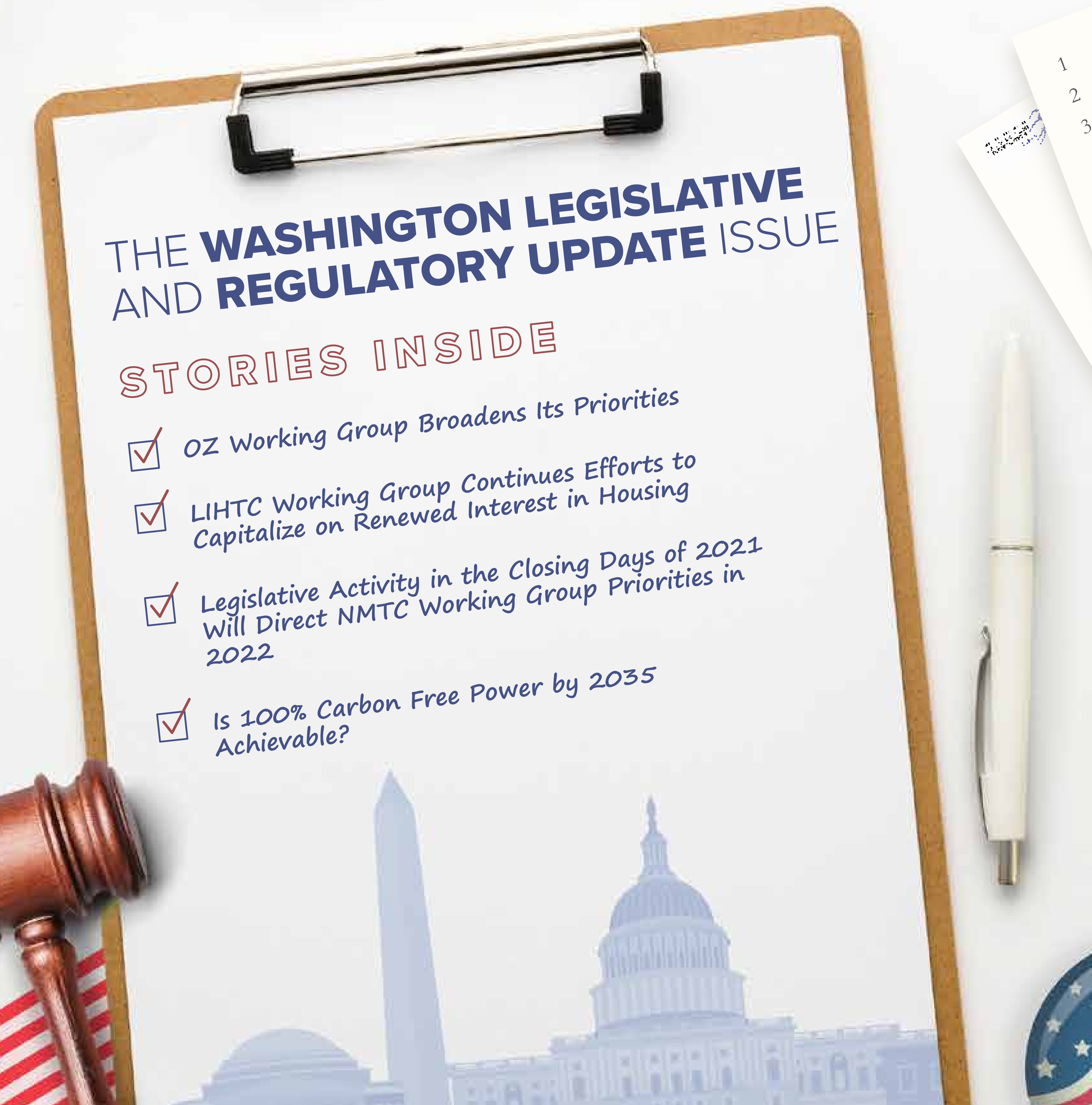
NOVOGRADAC

Journal of Tax Credits™

Insights On Affordable Housing, Community Development, Historic Preservation, Renewable Energy and Opportunity Zones

December 2021 • Volume XII • Issue XII

Published by Novogradac



THE WASHINGTON LEGISLATIVE AND REGULATORY UPDATE ISSUE

STORIES INSIDE

- OZ Working Group Broadens Its Priorities
- LIHTC Working Group Continues Efforts to Capitalize on Renewed Interest in Housing
- Legislative Activity in the Closing Days of 2021 Will Direct NMTC Working Group Priorities in 2022
- Is 100% Carbon Free Power by 2035 Achievable?

NMTC Equity Market Strong Heading into 2022, Novogradac Panelists Say

BRAD STANHOPE, SENIOR EDITOR, NOVOGRADAC

The new markets tax credit (NMTC) equity market is strong and appears set to remain so, according to members of an Investor Outlook panel Oct. 28 at the Novogradac 2021 Fall New Markets Tax Credit Conference in Austin, Texas.

"In 2022, we're going to be above our origination for the past year and appetite is going to increase significantly," said Spencer Gagnet, managing director and manager of the tax credit finance department at Capital One. "[Capital One's investment plan] is a gumbo of all the ingredients that drive appetite–CRA, tax outlook and now a big one is ESG [environmental, social and corporate governance] reporting. We're trying to find things that fit and support that agenda and our strategy. The longer-term outlook for 2023 is also very robust."

Laura Vowell, director of business development at U.S. Bancorp Community Development Corporation for the NMTC and historic tax credit, said she expects things to continue to grow in 2022. En Jung Kim, executive director of New Markets Tax Credit for community development banking at JPMorgan Chase, agreed.

"I expect 2022 to look similar to this year [surpassing the original goal]," said Kim. "Outside of the traditional national NMTC investors, we are seeing regional investors showing interest. How much of that investment gets absorbed into the $5 billion allocation will largely determine where we land. We certainly have the appetite for it."

The outlook for 2022 and beyond is shaped by financing for developments funded by allocations from the calendar year 2020 NMTC round, which was awarded Sept. 1.

CY 2020 Round, Appetite

Gagnet said that there still was some movement concerning which transactions would be financed by CY 2020 NMTCs.

"A lot of deals get soft-circled," Gagnet said. "They are in applications that get submitted, then [the CDEs] get awards, but all those deals don't necessarily make it to the finish line. You see priority deals moving through, but you have to wait to see which ones will not make it through and then the next wave of deals get credits that become available. That's sort of where we are now."

Vowell said that the timing of the CY 2020 allocations–and the fact that it was a jump from $3.5 billion in annual allocation to $5 billion–created some initial concern.

"Three or four months ago, I would have been concerned about the ability to absorb the extra allocation, but now I'd say I'm not concerned," Vowell said. "It feels right now like there is demand for those quality transactions that can close in certain time frames. Demand is there and the appetite is stronger than we were projecting."

Panelists were unsure on what the extra allocation would do to equity pricing and demand.

"I think the jury's out on that," said Kim. "It's a balancing act. You want volume, but it has to balance with pricing."

Gagnet said the finite nature of the NMTC world–that there's a specific allocation amount and a limited number of major investors–could result in major swings.

"You're seeing that the predominant investors are five to 10 large banks," he said. "If any two or three have to take a break–if they go on a pause, even for a little bit–it's a huge impact because the universe is so small."

Steady Price Range, Increased Variation

Panelists agreed that most NMTC transactions are seeing prices in the 70- to 80-cents-per-credit-dollar range, but said there was variance within that range.

"Directionally, pricing is up year over year, but the differential has gotten wider," said Gagnet. "It used to trade in a tighter range."

Kim agreed.

"We're seeing a fairly wide range [in prices]–as much as 15 cents in some instances," she said.

Health Care, Jobs, Outcomes

Panelists said that investors are interested in myriad types of developments, but that health care and other job-creating properties are very popular.

"Last year, a lot of health care projects were supported, which is not surprising because of the pandemic," said Kim. "We're also hearing about CDEs that are very focused on job growth. Health care is a great story, great impact and great jobs, so there's very strong interest–especially in rural areas and underserved states."

Gagnet said Capital One is focused on outcomes.

"Things we can track are really important," he said. "Environmental sustainability is also important. We like nonmetro deals, water security and others."

Social Impact Emphasis

Over the past few years, investors increased emphasis on social impact. Panelists said that affected investments.

"Over the past year, in response to the killing of George Floyd and social unrest, the CEO of US Bank made an emphasis to increase involvement in Black businesses," Vowell said. "We're trying to come up with different activations and how we use our allocation, how we underwrite, how we develop new projects. … We've identified a handful of specifically Black-owned projects over the past year and are starting early and investing small amounts early to move projects forward."

JPMorgan Chase increased its emphasis, too.

"At the end of last year, we implemented a special purpose credit program with a racial equity component," said Kim. "As part of that component, in addition to supporting high-impact NMTC projects, we're focused on doing more CDFI investing."

However, she stressed that transactions need to pencil out.

"When we look at any project, regardless of the racial equity component, we do underwriting," said Kim. "If you see a project that's challenging, but there's minority control or a minority developer, we're going to look at that much more strongly than a few years ago. We want to see those projects succeed."

Advice to QALICBs

Panelists concluded their discussion by providing counsel to qualified active low-income community businesses (QALICBs), the recipients of NMTC financing. The main point: Maximize your options.

"Start early, speak to people often and keep coming back," Vowell said. "I encourage any QALICB to find that tested service provider with NMTC experience. Talk to investors for recommendations, ask questions, build that team and get someone who has experience. When you're thinking about a project, share it with a service provider in the market early, so that you're in line before the announcement happens. If you're thinking about something next fall or in early 2023, you should think about shopping to CDEs now, so you're in their mind."

Brad Elphick, the panel moderator, Novogradac partner and the head of the New Markets Tax Credit Working Group, said more is better.

"You don't just shop to one CDE and hope they get an allocation," said Elphick. "The success rate last time was at about 50%, so a lot of great CDEs didn't get allocations."

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ISSN 2152-646X