Investment Opportunities in Fixed Income during COVID-19 – Multifamily Mortgage Backed Securities

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AFL-CIO HOUSING INVESTMENT TRUST

COMPETITIVE RETURNS | UNION CONSTRUCTION JOBS | HOUSING FINANCE

Agenda

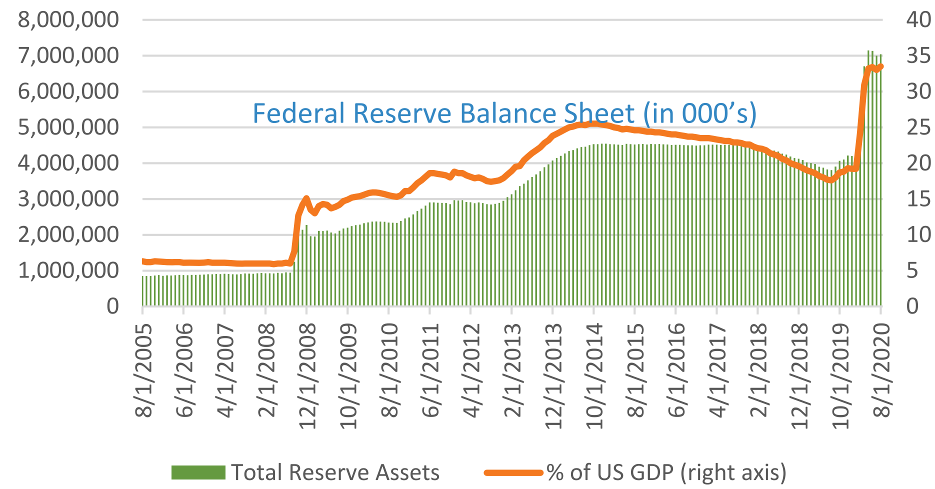
- Introduction to the AFL-CIO Housing Investment Trust
- COVID-19 Impact on the Economy
- Capital Market Overview
- COVID-19 Investment Opportunity – Multifamily Mortgage Backed Securities (MBS)
- Why Multifamily MBS
- Case Study: Old Colony
- Closing Remarks
- Q&A

AFL-CIO Housing Investment Trust

- ✓ $6.76 billion investment grade fixed-income portfolio as of August 31, 2020
- ✓ Mutual fund in operation since 1984 (successor to the Mortgage Investment Trust, 1965)
- ✓ Internally managed
- ✓ Created to pool together pension capital in order to:
  - Encourage and assist development of lower income housing while creating employment for the construction trades
  - Prudently invest in fixed income mortgage investments
- ✓ Investment strategy focused on high credit quality multifamily mortgage securities
- ✓ Multifamily Mortgage Investments offer significant relative value opportunities versus other investment grade products due to inefficiencies in the marketplace

Economic Impacts of COVID-19

- ✓ Devastating job loss resulting in high unemployment
- ✓ Highly impacted businesses declaring bankruptcy, industries permanently damaged, and small business struggling to keep the doors open
- ✓ 31% decline in 2nd quarter US GDP – worst since the depression
- ✓ Massive state and local municipality budget losses to tax revenues
- ✓ Global disinflationary pressures driving down prices
- ✓ Record fiscal and monetary stimulus to combat economic contraction



Economic Indicators	12/31/2019	3/31/2020	6/30/2020	9/30/2020
GDP (seasonally adj. annual rate)	2.4%	-5.0%	-31.4%	N/A
Unemployment Rate	3.5%	4.4%	11.1%	7.9%
Core Inflation (Personal Consumption Expenditures (PCE) less food and energy), yearly basis	1.6%	1.7%	1.1%	1.6%*
Lower Balance Federal Fund	1.5%	0.0%	0.0%	0.0%

Source: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve Board

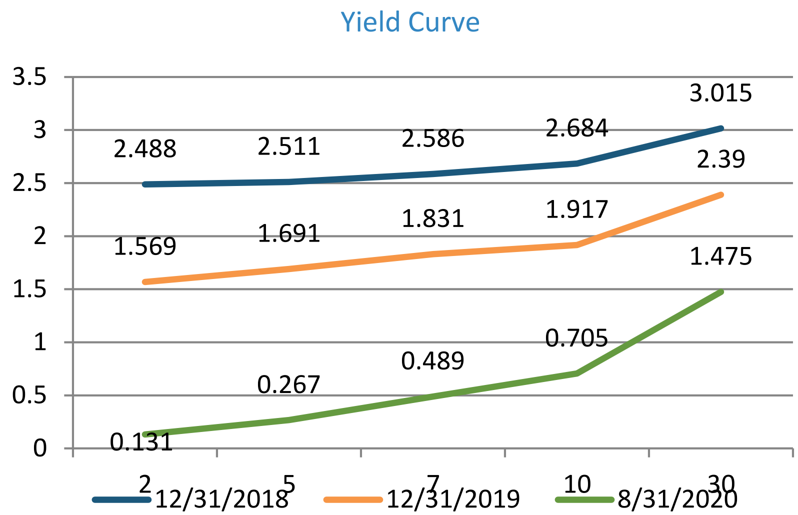
** As of 8/2020*

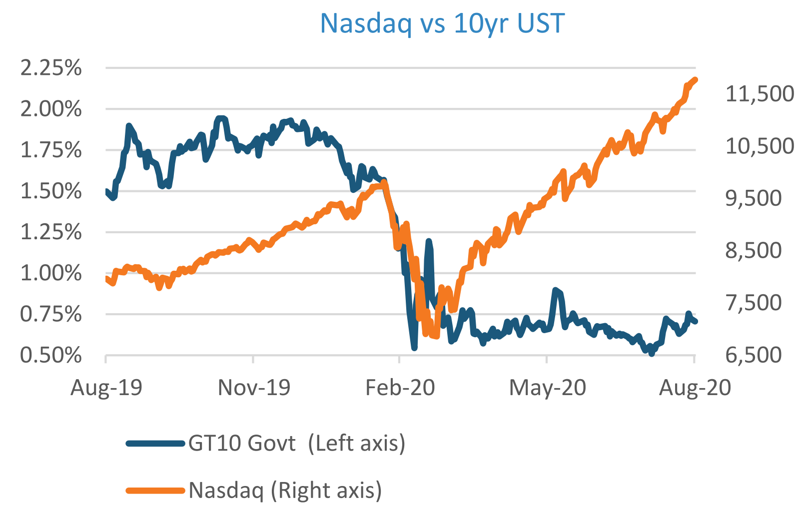
Capital Market Overview

- ✓ The pandemic has resulted in historic levels of uncertainty to the economy and the markets.
- ✓ Lasting structural damage poses a major risk to long term growth and employment as industries most affected by the pandemic (office, retail, hotel, and travel and leisure) may never fully recover. Investors should be prepared for an extended period of extraordinary high levels of volatility.
- ✓ The CARES act amounted to $2.3 trillion of spending for unemployment benefits, healthcare, student loan relief, state and local municipalities, small business PPP loans, and eviction moratoriums providing relief to millions of households and businesses limiting the severity of the crisis.
- ✓ Federal Reserve forecast now calls for no rate increase through 2023 and maintaining the same level of $120 billion of asset purchases for some time.
- ✓ The market is not expecting the Federal Reserve to raise interest rates until 2024. With inflation, inflation expectations and unemployment well below their projected targets, interest rates are likely to remain low in the near term.
- ✓ The Federal Reserve guided new principles and a framework to maximize employment while allowing higher inflation levels averaging above 2%.

Source: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve Board

Capital Market Divergence – Who's Right?





- ✓ Significant action out of Congress and the Federal Reserve stimulated spending and access to credit and liquidity in capital markets, driving equity market valuations to record highs and risk-free yields to all-time lows
- ✓ Fed cut rates to 0 and expanded balance sheet to over $7 trillion (35% of US GDP) while also expanding purchase authorities to include investment grade corporate bonds, Agency CMBS and municipal bonds
- ✓ Despite record fiscal deficits amounting to record Treasury issuance via the CARES act, central bank purchases kept interest rates historically low

COVID-19 Investment Opportunities in Fixed Income Multifamily Mortgage Backed Securities (MBS)

AFL-CIO HIT

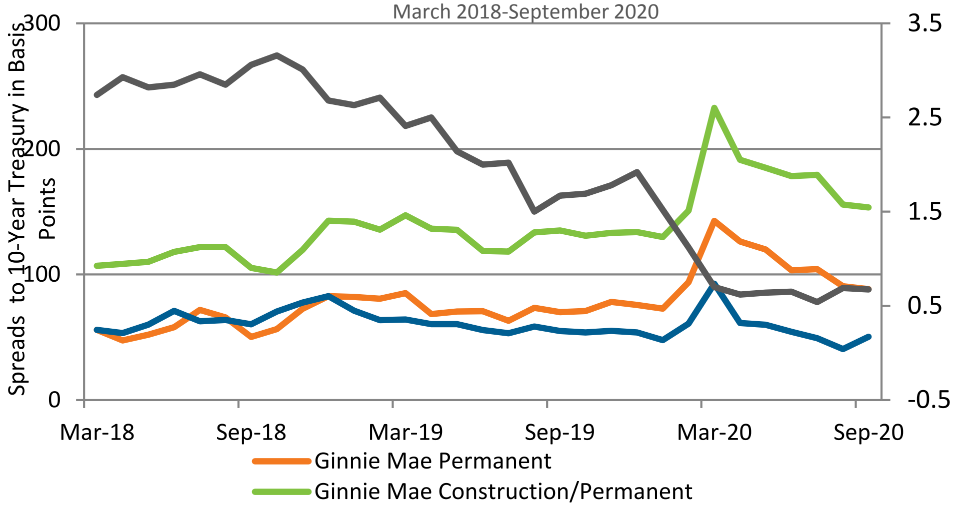
- ✓ With unpresented uncertainty in the outlook given the pandemic, agency multifamily securities offer investors looking to offset riskier portions in their portfolio:
  1. Capital preservation through government/agency credit quality
  2. Yield spread relative to credit-equivalent bonds, e.g. Treasuries, AAA corporate bonds
  3. Prepayment protection via call protection, providing a steady income stream unlike residential mortgage securities
- ✓ Multifamily MBS offer government credit quality equivalent to US Treasuries and generate spread similar to or higher than high credit quality corporate bonds
- ✓ Residential MBS experienced record prepayments resulting in the Index duration contracting by nearly ½ from 3.2 years ending 2019 to 2.1 years at the end of September 2020
- ✓ By comparison, year to date through September, the agency multifamily CMBS component of the Barclays Aggregate Index returned 8.38% relative to agency RMBS' total return of 3.62% – outperforming by more than double at 4.76%
- ✓ Fundamentally, agency multifamily can nearly double the income of a duration-equivalent Treasury that has the same credit quality with prepayment protection
- ✓ With the Federal Reserve projecting to keep interest rates at the zero bound for the next 3 years, agency multifamily securities offer investors yield spread over Treasuries in a liquid market having prepayment protection

Agency-insured Construction Securities: Inefficient Market with Attractive Return Profiles

- ✓ Government-guaranteed, multifamily construction-related loan spreads provide an attractive opportunity for risk-adjusted returns relative to other investment grade sectors as GNMA MBS construction loans offer one of the widest yield spreads to Treasuries in agency credit investments.
- ✓ Construction-related, HUD/FHA-insured securities give the investor additional yield spreads above permanent loans (50-60 bps typically) and could contribute 4-5 points of price appreciation at permanent conversion.
- ✓ As the project completes construction and stabilizes spread compression benefits returns and the loan becomes REMIC-eligible enhancing the liquidity and premium of the security.

Historical Multifamily Spreads and Treasury Yields

March 2018-September 2020



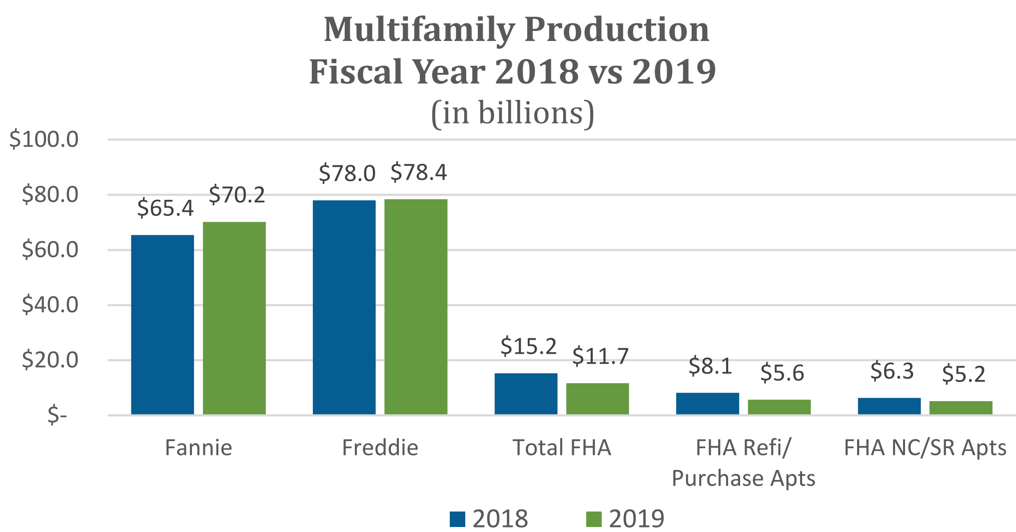
Investment Comparison

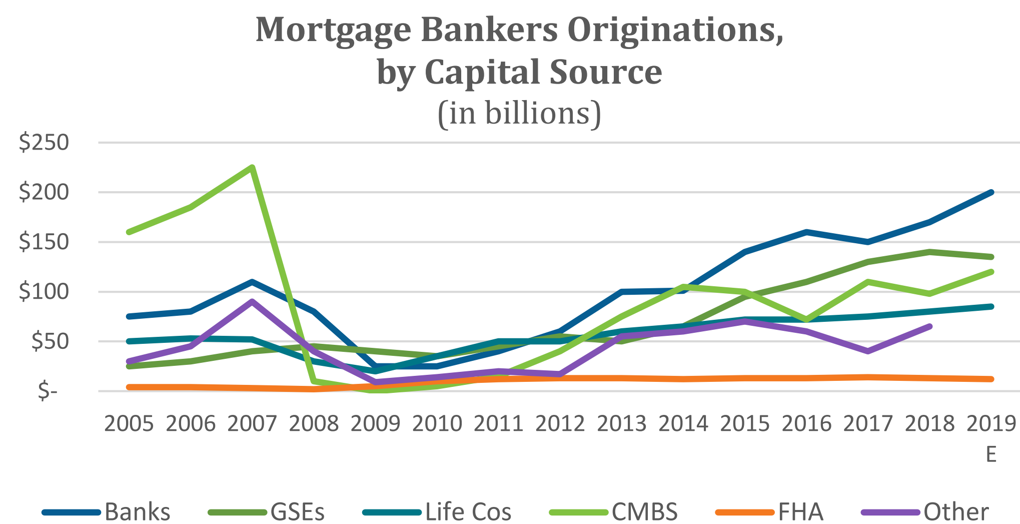
As of September 30, 2020

Investment Type	Effective Duration (Years)	Effective Convexity	Yield (%)	Spread to 10-Yr (bps)
10 Year UST	9.66	0.50	0.68%	0
GNMA Construction/Permanent	9.53	0.53	2.21%	153
GNMA Permanent	8.48	0.42	1.56%	88
Agency CMBS (e.g., GNR 2018-170 BE)	6.95	0.57	1.81%	113
FNMA Multifamily 10/9.5 DUS	8.35	0.41	1.18%	50
UMBS 2.5% 30yr MBS	3.40	-3.56	1.13%	45
GNMA 2.5% 30yr MBS	2.65	-3.62	1.29%	61
AAA Corporate Component of Barclays Aggregate	12.94	2.96	1.65%	97

Source: HIT and Securities Dealers

GSE Issuance Dominates the Agency Multifamily Market





- ✓ Historically, credit enhanced government/agency commercial loans were meant to be a counter-cyclical product that gave developers/borrowers access to debt financing in economic downturns when conventional bank financing dried up – no longer the case.
- ✓ Total multifamily origination from all capital sources for construction and/or permanent loans totaled $359 billion in 2019, a 6% increase over 2018. GSE (Fannie Mae and Freddie Mac) originations are the majority of security issuance in agency lending totaling $148.6 billion in 2019 (42% of total). GSEs do not originate construction loans.
- ✓ FHFA, the regulator of the GSEs, has required 37.5% of originations to be mission-related (affordable) to help combat the affordable housing crisis by credit enhancing the loans reducing the cost of funds for affordable developers.
- ✓ FHA origination is consistently low year over year with new construction and substantial renovation originations averaging $4-6 billion per year.
- ✓ Long processing times deter many borrowers from using HUD/FHA financing for construction development (opting for direct loans from balance sheet institutions). But there is no other, cheaper, financing like it on the market offering credit-enhanced construction to permanent loan in place at origination with a 40-year term and the ability to draw down funding to reduce negative arbitrage to the developer.

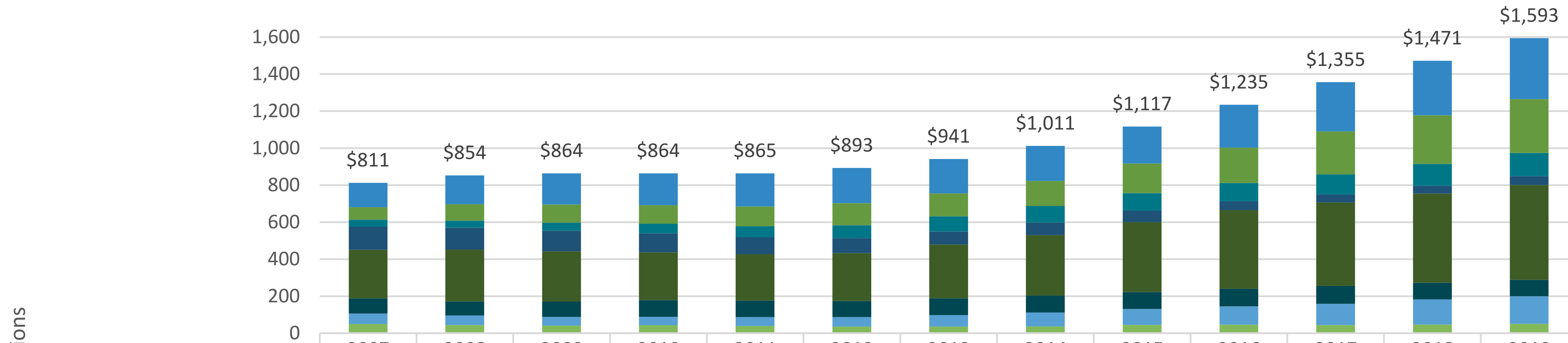
Multifamily Market –
Commercial Mortgage Debt Outstanding

- ✓ Typical capital sources for permanent multifamily mortgage loans originate from commercial banks, life companies, and government/agency credit enhanced lenders
- ✓ Market share of debt financed with agency and GSE guarantees has grown to become 47% at the end of 2019 from 29% in 2007 before the financial crisis
- ✓ Agency commercial multifamily is an inefficient market with issuance a fraction of other investment grade fixed income sectors:
  - According to the MBA, total commercial origination for multifamily loans across all sources will be down 40% in 2020
  - Agency CMBS annual issuance ranges from $140-$160 billion per year; expected to be 10-15% lower this year
  - Agency residential gross issuance expected to be over $2 trillion in 2020 with nearly $7 trillion outstanding

Church + State
Cleveland, OH

Gateway North
Lynn, MA

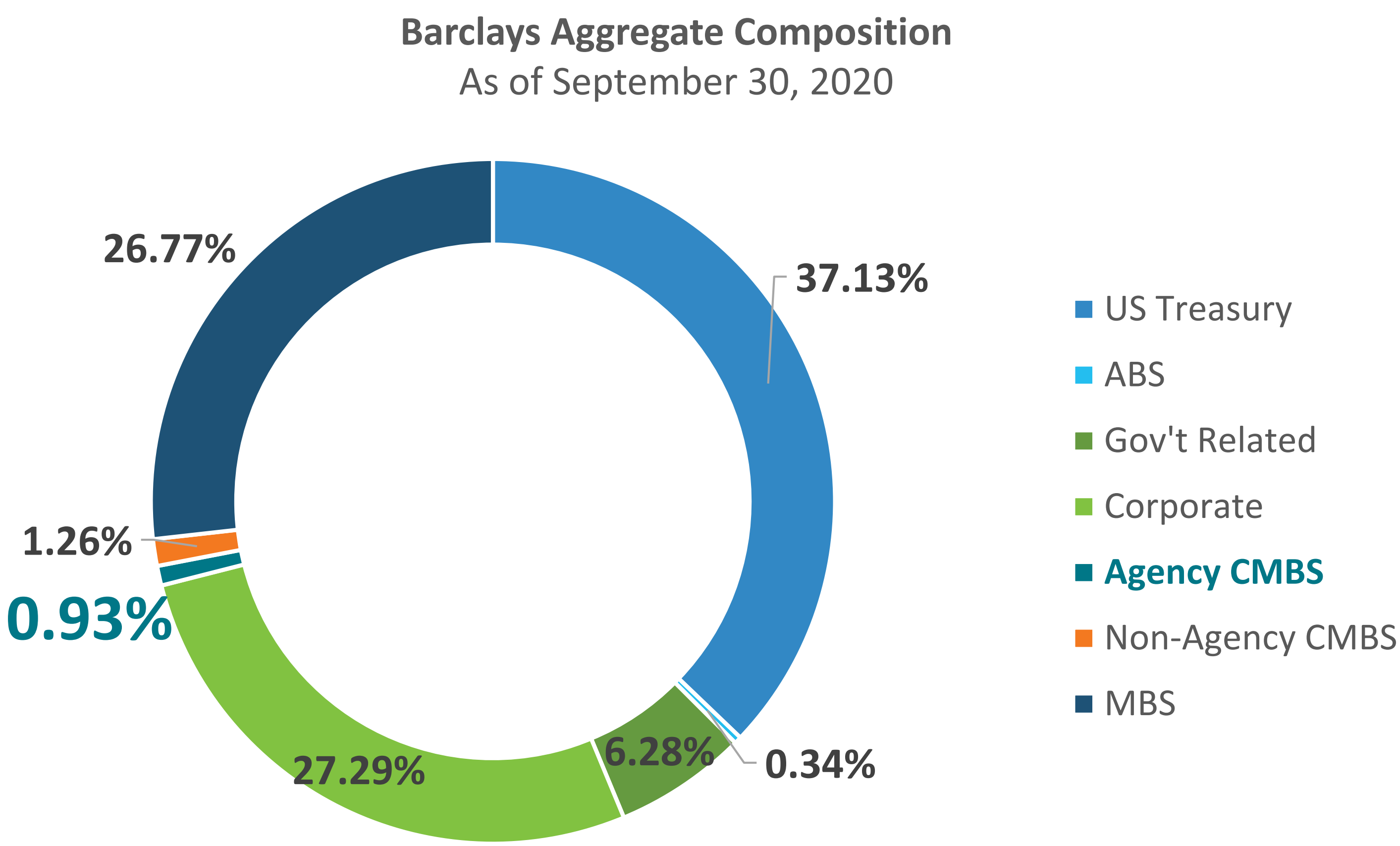
Commercial Mortgage Debt Outstanding



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total	811	854	864	864	865	893	941	1,011	1,117	1,235	1,355	1,471	1,593
Fannie Mae	132	156	168	172	179	190	185	189	200	231	266	295	329
Freddie Mac	67	88	98	100	107	119	124	135	160	191	231	262	291
Ginnie Mae	38	39	44	52	60	71	82	90	94	99	109	118	125
CMBS	126	118	112	103	91	80	71	68	62	48	43	42	48
Banks & Thrifts	261	280	271	258	251	259	290	327	379	425	451	482	513
State & Local Credit Agencies	83	76	83	90	89	87	91	91	91	95	97	90	88
Life Insurance Companies	56	52	47	46	48	51	62	75	86	99	115	136	149
Other	50	44	41	43	39	36	36	37	45	46	44	47	51

Source: Fannie Mae, numbers may not sum due to rounding

Agency Multifamily – a Smaller Market Share



Multifamily Market Attributes

- ✓ Investor base has grown with multifamily issuance primarily consisting of banks, money managers, and insurance companies.
- ✓ Relative value in call protected, income generating, high credit quality securities combined with favorable regulatory capital requirement treatment have driven the growing investor base for the agency CMBS sector.
- ✓ Liquidity for agency securities has been well supported throughout financial cycles due to its credit rating, size of the market, consistent new issue in primary markets, and growing number of Wall Street dealers (and now Federal Reserve) making liquidity readily available.
- ✓ Number of Wall Street firms, including regional banks, has grown from 5-7 pre-2008 crisis to over 12 now for project loans (Ginnie Mae multifamily securities). Nearly all of the primary dealers (21) trade GSE commercial securities.
- ✓ Typical bid/ask spreads in normalized markets can range from 1-5 bps. During spikes in volatility, bid/ask spreads can get as wide as 10-15 bps, but a market bid for liquidity is available.

Directly Sourcing Provides Additional Benefits

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✓**Most common way to invest is through broker/dealer syndications in structured agency multifamily products**

- Give up yield spread and pay transaction costs through bid/ask

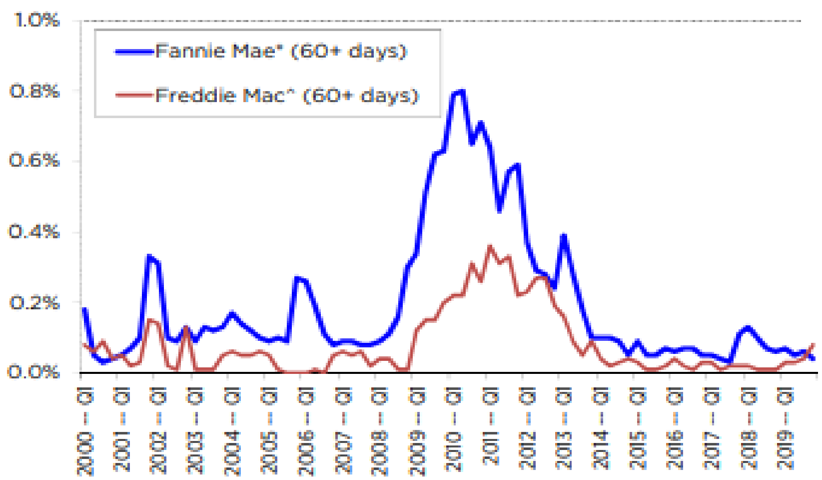
✓**With extensive knowledge, resources, experience and relationships, an investor's capacity to source directly generates substantial value:**

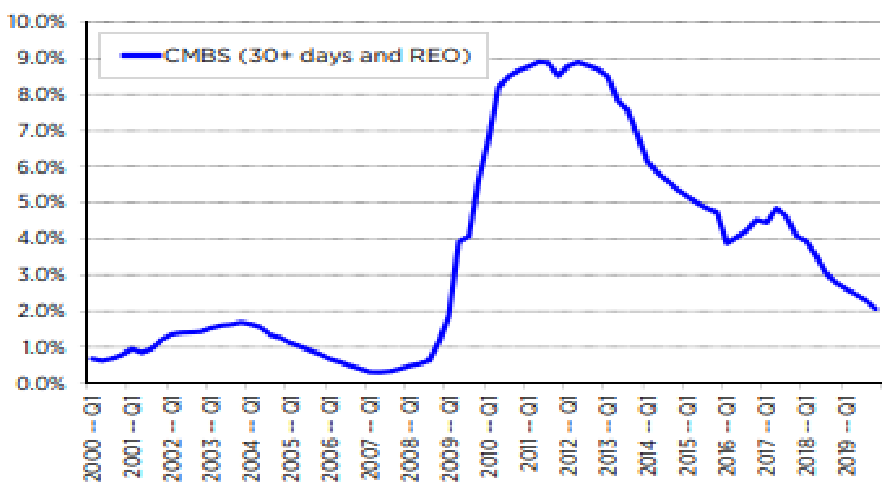
- Deep understanding of the real estate market
- Developing relationships with lenders, state housing authorities and agencies to execute complex transactions in various structures
- Providing capital in GNMA/FHA-insured construction/perm loans directly with sellers out of competition with the market
- Sourcing DUS bonds directly can pick up additional yield
- Benefits from government subsidies and guarantees

1490 Southern Boulevard
Bronx, NY

Fundamental Performance of Agency Multifamily Loans in Real Estate Cycles

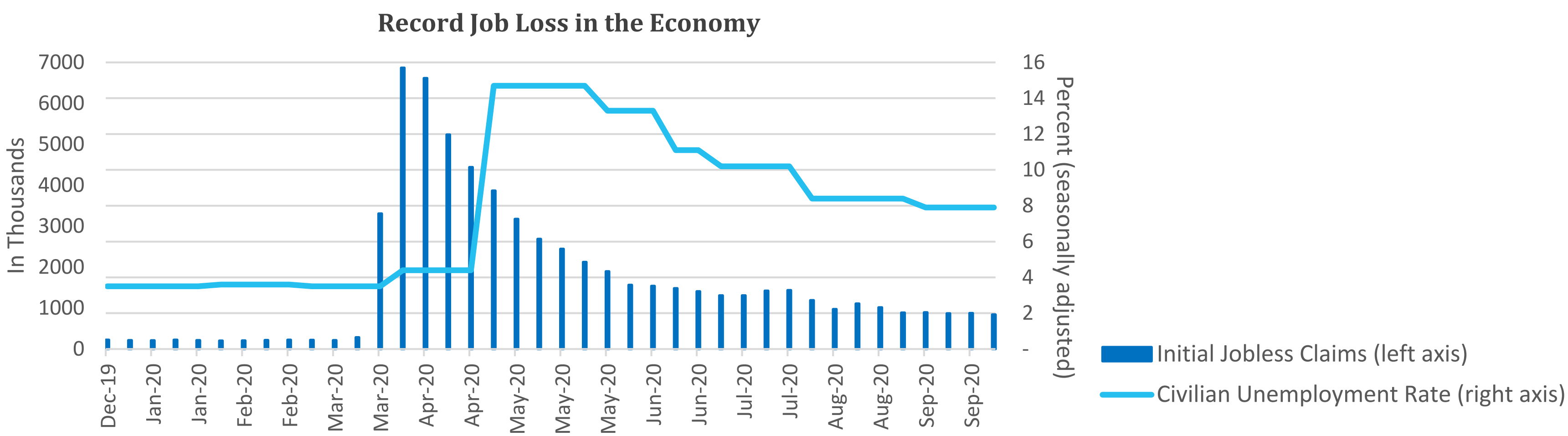
- ✓ Conservative agency underwriting on affordable properties and credit risk share combine for outperformance within multifamily investments resulting in much lower serious delinquency rates and credit losses compared to other multifamily financing types and other property sectors.
- ✓ Affordable housing experiences lower default rates than market rate properties.
- ✓ Fannie and Freddie 60+ delinquency rates peaked at 0.8% and 0.4%, respectively during the last housing/financial crisis. Currently, the 30+ delinquency rate stands at 0.1%. Forbearance rates for FNMA stand at 1.1% and 2.4% for Freddie Mac (mostly student & senior housing and small loans).
- ✓ Private sector in commercial mortgage-backed securities peaked at a 9% delinquency rate in 2011 and have risen to 3.6% as of Sept 2020.





Multifamily Housing Demand Dwarfs Supply

- ✓ Significant shifts in demographic trends such as increasing household formation are driving historic rental demand
- ✓ 40 million Americans live in multifamily apartments and that number could rise as the pandemic persists.
- ✓ Construction declined significantly in the second quarter. Construction spending is expected to continue to be impacted by the spread of the illness, social distancing and shortages of materials. Post crisis, construction is expected to rebound.
- ✓ According to a Freddie Mac study, less than 10% of rental units are affordable to households earning 50% of area median income
- ✓ Low income renters face a shortage of 7 million rental units; only 36 affordable homes exist for every 100 low income households-according to the National Low Income Housing Coalition study in 2020
- ✓ A weak and contracting economy will create more demand for affordable rental housing.



Source: National Multifamily Housing Council ; Bureau of Labor Statistics; Labor Department

Typical Term Sheet for Government Backed Construction to Perm Loan

General Terms	Non-recourse, assumable fixed rate financing for market rate or low-to-moderate and subsidized multifamily properties
Property Types	Multifamily
Amortization	Interest only through construction followed by 40-year amortization
Loan Term	Typically 2 year construction periods; 40 year fully amortizing permanent loan; one-time close
Prepayment Terms	10 years of prepay penalty points Prepayment terms can be flexible
Rate	One fixed rate consisting of the GN investor rate, servicing and guarantee fee plus Mortgage Insurance Premium
Underwriting	
LTV	Typically up to 85% for market rate; 90% for subsidized affordable
DSCR	Minimum 1.11x
Guarantee and servicing fee	0.25%. Plus mortgage insurance premium (MIP) of 25-65 bps

Case Study – Old Colony Redevelopment

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✓Old Colony was built in 1940 as an 845-unit public housing community, to serve low-income residents in the South Boston area. In 2010 Boston Housing Authority put forth a long-term master plan to modernize the outdated Old Colony site and rebuild the community through a series of complex redevelopment plans.

✓Complex financing structure of the redevelopment consisted of purchasing 5 separate credit-enhanced commitments of short and long-term, taxable and tax-exempt bonds, as well as construction loan notes, all supporting the construction and permanent financing for Old Colony Phase 3B & 3C.

Short Term Enhanced Construction Loan	HIT Investment Amount (Millions)	Coupon	Yield Spread to Treasury *
3yr AA-rated Construction Loan Note	$37	2.15	200
3yr tax-exempt AA-rated bridge loan	$10	0.50	35
Long Term Enhanced Permanent Debt			
40/10 permanent FHA risk share	$6	2.50	185
40yr t/e AA-rated private placement bond	$26	2.60	200
Weighted Average		2.12	178 bps

** At time of commitment*

This document contains information about a project or projects financed by the HIT which may or may not be reflective of other financed projects or refer to an asset currently held in the HIT's portfolio. It is intended as a representation of a real estate project, not an indication of actual pricing or deal terms.

Old Colony Phases 3B & 3C

✓Phase 3B - 115 affordable units, 4% and 9% Low Income Housing Tax Credit (LIHTC) transaction

✓Phase 3C - 55 affordable units, 4% LIHTC transaction

✓HIT Investment - $79 million; TDC $86 million

- $37 million Taxable Construction Loan Notes, Private Placement
  - Phase 3B 4% and Phase 3B 9%
- $10 million Tax exempt Bridge Loans, Private Placement Separate Series
  - Phase 3B 4% and Phase 3C
- $6 million Taxable Construction/ Perm Loan, Private Placement
  - Phase 3C
- $26 million Tax exempt Bonds, Private Placement Separate Series
  - Phase 3B 4% and Phase 3C

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Closing Remarks

- ✓ The COVID environment has led to unprecedented risks and a highly uncertain outlook
- ✓ Multifamily mortgage investments offer fixed income investors credit protection, liquidity and added yield in a low interest rate environment
- ✓ Multifamily MBS offers value and diversification in a highly uncertain environment

Q & A

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