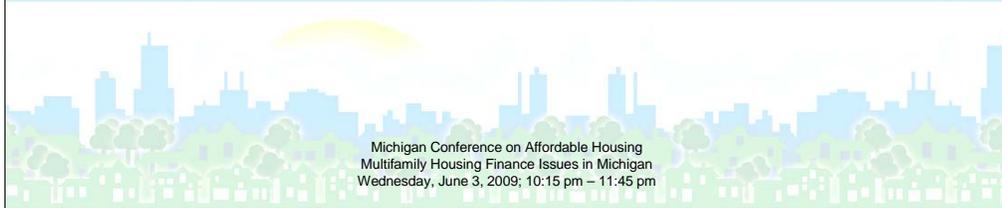


# Market Issues and Process



## Challenges in affordable housing development in Michigan continue



This conference is occurring in the 18<sup>th</sup> month of the current recession; it has been of longer duration in Michigan. Many of the state's primary industrial concentrations have been affected, including both construction and manufacturing. This has led (as these slides will show) to stagnant or decreasing wages, lower employment levels, and a depressed housing market that interferes directly with the ability of the state to add new rental units.



How?

By taking advantage of the opportunities that do exist. For example:

--decreased wages should, all other things being equal, strengthen demand for truly affordable housing.

--a huge amount of money is now available for a number of purposes, for deals that can use them easily.



## Market conditions are a major part of the challenges developers face

The snapshot of market conditions include a for-sale housing market that is slow to recover in terms of both housing values and sales volume, lack of a large-scale bounce back to renting from households transitioning from homeownership, and a senior market that is increasingly price-sensitive, and affected the stockpile of for-sale housing.

Successful developments are still out there to be produced!



In addition to the fact that a number of market segments still need particular types of housing—namely, those that have been most impacted by the current economic situation.

**Understanding market dynamics  
is key to finding success**





Market  
demand in  
Michigan  
varies from  
place to  
place

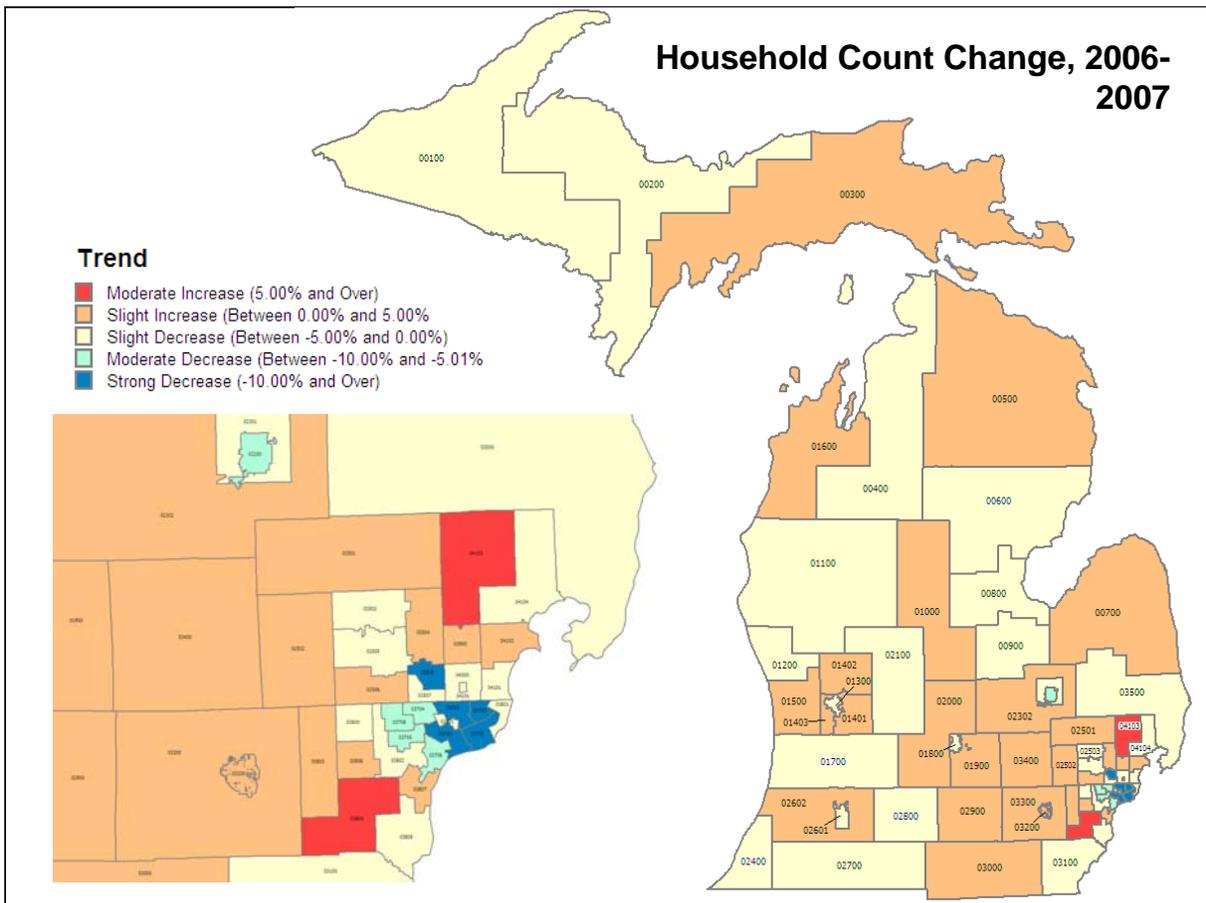
Demand for some types of project has cooled recently, while others tend to see rapid lease-up periods.

Demand is a function of a number of factors that interact. The ones I am concentrating on in this presentation are the basic totals that are important to track.

# Household Change



Collage typifies a number of household types that search for housing: young professionals, young families, new households, elderly. Each has different needs, desires, and preferences in both product and place. Successful developments target their appeals to these households.



Slide sets up a number of re-occurring patterns, like:

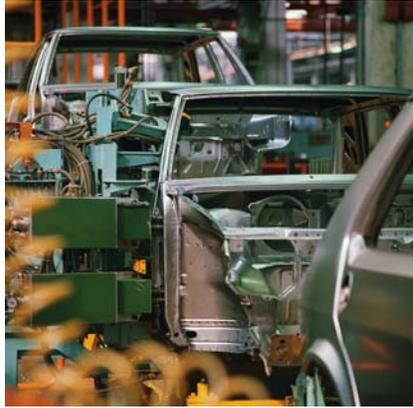
Detroit vs. outstate

Core City vs. Inner Suburban vs. Outer Suburban vs. Rural

In most of these slides—Detroit areas often show distress, in terms of household loss, incomes, etc.—but not in a uniform manner

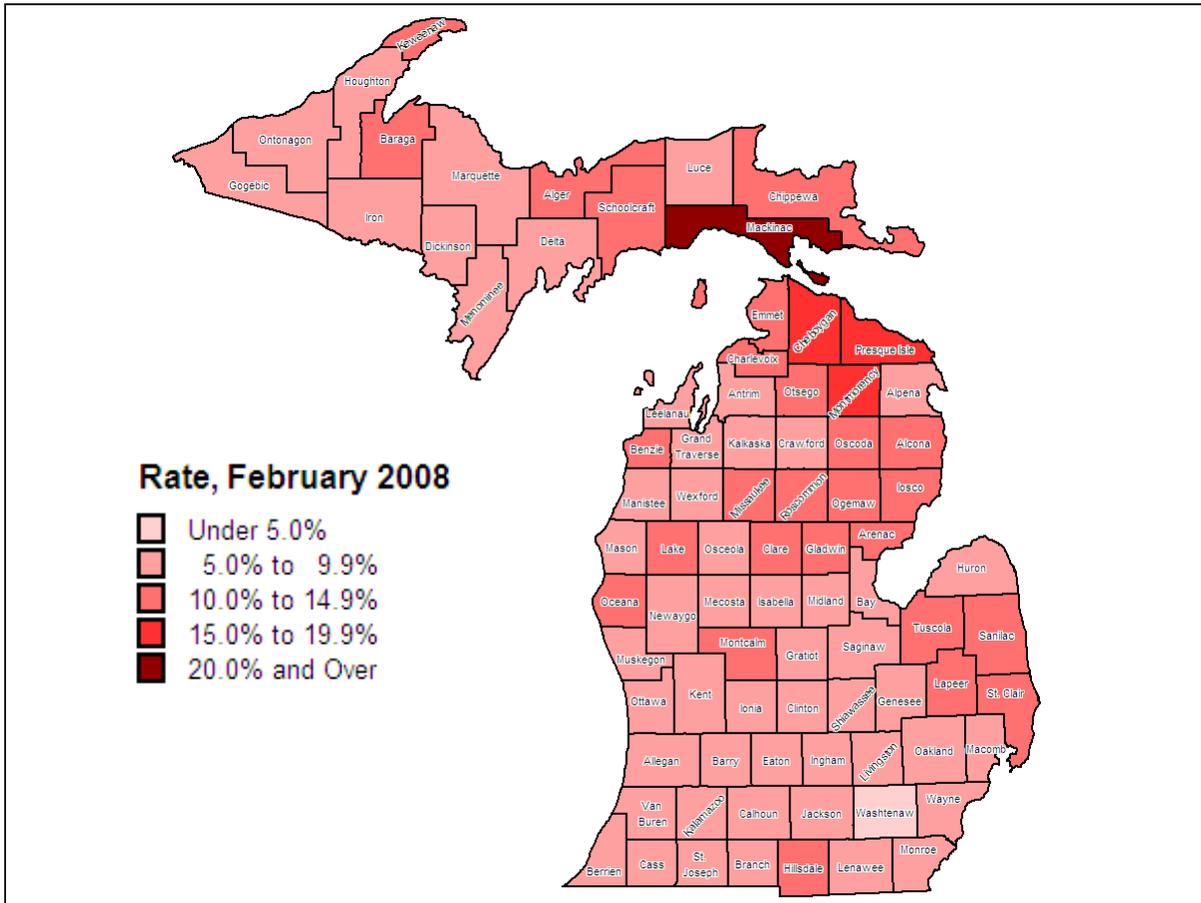
Most areas in the state have not changed much this year, and show either slight increases or decreases. Areas in SE Michigan are different from this pattern, with Detroit, Flint and the Royal Oak area showing steep decreases, and northwestern Macomb and Southwestern Wayne Counties showing moderate increases

# Employment Factors



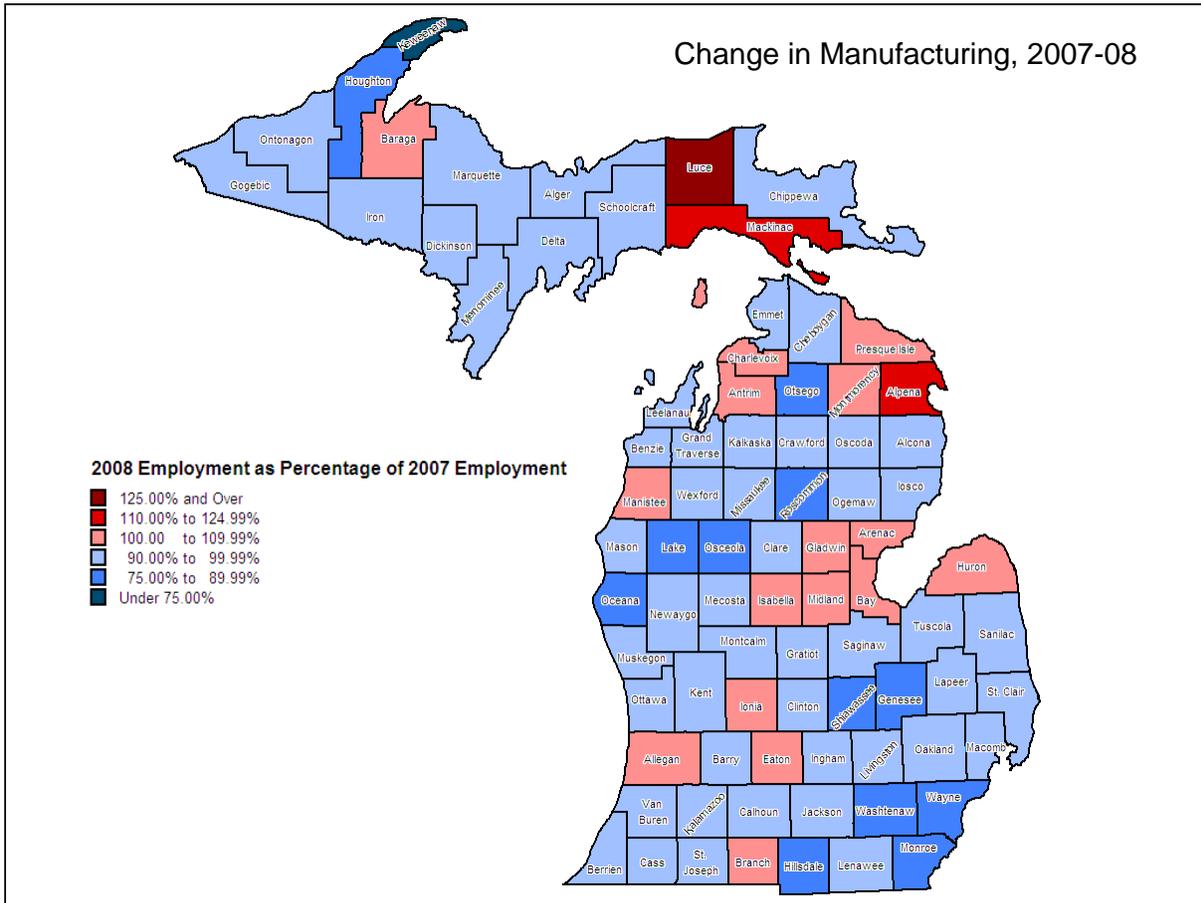
Collage: notes main employers in state—auto-related manufacturing, services.  
Lower rank shows growing areas of promise and attention: IT, life sciences.





This map of unemployment in February 2008 does not show much change from the previous 12 months. Some increase is noted in the Thumb, along with other counties in the northern LP and



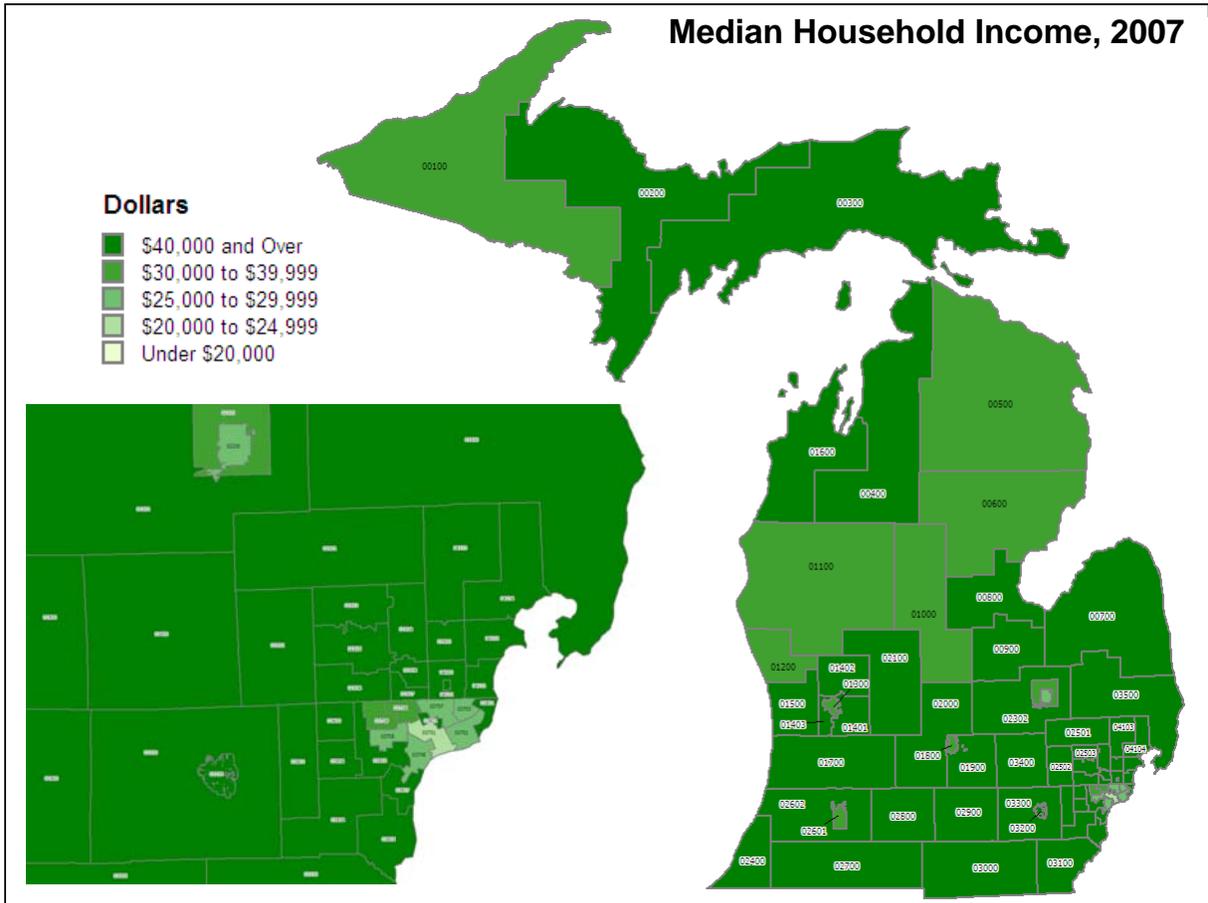


Manufacturing Change map: this map shows that most counties in the state lost manufacturing jobs between Q2 2007 and Q2 2008. Big gains occurred in some northern counties, but they started with small manufacturing numbers, so a moderate increase would register as large in percentage terms. Some of the major manufacturing centers of the state (Wayne and Genesee counties) show major losses, while others (Macomb, Kent, Saginaw) saw fewer losses during this time frame.

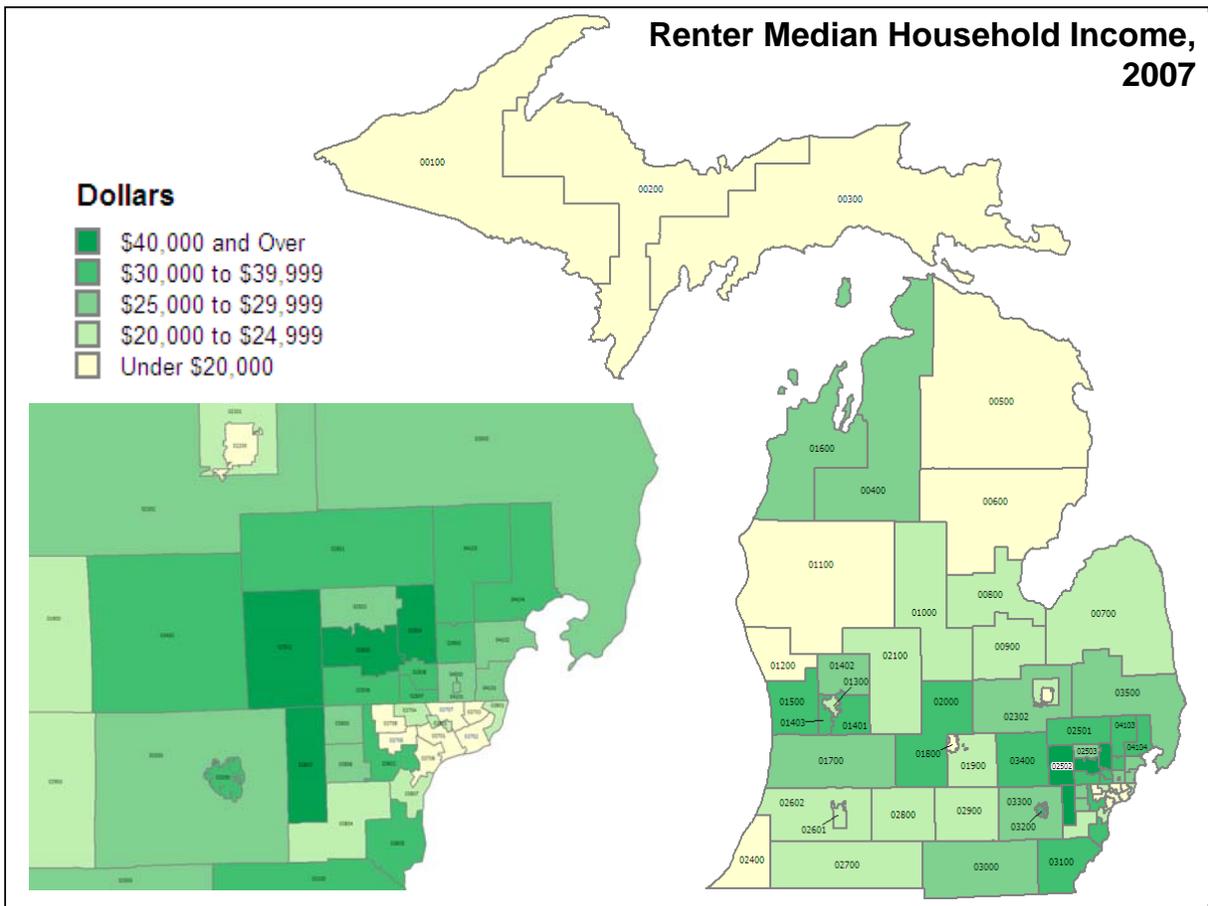
# Income Change



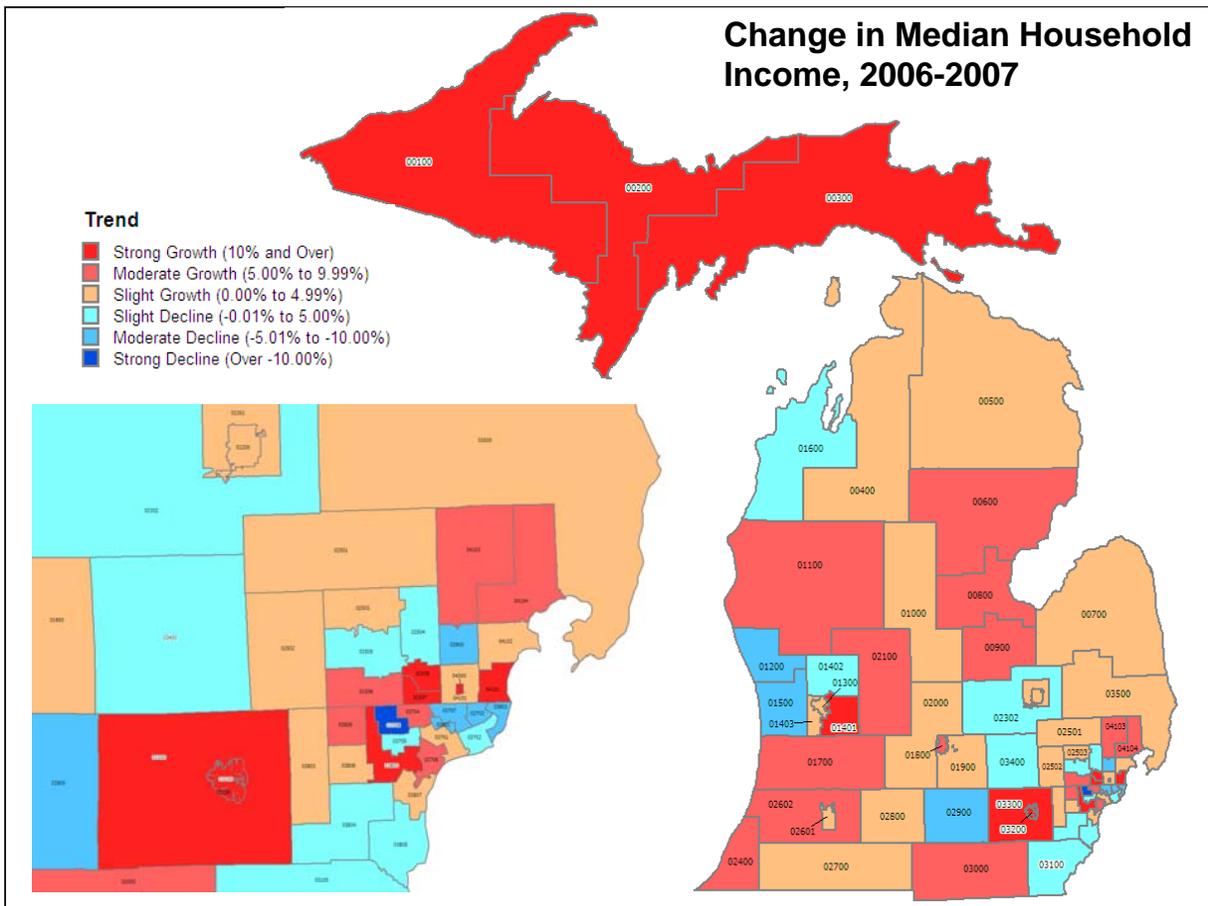
Challenging, as incomes have stagnated for most consumers of housing, driven by losses in hours worked and unemployment increasing.



Household Incomes, 2006: Little change in distribution of wealth across the state, with Detroit suburbs still on top, and northern Michigan and central cities at lower levels.



This map shows the median income of renter households in each area. Note that the map is much lighter in color, due to the fact that renter incomes are much lower than either the overall income figure or the median income for owner households. The situation is worse in most of the state's central cities, and northern rural areas (both Lower and Upper Peninsulas)



Change in Median Household Incomes, 2006-2007: Many areas around the state showed at least slight gains, but these figures are not adjusted for inflation between 2006 and 2007. (2.85% during that period). As this percentage takes up a good proportion of the slight growth category, the situation in median income is more complicated.

Spatially, many areas in Detroit, as well as some smaller centers in the state, have seen incomes decrease in real terms through that year. The situation since then has probably led to a deepening of this condition, as well as a broadening into other areas (especially the Thumb, and areas of Mid-Michigan that are dependent on the auto industry).

**Market supply has been affected in some areas by a lack of demand for certain product types**



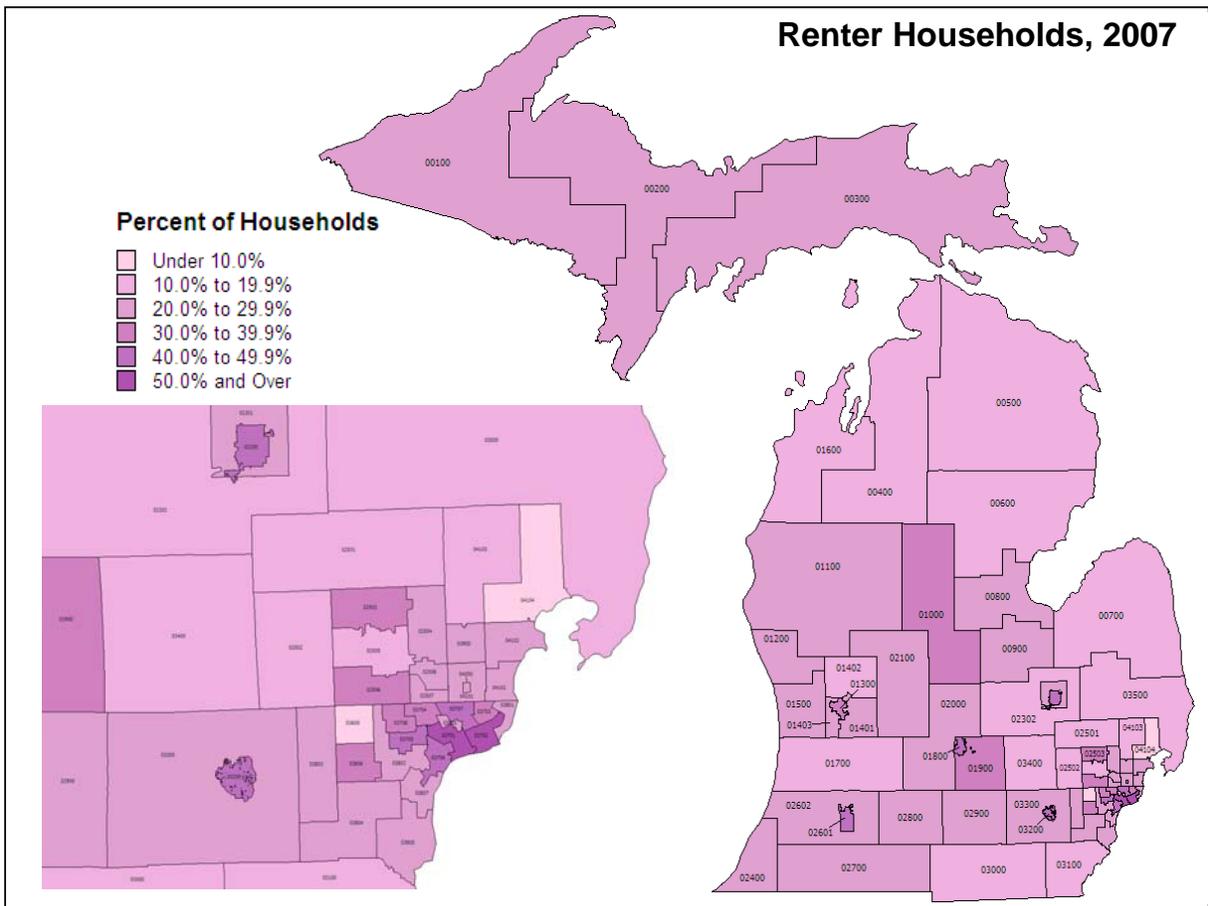
Which types?

New-construction senior in smaller markets has been more difficult to fill, as seniors are having difficulty selling their homes and the number of 60% AMI units increases.

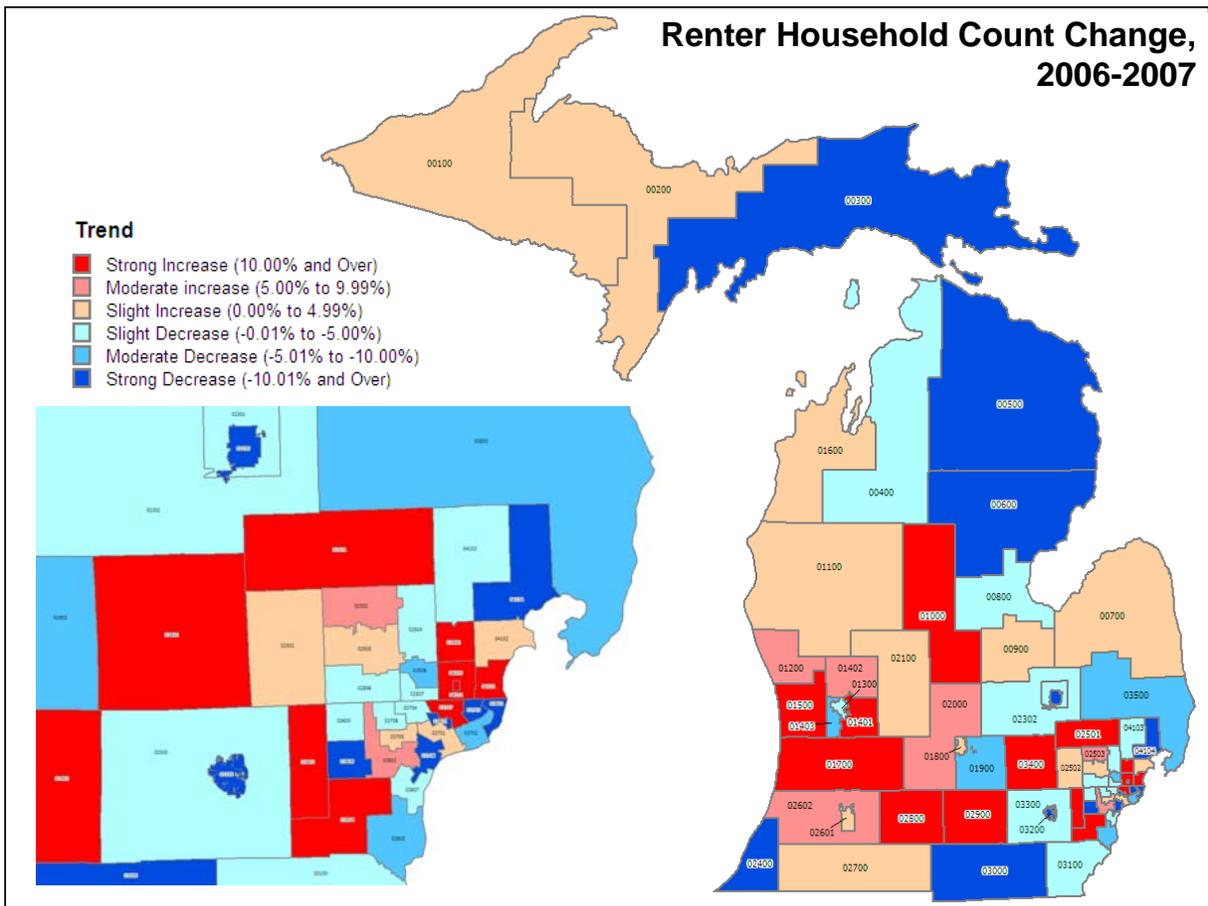
# Tenure



Tenure (the manner in which property is held—owned or leased) is an important factor in determining housing demand. People move between tenure types (owning and renting); renters more so than owners in general. Also, the costs associated with each tenure type differ significantly.



Distribution of Renter Households, 2007: Concentrations are as expected, with higher levels in cities and college areas.

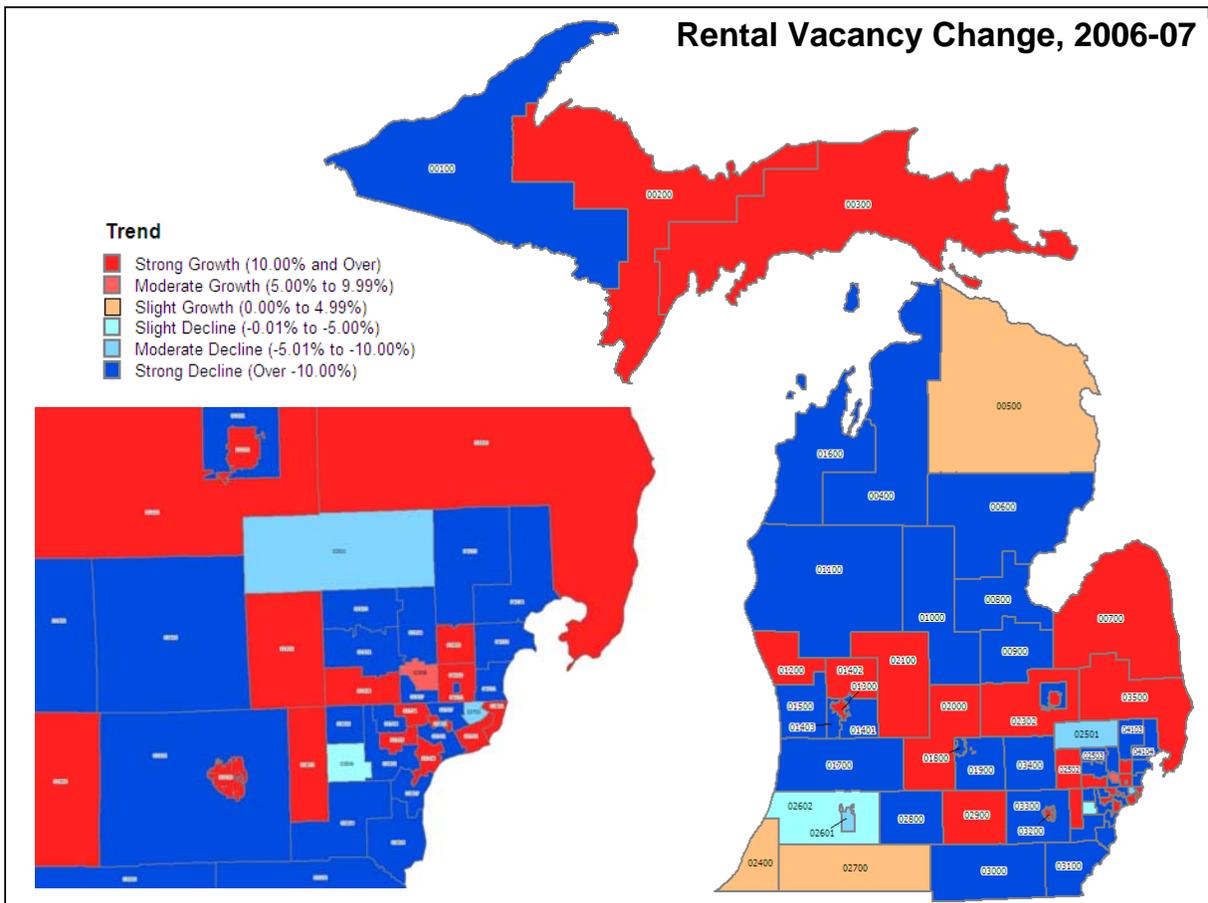


Change in Renter Households, 2006-07: This variable probably fluctuates too much to put much stock in a year-over-year change, but some of the facts are interesting. For example, in a significant number of larger cities (Grand Rapids, much of Detroit, Ann Arbor, Flint) renters decreased significantly. In just a few others (Kzoo, Lansing) numbers were relatively stable or slightly increasing. In general, areas that saw the sharpest increase in renting had relatively low levels to begin with

# Vacancy Rates



“Shadow rental market” is a growing issue—homes or condos that don’t sell and are instead rented to tide owners over. This should be an important source of new (albeit probably temporary) units on the rental market, which may be attractive to newly-foreclosed-upon households.



Change in Rental Vacancy Rate, 2006-2007: Overall vacancy, not just for affordable units. The polarization shown on the map is quite interesting; most of the state saw either strong growth or decline in vacancy rates.

Interesting Patterns: situation is polarized, with large increases and decreases; not much in the middle.

Many urban centers have seen increased vacancy (GR, Ann Arbor, Flint, certain markets in Detroit, Muskegon); as well as smaller out-state centers, the UP and the Thumb

Occupancy has increased in KZoo and Lansing, many suburban areas, and those exhibiting larger rates of household growth.

Affordability is  
the key issue in  
Michigan



Yep, and the Pig should be worried!

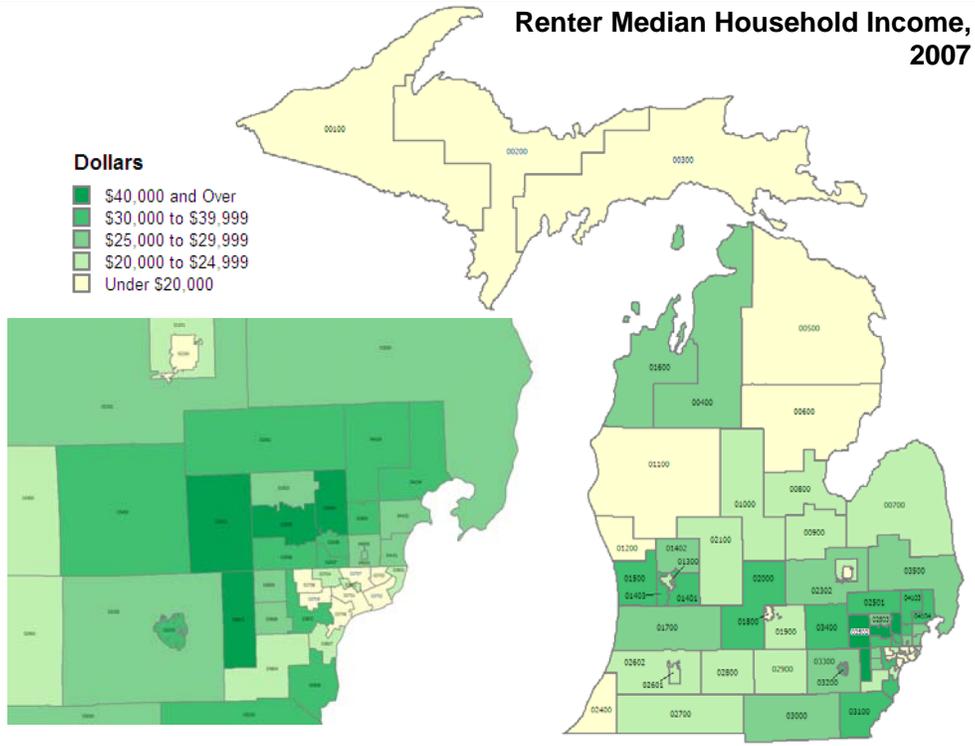
## Owner vs. Renter Incomes



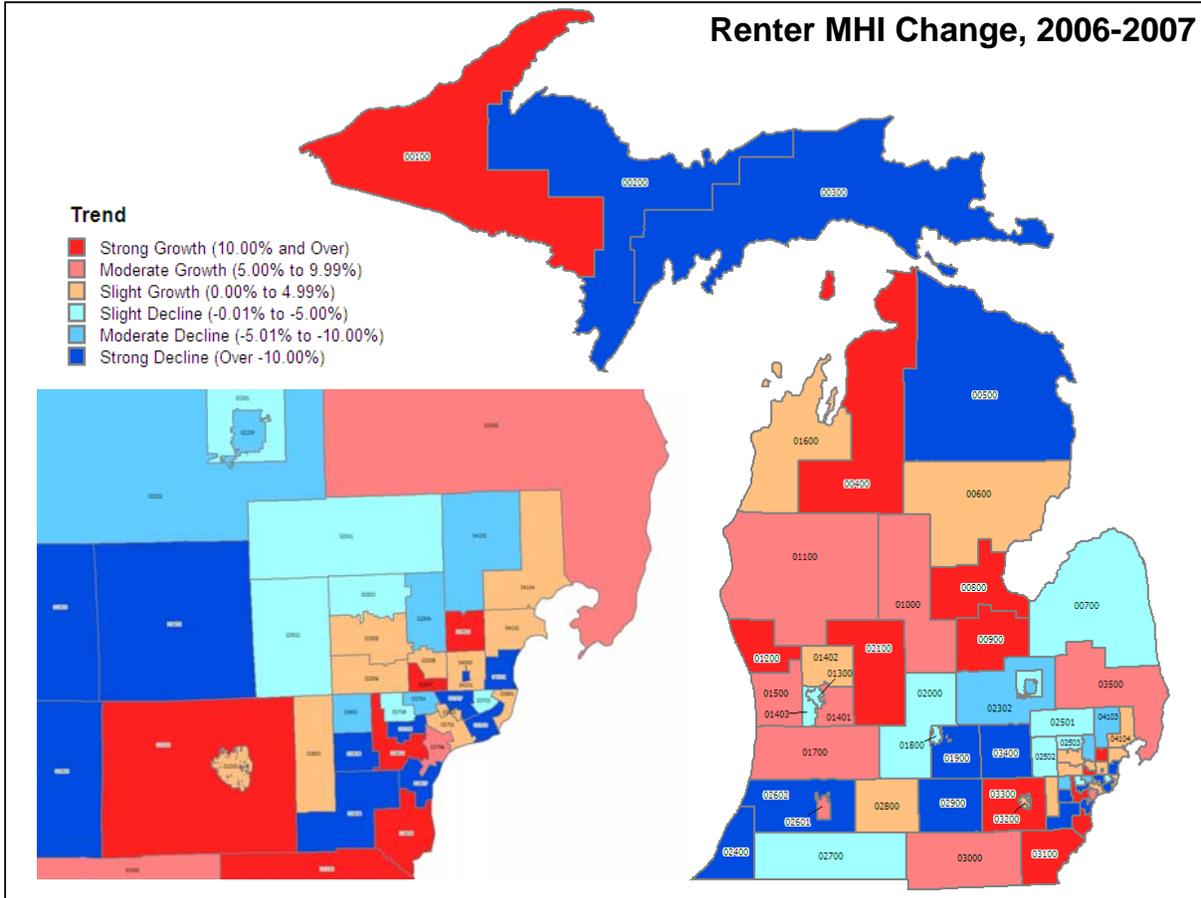
Trend in this statistics is troublesome, as the gap between owner and renter incomes has increased substantially.

# Renter Median Household Income, 2007

- Dollars**
- \$40,000 and Over
  - \$30,000 to \$39,999
  - \$25,000 to \$29,999
  - \$20,000 to \$24,999
  - Under \$20,000



## Renter MHI Change, 2006-2007



Most larger cities in the state have seen decreased renter incomes; KZoo is the exception to this.

# Foreclosures







Given these patterns, what  
are the ways ahead?

**Understanding market dynamics  
is key to finding success**



Opportunities exist for different types of product, targeted to underserved populations, dependent on local market conditions—Flight to Quality



## “Flight to Quality”

- What is quality in this market?
  - Preservation of subsidy
  - Projects with rent advantages—do not push upper AMI limits
  - Mixed-use projects supporting downtowns
  - Other “Niche” products—affordable assisted living (given that it is affordable), supportive housing with project-based vouchers and strong service providers, etc.

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Used to say “do not push 60% AMI limits”, but due to limits on increases in HUD-generated AMIs (and therefore rents), to ensure that contract rents do not have to change due to increasing utility allowances, some buffer even at lower targeted percentages is advisable.

# Market Analysis System

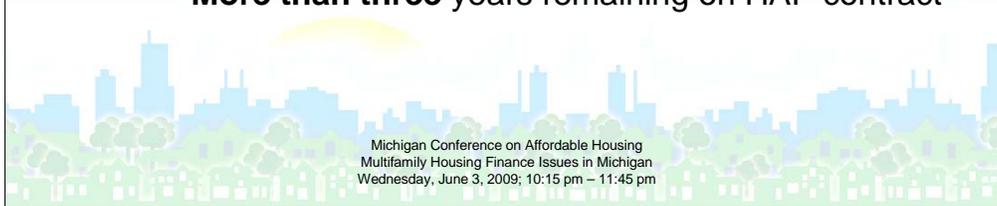
- On first contact with developer regarding proposal:
  - Provide list of firms, two-firm veto (list in Tab C, Combined App (on website))
  - Fee: \$5,700 full study; \$6,300 for New Economy/Downtown/Niche Market study; \$3,000 prelim or reduced scope, \$1,500 for most updates (new this year)
  - On successful completion of prelim, \$2,700 for a full study on same project
- See “Market Study Initiation Request” (included in handouts)



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

# New Market Analysis System

- Reduced Scope Studies
  - Meant specifically for preservation of projects with tenant subsidy (Section 8, etc.)
  - Project qualifies if it meets all of the following:
    - Rent subsidies cover **at least 95%** of units
    - **At least 90%** occupied
    - Rent increases after rehab **less than 10%**
    - **More than three** years remaining on HAP contract



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# New Market Analysis System

- Call David Allen to set up work
  - Provide site map, project narrative, amenity information, pro forma, or anything else that will aid the analyst in setting up market analysis for subject
  - Provide names of two vetoed firms
  - On receipt of check, work will be assigned to a non-vetoed analyst
  - Phone: 517-335-4786
  - Email: [allend1@michigan.gov](mailto:allend1@michigan.gov)

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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

# New Market Analysis System

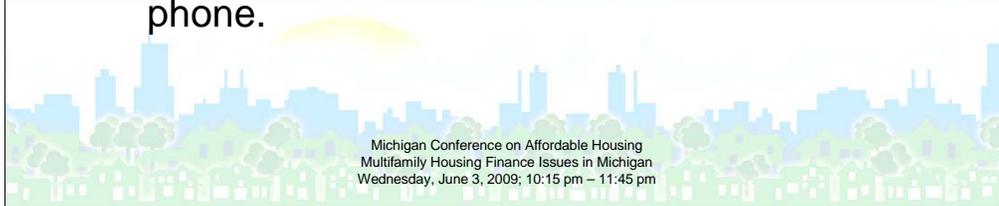
- On assignment of work:
  - Two weeks until Primary Market Area (PMA) is due, MSHDA OK's PMA within 2 days of receipt
  - After PMA is approved, three weeks to finish work on study. Developer contact with analyst is minimal, and must be carried out through email, with MSHDA marketing staff CC'd.



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

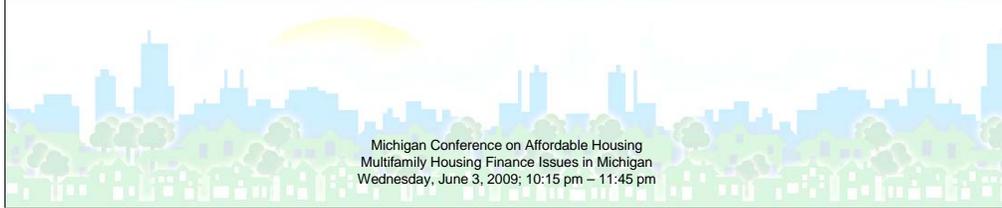
# New Market Analysis System

- On completion of study:
  - It is sent to developer and MSHDA.
  - After all parties review the study, a meeting between MSHDA Marketing staff, market analyst and developer (as well as HDO, if applicable) is convened to discuss results. This has often been done over email and the phone.



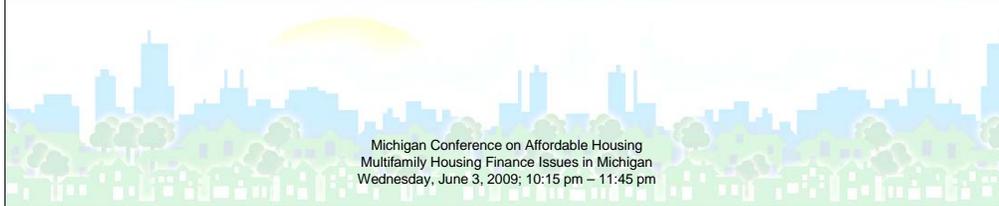
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# MSHDA's New Lending Parameters and Loan Process



## Reasons for Parameter Changes

- Soft Rental Market Conditions
- The decline in the tax credit equity market
- The Housing Economic Recovery Act (HERA)
- The American Recovery and Reinvestment Act (ARRA)



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

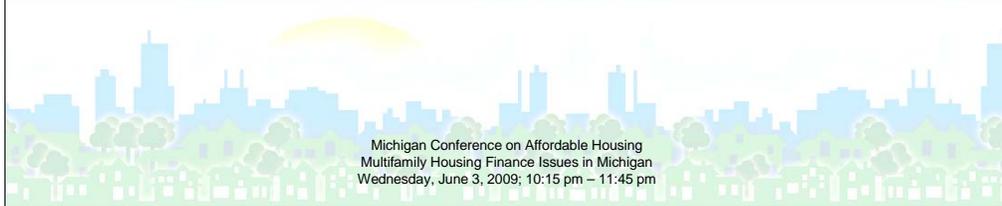
## Areas of Parameter Changes

- Consolidate and Clean Up
- Conservative Underwriting Assumptions and More Consistent with 2009 Qualified Allocation Plan (QAP)
- Include Criteria of the Preliminary Implementation Plan
- Loan Processing Changes
- Priority Award of Soft/Gap Funding

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# Consolidate and Clean Up

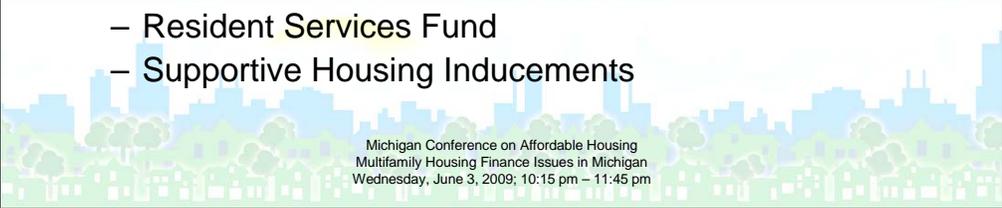
- Six previous sets into one version
  - HOME Team Advantage, TEAM, Taxable and three sets of Preservation Programs
- Distinctions between Project Types



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## Consolidate and Clean Up cont.

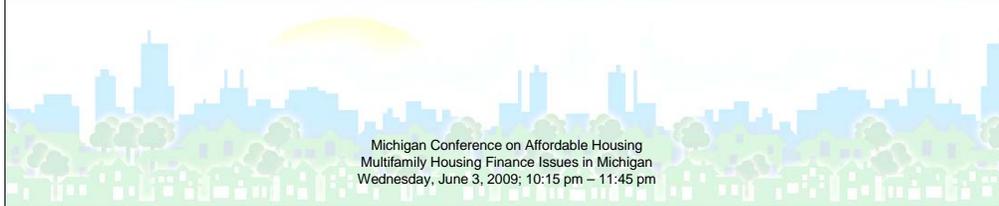
- Housekeeping Changes Included the following Sections:
  - Prepayment
  - Subordinate Loan
  - Syndication Pay-In Section
  - Operating Deficit Reserve
- Current Practice Changes Included the following Additions:
  - Project Based Vouchers
  - Resident Services Fund
  - Supportive Housing Inducements



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## Additions to Parameters

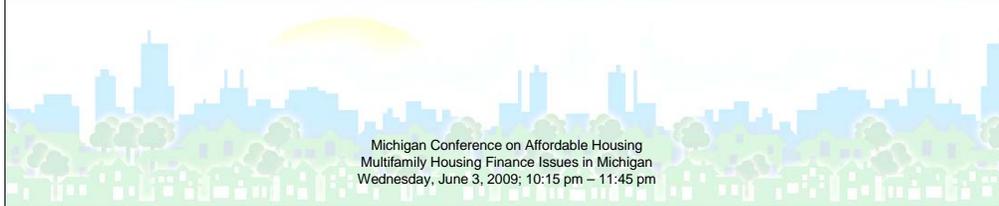
- Tax Abatement – now required of all projects
- Appraisals – MSHDA contracts for preservation and acquisition rehab proposals



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

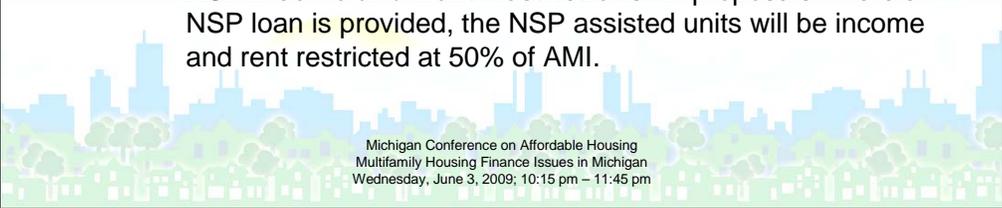
## Conservative Underwriting Assumptions and Consistent with 2009 Qualified Allocation Plan

- Increased Debt Coverage Ratio to 1.25
- Increased Minimum Vacancy Loss to 8%
- Implemented New Trending Assumptions
- Deeper Rental Targeting



## Include Criteria of Preliminary Implementation Plan

- NSP, TCAP and Section 1602 Program Funding Sources
  - Loan or Grant terms
  - Income and Rent Restrictions
    - **TCAP and Monetized Income and Rent Restrictions:** In proposals where a TCAP loan or Monetized Credits is provided, income and rent limits will be consistent with the Low Income Housing Tax Credit requirements
    - **NSP Income and Rent Restrictions:** In proposals where a NSP loan is provided, the NSP assisted units will be income and rent restricted at 50% of AMI.



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

## Include Criteria of Preliminary Implementation Plan Cont.

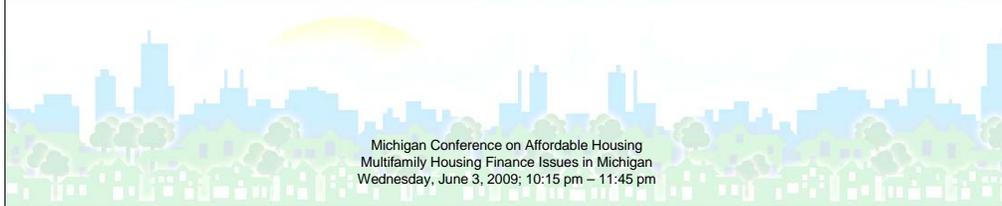
Determining the number of designated ARRA or HERA units

- TCAP and Monetized assisted units will be subject to forthcoming federal regulations. But generally, any Low Income Housing Tax Credit designated unit will also be a TCAP or Monetized assisted unit.
- If an NSP funded Subordinate Loan is provided, the number of NSP designated units will be calculated based the prorata share of total development cost funded with NSP.

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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

# Loan Processing Changes

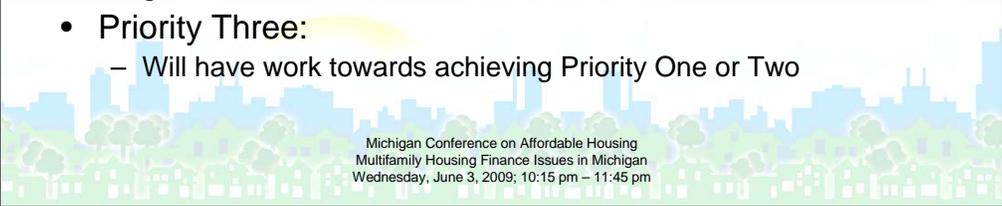
- Preliminary Project Assessment
- Threshold Review
- Commitment
- Initial Closing



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

# Priority Awarded Soft/Gap Funding

- **Priority One:**
  - Targets preservation projects with remaining rental subsidy terms, or –
  - New Construction transactions with greater level requirement of leveraged funding, or –
  - NSP Eligible
- **Priority Two:**
  - Targets those preservation projects without remaining rental subsidy, or
  - New Construction transactions with a level of leveraged funding greater than the threshold
- **Priority Three:**
  - Will have work towards achieving Priority One or Two



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

## 4% Tax Credit Projects Subject to the Updated Parameters?

- **Without** MSHDA soft/gap funding, or when stacked with monetized credits, 4% transactions are subject to Sections I – VI only. Prioritization is not necessary.
- **With** any MSHDA soft/gap funding, unless monetized credits alone are used, 4% transactions are subject to Sections I – VII. This then includes the Priority Selection Process for awarding the funding.

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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

## 9% Tax Credit Projects Subject to the Updated Parameters?

Under the May 1, 2009 funding round:

- **Without** TCAP assistance or MSHDA Taxable Bond financing, the 9% transaction is not subject to the updated parameters.
- **With** TCAP assistance, but without MSHDA Taxable Bond financing, the project is subject to Sections I – V of the parameters.
- **With or Without** TCAP assistance, but with MSHDA Taxable Bond financing, the project is subject to Sections I – VI of the parameters.

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Multifamily Housing Finance Issues in Michigan  
Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

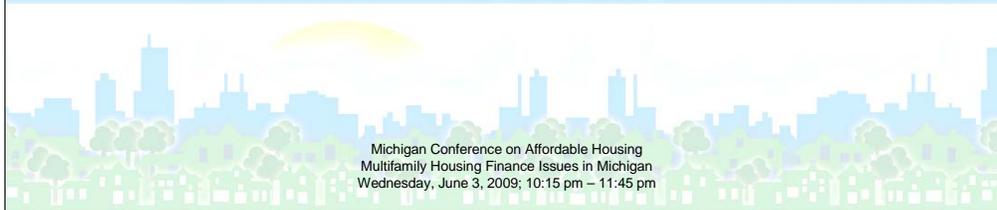
## 2007 – 08 Exchange Projects Subject to the Updated Parameters?

- **Without** Section 1602 Program funds or Taxable or Tax-Exempt financing, the project is not subject to the updated parameters.
- **With** Section 1602 Program funds, but without Taxable or Tax-Exempt financing, the project is subject to Sections I – V.
- **With or Without** Section 1602 Program funding, but with MSHDA Taxable or Tax-Exempt financing, the project is subject to Sections I – VI of the parameters.

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Multifamily Housing Finance Issues in Michigan  
Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

## Web Site for Parameter Posting

- [www.michigan.gov/mshda](http://www.michigan.gov/mshda)
- For questions or comments contact:
  - John A. Hundt at: [Hundtj1@michigan.gov](mailto:Hundtj1@michigan.gov)
  - 517-241-7207



Talk about the application for 9% transactions under the 07-08 funding rounds, or the 9% transaction from May 1<sup>st</sup>.

The Authority has placed the Board approved Direct Lending Parameters on the website for public review and comment at [www.michigan.gov/mshda](http://www.michigan.gov/mshda). Click on Developers and Contractors, and look for Multi-Family Direct Lending Programs.

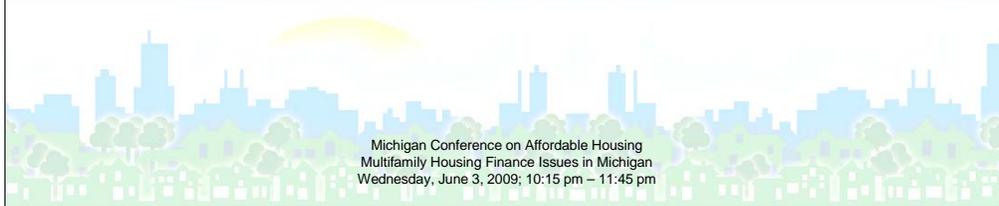
Again, the changes with the parameters were to address concerns with the rental market, make our program more attractive to the equity investors, and implement HERA and ARRA to help the economy recover. We believe they will help.

Any questions?

If you have any questions or comments please feel free to contact me.

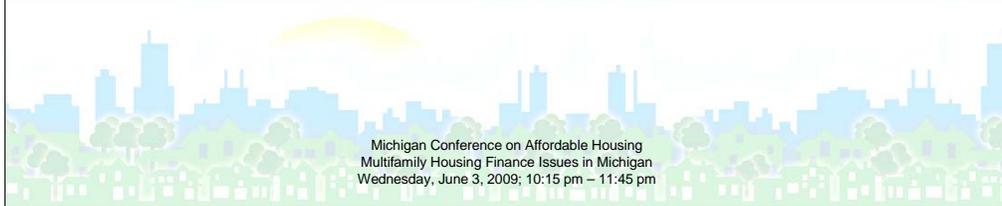
## Standards of Design for Preservation

- First written version
- Process is not new
- Process is still evolving
- We are flexible to development team's work already completed.
- Flexibility has lead to confusion.



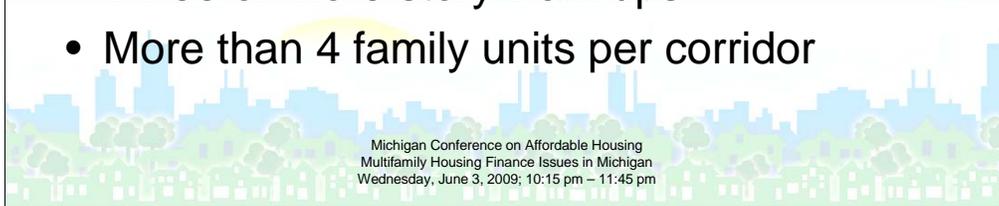
## Positive Site Attributes

- Parking, safe and sufficient
- Secure area
- Outdoor spaces
- Nearby amenities
- Walkable area



## Short list of obsolete building designs

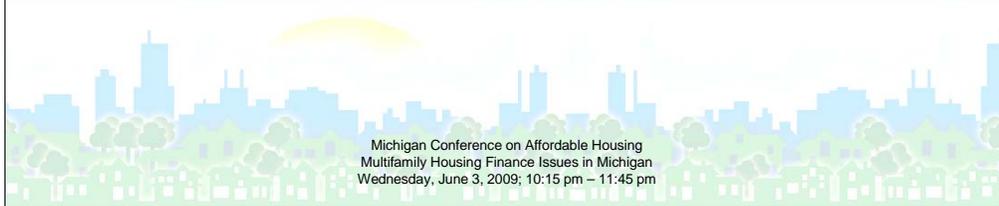
- No central air conditioning
- No private patios and balconies
- No interior community spaces
- Unacceptable views
- Mid-rise and high-rise family units
- Three or more story walk-ups
- More than 4 family units per corridor



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

## Other requirements

- Other building uses must be compatible with target population
- Preservation Capital Needs Assessment
- All replacement materials shall be equal to materials required for new construction
- Minimum 5% construction contingency fee



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Multifamily Housing Finance Issues in Michigan  
Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

# Design Process

- Site Visit with Scope of Work and Preliminary Preservation Capital Needs Assessment (PCNA)
- Meeting to determine Final Scope of Work and Replacement Reserves
- Final PCNA ordered
- Construction Documents/Commitment
- Wish list approved by MSHDA



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Wednesday, June 3, 2009; 10:15 pm – 11:45 pm

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