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## The Critical Verdict

### Market Studies Form the Essential Underpinning for Successful LIHTC Projects

**M**arket studies for proposed low-income housing tax credit projects have become more sophisticated and refined in recent years – and more necessary with the ever-growing LIHTC inventory.

A market study is required by state housing credit agencies for every new proposed LIHTC project. While all state agencies have their own requirements for market studies, most have adopted in whole or part the model content standards of the National Council of Housing Market Analysts (NCHMA). (See pp. 44-45 for chart on state-by-state market study requirements.)

A market study is a comprehensive written assessment of the feasibility – the likelihood of success – of a proposed multifamily housing project in a given location. The conclusion is based on the evaluation of a wide range of collected data and information on the characteristics of the project, neighborhood, and economy, and on the current and projected near-term supply

and demand of affordable rental housing units. Among other things, the analysis estimates the number of qualified renter households within the designated primary market area and identifies other existing and planned multifamily properties that would compete for tenants (“comps”).

Market studies are generally prepared by professional market analysts. Clients/users include developers, state housing credit agencies, syndicators, tax credit investors, and lenders. The studies are usually ordered by developers to submit with tax credit applications. But they are also commissioned by some housing credit agencies and by syndicators and investors. A market study is distinguished from an appraisal, which is an estimate of the market value of a proposed project.

Market studies for LIHTC projects are important for several reasons.

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“Because the resources for affordable housing development are so limited, the market study is the tool that enables us to pick the best of all the proposed projects and provide the biggest bang for the public fund,” says market analyst Mary Ellen Shay, President of Sacramento, Calif.-based M.E. Shay & Co. and the current chair of NCHMA. “There’s a lot of competition and a good market study can really identify those markets where there is significant need.”



Mary Ellen Shay

“With the income restrictions on LIHTC properties, if you get the market wrong, if you get the rent wrong, you’re wrong for at least 15 years,” says NCHMA Executive Director Thom Amdur. “So it’s paramount that the owner, the investor, and the lender understand the potential rent and the renter base at any particular property.”

Critical components of the market study are deter-

mining the achievable restricted rent for a proposed LIHTC project and the depth of the market for those units. The proposed monthly rent should enjoy a sufficient competitive advantage to justify the use of the tax credit. According to market analyst Bob Lefenfeld, of Columbia, Md.-based Real Property Research Group, Inc., while housing tax credit income and rent limits are computed by region or county, the maximum tax credit rents may be near or exceed the actual market rents in any given market area. In addition, he said that analysts must make sure that the estimated number of units addressing households at a certain income level does not require an excessive capture rate in order to assure that all of the units will be leased. Lefenfeld suggested that tax-exempt bond-financed projects targeting renter households at 60% of AMI can be especially vulnerable if located in an area where there has been aggressive LIHTC development at that price position.



Bob Lefenfeld

**Changing Trends in Market Studies**

According to industry officials, today’s market studies for LIHTC projects are more sophisticated and refined from those of five or so years ago.

“The market methodology is evolving quickly in response to the every-growing need for different types of housing projects and the availability of more precise demographic data,” says Shay.

Changes include:

- **Use of more accurate, often customized data.** Many analysts use HISTA, a proprietary data product offered by California-based Ribbon Demographics, LLC. This product generates more accurate and precise estimates of the number of qualified renter households in a primary market area for a proposed LIHTC project, by cross tabulating households by income level, household size, age group, and tenure (i.e. whether renter or homeowner). As an example, for a seniors project, an analyst could quickly find out the number of households in a primary market area that rent, are comprised of one or two persons, are 65 or older, and make \$10,000 to \$20,000 a year. The basis of the HISTA data is a cross tabulation

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that Ribbon pays the Census Bureau to prepare, with current-year estimates and five-year projections developed for Ribbon by Claritas (now part of Nielsen). Julia LaVigne, Ribbon's sole proprietor, says HISTA data saves analysts time while providing more accurate estimates of the number of qualified potential renter households than is possible using standard Census Bureau data and making multiple calculations. "You don't have to go through the tedious process of trying to make estimates," she says. "The numbers are already there. You can take the tables that we provide and put them straight into your report or spreadsheet." According to market analyst Rob Vogt, a partner at Vogt Santer Insights in Columbus, Ohio, HISTA data "does a nice job of slicing down to the specific audience that's going to live in that project."



Julia LaVigne



Robert Vogt

- Greater refinement of projected demand.** "Using one of our tools, we can now provide a more detailed breakdown of demand by bedroom type," Vogt explains. "So we can calculate the capture rate for a one-bedroom unit, the capture rate for a two-bedroom unit, and the capture rate for a three-bedroom unit." The capture rate is the estimated percentage of age, size, and income qualified households in the primary market area that the project must attract as tenants to fill up within a defined lease-up period.
- More user-friendly features.** Many analysts now incorporate Google Maps into their market studies to give readers a fuller understanding of the proposed project and how it fits into the submarket. These maps might show the boundaries of the primary market area, the location of the proposed project and comparable properties, and other features. Many analysts impose data from databases or other sources on these maps (so-called data mapping), and some also produce heat maps. "You've seen maps of the U.S. or a state where a certain percentage rate of population growth is red and a certain

percentage growth might be blue," says market analyst H. Blair Kincer, a partner at Novogradac & Company LLP in Bethesda, Md. "With a heat map, we can show which parts of the market area are growing faster and which are growing slower by shading them different colors...The easier we can communicate the big picture story, the better it is for our clients and the reader."

- Greater standardization.** Most state housing credit agencies have fully or partially incorporated NCHMA's model content standards in their LIHTC program requirements. Some require the market study to be prepared by a certified NCHMA member market analyst. In addition, a number of housing industry groups follow or make reference to NCHMA's model content standards.
- Deeper analysis.** "For many of our clients, we're going well beyond [the NCHMA standards, doing things like operating expense analysis and a very, very thorough comparable rental analysis," says Kincer, noting that Novogradac & Company prepares LIHTC project market studies mostly for syndicators, investors, and lenders. "It's becoming more apparent that in many markets operating expenses are outpacing revenue growth (from rents), which could be an issue. So people want to get their hands around that issue earlier than later." Several sources said they now provide or require greater analysis and discussion of economic trends in the market area, including whether HUD's annual area median income limits and the market rents have been rising, falling, or staying flat and what is the likely trend in the near future. Also common are assessment of how a project with a Section 8 contract would likely fare if its project-based rent subsidies were curtailed.

**Variations on Market Study Content**

While more standardized than ever, market studies for LIHTC projects can vary widely in format and in content, depending on the client.

Most state housing credit agencies require developers to submit a market study when they apply for 9% housing credits. The developer usually selects the market analyst, though many states maintain a list of

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approved analysts that sponsors must pick from. Some state agencies commission the market study from outside providers that they utilize.

Syndicators usually commission their own market study, separate from the one prepared for the tax credit application. For instance, Enterprise Community Investment, Inc. orders market studies for proposed LIHTC projects in which it is considering making an equity investment. The study is typically ordered once Enterprise has issued a signed letter of intent, says John Brandenburg, Vice President, Credit.



John Brandenburg

“We have a proprietary report format and guidance that we give to our market consultants and they follow that. We have two separate formats – one for senior projects and one for family – that is an Excel template in which the consultants do their writing and analysis.”

Enterprise also reviews the developer’s market study and gives it to its market consultants but doesn’t rely upon it, says Brandenburg.

Boston Financial Investment Management is unusual in that it prepares its own market studies in-house for LIHTC projects in which it is considering an equity investment. According to Bud Clarke, who oversees this department, Boston Financial “is the only syndicator in the business that has invested the financial resources in an independent group of market analysts whose sole function is to analyze real estate markets.”



Bud Clarke

He said Boston Financial, a member of NCHMA, follows the NCHMA model content standards for its in-house market studies.

Clarke states that the advantages of doing the market studies in-house rather than relying on third-party studies lie in being able to utilize the company’s vast proprietary database of information on the characteristics, operating expenses, and performance of thousands of LIHTC properties that Boston Financial has syndicated and asset manages. “Third-party market analysts don’t have the luxury of that much information on the operating performance of tax credit properties to be

### LIHTC Investors’ Group Releases New Tool

The Affordable Housing Investors Council has created a new resource for evaluating the long-term viability of a low-income housing credit project supported with public operating subsidies. While LIHTC investments are underwritten for a 15-year term, most operating subsidies are appropriated yearly. The *Operating Subsidy Review Guidelines* help an investor assess risks related to: the legislative and budgetary environment; the likelihood that a property can weather a financial transition if the subsidies are lost; and the developer’s capacity to aid that transition. It includes options for structuring a deal to protect the affordable housing and the equity investment in it if funds are eliminated. The *Guidelines* include a fillable Underwriting Analysis Grid that delves into key factors such as the extent of the property’s reliance on subsidies, market and building conditions, and financial resources for mitigating subsidy loss.

(<http://www.ahic.org/tools-resources> – click on Acquisitions/Underwriting) **TCA**

able to get that in their market studies and that allows them to benefit from the lessons of past assignments.”

Using data mapping, Boston Financial has imposed its entire portfolio of properties on maps, enabling analysts to click on a dot that represents a property to access detailed information about that property (e.g., rents, occupancy history, income limits) and on the market. The system can generate reports and maps both for Boston Financial’s portfolio and for any uploaded state agency or HUD database.

Doug Lloyd, a Chicago-based Executive Director at JP Morgan Capital Corporation, a LIHTC investor, and co-chairman of AHIC’s Acquisition and Underwriting Committee, feels that tax credit investors generally believe that market studies for proposed LIHTC projects are valuable but that each investor “probably has a different viewpoint of how important they are.”



Doug Lloyd

“We find them incredibly valuable,” says Lloyd, who noted that JP Morgan Capital Corporation primarily invests in LIHTC properties through single-investor funds. As such, he said his firm reviews the market study that the syndicator has commissioned or done in-house; the developer’s third-party market study (if one has

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been received); and the appraisal report. It also develops its own “mini” market study, which is prepared internally by the firm’s acquisition team. This study uses third-party demographic and rental data and information from the company’s portfolio as well as that gathered in the team’s site visit, which includes interviews with the developer, property manager, property managers at comparable properties, and the municipal planning and police departments. “We dig through [the different reports] and poke holes in them,” says Lloyd, looking for agreement or differences in identified comp properties, market rents, etc.

Lloyd especially wants future economic, demographic, and rent projections. “As an investor we’d like to know not just where the property is going to be the minute it comes on line at stabilization but we’d like to get a feel that the market is going to be okay for the next couple years. Nobody can predict out 15 years, but looking at all the factors, does the market look pretty good for several years beyond stabilization?”

Lenders may have different requirements when it comes to market studies.

Red Mortgage Capital, an FHA and Fannie Mae multifamily lender based in Columbus, Ohio, requires a market study that satisfies the requirements of FHA’s Multifamily Accelerated Processing (MAP) program, or of Fannie Mae’s requirements, depending on whether it is evaluating an application for an FHA-insured loan (e.g., Section 221(d)(4)) or a Fannie Mae loan, explains Tracy Peters, Senior Managing Director of Red Capital Markets, LLC. The market studies are usually ordered by the developer.

In the case of FHA mortgages, Red Capital generally prefers to see the market studies prepared by NCHMA-certified market analysts, said Joe Mandeville, a vice president of Red Capital Group LLC who co-heads a department that reviews market studies and conducts in-house real estate market research and analysis.

Peters and Mandeville compare the information in the market studies with that in the appraisal report and with market data in



Tracy Peters



Joe Mandeville

Red Capital’s database of \$17 billion to \$18 billion worth of multifamily loans that the company services. “We can tap into that to make sure that what we’re seeing in the market studies is consistent with what we’re seeing for similar types of properties in similar geographic areas,” says Peters.

### Flexibility Is Needed

Sometimes, though, standard market study analysis needs to be tweaked to come up with a more appropriate and accurate assessment of the viability of a proposed affordable housing project.

This is typically the case with the LIHTC projects that Oregon, Wisc.-based Gorman & Company, Inc. develops in “revitalizing” and “challenged” areas, says Chief Operating Officer Tom Capp. Classic market study methodology often won’t work here, he notes, because the proposed project will be a different, new type of housing product in the neighborhood (i.e. high quality new construction with higher rents) compared to the existing housing. “So you often don’t have good comparables and you have to look to analogous areas, analogous situations for comparables, sometimes regionally.”

Similarly, Capps says reference to an area’s historical apartment absorption rates may not be relevant when assessing demand for a downtown or near-downtown development, which often rents up quickly.

### Designing a Better Product

Market analysts can also help developers improve the original design for their proposed LIHTC projects.

“One of the questions you always hear,” says Rob Vogt, “is, ‘Why don’t you see a negative market study?’”

“The reason is that the analyst has taken the time to talk to the developer to tell him that his or her proposal isn’t going to be supported in this market area as it’s currently laid out. But if you add some three-bedroom units, if you reduce the rent on your two-bedroom units, if you add a bath to that two-bedroom unit, or if you add some dishwashers, then you have a project that can be supported.”

“In probably 80% to 90% of the projects that we work on,” says Vogt, “we provide feedback to the developers to help them refine the project, so that when they submit their tax credit application, it’s a better project, at least from a market perspective.” **TCA**

## State 9% LIHTC Program Market Study Requirements<sup>1</sup>

State Housing Credit Agency	Market Study Required in Seeking 9% Allocation?	Who Prepares Market Study?	Does Agency Maintain List of Approved Market Analysts? How do Analysts Get on List?	Does Agency's Market Study Requirements Use NCHMA Model Content Standards?
Alabama HFA (NR)	Yes	Developer selects analyst.	NA	NA
Alaska HFC	Yes	Agency commissions market study from contractor.	No	Yes, plus some agency specific add-ons
Arizona DOH	Yes	Developer selects qualified analyst.	Not an approved list, but has list of interested market analysts available upon request.	No, but ADOH's requirements are similar.
Arkansas DFA	Yes	Developer selects from agency's approved list.	Yes. Submit request to be added to list after providing sample market study that meets all of ADFA's standards and requirements.	No
California TCAC	Yes	Developer picks market analyst.	No	CTCAC/CDLAC joint market study guidelines incorporate aspects of model content standards.
Colorado HFA	Yes	Developer picks market analyst from agency's approved list.	Yes. Analysts must submit proof of experience and attend required training.	No
Connecticut HFA	Yes	Agency commissions from agency's approved list of market analysts.	Yes. Agency issues RFQ.	No
Delaware SHA	Yes	Developer selects analyst from agency's approved list.	Yes. Analysts have to meet agency criteria (3 LIHTC samples and state HFA and developer references).	No, but we may revise our standards for the 2015 round.
Florida HFC	Yes	Agency's outside contracted underwriters order third-party market studies.	No	Market study is ordered after a project wins a housing credit award and is invited into credit underwriting.
Georgia DCA	Yes	Developer picks market analyst from agency's approved list.	Yes. Agency issues RFP.	Yes, substantially so.
Hawaii HFDC	Yes	Developer selects market analyst.	No	No
Idaho HFA	Yes	Developer chooses market study provider from agency's approved list.	Yes, but not currently adding to list.	QAP lists market study requirements which are based on the recommended practices of the National Council of State Housing Agencies.
Illinois HDA	Yes	Developer picks analyst.	No	Are based on NCHMA standards but not 100%. NCHMA membership required for all firms producing site and market studies reviewed by IHDA.
Ill.-Chicago DPD	Yes	Developer selects analyst.	No	Yes
Indiana HCDA	Yes	Developer picks market analyst.	Yes. Must submit application/proposal to get on list.	Yes
Iowa FA	Yes	IFA selects market study provider through RFP process.	No	Utilizes similar standards.
Kansas HRC	Yes	Developer selects market analyst.	Yes. Analyst submits request to agency.	Yes
Kentucky HC	Yes (except for transitional housing projects)	Developer selects market analyst from agency's approved list.	Yes. Through periodic RFQs that call for submission of required credentials and examples of reports.	No, but requirements are similar.
Louisiana HC	Yes	Agency commissions market study from approved list.	Yes. Is updated through RFP process.	Yes. Also, market analysts must be a member of NCHMA or a similar professional organization.
Maine SHA	Yes	Developer selects market analyst.	No	Yes
Maryland DHCD	Yes	Developer picks from agency's approved list of vendors.	Yes. To be added, submit cover letter, two examples of work, and resume with references. Details at <a href="http://tinyurl.com/p8sazx9">http://tinyurl.com/p8sazx9</a> .	Yes
Massachusetts DHCD	Yes	Developer picks analyst (must be a certified appraiser).	No	Yes
Michigan SHDA	Yes	Agency commissions market study from approved list.	Yes. Is product of annual RFP process.	Use about 95% of NCHMA standards.
Minnesota HFA	Yes	Developer picks analyst.	Yes. Initial solicitation was RFP. Contractors must re-apply after three years to stay on list.	Yes

<sup>1</sup> Information from responses by state housing credit agencies to Tax Credit Advisor survey in May 2014. Information shaded in red from Web sites of non-responding agencies. NA = Not Available.

<b>State Housing Credit Agency</b>	<b>Market Study Required in Seeking 9% Allocation?</b>	<b>Who Prepares Market Study?</b>	<b>Does Agency Maintain List of Approved Market Analysts? How do Analysts Get on List?</b>	<b>Does Agency's Market Study Requirements Use NCHMA Model Content Standards?</b>
Mississippi HC	Yes	Developer selects analyst.	No	Agency refers applicants/analysts to NCHMA model content standards.
Missouri HDC	Yes	Developer selects analyst from agency's approved list.	Yes. MHDC RFQ is soliciting applications for newly revised list.	Yes, with modifications.
Montana Bd. of Hsg.	Yes	Developer picks analyst.	No	Yes
Nebraska IFA	Yes	Developer picks analyst.	No	Yes
Nevada Hsg. Div.	Yes	Developer selects analyst.	No	No. Use in-house criteria.
New Hampshire HFA	Yes	Agency commissions market study.	Yes. Must submit sample market study to agency and be approved for addition to list.	Yes
New Jersey HMFA	Yes	Developer picks analyst.	No	Yes
New Mexico MFA	Yes <sup>2</sup>	Agency contracts for market study for each of the top scoring projects.	Agency conducts RFQ every two years to select 1 or 2 firms as contractors to perform market studies.	Yes
New York State HCR	Yes except for projects in New York City	Developer picks analyst from agency's approved list.	Yes, but not currently issuing RFQ to add new market analysts.	Yes, mirror NCHMA standards to a large extent.
North Carolina HFA	Yes	Agency commissions study.	NA	No. Agency maintains own standards.
North Dakota HFA	Yes	Developer selects analyst.	No. But provide upon request list of analysts who have done or expressed interest in doing work in North Dakota.	Yes
Ohio HFA	Yes	Developer selects analyst.	Yes. Analyst must submit application for agency approval.	Yes
Oklahoma HFA	Yes	Developer picks. Must be experienced, independent third-party analyst.	No	Are based on NCHMA standards.
Oregon HCS	Yes	Developer picks analyst.	Yes. Must submit request and qualifications for analysis.	No
Pennsylvania HFA	Yes	Developer selects. Analyst must be independent, experienced and qualified in Pennsylvania's affordable rental markets. Agency reserves right to order own market study.	No, but has a contact list of market analysts compiled from applications/ information submitted to agency.	Closely follow NCHMA standards.
Rhode Island Hsg.	Yes <sup>3</sup>	Agency commissions for projects that receive 9% allocations.	Agency periodically issues RFQ to establish list of qualified analysts and selects vendors from list.	Yes
South Carolina SHFDA	Yes	Developer picks market study from authority's approved market analyst list.	Yes. Analysts can request to be added through authority's procurement office by submitting a RFQ.	In some areas, yes. Market analysts must be certified NCHMA member in good standing.
South Dakota HDA	Yes	Developer picks analyst from agency's approved list.	Yes. Must submit company resume to agency for review and approval.	Yes
Tennessee HDA	Yes	Developer picks from agency's approved list.	Yes. Agency issues RFP.	No
Texas DHCA	Yes	Developer chooses analyst from agency list.	Yes. Analyst must provide certain documentation to Dept.	No, but are similarities.
Utah HC	Yes	Developers chooses analyst.	No	Yes
Vermont HFA	Yes	Developer picks analyst.	No	Yes, with some modification.
Virginia HDA	Yes	Developer picks analyst from agency's approved list.	Yes. RFP process.	Yes, and ask for additional information.
Washington SHFC	Yes	Developers chooses analyst from agency's approved list.	Yes, through RFQ. Details at <a href="http://tinyurl.com/lzz89vp">http://tinyurl.com/lzz89vp</a>	Yes
West Virginia HDF	Yes	Developer selects analyst.	No	No
Wisconsin HEDA (NR)	NA	NA	NA	NA
Wyoming CDA	Yes	Developer picks provider.	No	NA

<sup>2</sup> Applications must include deposit for cost of a market study.

<sup>3</sup> Only market information required in applications.