

Meyer Sustaining Portfolios Strategy Analysis of Performance and Trends

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Housing Development Center:

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Thank You

- Meyer Memorial Trust for leadership on the Affordable Housing Initiative, and for funding the Sustaining Portfolios Strategy program
- The JPMorgan Chase Foundation for funding Cohort 1 data analysis
- Meyer Memorial Trust for funding Cohort 2 data analysis

Presentation Outline

- Project Background
- Describe Data
- Describe Portfolio
- Review Financial Performance
- Impact of Project-Based Assistance
- Describe Capital Needs
- Discuss Key Findings and Observations



Meyer Memorial Trust's Sustaining Portfolios Strategy

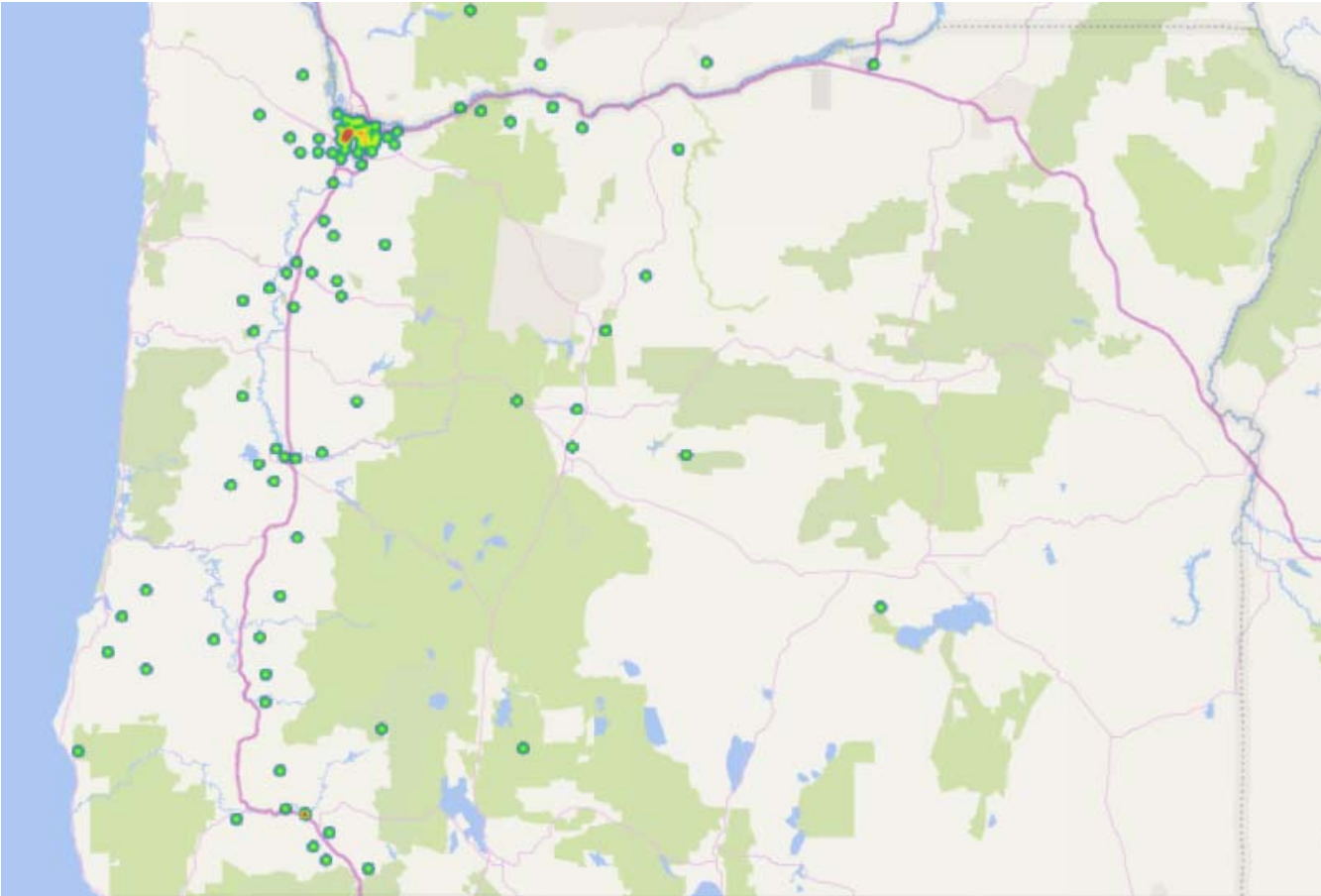
- Improving the long-term sustainability of Oregon's existing affordable housing
- Multi-year program for 19 organizations across Oregon
- Program includes: portfolio assessment, sustainability planning, and technical assistance during plan implementation
- Meyer awarded to each organization: \$75,000 in flexible funding per year and up to 180 hours of technical assistance
- For more information, visit: mmt.org/initiatives/AHI

Data Sources

- Meyer's Sustaining Portfolios Strategy (SPS)
- Multifamily properties in service before 2012, 4+ units
- 2-3 years of financial information, detailed property and portfolio information
 - Audits, financial reports/dashboards, interviews, Capital Needs Assessments (CNAs) and internal staff knowledge
- Most recent full year of operations
 - 2014 for Cohort 1
 - 2015 for Cohort 2
- Performed data quality checks, omitted some properties and outliers

241 Properties and 9,816 units across Oregon

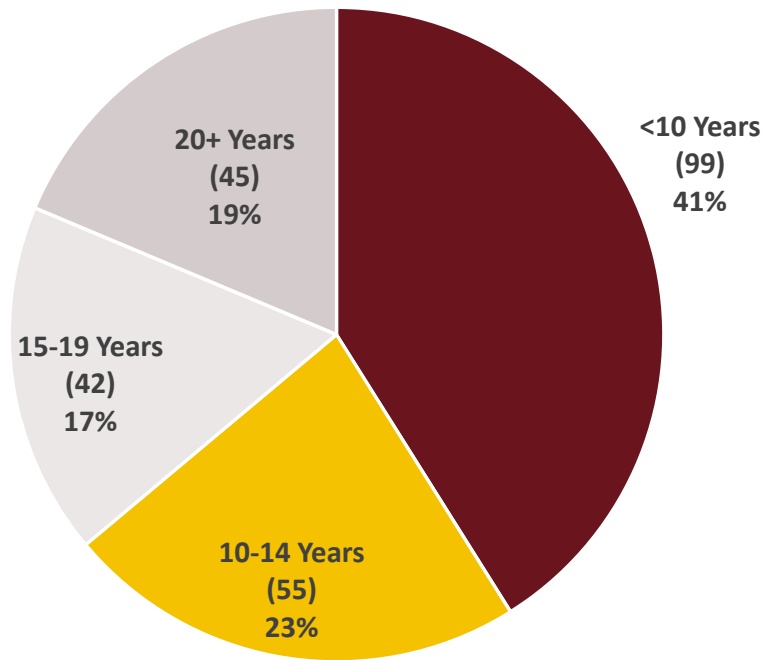
Description of the Portfolio



- 48% of properties in Portland MSA
- 58% of units in Portland MSA
- 53% of properties are self-managed
- 12.7 average age
- 41 average # units
- 43% have C.N.A.
- 81% have must-pay debt

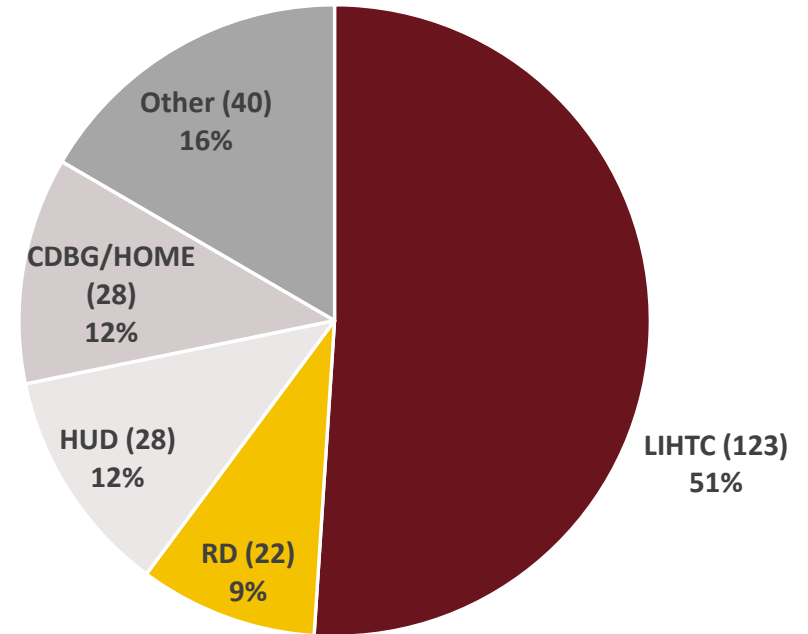
Description of the Portfolio

Age Since Placed in Service



Average is 12.7 years
(#) indicates number of properties in each category

Properties by Funding Type



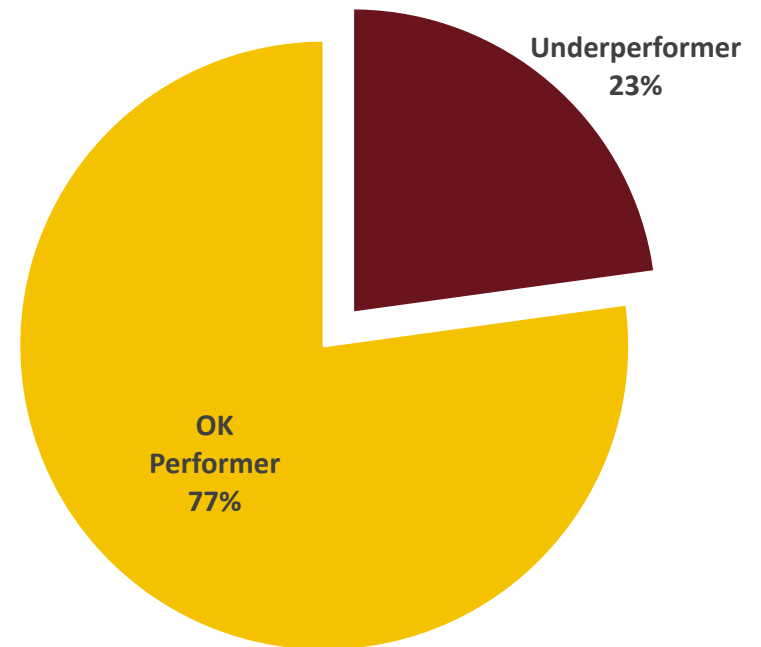
LIHTC: 4% and 9%, past and present
RD: includes properties with both LIHTC & RD funding
HUD: includes properties with LIHTC & HUD, properties with HOME & HUD

Key Performance Metrics – Total Portfolio

- Economic Occupancy: 96.8% average (2014/2015)
- Hard Debt Coverage Ratio: 1.48 average*
 - 61% of properties have hard debt DCR \geq 1.20*
- Operating expenses per unit: \$5,193 average 2014/2015*
- Net cash flow per unit: \$690 average 2014/2015*
 - This is **before waterfall payments** such as: soft debt, investor service fees, deferred developer fees, or asset management & resident services fees

Overall, the Portfolio is Performing Well

- Can define “underperformers” financially or physically
- This definition **only considers financial performance**
- If a property had 2 of 3 indicators of financial distress it is an “underperformer”
 - Negative Net Cash Flow (41 properties)
 - $DCR \leq 1.10$ (60 properties)
 - Expense-to-Revenue Ratio $> 70\%$ (120 properties)
- **23% (55 properties) are defined as underperformers**



Underperformers Have Many Characteristics

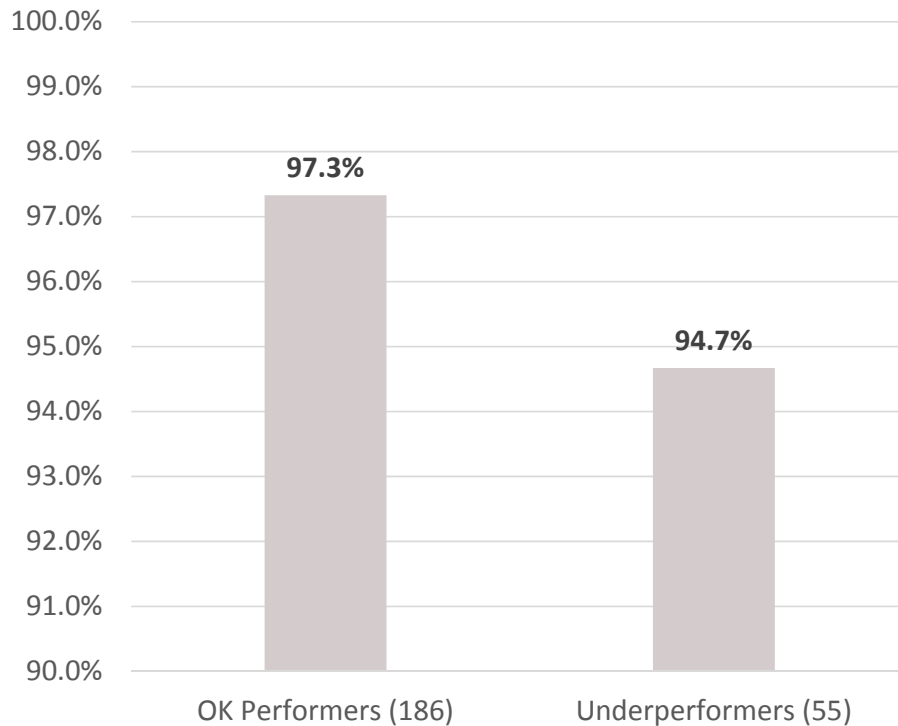
Characteristic	% of Total Portfolio	% of Underperformers	Disproportionate by:
RD, HUD, other funding source	37%	53%	16 percentage points
Fewer than 10 units per building	64%	78%	14 percentage points
2.0+ bedrooms per unit	45%	55%	10 percentage points
Properties 10-19 years old	40%	49%	9 percentage points
3 rd party managed	47%	56%	9 percentage points

Underperformers...

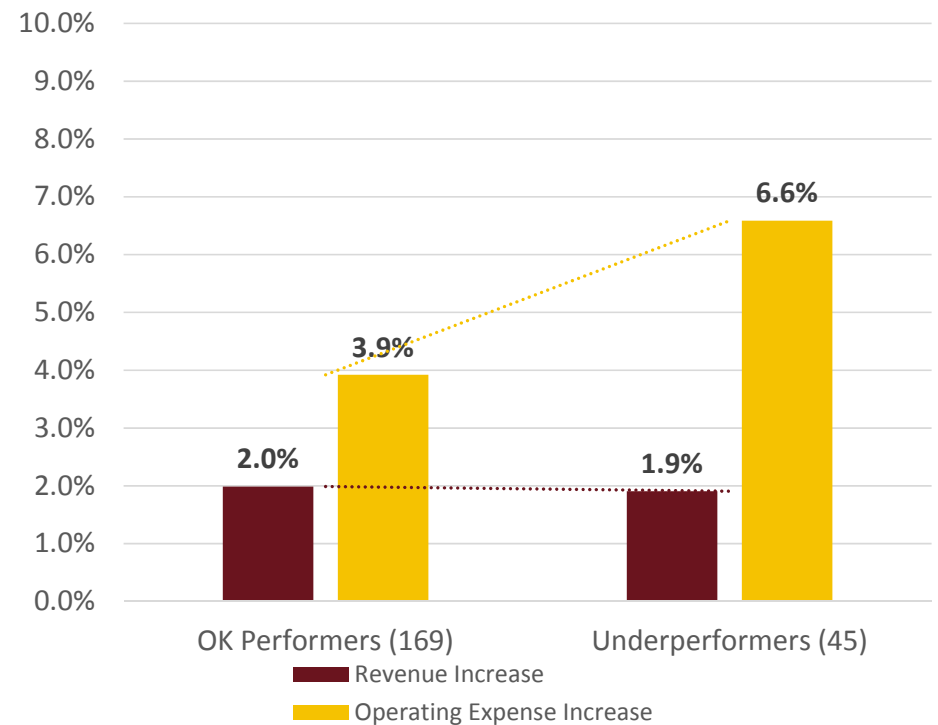
- Are not concentrated in any single organization, PJ or region
- Have almost equal hard debt profiles compared to OK performers

Underperformers Have Higher Vacancy and Expenses

Economic Occupancy Differs



Revenues and Operating Expenses Differ



Nominal change from 2013-14 or 2014-15
Averages exclude outliers

Expenses Differ by Property Structure

- Different properties types have different financial realities
- Underwriting by unit count is not specific enough
 - Bedroom density (average number of bedrooms per unit)
 - Unit density (average number of units in a building)
 - Population
 - Location

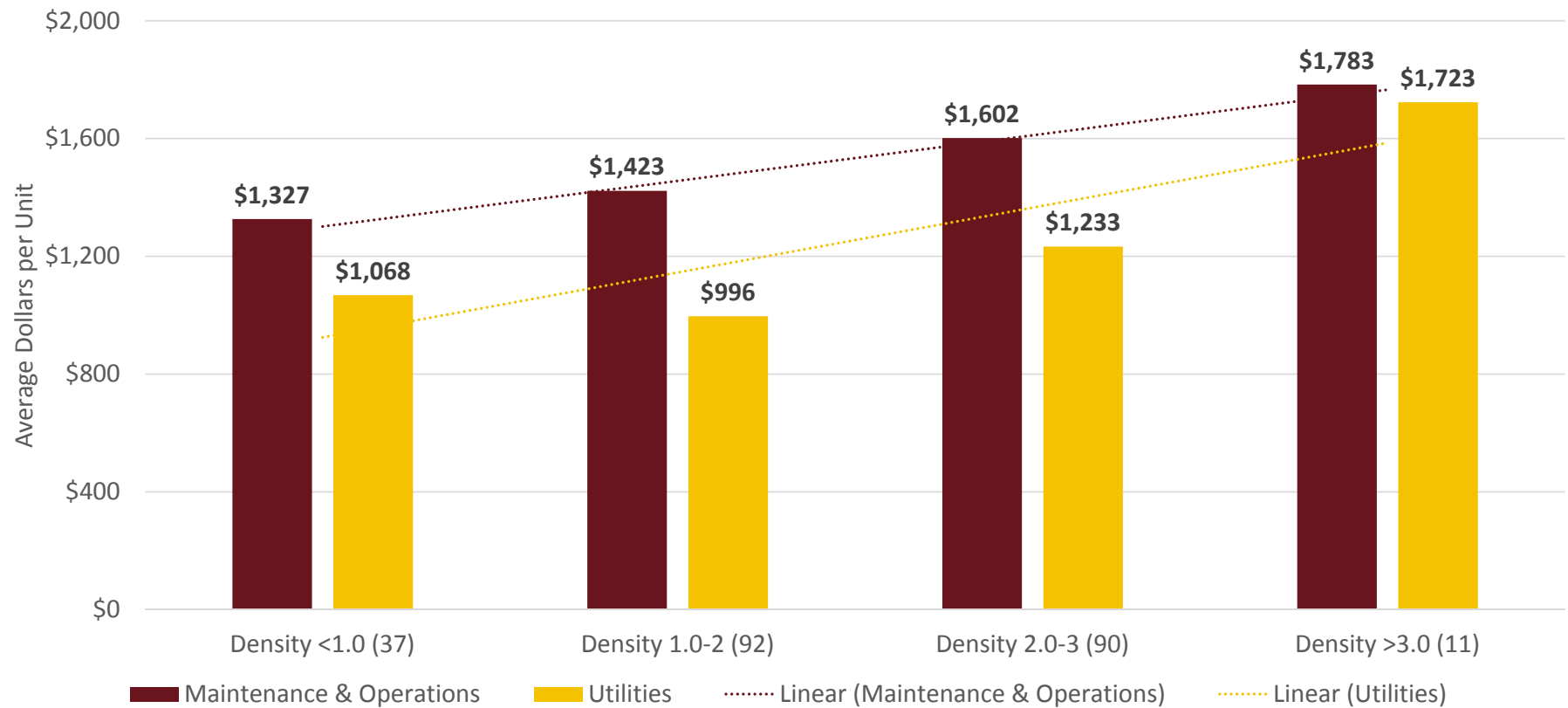
Property Characteristic	# of Properties	Average PUPY Total Operating Expense	Average PUPY Operating & Maintenance
Whole sample	241	\$5,193	\$1,496
Larger families	109	\$5,572 (+\$379)	\$1,621 (+\$125)
30% AMI units	6	\$5,258 (+\$65)	\$1,499 (-\$3)
Lower density	153	\$5,198 (+\$5)	\$1,536 (+\$40)
Rural	104	\$4,856 (-\$337)	\$1,418 (-\$78)
Seniors	36	\$4,841 (-\$352)	\$1,362 (-\$134)

Averages exclude outliers

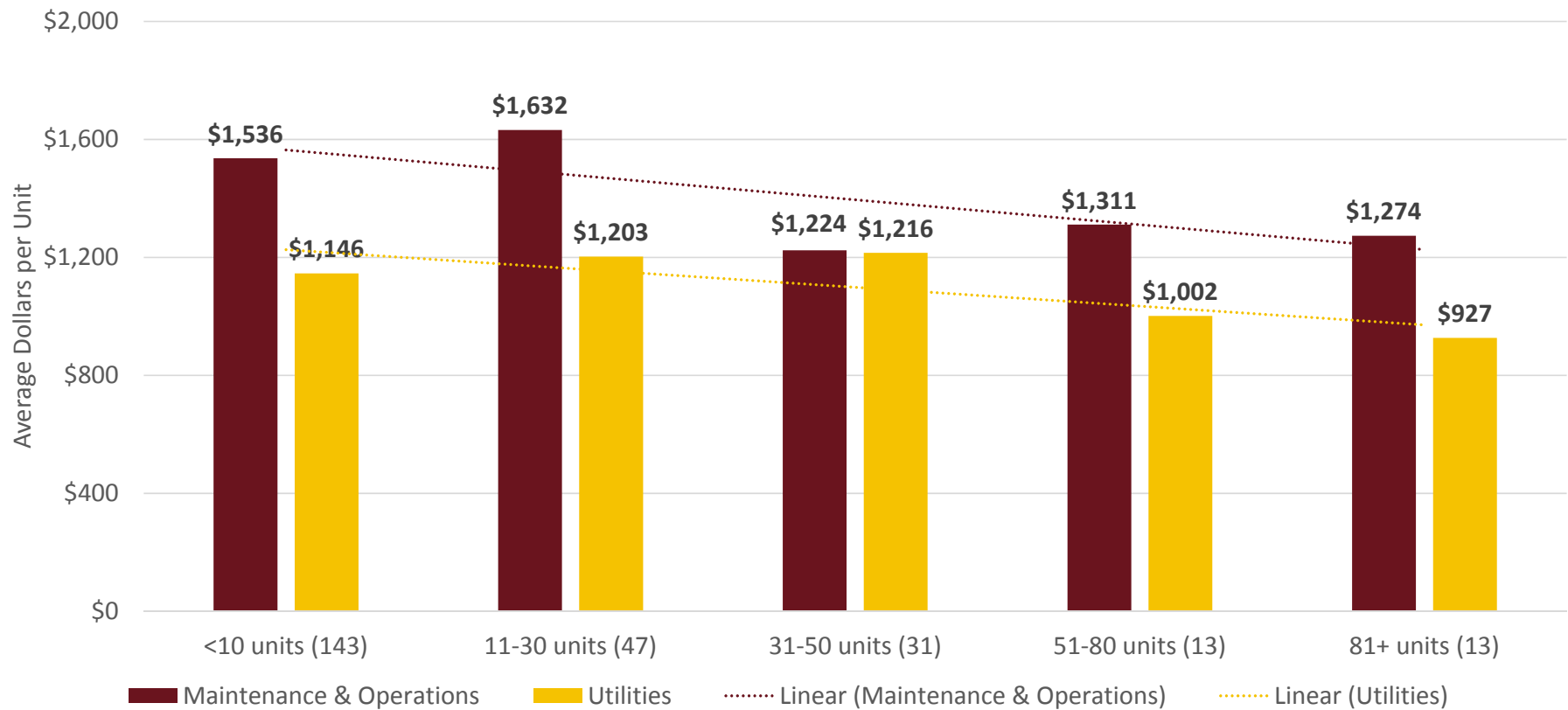
Number in () is the difference from the whole sample average

Total operating expenses include reserve deposits net of withdrawals

Maintenance Costs Increase with More Bedrooms



Maintenance Costs Decline with Fewer Buildings

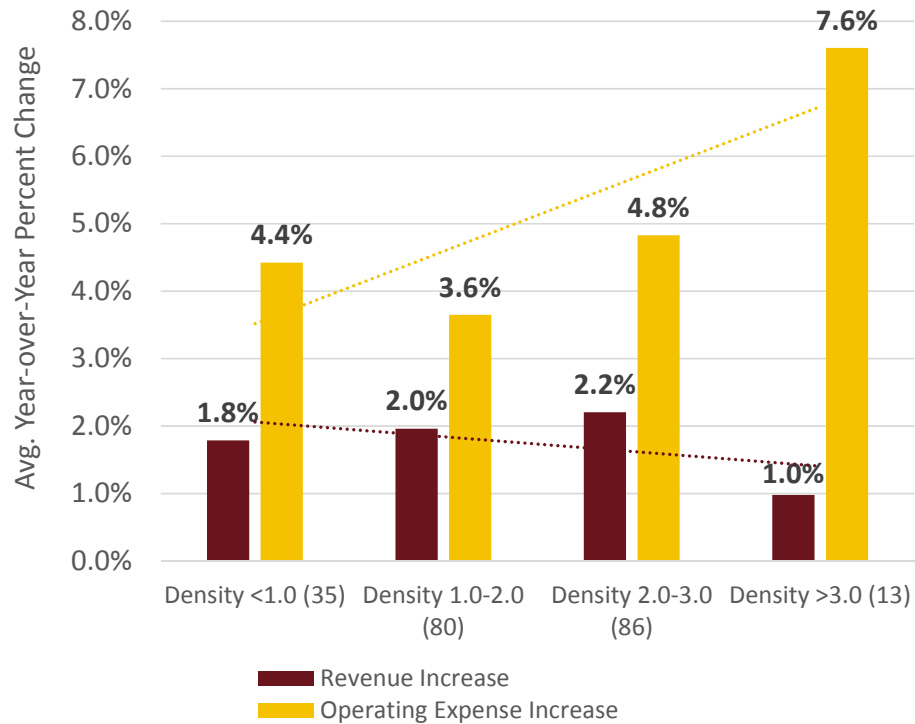


Underperformers have 12.7 units per building compared to 21.5 for OK properties

Averages exclude outliers

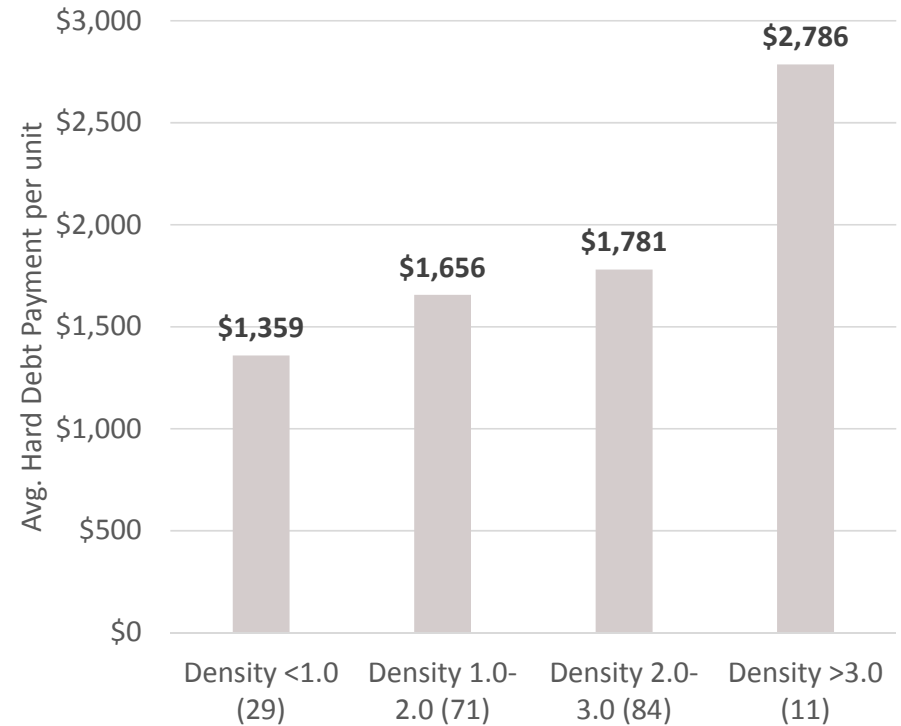
Large Bedroom Properties More Expensive to Operate

Revenue and Operating Expenses Diverge



Nominal change from 2013-14 or 2014-15
Averages exclude outliers

Higher Debt Payments



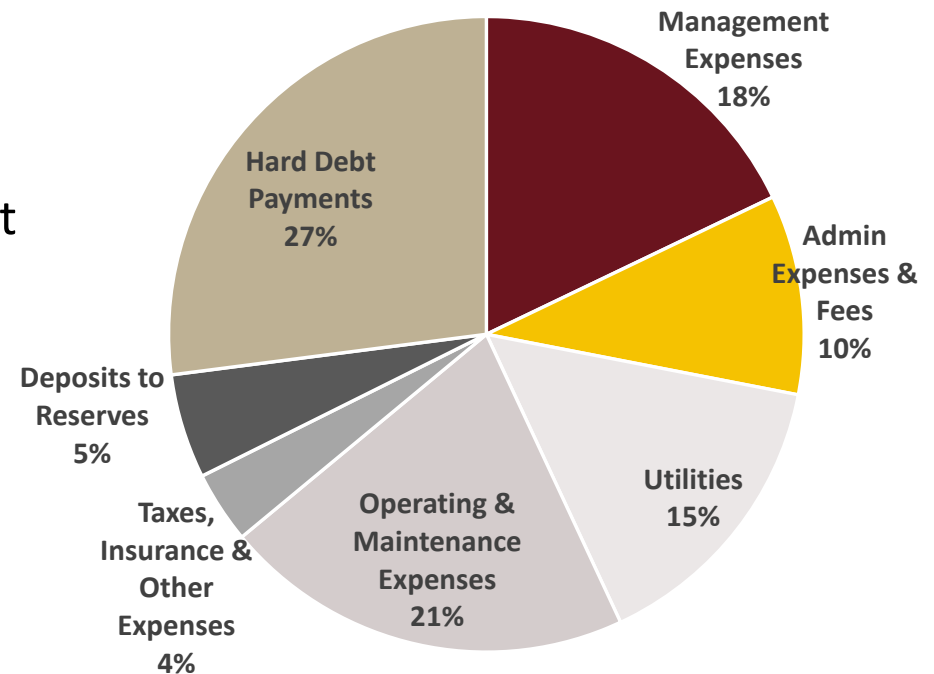
Averages exclude outliers

Debt Is the Largest Financial Outlay

- 81% of properties have hard debt
 - \$23,644 average balance per unit
- 86% of properties have some debt
 - 5% of properties have only soft debt
 - \$38,090 average *total* balance per unit
- 61% of properties have hard debt DCR ≥ 1.20

- 14% of properties have no debt

2014/2015 Total Operating Expenses and Debt



Project-Based Rent Assistance – Descriptive Statistics

- Shift focus to revenues
- 27.2% of units have PBRA (42.7% of properties)
- Of 6 properties with $\leq 30\%$ rent restriction*
 - 4 properties have *some* PBRA
 - Average is 77.3% of units have PBRA
- Of 19 properties with $>60\%$ rent restriction*
 - 6 properties have *some* PBRA
 - Average is 66.0% of units have PBRA
- PBRA mostly going toward smaller units
 - 1-BR units had more PBRA – overrepresented by 12.5 percentage points
 - 2-BR units had less PBRA – underrepresented by -15.8 percentage points



Project-Based Rent Assistance – Small Sample Size

- Looked at relationships between PBRA and:
 - Net Cash Flow
 - Operating Expenses (Management, Admin & Fees, Maintenance)
 - Hard Debt
 - Capital Needs
- Only 103 properties have PBRA – 42.7% of properties – limited sample size
 - Too few properties in each category to confidently draw conclusions
 - Small properties, hard turns, long vacancies, only 1 year of financials – easy to throw off relationships
- **Hard to extrapolate these relationships into key findings and policy recommendations**

Project-Based Rent Assistance – Impact on Cash Flow

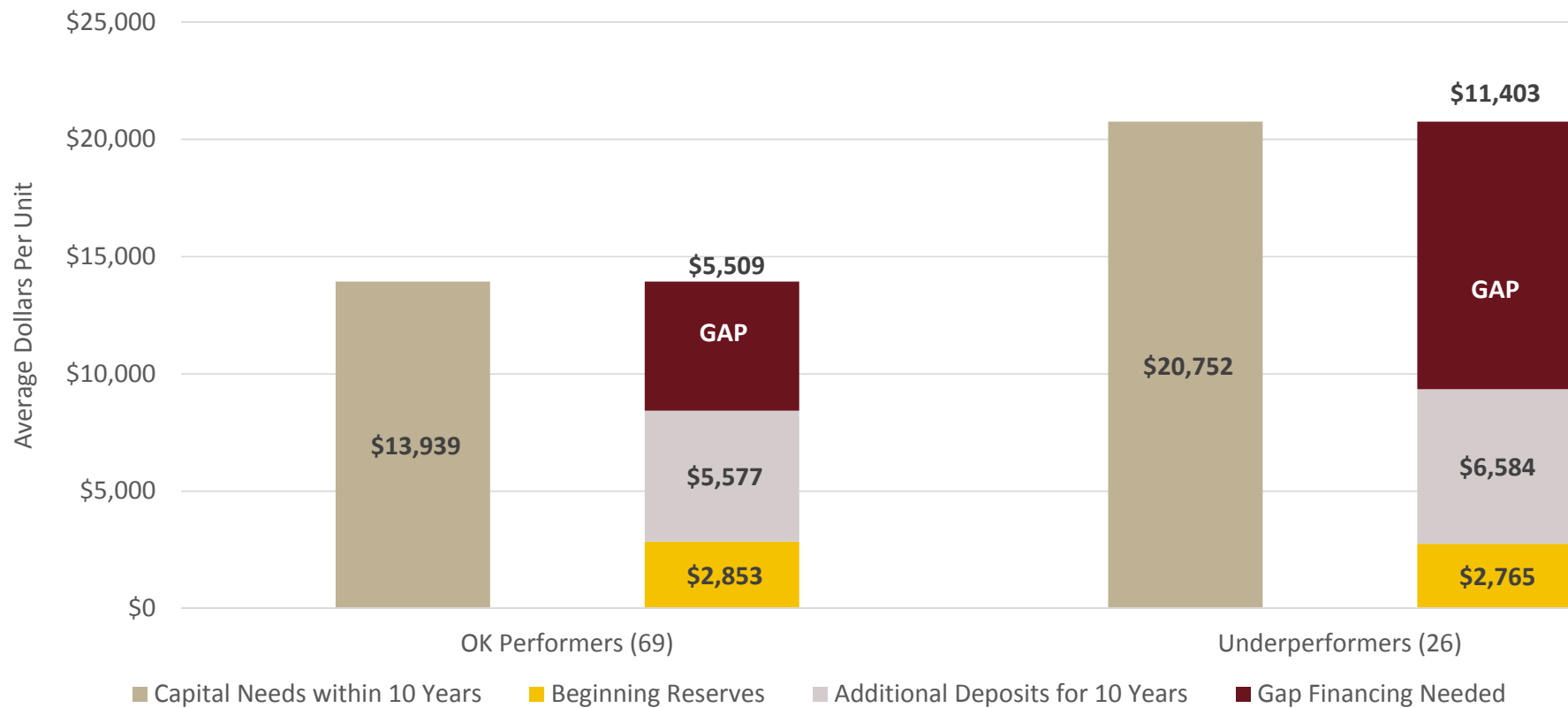
- PBRA has big impact on NCF at lower rent-restricted* properties
 - Smaller impact at higher rent-restricted* properties
- Properties with $\leq 30\%$ rent restriction* (6)
 - Avg. NCF for all 6: \$593 per unit
 - Avg. NCF for 2 without PBRA: \$142 per unit
 - Avg. NCF for 4 with PBRA: \$819 per unit
- PBRA has big impact on NCF at large-bedroom properties
 - Smaller impact at smaller bedroom properties
- Properties with BR Density > 3.0 (14)
 - Avg. NCF for all 14: \$378 per unit
 - Avg. NCF for 8 without PBRA: \$117 per unit
 - Avg. NCF for 6 with PBRA: \$727 per unit

Physical Condition Is Also a Big Factor in Performance

- Many factors determine extent of capital needs:
 - Design, materials, construction quality assurance, level of maintenance
- 42% of properties submitted physical reports with cost information
- Reports have varying levels of rehab and cost accuracy
- Average \$15k in capital needs per unit over next 10 years
 - 31 properties have more than \$20k per unit
 - 15 properties have more than \$40k per unit



Underperformers Have Higher Capital Needs

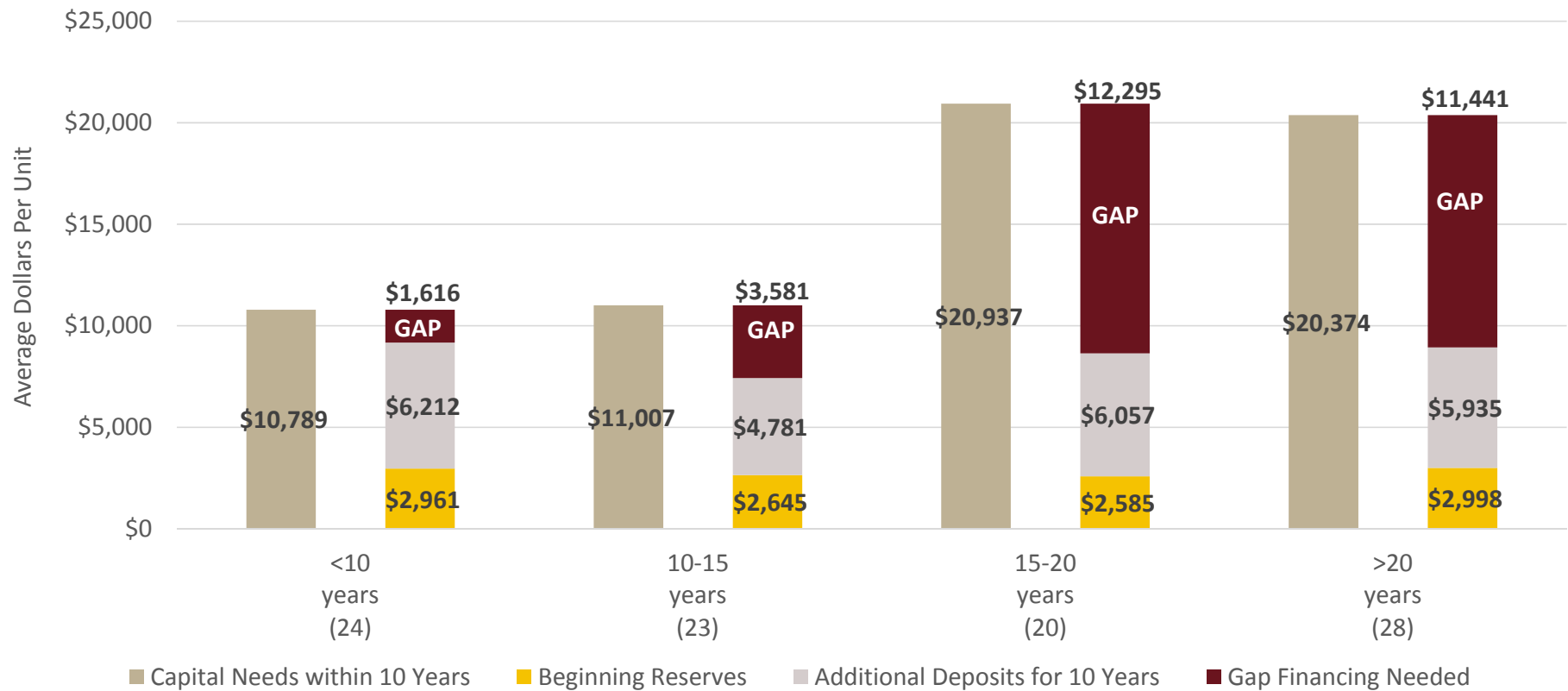


Averages exclude outliers

Analysis is limited to the 94 properties with reserves and non-outlier, immediate capital needs estimates (10-year hard construction costs only)

Capital Needs Gap: we assumed the 2014/2015 deposit was made annually for 10 years, escalating 3% annually and no withdrawals were taken

Capital Needs Gap Grows as Properties Age



Averages exclude outliers

Analysis is limited to the 94 properties with reserves and non-outlier, immediate capital needs estimates (10-year hard construction costs only)

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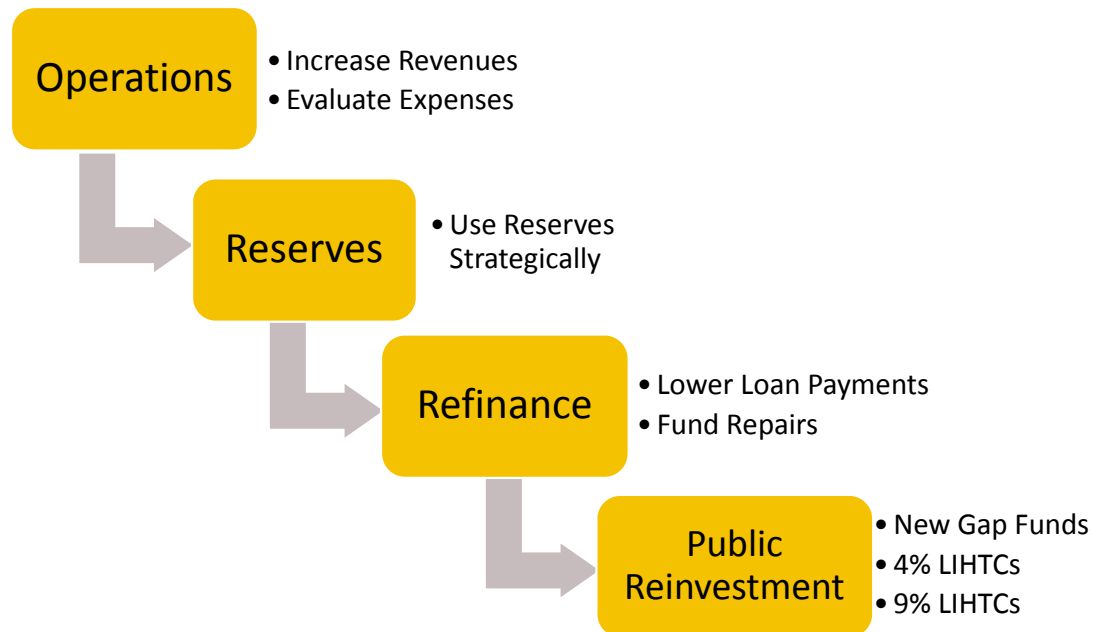
Refinancing Can Help Cover Capital Needs

- How many properties could potentially refinance to cover all their capital needs?
 - Sources: Existing replacement reserves + New debt
 - Uses: Retire current debt + Pay for capital needs (assumes 25% soft costs)
 - **Not considering maturity dates, prepayment penalties, restriction periods, etc.**
- Consider properties with: C.N.A., reserves, and positive NOI
 - 92 properties met these 3 criteria for potential refinancing
- New debt assumptions
 - 1.20 DCR requirement
 - 6% interest rate
 - 25 year amortization

1/3 Properties Can Refinance to Cover Capital Needs

- How many properties could potentially refinance to cover capital needs?
 - 30 properties could potentially retire current debt and cover all 10-year capital needs
 - out of 92, or 32.6%
 - An additional 8 properties could potentially retire current debt and cover 75% of 10-year capital needs
 - 38 of 92 or 41.3%
 - An additional 13 could potentially retire current debt and cover 50% of 10-year capital needs
 - 51 out of 92 or 55.4%
- Of the 55 underperforming properties:
 - 19 met the refinancing criteria (+NOI, some reserves, and C.N.A.)
 - 1 property could potentially retire current debt and cover all 10-year capital needs
 - 2 additional properties could potentially retire current debt and cover 50% of 10-year capital needs

Owners Are Working to Improve Conditions



Workout waterfall for owners

- Improve operations
- Use reserves
- Consider refinancing
- Then consider new funding sources

Key Findings from Data – Operations

- Owners are meeting mission, very strong economic occupancy
- Underperformers are not concentrated by location or owner
- Expenses are increasing much faster than underwritten
- Properties with larger bedroom sizes are more expensive to operate
- Building density impacts utility and maintenance expenses
- Not a lot of room to improve operations, problems mostly structural

Key Findings from Data – Capital Needs

- Significant capital needs gap in Oregon, widens with age
- Reserves can help, but are insufficient to address capital needs
- Only a few properties can solve their problems without additional resources
- Properties that underperform financially and face backlogged capital needs have compounding problems
- Difficult to accurately quantify capital needs—and approximate future demand for public resources—across 241 properties

Observations from Technical Assistance

- Owners are optimizing property performance, using available resources
- No dedicated funding available for recapitalization
- Building component useful life is shorter than affordability period
- Need to consider a variety of factors when underwriting operating expenses
- Poor material choices and lack of quality control during construction have lead to expensive failures
- Different tools and strategies are required for large, urban properties and small, rural properties

Preservation Convening - Upcoming Work

- Development of policies to assist affordable housing providers with preservation of rent-restricted properties
- Convening a workgroup of practitioners to identify, fully develop and prioritize policy proposals
- HDC is convening workgroup, other entities will take on advocacy
- This work includes developing messaging concepts to help us talk about the necessity of preserving rent-restricted properties

Questions and Discussion

Thank you

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