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Asset-Backed ALERT

THE WEEKLY UPDATE ON WORLDWIDE SECURITIZATION

PACE Lenders Riding Out Crisis

The coronavirus crisis is disrupting the businesses of Property Assessed Clean Energy lenders, many of which are adjusting their near-term strategies in ways that eventually could affect the types and volumes of assets available for them to securitize.

Consider commercial-property projects. As new construction slows, some lenders in that area have placed more emphasis on financing energy- and water-efficiency retrofits of existing facilities and refinancing borrowers' current debts.

The shift is tied to a situation in which banks increasingly have halted senior mortgages for new construction, leading warehouse lenders to freeze financing for the PACE portions of those projects as well. That could set back PACE lenders by 3-4 months. Without a senior mortgage, "someone's got to fill the gap in the capital stack, and that money's not easy to come by right now," **Petros PACE Finance** chief executive **Mansoor Ghori** said.

By comparison, financing of upgrades to existing buildings is less vulnerable because there's no mortgage lender involved. PACE lenders had placed less emphasis on such projects in favor of new-construction loans, which tend to be larger. Now, they're reversing course.

Some commercial PACE programs allow for the refinancing of recently completely energy efficiency improvements as well. Petros, for example, is in the process of funding separate refinancings of $10 million and $5.5 million. "We're going to see more of those in the short-term," Ghori said.

Ghori's Austin-based operation also closed on one refinancing arrangement last week and expects to close on a new-construction transaction this week.

Residential PACE lenders also are pitching the idea of refinancing recently completed projects. Part of the appeal in that case is that because the financing is levied alongside property taxes, the homeowners can stretch payments out over long periods. "We can come in post-facto and put money back in their pockets," said **Greg Saunders,** chief financial officer at **Ygrene Energy.** "It's like a line of credit people don't know they have."

While some of Ygrene's key residential markets are under shelter orders, including certain areas of Florida and California, the Petaluma, Calif., company believes it can keep business flowing because it markets its loans through contractors, which are allowed to continue operating as essential services. "The question is whether homeowners are comfortable engaging with a contractor. Do they have the time and money to think about taking on a new obligation?" Saunders asked.

Saunders acknowledged that Ygrene has seen a dip of about 10% in applications from residential borrowers in the past two weeks and anticipates a further decline. Still, he believes PACE lenders have an advantage over others that finance similar energy-saving improvements. Unsecured-loan originators, for example, have seen major declines in their access to warehouse financing amid the outbreak.

When it comes to loan performance, and ultimately collateral quality for the lenders' asset-backed bonds, the economic slowdown poses some risk. "As far as residential PACE is concerned, I'm waiting to see if there's any fallout from the fact that millions of people have been laid off," Ghori said. "If some have recently done PACE projects, they may not be able to pay their PACE assessments."

That said, PACE financing for commercial projects typically carries loan-to-value ratios of less than 20%. The upshot is that the primary risk would be a delay in payments, as opposed to a loss of principal. "I think when you have a retail mall that's either shut down for some period or tenants are saying they can't make the rent, at some point you're going to see requests for deferrals, though that probably won't happen until the second quarter," Ghori said.

For now, the market for new PACE-loan bonds has frozen along with the rest of the asset-backed bond sector. **Renovate America** of San Diego squeezed in a Rule-144a deal of $54.4 million on March 11, just before the market downturn accelerated. In that case, the company's funding costs benefited from low benchmark rates. The deal was the only PACE-loan securitization to price during the first quarter.

PACEFunding of Los Gatos, Calif., had been aiming to complete a Rule-144a transaction in late April, but that offering now is on hold. Ygrene hopes to come to market in May with a deal that will be a bit smaller than its previous one, perhaps $230 million to $240 million. Like several of the company's previous issues, it will be backed by a mix of residential and commercial PACE loans.

PACE lenders completed four securitizations totaling $760 million in 2019, down from six deals for $896.9 million in 2018, according to **Asset-Backed Alert's** ABS Database. ❖