

LIHC MONTHLY REPORT

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Industry Pros are Cautiously Optimistic After September 11

By Jane Bowar Zastrow, Editor, Novogradac & Company LLP

In the days following the tragic events of September 11, several multifamily housing forecasts were released that touted the industry's "positive territory." A September 14 University of California, Los Angeles forecast predicted that the Los Angeles County apartment market would experience slower growth for the rest of this year, but that the long term investment outlook was bullish due to the potential for substantial rent growth, small increases in capitalization rates and slower price appreciation.

Three days later, another UCLA Anderson Forecast predicted the terrorist attacks on the World Trade Center and the Pentagon would have little impact on a national economy that was already headed for a recession and reeling from the downfall of the technology sector. The report contends that, historically, attacks like those on the World Trade Center and Pentagon have only brief and limited economic consequences for the United States overall. A third report, by the Mortgage Bankers Association and National Association of Realtors, took the view that the attacks would take "at least a short-term toll" on the national economy. It pointed to reduced airline traffic, canceled sports events and the huge losses suffered by investment banking, financial services and casualty insurance companies.

Those opinions pretty much parallel those of affordable housing industry professionals who perceive unyielding demand for their product. "We see no wavering in the industry," says Mike Costa, president of Simpson Housing Solutions. "We've talked to a couple of our investors who closed deals in late September and neither has altered anything in their underwriting or position."

There is, however, a time-will-tell cautionary note. "So far we've seen no evidence [that investors are pulling back]," says Jenny Netzer, the head of housing and community investing for LendLease Real Estate Investments. However, Netzer puts the future of the industry straight on the economy's shoulders. "If the economy gets much worse, a lot of folks will be less profitable, have less money to invest and less tax liability to shelter," she says.

Rich McCauley, of the Richman Group, also questions the disaster's effect on investors' wherewithal. "In a large recessionary period, will they need credits and losses like they did a year ago?" he asks. Given that uncertainty, he still doesn't foresee a market meltdown like that of 1998. "There are enough strong investors that will continue the demand. I'm optimistic," he says.

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LIHC WATCH

IRS: Out-of-Service Properties

The national office of the IRS, in examining treatment of casualty losses to low-income housing tax credit properties under IRC 42(j)(4)(E), has ruled that state housing credit agencies must report to the IRS via Form 8823 any casualty loss that takes low-income property in whole or in part out of service and results in a reduction in qualified basis. A previous informal examination advised state housing credit

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Interest rates bring up a whole new set of issues, according to Netzer. She notes that the continued lowering of long-term interest rates will bring down investor yield requirements and provide more equity and debt dollars in support of greater costs and getting deals done.

While most investors in the tax credit business are not on the front line of the disaster's impact, many are in financial services that support those who were and remain on the front line. "I am concerned about the significant financial losses," admits Costa. Given the magnitude of the attacks, Costa acknowledges that weary and wary investors could indeed pull back: "We haven't seen any effect yet, that is yet to come and its magnitude is yet to be felt," he says.

Among the markets to bear the brunt of the tragedies, the hospitality industry experienced a 33 percent fall off immediately following the attacks. "It's started to jump back up, but they're still operating negatively," says Costa.

From his office in Connecticut, McCauley sees outlying suburban office markets in the northeast experiencing a temporary boon as those displaced Manhattan businesses occupy whatever space they can find.

Also feeling the force of the falling economy are markets like San Jose, Calif. that are weakening in the top end of the market. That Silicon Valley city has seen high-end rents drop 20 percent to 30 percent while affordable housing occupancies and rents remain strong.

At this point, there is little to suggest that economic forces will put the affordable housing industry into a tailspin. "Of the players we have been selling our credits to, none have indicated a drop in revenues significant enough to alter plans or goals for 2002, but nobody knows what will happen in the future," says Costa. Fresh from a multifamily housing conference, he says all the panelists— investors, lenders, developers — had the same response. "The stability of the industry today will allow us to weather this in a positive way. Nothing in the short term will have that drastic effect on our industry."

There is no argument that the shock of the terrorist attacks has taken an emotional toll, but no one expects people to run from cities to live in the hills. "Everyone's afraid now but you get to a point where you can't live that way," says McCauley. "The industry is going to be OK because there is still significant demand in urban areas that need housing built." ❖

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