Moody's Investors Service

Rating Update: **California HFA - Issuer Long Term Rating**

MOODY'S ISSUER RATING ON CALIFORNIA HOUSING FINANCE AGENCY CONTINUES TO BE ON WATCH FOR POSSIBLE DOWNGRADE

Review continues with focus on potential mortgage loan losses and challenges posed by variable rate debt

Housing
CA

Opinion

NEW YORK, Dec 28, 2008 -- Moody's Investors Service's Aa3 issuer rating on the California Housing Finance Agency continues to be under review for possible downgrade. The outcome of the review will be contingent upon completion of Moody's review of the Agency's financial strength particularly with respect to potential losses from single family lending and from exposure to the troubled variable rate debt markets and related counterparty exposure.

Moody's placed the Agency's issuer rating on watch on September 29, 2008. In its report as of that date, Moody's stated that this action was based on the combined effects of increased losses from delinquencies and foreclosures from single family mortgages, heightened risk related to the Agency's variable rate debt resulting from a volatile market and counterparty risk, and a lending initiative that had placed additional leverage on the Agency's balance sheet. This action affected approximately $1.415 billion of bonds outstanding under bond programs supported by the Agency's issuer rating. The rating on the Agency's Home Mortgage Revenue Bond program (Aa2, with a stable outlook) was not affected. The Agency is an instrumentality of the State of California, and its debt obligations are not obligations of the State.

Since the time of Moody's action on September 29, the Agency has taken additional steps to address its financial position, including modification of standards for single family lending going forward, reduction of the number of bank bonds held by external liquidity banks through remarketings of those bonds, reallocation of remarketing responsibility for some series of variable rate demand obligations, replacement of interest rate swaps in which the Agency formerly faced entities affiliated with Lehman Brothers, and termination of investment contracts with other counterparties whose ratings have been lowered. Further steps aimed at strengthening the Agency's balance sheet and reducing risk are ongoing. In addition, the Agency has provided Moody's with additional information on the financial performance of mortgage loan assets and its bond programs.

Moody's is continuing its active assessment of all of this information. In completing this review, Moody's will evaluate the following: (1) projected loss levels for the California Housing Loan Insurance Fund (the Agency's mortgage insurance fund) under Moody's updated loss assumptions for appropriate rating levels; (2) review of the Agency's progress and plans to mitigate current stresses on the single family portfolio; (3) review of the Agency's plans for dealing with potential and/or unforeseen events relating to variable rate debt and counterparties (such as continued market stress or decline in counterparty credit quality); (4) analysis of the effects of current market conditions on current and future fund balances and profitability, including whether capital balances (both total balances and immediately available liquid resources) are consistent with the current rating level. Moody's will also follow the Agency's management transition in light of the recent retirement of the executive director, which was required by the end of her legally prescribed term, to confirm that management continues the focus on enhancement of financial strength. Another factor that may have an impact on the Agency's rating is the outcome of Moody's review of Genworth Mortgage Insurance Corporation (rating Aa3, on watch for downgrade). The California Housing Loan Insurance Fund benefits from reinsurance agreements with Genworth on certain of its mortgage insurance obligations, and reduction in Genworth's rating could be a source of further stress.

The following ratings are also on watch for downgrade as a result as the watch on the Agency's issuer rating (balances at 12/1/08):

Multifamily Housing Revenue Bonds III ($1,212,835,000 outstanding)

Multifamily Housing Revenue Bonds II ($59,930,000 outstanding)

Housing Program Bonds ($142,425,000 outstanding)

The last rating action with respect to these ratings was on September 29, 2008, when ratings were placed on under review for possible downgrade.

The principal methodology used in rating this issue was Moody's Methodology for Assigning Issuer Ratings to Housing Finance Agencies, which can be found at www.moodys.com in the Credit Policy & Methodologies directory, in the Ratings Methodologies subdirectory. Other methodologies and factors that may have been considered in the process of rating this issue can also be found in the Credit Policy & Methodologies directory.

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