TIMOTHY R. LEONHARD: *THE DEBT CORNER*

Not Business as Usual

Since our last report in August, we have seen the recent federal government shutdown, which stalled operations at the U.S. Department of Housing and Urban Development (HUD), along with a sharp drop in multifamily mortgage interest rates.

The primary debt options today for affordable multifamily properties, including those funded with low-income housing tax credits, are still the programs offered by Fannie Mae, Freddie Mac, and HUD/FHA. Banks remain a viable source of construction financing and in some cases, permanent loans.

HUD's Closure and Reopening

The negative effects from the shutdown that lasted from October 1st through 16th will likely persist for a while.

The shutdown halted the majority of HUD's operations and caused backlogs and delays of at least three weeks in most of the agency's departments, including those critical to the multifamily housing industry such as the FHA mortgage insurance programs.

Now that HUD has reopened, priority will be given to facilitate closings on FHA transactions that have rate-locked and face mandatory loan delivery deadlines. Priority will also be given to renewals of Section 8 Housing Assistance Payment contracts and other HUD functions vital for affordable housing.


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Although the length of the shutdown does not seem like much out of a 52-week year, HUD has already lost productivity from "sequestration days" in 2013, and will soon experience further delays from the Thanksgiving and Christmas holidays and year-end vacations.

The bottom line is that multifamily developers and owners planning year-end financings requiring HUD's involvement would be wise to plan for longer processing times than normal.

FHA Commitment Authority

The enacted continuing resolution (CR) that enabled the federal government to reopen is retroactive to October 1, 2013 (the start of FY 2014), but only funds the government through January 15, 2014.

The CR allows FHA to resume issuing commitments

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Current FHA, Fannie Mae, Freddie Mac Financing Options

FHA/HUD – Taxable New Construction or Sub Rehab Loan Parameters [Section 221(d)(4)]

DSCR: 1.11 to 1.20 | **LTC:** 83% to 90% | **Rate:** 5.25% (plus MIP) | **Loan term:** Up to 40 years | **Amortization:** Up to 40 years

FHA/HUD – Taxable Acquisition or Refinancing Loan Sizing Parameters [Section 223(a)(7), 223(f)]

DSCR: 1.15 to 1.20 | **LTV:** Up to 85% | **Rate:** 4.40% (plus MIP) | **Loan term:** Up to 35 years | **Amortization:** Up to 35 years

Fannie Mae/Freddie Mac Taxable Acquisition or Refinancing Loan Parameters (without new LIHTC)

DSCR: 1.20 to 1.25 | **LTV:** 75% to 80% | **Rate:** 3.85% to 5.75% | **Loan term:** 5 to 30 years | **Amortization:** 30 years

Fannie Mae/Freddie Mac Taxable Acquisition or Refinancing Loan Parameters (with new LIHTC)

DSCR: 1.15 | **LTV:** 90% | **Rate:** 5.35% to 6.15% | **Loan term:** 15 to 30 years | **Amortization:** Up to 35 years

Fannie Mae/Freddie Mac Taxable Adjustable Rate Acquisition or Refinancing Loan Parameters (without new LIHTC)

DSCR: 1.20 to 1.25 | **LTV:** 75% to 80% | **Rate:** 2.50% to 3.75% over 1M LIBOR | **Loan term:** 5 to 10 years | **Amortization:** 30 years

* Note: All rates quotes above assume a full leverage transaction. Transactions with LTV of 70% or less can generate interest rate savings of between 15 and 40 basis points.

Source: Timothy R. Leonhard is the Managing Director of Affordable Housing at Oak Grove Capital, a Fannie Mae, Freddie Mac, and FHA multifamily lender based in Dallas, Texas. Figures as of October 10, 2013. Leonhard may be reached at 817-310-5800, tleonhard@oakgrovecap.com

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for HUD-insured multifamily mortgages.

There is a little over $7.3 billion in commitment authority available through January 15, 2014. HUD will apportion this amount in one lump sum and should be able to clear the backlog of loans that were approved in FY 2013 but had not yet received a commitment from FHA because of the temporary exhaustion of commitment authority. There should be enough commitment authority now to process all pending and new loan applications.

Interest Rate Decline, GSEs

Multifamily mortgage interest rates have generally declined sharply since mid-September, driven primarily by the Fed's announcement on September 18th that it would delay decreasing its quantitative easing program, or "tapering." This recent trend is in contrast to the upward movement in rates earlier in the year.

Fannie Mae's and Freddie Mac's multifamily mortgage rates have decreased by approximately 30 basis points since the Fed's announcement. However, rates on FHA-insured multifamily mortgages have remained relatively flat during this same period due to widening investor spreads driven by continued illiquidity in the GNMA secondary mortgage-backed securities market.

With 2014 drawing nearer, Fannie and Freddie have recently become more aggressive in pricing new multifamily loan originations in an attempt to reach the 2013 loan production caps imposed on them by the Federal Housing Finance Agency (FHFA) earlier this year. At that time, FHFA directed Fannie and Freddie to each reduce their loan production volumes for 2013 by 10% from their 2012 volumes.

As a result, earlier this year the two GSEs, fearing they would hit the 2013 caps before year end, were stingier in their terms. Credit enhancement pricing waivers became very hard to obtain from either GSE as they attempted to temper their loan production and increase profitability. However, now that the GSEs are trying to accelerate their production, the pricing being offered is more favorable.

What to Expect in 2014?

At HUD, one of the most significant developments

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will be the commencement of the Department's plan to close 41 of its 51 multifamily offices. HUD still needs to issue guidance for the transition of business from the closed offices to the remaining large national Multifamily Hubs.

As part of its field office restructuring and reorganization of the Office of Multifamily Housing, HUD will be consolidating the employees in 51 offices around the country into 10 offices consisting of five Multifamily Hubs (New York, Atlanta, Chicago, Fort Worth, San Francisco), each with a satellite office (Boston, Jacksonville, Detroit, Kansas City, and Denver). Many employees will leave HUD rather than move.

In November, FHFA is expected to announce its 2014 requirements for Fannie Mae and Freddie Mac (e.g., 2014 loan production volume caps, eligible mortgages, affordability constraints). While it is unclear what this will include, it appears likely that FHFA at a minimum will limit the ability of the GSEs to lend in the "luxury" multifamily housing market. FHFA will likely try to achieve this goal through per-unit loan limits or maximum rents per unit as a percentage of the area median income.

It is very difficult to predict with any confidence the future trend in multifamily mortgage rates. While most current signs point to an attractive and stable interest rate market heading into 2014, there are many significant variables that will affect mortgage rates (e.g., timing of Fed tapering, worldwide demand for Treasuries, FHFA's 2014 regulations for the GSEs) and Washington politics is always a wild card.

Freddie Mac's VLI Initiative

Freddie Mac has announced a goal to finance more than 40,000 very low-income housing (VLI) units in 2014 – down from a goal of 50,000 units in 2013. VLI is defined as a rental unit with the tenant-paid portion of rent at or below 50% of the area median income calculated rent.

Eligible financings are standard acquisitions, acquisition/rehabs, and refinances. Freddie has been very creative in structuring several products for this space in order to land these financings. If you own or plan to develop a property with at least 50 VLI units, contact your Freddie Mac lender before year end to discuss your options. TCA