (e.g. acquisition versus joint venture) and sourcing strategies (existing developer networks, on-market transactions, off-market transactions, etc.) and fall along a spectrum as it relates to qualifying as a PWI. Currently, banks make up the majority of investor equity as investments in some of these funds qualify for their CRA investment test (and lending test if also providing debt to the fund). Other investor cohorts include a limited number of insurance companies as well as endowments, foundations, family offices and high net worth individuals. Investments by insurance companies have been limited presumably because of risk-based capital charges relative to returns, but interest seems to be increasing.

Unlike LIHTC funds where properties are largely specified to the fund prior to investor equity closing, preservation funds are typically less specified during the marketing period. As a result, CRA investors may have to get comfortable making capital commitments without specific properties for CRA identified at closing. Subsequent geographic CRA targeting by the fund sponsor is often done on a best-efforts basis.

We currently work with a number of fund sponsors and, similar to the LIHTC market, pricing appears to have adjusted downward in the wake of the pandemic. According to one of our sponsors, they were seeing an uptick in the number of available transactions and a 5-10% downward price adjustment for transactions with a value-add strategy (i.e. strategic renovation to maximize net operating income) in 2020. In contrast, they reported increased demand for properties with government rental assistance and strong "core" transactions (i.e. the best properties in the best markets). Investor demand softened somewhat during 2020. We saw fewer funds and somewhat smaller fund sizes in 2020 and expect a similar environment in 2021. Partially offsetting the more conservative approach to value-add strategies is the availability of significantly lower mortgage rates, particularly HUD (Fannie/Freddie) debt.

Across these sponsors, multi-investor fund sizes range from $50 million to $1.5 billion with $100-200 million being more typical. Preferred returns have generally been in the 7.00%-8.00% range on a pre-tax basis with total returns in the 10.00%–14.00% range. We are assuming yields may continue to trend up, though not dramatically, in the first half of 2021.

Rent collections for preservation portfolios were also down somewhat, about 5%-10%, but again less than feared at the outbreak of the pandemic. Similar to LIHTC properties, the relatively modest loss in rent collections is due to support from the Payroll Protection Program, enhanced unemployment benefits, and the fact that a large percentage of tenants are classified as "essential" workers. As highlighted earlier, the specter of declining rent collections still looms for 2021 without additional federal fiscal support. While the eviction moratorium is set to expire on January 31, 2021, we expect the incoming Biden Administration will extend it.

See state by state eviction extensions, some beyond 1.31.21 - https://www.nolo.com/legal-encyclopedia/emergency-bans-on-evictions-and-other-tenant-protections-related-to-coronavirus.html

CRA Reform & Modernization

In late May 2020, the Office of the Comptroller of the Currency (OCC) issued final rule changes to CRA for the banking institutions it regulates. Historically, the three banking regulators have coordinated with each other, however, the Federal Reserve Board did not participate in the rule making process, and while the Federal Deposit Insurance Corp. (FDIC) did participate in the process, ultimately it did not join the OCC in issuing these final rules.

It is also important to note that there was significant industry pushback to the OCC rule changes including several organizations announcing their intent to sue the OCC over the new rules. This could result in postponement or modification, to even a rollback, of the rule changes.

Given that the incoming Administration will be able to appoint a new head of the OCC, it is likely that there will be some changes to the OCC's direction with respect to CRA. For one, we would expect increased coordination with the other two regulatory agencies with respect to CRA modernization. Another reason why we are expecting no immediate impact to the LIHTC market is that compliance with the recent rule changes is not required until 2023 for larger institutions and 2024 for smaller ones. Furthermore, the adoption of the new rules will occur on a rolling basis rather than across all institutions at the same time. OCC-regulated institutions will be allowed to complete their current CRA cycle prior to application and enforcement of the new rules.

Over the long term, it is important to highlight the OCC is the largest bank regulator, covering about 70% of U.S. banks. These rule changes, if they stand, will likely impact these large banks future LIHTC investment behavior, and therefore the broader market. As a result, it is useful to review the list of the 10 largest OCC regulated banking institutions, all of which are large LIHTC equity investors. They are JPMorgan Chase, Bank of America Merrill Lynch, Citibank, Wells Fargo, US Bank, PNC, Capital One, Bank of New York Mellon, TD Bank and Citizens Bank.

We refer you to the July 2020 issue of our newsletter for a summary of recent rule changes for OCC regulated banks at www.StrategicTaxCreditInvestments.com

Wrap Up

We will send out an updated summary of fund offerings at the end of Q1 to capture any pricing changes before our next newsletter in early July. Please feel free to contact us with any questions or if you'd like to discuss the LIHTC market and fund offerings in more detail.

As always, we appreciate your feedback and welcome your questions and comments. If you would like to be removed from our mailing list, just let us know. In the meantime, be well and stay healthy.

You can reach Dave Robbins at 617-340-7040

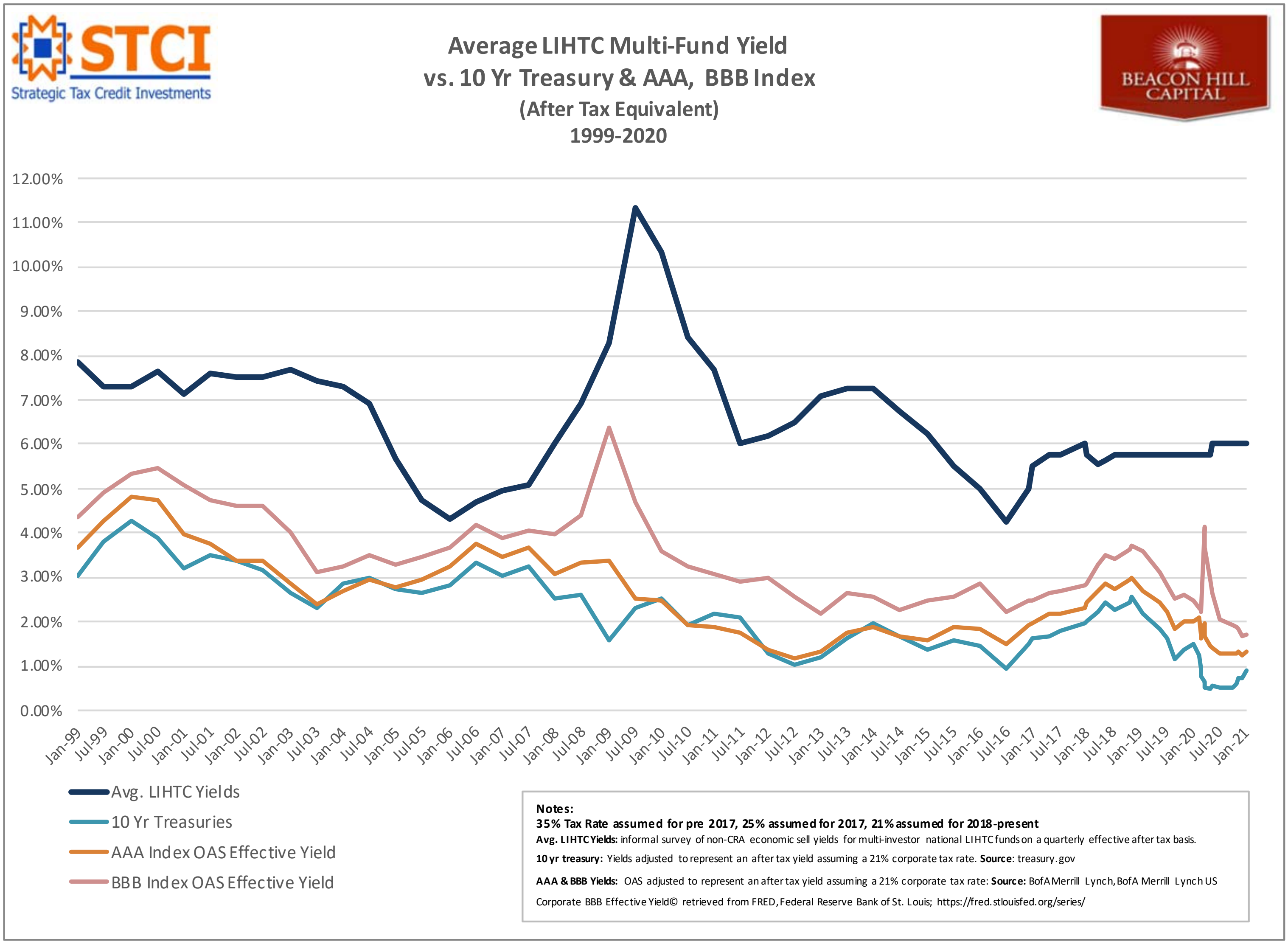
& Brian Rajotte at 503-575-9232.

You can reach Mike Connolly, Chris McCarthy and Garret Daigler of

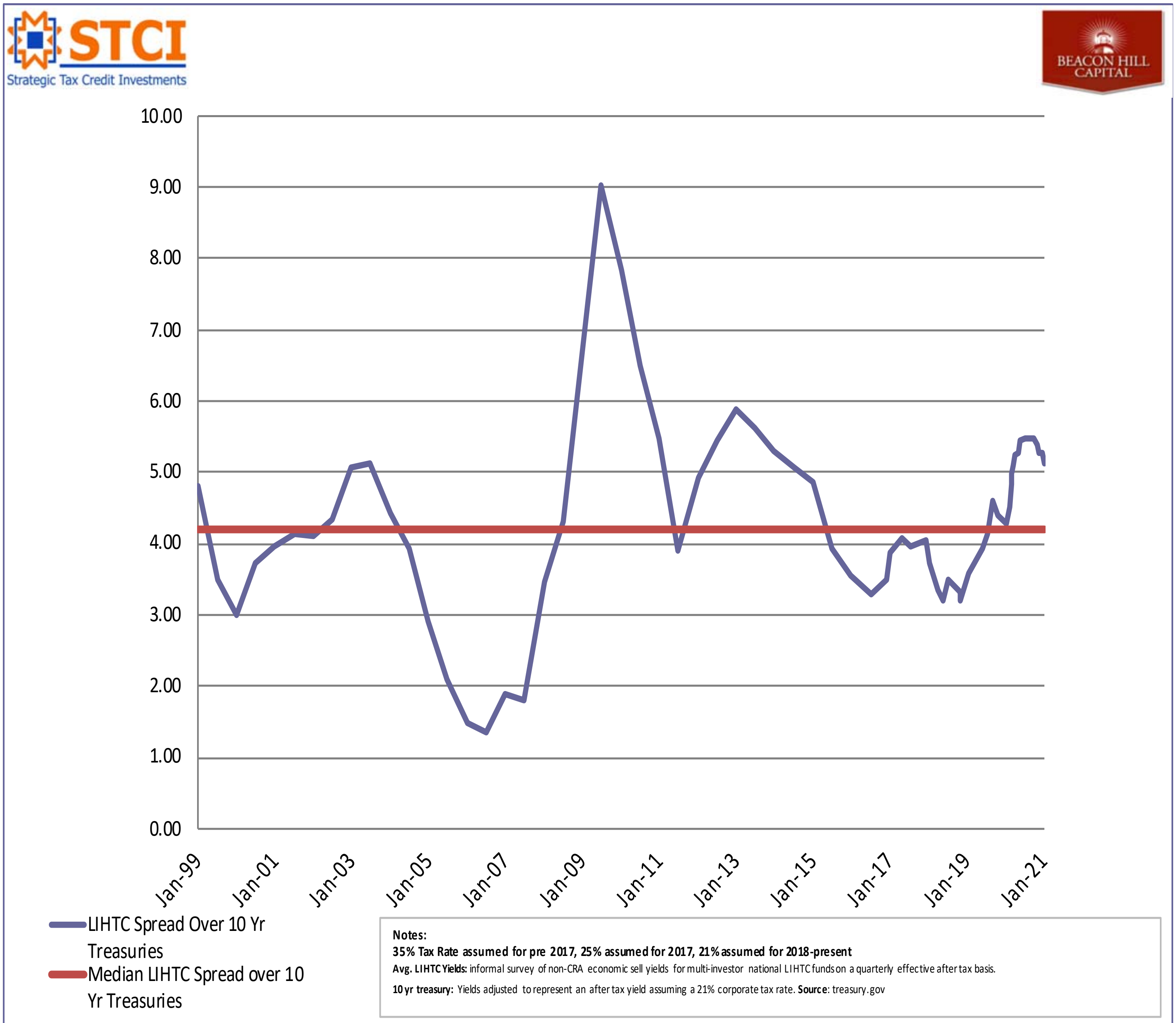
Beacon Hill Capital at 781-740-8981.

Exhibit A

LIHTC Yields vs. Alternatives



LIHTC Historical Spread Over 10-Year Treasuries



An Institutional Division of Compass Securities Corp.

LIHTC National Funds

Q4 2020 - Q1 2021

National Funds																	
Sponsor	Fund	Close	Approx. Size ($MM)	Status	Investment Pricing After Tax Quarterly Effective IRR (%) Price Per Credit ($) Investment Class							Hard Debt %	9% / 4%	Gut Rehab & New Construction / Rehab	Loss Ratio	Notes
Alliant	107	June	150	Prelim	6.40% TBD >=$35M	6.25% TBD <+$25M	6.00% TBD Base	4.50% TBD TBD	5.50% TBD CRA			<35%	50% / 50%	50% / 50%	TBD	February launch, 80% repeat developers
CREA	80	Dec	279	Closed	6.40% $1.000 >$30M	5.80% $1.000 >$20M	5.25% $1.040 <$20M	5.00% $1.050 CRA 1	4.50% $1.06 CRA 2	4.25% $1.07 CRA 3	3.50% $1.09 CRA 5	34%	39% / 61%	83% / 17%	106%	25 properties in 13 states + D.C. 83% new construction/gut rehab, 94% repeat developers, 42% senior/special needs.
	85	June	225-275	Available	6.50% TBD >=$30<M	6.25% TBD >=$20M	5.75% TBD <$20M	5.50% TBD CRA I	5.00% TBD CRA II	4.50% TBD CRA III	4.00% TBD CRA IV	35%	46% / 54%	64% / 26%	84%	85% closed or under LOI, 78% repeat developers, 27 properties in 17 states. 28% senior/special needs, > 20% rental subsidy.
Enterprise	34	Feb	200	Circled	6.15% $0.980 Base	5.00% N/A CRA	4.50% N/A CRA	4.15% N/A CRA	4.00% N/A CRA	3.40% N/A CRA	3.00% $1.070 CRA	46%	22% / 78%	80% / 20%	TBD	17 properties in 11 states. 86% repeat developer. 55% of equity either senior tenancy or subsidized.
PNC	80	June	175	Prelim	6.40% TBD >=$35M	6.25% TBD >=$25M	6.00% TBD Base	5.00% TBD CRA	4.50% TBD CRA			<35%	50% / 50%	TBD	TBD	February launch, Accelerated ramp up of credits due to secondary product, 10% Co-investment by PNC Bank
RBC	31	April	194	Prelim	6.25% $0.960 >=$25M	6.00% $0.960 >10 <25M	5.75% $0.960 < 10M	5.50% TBD CRA	5.00% TBD CRA	4.25% TBD CRA	3.85% TBD CRA	32%	43% / 56%	76% / 24%	124%	24 properties, 19 states. 60% of equity has some rental subsidy, 74% repeat developer. Expected to be 100% under LOI or closed.
Red Stone	84	Mar-Apr	150-200	Available	6.50% $0.953 >= $25M	6.25% $0.945 >=$25M*	5.75% $0.976 >10 <25	5.00% $1.000 < $10M				31%	41% / 59%	81% / 19%%	122%	6.25% IRR is cash needs. 22 properties in 9 states. 80% under LOI. Rental subsidy on > 52% of units. 30% senior properties. 70% repeat developer.
Richman	135	June	200	Available	6.40% $0.950 >=$35M	6.00% $0.970 >=$10mm		4.00% TBD CRA	5.50% TBD CRA			39%	40% / 60%	40% / 60%	116%	90% of hard debt covered by rental subsidy, 26 properties, 92% Repeat Develpers
WNC	50	Q1	125-150	Prelim	6.60% N/A >$35mm	6.40% $0.950 >$25mm	6.15% $0.945 > $25M *	6.00% $0.950 < $25M	5.50% N/A CRA	4.75% N/A CRA		<25%	65% / 35%	60% / 40%	94%	6.15% IRR unbridged class with ltd availability. 24 properties in 17 states; 59% of equity with subsidy; 30 % senior. 89% repeat developer.

Loss Ratio: Tax losses before dispoition as a percentage of capital invested

This information does not constitute an offering. All information subject to change.

STCI is an institutional division of Compass Securities Corporation. Securities offered through Compass Securities Corp, member FINRA SIPC; www.CompassSecurities.com

STCI
Strategic Tax Credit Investments
An institutional division of Compass Securities Corp.

BEACON HILL CAPITAL

LIHTC California Regional Funds

Q4 2020 - Q1 2021

Sponsor	Fund	Close	Approx. Size ($MM)	Status	Investment Pricing After Tax Quarterly Effective IRR (%) Price Per Credit ($) Investment Class					Hard Debt %	Notes
CREA	84	April	100-130	Available	6.40%	6.25%	5.50%	5.00%	4.50%	20%	8 properties. 54% subsidized or senior units, 90% repeat developer. 90% 9% transactions.
					N/A	$0.950	$0.980	$1.000	$1.020		
					> $35M	> $25M	<25M	CRA 1	CRA 2		
Enterprise	CAG 8	May/June	100+	Prelim	6.00%	TBD	TBD	4.25%		14%	60% of properties closed/secured, 91% new construction or substantial rehab, 60 repeat developer, 40% of equity with rental subsidy
					TBD	TBD	TBD	TBD			
					>=$25M	< $25M	CRA	CRA			
RBC	CA 6	June	50-75	Prelim		TBD	TBD			<25%	Los Angeles and San Francisco locations
						TBD	TBD				
						LA CRA	SF CRA				
Red Stone	CA-2020	Dec/Jan	105-120	Closed	6.00%	5.00%	4.75%			19%	7 properties: six of seven with subsidy or senior, 88% new construction. 81% under LOI
					$0.960	$0.986	$0.994				
					>=$20M	>=$10M	<$10M				
WNC	CA 19	June	80+	Prelim	6.25%	6.00%		TBD		TBD	Late January launch
					TBD	TBD		TBD			
					>=$20M	< $20M		CRA			

This information does not consititute an offering. All information subject to change.
STCI is an institutional division of Compass Securities Corporation. Securities offered through Compass Securities Corp, member FINRA SIPC; www.CompassSecurities.com

LIHTC Disclosure

This is not a solicitation. This material is for educational purposes only and is not meant to be investment advice. This material may represent an assessment of the LIHTC market environment at a at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. To determine if the LIHTC Fund(s) are an appropriate investment, carefully consider the investment objectives, risk factors, charges and expenses before making any investment. This and other information can be found in a fund's private placement private placement offering memorandum, or other offering information specific to the investment structure, which can be obtained by calling 781-740-8981 or the specific contact information provided in the investment materials. Read all materials carefully before considering investing. Diversification may not protect against market risk. Current and future portfolio holdings are subject to risks as well. LIHTC private placements involve risk including failure to achieve desired tax benefits and the possible loss of principal.
Past performance does not guarantee future results. Not FDIC Insured. No Bank Guarantee. May Lose Value.

STCI
Strategic Tax Credit Investments
An institutional division of Compass Securities Corp.

BEACON HILL CAPITAL

Preservation & Workforce Housing Funds

Q4 2020 - Q1 2021

Sponsor	Fund	Close	Commitment Period/Hold (in Yrs)	Asset Mgmt Fees	Approx. Size (millions)	Pre-Tax IRR %		Co Investment	Minimum Investment Size	Approx. Available $MM	Notes
						Pref Return	Net/Residual				
Alliant	3	2021	3/7	1.5%	100	8.00%	11-14%	2% to 5%	$3M	75.00	Q1 2021 Launch. 2%-5% Alliant Co-investment. Maximim, aggregate fund level leverage of 65%, max of 20% of total fund for a single asset. 50/50 catch-up, 80/20 Promote.
Bridge Investment Group	2	Qrtly	4 / 10-12	1.5-2.0%	1500	7.00%	10-12%	2% up to $10M	$250K	est 1000	$225M equity closed as of Q3. Estimating $400M to be closed by Q1. PWI compliant, tenant programs & svs, 65-85% acquisition of Class B&C, 10-20% new development, 5-15% manuf. housing. Target leverage of 60-65%.
Enterprise	4	July	3 / 10	1.5%	208-238	7.00%	9-11%	2.5% upto $2.5M	$500k	50+	Target returns for CRA investors are 100 basis points lower. Preferred Return of Capital. 50/50 until yields hit, then 20% after preferred return & 30% after net return to LP's thereafter. Max 15% of equity in 1 transaction
PNC	3	2021	3/5	2%	100	7.00%	11.00%	up to 24.99%	$5M	0.00	Q2 2021 Launch. PNC Bank Co-investment. Leverage of underlying assets of no more thand 65% LTV. Distributions-100% to investor until 7% annual return, 100% until return of capital, 95% until a non-compounded 11% annual return, 80% thereafter
RBC	1	2021	2 / 7	1.5%	100	8.00%	10-12%	3% upto $3M	$1M	100.00	PWI Compliant. Target Fund level leverage of 65% to 75%. Max 20% equity in single transaction; 100% of cash flow to investors until pref return and return of capital, then 80/20 split.
WNC	2	2021	3 / 8	1.5%	75	8.00%	11-13%	5% up to $1.5M	$2.5M	50.00	PWI compliant, 100% return of capital to LPs; next 100% to LPs until cumulative 8% pref., 50% to LPs until 20% catch up to GP, then 80/20 split

* Funds **shown in bold** are open to investors.

This information does not consititute an offering. All information subject to change.
STCI is an institutional division of Compass Securities Corporation. Securities offered through Compass Securities Corp, member FINRA SIPC; www.CompassSecurities.com

Disclosure