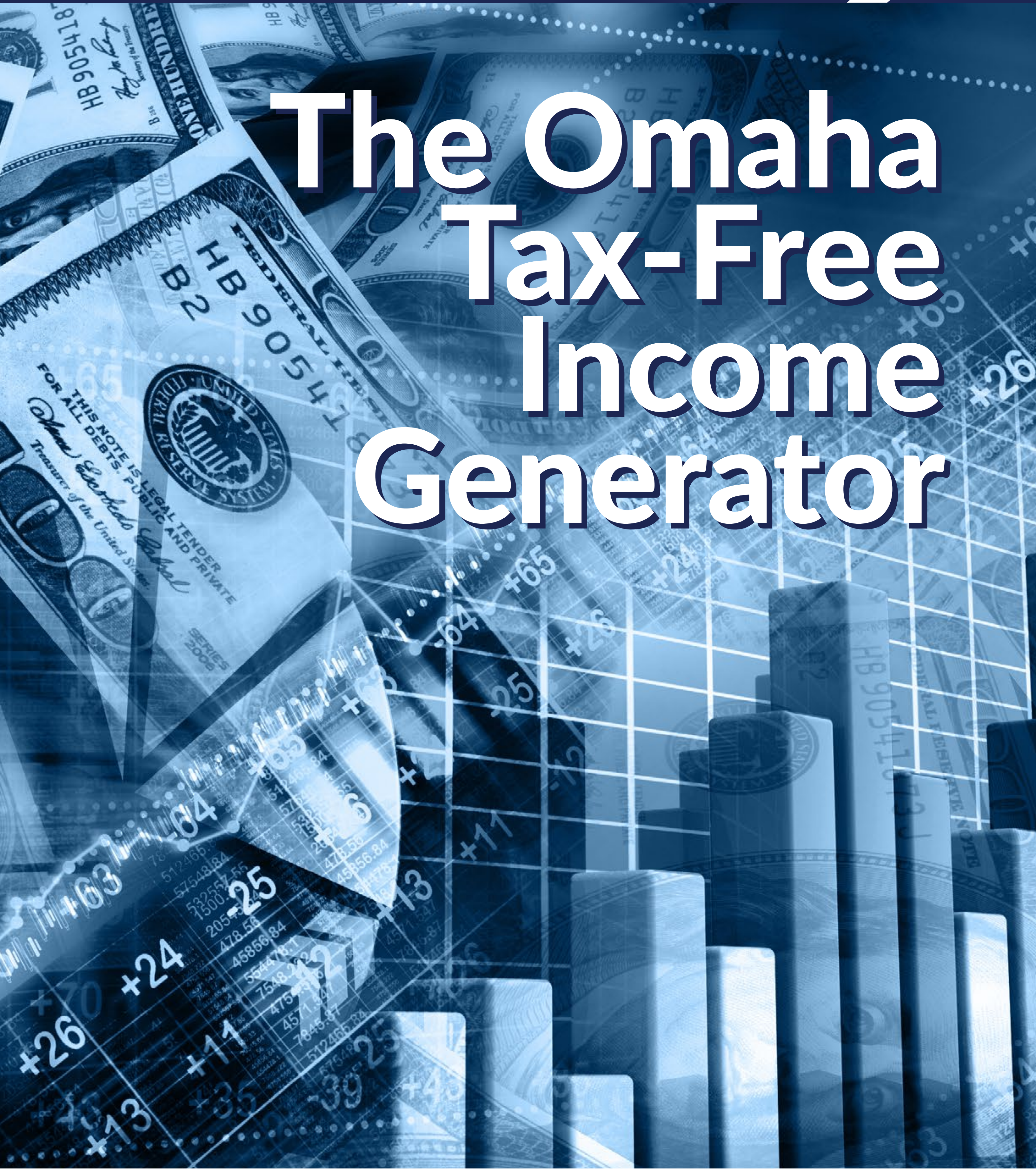
The Omaha Tax-Free Income Generator



PEAK INCOME

THE OMAHA TAX-FREEINCOME GENERATOR

Let me introduce the **America First Multifamily Investors LP (Nasdaq: ATAX)**.

ATAX manages a portfolio of mortgage revenue bonds (MRBs) that are issued by state and local housing authorities to provide construction or permanent financing for affordable multifamily and student housing, and residential and commercial properties. As of the end of 2018, the company held interests in 63 different MRBs — provided financing for 63 properties with a total of 10,650 rental units.

More importantly, ATAX is **not** in the business of making mortgage loans on single family residences, nor does it invest in mortgage-backed securities.

There's nothing wrong with those businesses, of course. I've invested in mortgage REITs in the past, and would happily do so again at the right prices and yield. But mortgage revenue bonds are a different breed of animal. It's important to understand the differences.

A mortgage-backed security is a pool of good old-fashioned home mortgages packaged into bonds by government sponsored entities like Fannie Mae or Freddie Mac, or by private banks. They are collateralized by individual mortgages paid by ordinary people like you and me. As with Treasury or corporate bonds, these are fully taxable.

It's highly likely that someone in your family owns or has owned these kinds of bonds, or a bond mutual fund or ETF that owned them. My grandparents had a portfolio full of them.

Mortgage revenue bonds are different though.

For starters, the issuers are the departments of state and local governments. That makes them tax-free, just like the regular municipal bonds held by our tax-free muni closed-end funds. Because of its large allocation to the tax-free mortgage revenue bonds, ATAX's distributions are mostly tax-free. The yields with property sales, the distributions can have a larger taxable component, but it tends to be no more than 20% to 25% of the total.

Second, there's a lot more flexibility in what is financed. Some are similar to mortgage-backed securities in that they are backed by single-family home mortgages. Others are collateralized by multifamily apartment buildings. This second category is ATAX's specialty, with 75% of its portfolio made up of multifamily mortgage revenue bonds, and the remaining 25% scattered across a variety of other real estate investments and property loans.

Whenever you see the word "mortgage" in the description of an investment, the first question you should ask is: "How did it do during the 2008 meltdown?"

Well, pretty darn well in the case of ATAX. In early 2009, it lowered its quarterly distribution from $0.135 per share to $0.125 per share. To have survived the worst housing-related crisis of our lifetimes with such minimal damage is something to be proud of.

Much of this is due to the company's lack of exposure to single-family homes. When the price of housing collapsed, many homeowners found themselves hopelessly underwater and decided to simply walk away from their mortgages. That was a nightmare for Fannie Mae and Freddie Mac, and virtually every bank in America.

But here's the thing… you still have to live *somewhere*.

When the economy gets rough, demand for affordable rental housing actually increases as cash-strapped Americans avoid buying houses and even trade down to more affordable living options.

It's a quirky, niche business, but that's what makes it interesting. ATAX is essentially a muni bond fund secured by affordable, cash-flowing apartments.

I should be clear that ATAX is not technically a "fund." It's organized as a limited partnership and not as an investment company, as mutual funds and ETFs are. But in practice, it functions like a closed-end bond mutual fund, holding a diversified portfolio of fixed-income assets.

ATAX shares trade for $6.90 and yield a very handsome 7.27%. And again, that payout is mostly tax-free!

Let's play with the numbers:

If Your Tax Bracket Is...	Your Tax-Equivalent Yield Would Be...
10%	8.08%
12%	8.26%
22%	9.32%
24%	9.57%
32%	10.69%
35%	11.54%

If you're in a relatively low bracket, the tax benefits of owning America First Multifamily are relatively limited. In the 10% bracket, a 7.27% yield is equivalent to an 8.08% yield.

But as you climb up the income scale, the numbers start looking a lot better. At the 24% bracket (family income over $315,000), that 7.27% tax-free yield is equivalent to an 9.57% taxable yield. And if you're a real heavy hitter in the top tax bracket (family income of $600,000 or higher), the tax-equivalent yield jumps to 11.54%.

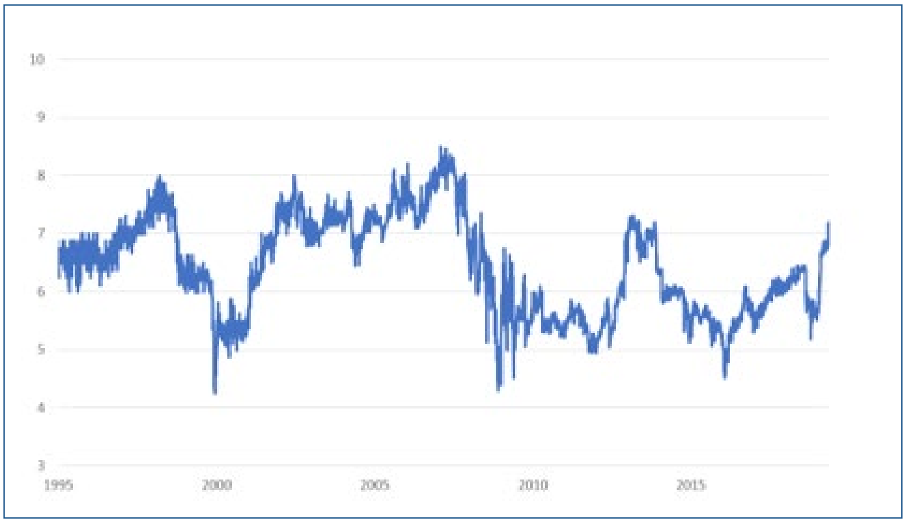
An 11.54% yield on a bond fund isn't too shabby.

Now, in reality, your tax-equivalent yield might be a little lower, as some portion of the distribution could be taxable in any given year. But again, the taxable component tends to be a relatively small amount — 75% to 80% of the distributions are generally tax-free.

WHAT TO EXPECT

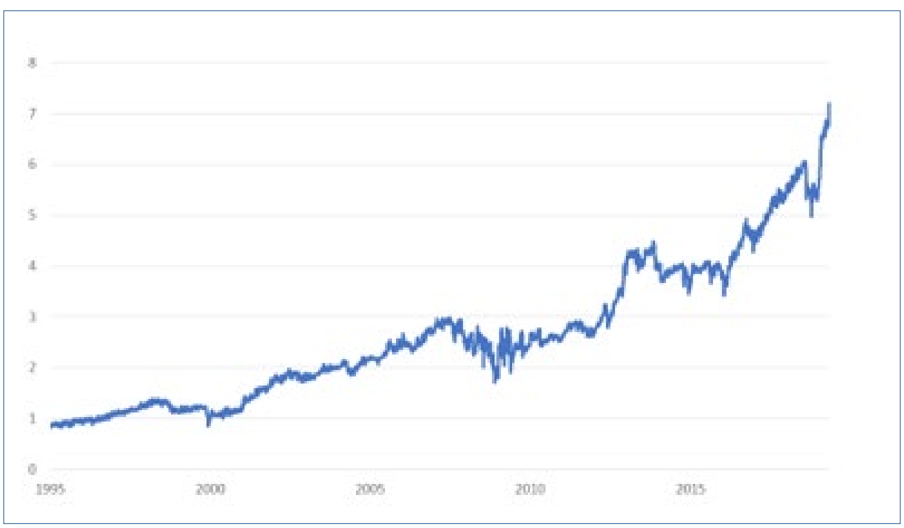
America First Multifamily Investors is, first and foremost, an income investment. You really shouldn't expect much in the way of capital gains. Though the share price has had its ups and downs, ATAX is priced today at roughly the level it was in 1995.

AMERICA FIRST MULTIFAMILY PRICE PER SHARE



But that doesn't mean that ATAX has been a slouch. Assuming reinvestment of dividends, a dollar invested in ATAX back in 1995 would be worth over $7 today. That works out to a compound annual growth rate of just shy of 9%... *tax free*… and in boring, stable bonds.

AMERICA FIRST MULTIFAMILY



I can't promise you the stock market will keep rising from here. Honestly, I'm surprised it is as high as it is. From what I can see, monetary stimulus from the Fed seems to be the only thing propping up this house of cards.

Personally, I'd rather put my money in something like ATAX. It's a proven operator that has successfully navigated multiple recessions without a major blow up, and its returns come in the form of cold, hard, tax-free cash.

So, what's the risk?

There's no free lunch in economics, but I consider the risks in ATAX to be very manageable. Its mortgage revenue bonds are secured by cash-flowing real estate. So, if the worst were to happen and the borrower were to default (which would be extremely unlikely), ATAX would simply assume ownership of the property and continue to manage it.

This doesn't mean that losses are impossible. Were ATAX to see a wave of defaults, that would likely mean that the economy was in bad enough shape to tank the property market. Furthermore, ATAX itself uses leverage to boost its return, and it could be affected if the credit markets were to seize up.

But, frankly, ATAX navigated 2008 with its business intact. So it should be able to survive whatever comes next without any major hiccups.

So, let's get to it…

Action to Take: Buy shares of America First Multifamily Investors LP (NYSE: ATAX) up to $7.15. Set an initial stop-loss at $6.20 based on closing prices.

Use a limit order when you buy your shares. ATAX is a small stock with a market capitalization of just $418 million and relatively low daily trading. **If you place a large market order, there is a very good chance you will move it and get filled at a lousy price.**

So, please be careful here. I consider this a very attractive income investment for us, but if we all pile in at the same time with market orders, we're going to move the market.

I'm initially instructing you to buy up to $7 per share. I may revise that number higher over the next few days depending on how the stock behaves. But please stick to this rule as we get started. It's important to be disciplined on smaller, less liquid stocks.

I would also point out that **ATAX is <u>not</u> IRA friendly**. In its SEC filings, the company specifically mentions that it expects to periodically generate unrelated business taxable income (UBTI), which is the bane of every income investor's existence.

If you end up with UBTI in your IRA account, it's a real mess to clean up. IRS agents aren't going to kick down your door and drag you out in the dead of the night, but you could have to pay taxes out of your IRA account, and who wants to do that?

Make your life easy and only buy shares of ATAX in a taxable account.

One more note on taxes…

Like many MLPs, America First Multifamily Investors issues a K-1 at tax season and not the standard 1099 you're used to getting from your broker. Personally, I don't mind. My tax return is already as thick and as complicated as a calculus textbook. One more K-1 form isn't going to make much of a difference.

But for some investors, this is a big deal. So, just be advised that you'll have an extra tax form to deal with come next April.

If you like tax-free opportunities like these, *Peak Income* routinely recommends tax-free municipal funds and other tax-free or tax-advantaged investments.

Bonds issued by states, counties, cities and other local governmental entities are generally tax-free at the federal level, though they may be taxable at the state level depending on where you live. Closed-end municipal bond funds will construct diversified portfolios of municipal bonds and juice their returns by adding a little leverage. At today's prices, it's usually possible to get tax-free yields in excess of 5%.

Unlike ATAX, which issues a K-1 come tax season, your income and capital gains from muni funds will generally show up on the regular 1099 your broker sends you.

If you're in a high-tax bracket — or just hate paying more in taxes than you have to — then these investments might be a perfect addition to your portfolio.