National Council of Housing Market Analysts

AN AFFILIATE OF NATIONAL HOUSING & REHABILITATION ASSOCIATION

National Council of Housing Market Analysts 2013 Annual Meeting

October 23-24, 2013

Renaissance Columbus Downtown Hotel

Columbus, Ohio

Tax Exempt Bond Update

Speakers

- **Cody Wilson, Merchant Capital, Montgomery, AL**

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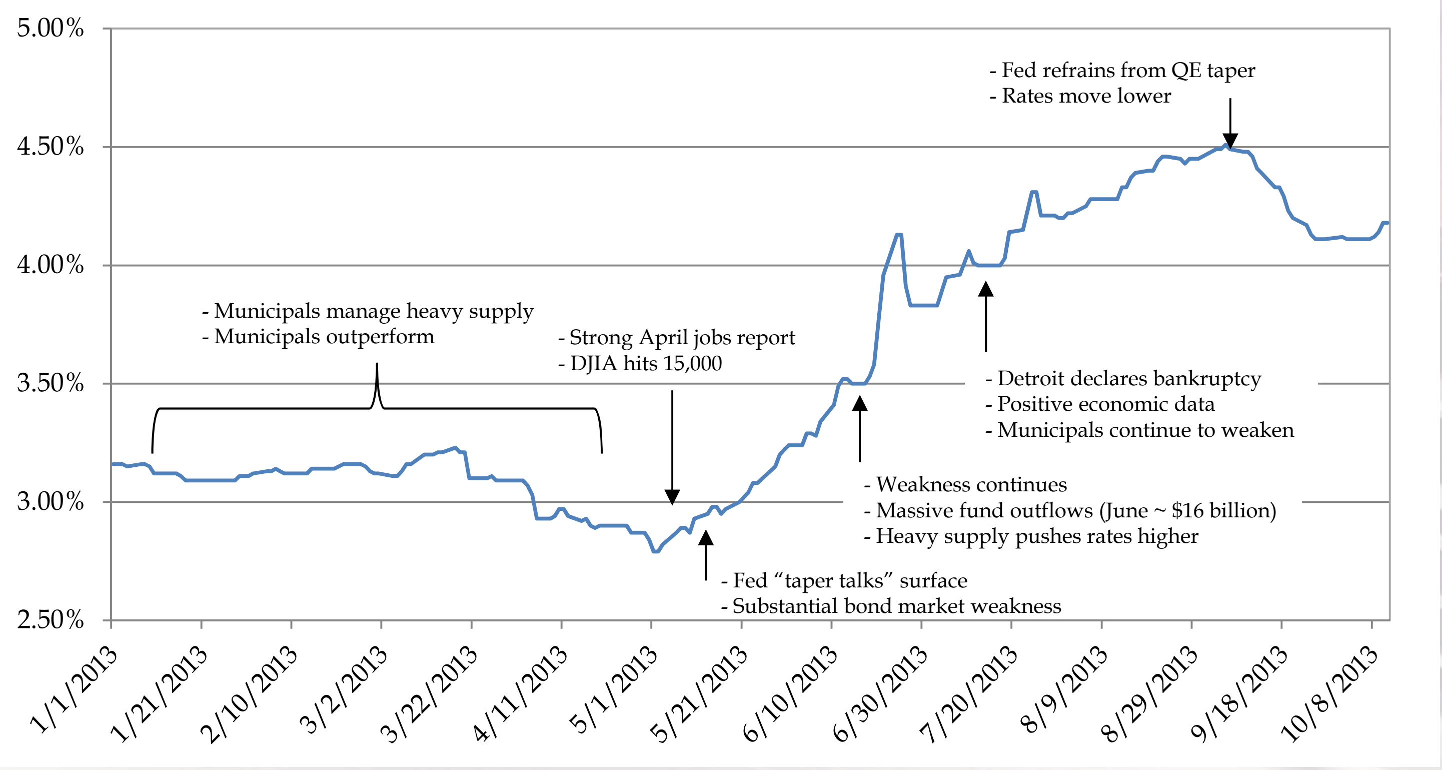
Interest rates began to move sharply higher in May when the Fed turned hawkish.

- The yield on the 30-year MMD benchmark has risen by more than 139 basis points from May to October, one of the most rapid increases on record.

Year-to-date Performance of 30-year MMD[1,2]

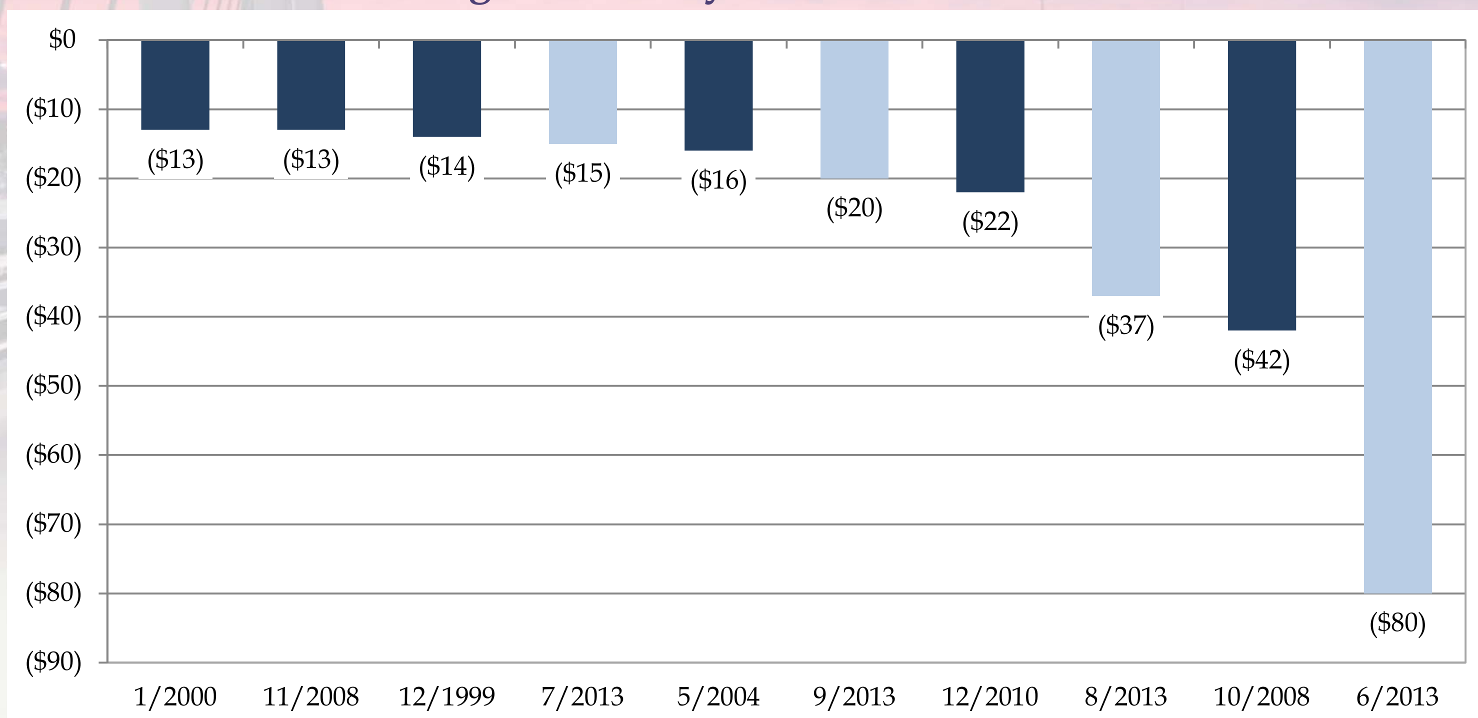


Source: Bloomberg
1 Reflects market conditions as of October 15, 2013
2 Thomson Reuters Municipal Market Data (MMD) AAA curve is a proprietary yield curve that provides the offer-side of AAA rated state general obligation bonds

The market dislocation has been exacerbated because of the lack of liquidity.

- The spike in yields has caused havoc in the bond market, leading many investors to liquidate their bond fund holdings.
- As noted below, four of the largest monthly outflows on record have occurred in the past four months.

Largest Monthly Bond Outflows[1]



Source: Bloomberg. Numbers are in Billions
1 Reflects market conditions as of October 15, 2013

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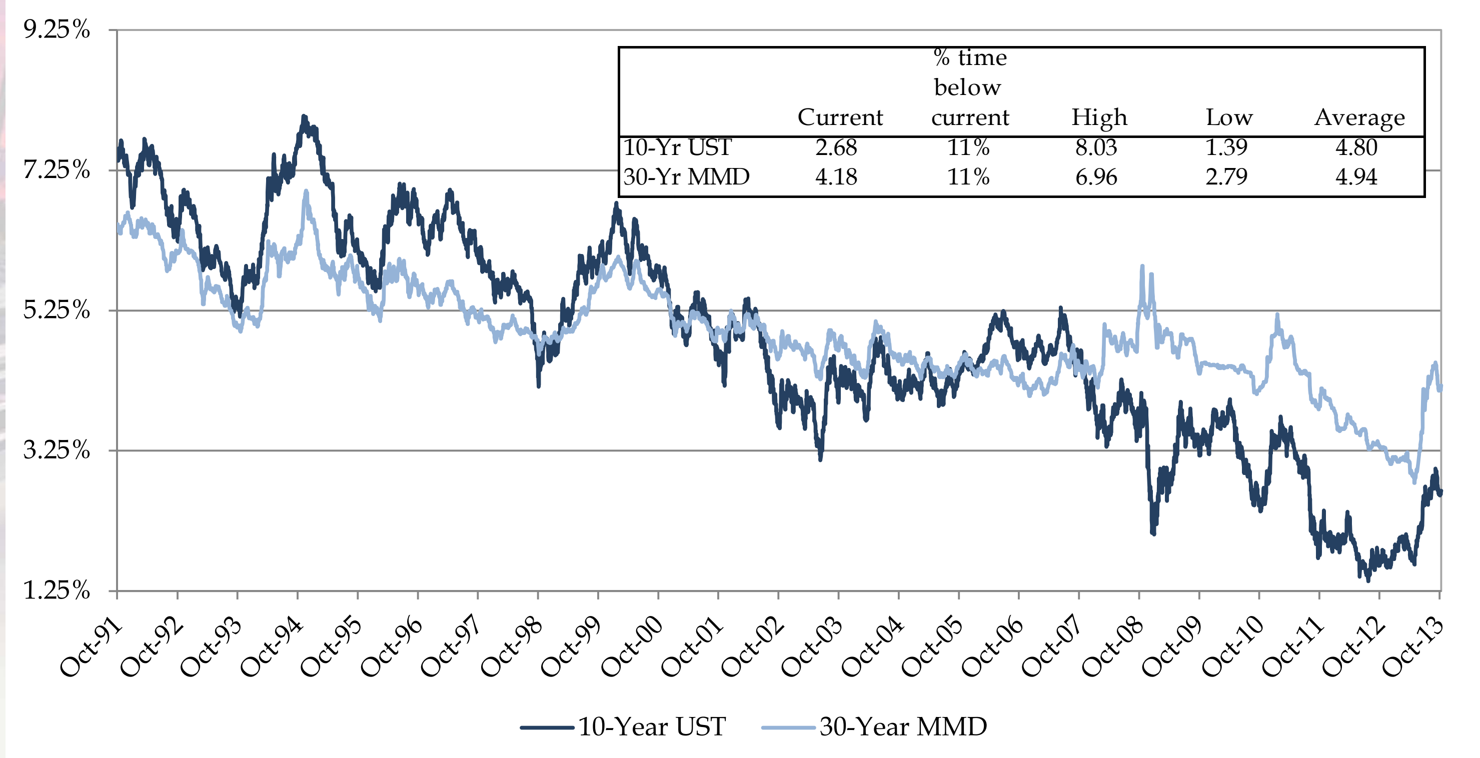
Despite the run-up in yields, rates remain below their historical averages.

- Despite the run-up in yields, taxable and tax-exempt rates remain below their historical averages.

Historical Performance for Taxable and Tax-exempt Yields[1]



	Current	% time below current	High	Low	Average
10-Yr UST	2.68	11%	8.03	1.39	4.80
30-Yr MMD	4.18	11%	6.96	2.79	4.94

Source: Bloomberg
1 Reflects market conditions as of October 15, 2013

Taxable loan coupled with short-term tax-exempt bonds

- Since the credit crisis of 2008, US government backed debt has traded at yields well below tax-exempt debt. Additionally, the Fed has used various policy tools to steepen the yield curve.
- In the current market environment, the most popular execution is obtaining a taxable loan combined with short-term tax-exempt bonds (the “Bonds”)[1].
- Financing observations include:
  - Issue Bonds in an amount to meet the “50% test” under LIHTC program requirements[2]
  - Bonds are collateralized with proceeds from a taxable mortgage loan
  - Under the bond documents, each time the borrower uses Bond proceeds, a like amount of proceeds from the taxable mortgage loan is deposited in the Collateral Account
  - After the project is placed in service, the Bonds are redeemed with proceeds from the taxable mortgage loan
  - Full syndication value of 4% LIHTC
- Due to the underwriting delays and slow processing at HUD, most developers are looking at a Fannie Mae or Freddie Mac taxable loan.

Notes:
1 Assumes a 4% Low Income Housing Tax Credit (LIHTC) transaction
2 Under Section 42, in order to qualify for the full value of 4% Low Income Housing Tax Credits, at least 50% of the aggregate basis of the building and land must be financed from tax-exempt bond proceeds. However, these tax-exempt bonds only need to remain outstanding until the project’s “placed-in-service” date.

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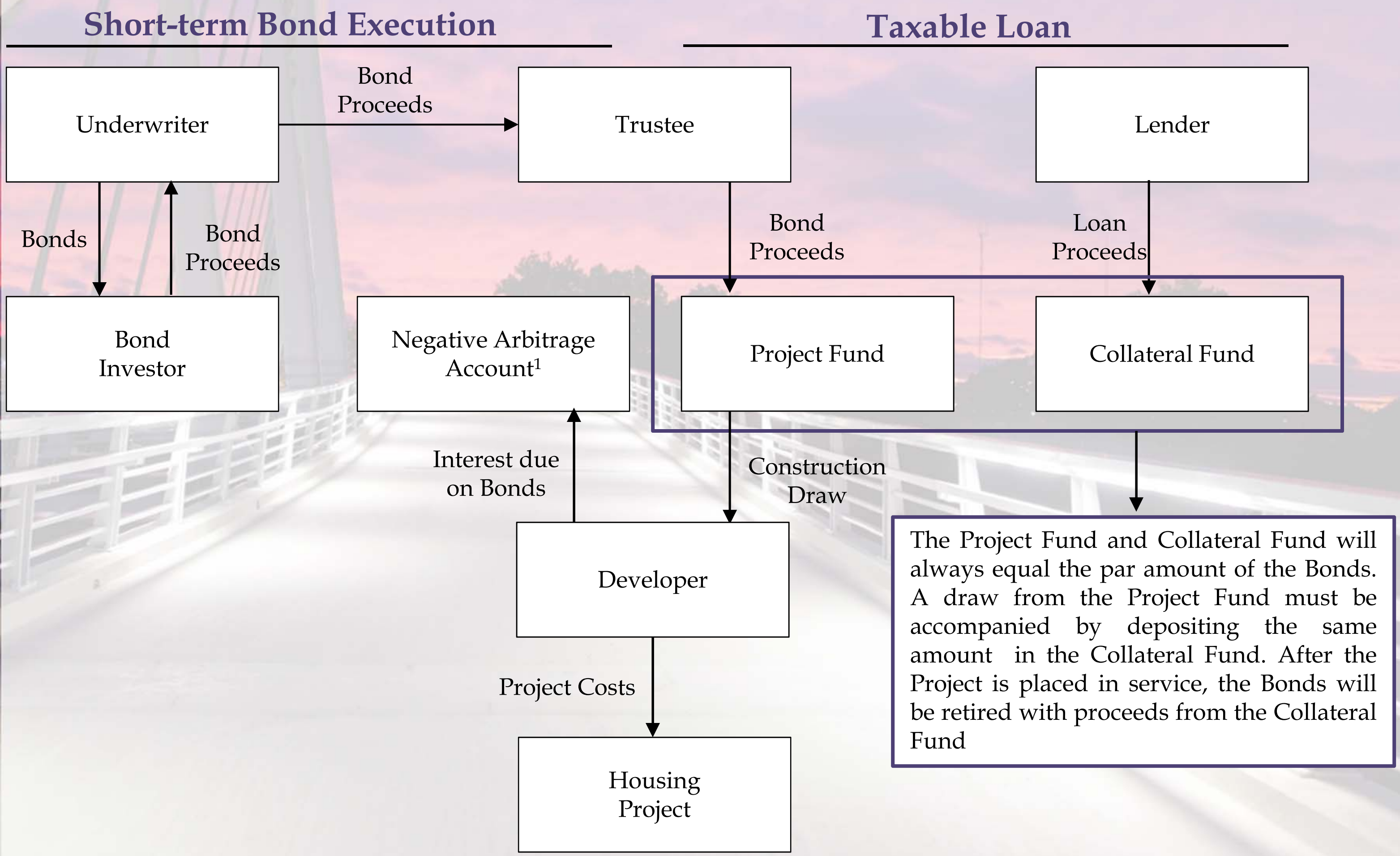
Taxable loan coupled with short-term tax-exempt bonds (cont'd)



Notes:

1 At closing, the Developer will need to deposit the interest due on the Bonds through the Mandatory Tender Date or Final Maturity Date

Standard & Poor’s Unenhanced Bond Program

- Standard & Poor’s currently rates unenhanced affordable housing projects in the investment grade category, typically in the “A” category.
- Underwriting assumptions include:
  - 1.20x DSC (HAP properties); 1.40x DSC (non-HAP properties)
  - Vacancy loss assumptions based on historical trends
  - Occupancy capped at 95%; Occupancy capped at 97% (Senior housing)
  - Operating expense savings accepted, but must be validated
  - Repair and replacement reserves based on physical needs assessment report
- Financing observations include:
  - No credit enhancement or mortgage insurance
  - 35-year interest rate currently ~ 5.75%
  - 35-year amortization with 10-year par call
  - Financial disclosure includes annual audit and occupancy data
  - 75-90 days for closing
  - 100% loan-to-value
  - Non-recourse
  - Bonds priced off the MMD index[1]

Source: Standard & Poor’s

1 Thomson Reuters Municipal Market Data (MMD) AAA curve is a proprietary yield curve that provides the offer-side of AAA rated state general obligation bonds

Private Placements

- A private placement execution is one where the bonds are acquired directly by one (or multiple) investor(s), usually financial institutions with intimate knowledge of the bond issuance and collateral securing the bond.
- Financing observations include[1]:
  - No credit enhancement or mortgage insurance
  - Bond costs of issuance ~3%
  - 40-year interest rate currently ~ 6.15%
  - 40-year amortization
  - Financial disclosure includes annual audit and occupancy data
  - 75-90 days for closing
  - 16-year mandatory tender
  - Debt service coverage of 1.20x
  - 85% loan-to-value
  - Non-recourse (subject to carve-outs)
  - Sponsor shall provide specific guarantees (net worth and liquidity, construction completion)

Notes:
1 Based on a private placement term sheet dated September 2013