STATE OF CALIFORNIA

CALIFORNIA HOUSING FINANCE AGENCY

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BOARD OF DIRECTORS

PUBLIC MEETING

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Burbank Airport Marriott & Convention Center
2500 Hollywood Way, Pasadena Room
Burbank, California

Monday, March 17, 2014
10:00 a.m. to 12:30 p.m.

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Minutes approved by the Board of Directors at its meeting held:
May 13, 2014
Attest:

Reported By: YVONNE K. FENNER, CSR #10909, RPR

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A P P E A R A N C E S

Board of Directors Present:

MATTHEW JACOBS, Chairperson
Co-Managing Partner
Bulldog Partners, LLC

ANNA CABALLERO
Secretary
Business, Consumer Services & Housing Agency
State of California

CLAUDIA CAPPIO
Executive Director
California Housing Finance Agency
State of California

KATIE CARROLL
for Bill Lockyer
State Treasurer
State of California

THERESA GUNN
Deputy Secretary, Farm and Home Loan Division
CalVet Home Loans
State of California

JONATHAN HUNTER
Managing Director, Region 2
Corporation for Supportive Housing

TIA BOATMAN PATTERSON
General Counsel
Sacramento Housing & Redevelopment Agency

PRESTON PRINCE
CEO & Executive Director
Fresno Housing Authority

DALILA SOTELO
Principal
The Sotelo Group

A P P E A R A N C E S

Participating CalHFA Staff:

SHERYL ANGST
Housing Finance Specialist

KENNETH H. GIEBEL
Director of Marketing

TIM HSU
Director of Financing

VICTOR J. JAMES
General Counsel

JOJO OJIMA
Office of the General Counsel
Legal Division

RICK OKIKAWA
Programs Administrator

JACKLYNNE M. RILEY
Director
Administration Division

ANTHONY SERTICH
Manager
Financing Risk Division

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Public Testimony:

PETE SERBANTES
HomeStrong USA

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BE IT REMEMBERED that on Monday, March 17, 2014, commencing at the hour of 10:00 a.m., at the Burbank Airport Marriott Hotel & Convention Center, 2500 Hollywood Way, Pasadena Room, Burbank, California, before me, YVONNE K. FENNER, CSR #10909, RPR, the following proceedings were held:

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CHAIRPERSON JACOBS: I'm going to call to order -- first of all, welcome, everyone, and I'm going to call to order the March 17th, 2014 meeting of the California Housing Finance Agency Board of Directors. Welcome, everybody. Sorry for the little earthquake. That's L.A.'s way of saying we love you.

I'm going to pass around for people. We've got parking ticket vouchers. I'm going to pass these around going this way.

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Item 1. Roll Call.

CHAIRPERSON JACOBS: All right. Let's, JoJo, start with the roll call.

MS. OJIMA: Thank you.

Ms. Caballero.

MS. CABALLERO: Present.

MS. OJIMA: Mr. Deems.

(No audible response.)

MS. OJIMA: Ms. Falk.

(No audible response.)

MS. OJIMA: Ms. Gunn for Mr. Gravett.

MS. GUNN: Present.

MS. OJIMA: Mr. Gunning.

(No audible response.)

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Present.

MS. OJIMA: Ms. Carroll for Mr. Lockyer.

MS. CARROLL: Here.

MS. OJIMA: Ms. Patterson.

MS. PATTERSON: Here.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Here.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Present.

MS. OJIMA: Mr. Alex.

(No audible response.)

MS. OJIMA: Mr. Cohen.

(No audible response.)

MS. OJIMA: Ms. Cappio.

MS. CAPPIO: Here.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Here.

MS. OJIMA: We have a quorum.

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Item 2. Approval of the minutes of the January 14, 2014 Board of Directors meeting.

CHAIRPERSON JACOBS: All right. Let's jump into the minutes from the January 14th meeting, the approval of the minutes. Does anyone --

MR. PRINCE: I'll so move.

MR. HUNTER: I'll second.

CHAIRPERSON JACOBS: Great.

MS. OJIMA: Thank you.

CHAIRPERSON JACOBS: And if there are ever corrections on the minutes, just make sure you e-mail back saying I think you got the speaker wrong or real simple.

Let's do it.

MS. OJIMA: Okay. Ms. Caballero.

MS. CABALLERO: Aye.

MS. OJIMA: Ms. Gunn.

MS. GUNN: I abstain.

MS. OJIMA: Thank you.

Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Ms. Patterson.

MS. PATTERSON: Aye.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: The minutes have been approved.

CHAIRPERSON JACOBS: Great. Thank you, JoJo.

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Item 3. Chairman/Executive Director comments.

CHAIRPERSON JACOBS: I think just before we get into this meeting, I do want to encourage people to ask questions. The main reason we are here is to ask questions, make sure that we are really comfortable with the way that policy is moving forward, make sure we're comfortable with what the Agency is doing and that we're doing the right kinds of policies to promote home ownership and affordable housing in the state of California.

Does anyone have any additions to the agenda or any changes, new items?

If you wouldn't mind just introducing yourself, Theresa Gunn, please. Just tell everyone a little bit about who you are and...

MS. GUNN: All right. Theresa Gunn. I'm the deputy secretary for the Farm and Home Loan Division of CalVet. I have recently taken this assignment, just about a year ago. Before that I spent about 13 years in the Department of Finance, ten of which were in the capital outlay assignment with a majority of the state under my belt, pretty much everything except housing and parks. And before that I was in private industry.

CHAIRPERSON JACOBS: Great, thanks. Welcome and look forward to working with you.

Does the executive director have any comments at this time before we --

MS. CAPPIO: Just a few.

CHAIRPERSON JACOBS: -- jump in?

MS. CAPPIO: Good morning. Happy St. Patrick's Day. I think instead of L.A. welcoming in -- the earthquake welcoming us to L.A., maybe it was a happy St. Patrick's Day earthquake.

So --

MR. PRINCE: The epicenter was in Westwood, and as a Bruin I think it was just UCLA, like --

MS. CAPPIO: That's right.

MR. PRINCE: -- a bunch of fans just kicking off --

MS. CAPPIO: Maybe that's a good omen.

MR. PRINCE: I think so.

MS. CAPPIO: I'll trade --

MR. PRINCE: I'm taking it.

MS. CAPPIO: Could we trade bracket predictions later? I'm after that billion dollars.

MR. PRINCE: I have UCLA winning it all.

MS. CAPPIO: Anyway, in all seriousness, a report on the cost study is -- I know I sound like a broken record -- we continue to work on that study. I -- if it's going to result in my injury or death, it will be out by our March meeting -- I mean by our May meeting. And we just continue to refine and revise it to make sure that we have the most accurate data and analysis in there.

I want to report that there's a new agency deputy secretary for housing at Business and Consumer Services. Her name is Susan Riggs, and she most recently was the executive director of the San Diego Housing Federation. She's got a lot of good experience, and she's a great new addition to the housing issue -- issue area in Sacramento, and we look forward to working with her.

We have news about Moody's ratings. As you may know, at the January meeting they were still working on their analysis, and we have some good news, although not as good as we would have hoped, but, hey, anything is -- is good. In terms of the single-family bond fund, that remained -- the rating remained unchanged, but the outlook went from negative to positive. In terms of the general obligation rating, that remained unchanged but the outlook went from negative to stable. And the multiple-family bond fund was put on watch for an upgrade, and they -- Moody's indicated that they were hopeful that the general obligation and multiple-family fund could be decoupled, which is very strategic for us in unwinding ourselves from the temporary liquidity -- not problem, the temporary liquidity program with the Treasurer.

So I end my remarks there, would be glad to take any questions or comments.

CHAIRPERSON JACOBS: We've got time for members of the public towards the end of the meeting, but if there's any member of the public who's here who has a time pressure and would like to address the Board now, this would be a great time.

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Item 4. Discussion, recommendation and possible action regarding the adoption of a resolution authorizing the Agency's single family bond indentures, the issuance of single family bonds,

short term credit facilities for homeownership purposes, and related financial agreements and contracts for services. (Resolution 14-01)

CHAIRPERSON JACOBS: All right. Seeing none, let's move on to agenda item 4. Is Tim going to be presenting this?

MR. HSU: Good morning, Mr. Chairman. Good morning, Members of the Board. This is a little bit of a different setting from the last time. I kind of feel like this whole setting kind of shrunk, like Alice in Wonderland.

I'd like to continue the comment that Claudia had on our rating actions recently from Moody's. I just thought that this was a good way to illustrate how far we have come. You can see -- what you have in front of you on page 2 is a history of our ratings from Moody's over the last five or six years. You can see that in that 2009-to-2011 era, which coincides with the financial crisis, things were quite difficult for the Agency. And we were able to stabilize our ratings with the 2013 update maintaining the same rating, and this year, we also kept the same rating.

The changes this year are very subtle, but positive nonetheless. Our outlook for HMRB, despite the fact that it stayed the same rating, the outlook would change to positive. We had a negative outlook before. And for our general obligation, the rating stayed the same, just like Claudia mentioned, A3, but the outlook was changed to stable. The Multi-Family III rating is on a watch for upgrade, and we're hopeful that that will conclude sometime this month.

And here's the history. This is a chart I showed you at the January Board meeting. The one thing that we are -- we are very delighted that S&P did for us is this whole idea that I've shown you previously of this decoupling. Decoupling, that is the rating of the general obligation being different from the rating of the Multi-Family III.

And that's important for several reasons, one, that Claudia mentioned, which is that our TCLP program is housed in this Multi-Family III indenture, so having a much better credit rating there will improve our options in exiting the program next year. So I thought that this is something that I sort of find helpful as I think about our ratings over time, and I hope you find it to be helpful as well.

So without further ado, agenda item 4. One of the key actions that the Board takes every year in March is passing or authorizing the financing resolutions for staff. And the resolutions that the Board authorizes are in three parts. There's one for single family, one for multi-family and also one to apply for private activity volume cap from CDLAC.

At the January Board meeting, I had mentioned that we would include the hedging piece in the resolutions. I believe we sent out an e-mail to clarify. This was a question raised by Katie, so thank you, Katie. We sent out an e-mail around to clarify that the resolutions that are in front of you do not include this hedging piece. At the January Board meeting, we felt that there numerous questions raised. Janet had asked a question about maximum loss allowance, and the Secretary had asked about having a more in-depth discussion about risks, and I believe Dalila also asked about having more of a focus on the operational risks.

So we felt that with these questions and concerns still bubbling that it's best that we continue in the dialogue with the Board. And if and when the Board is ready and comfortable, we'll introduce amendments that are resolutions at a later point during the year. We just felt that that way we didn't make you feel as if we are rushing this through, and you had the proper time and also space to consider these questions.

So the resolutions, again, do not include the hedging piece. And after we pass the -- after we ask you to authorize the resolutions, we'll continue the dialogue. And Tony is going to be the person who will have the fun to introduce the hedging policies and also the discussion about risks at a later point.

So first, the resolution on single family. In general, the financing resolutions themselves are broken out in three parts. The first part authorizes the issuance of what we refer to as debt management bonds. So these are refunding bonds that would help us continue to deleverage our balance sheet.

And the reason why this provision -- I highlighted sort of key provisions on the slide. The reason why this provision of giving us the flexibility to deposit another $50 million to facilitate the restructuring is that about two-thirds of our loans inside these single-family bonds are still conventionally insured. And these are the loans that over the last four or five years that we have sustained some losses on.

So, for example, about two years ago, two summers ago, we did a refunding of about $466 million, and for that deal, we had to pledge nearly $50 million to facilitate the refunding getting done. By getting it done we mean achieve a certain rating so that the sale of the bonds is viable.

And the second section of the resolution is authorizing the issuance of new bonds. So at the January Board meeting, we had talked about this idea that, well, at the moment we're delivering all the mortgage-backed securities that we're originating into the mortgage market. But if at a later point we decided to keep some of these mortgage-backed securities and issue our own bonds to purchase those mortgage-backed securities, we can create an annuity so that we can have more clarity about the future of the Agency. So those new bonds that we might potentially issue comes from this section of the resolution.

And the third section of the resolution deals with all the related documents to do one and two. So if we're executing certain financial statements, financial contracts, or let's say offering documents or disclosure documents related to either the debt management bonds or the new bonds, the third section authorizes staff to be able to execute those kind of documents.

If you have any questions, I can answer them.

CHAIRPERSON JACOBS: Ms. Sotelo.

MS. SOTELO: Thank you so much, Tim. I just had a brief question. In your staff report you mentioned 200 million for operating capital. And I wasn't sure where in the resolution that was authorized and what that 200 million is for. Is that -- can you explain a little bit more about that?

MR. HSU: I believe the section you're talking about, is that in section 3?

MS. SOTELO: Section 3, short-term credit facilities and 200 million in operating.

MR. HSU: So under section 3, there's also that $200 million. So at the January Board, I had talked about that. At the moment the loans that we're making are going into these mortgage-backed securities and, again, delivered into the mortgage market. So if we decided to issue bonds against -- issue -- if we decided to issue bonds and purchase these mortgage-backed securities so that we're creating an annuity and then building our balance sheet then, it's quite possible that after the mortgage-backed security is being made or created, that there is a time gap between the securitization of the MBS to the issuance of the bond, and that gap could require us to go out there and get a warehouse line.

So if we get a secured warehouse line, meaning that we say that we'll give you these MBSs and you give us a warehouse line, we know something like that is viable. And that speaks to this ability to go out there and get these warehouse lines so that we could be warehousing our loans over time with like a line of credit for that purpose.

So the $200 million, the way we ask the Board to authorize this is that it's $200 million both single family and multi-family.

MS. SOTELO: Thank you.

CHAIRPERSON JACOBS: Just one question. Given our projections internally for the way the Agency is going to grow, is this size anticipating a growth we might see as the health of the State recovers a little bit?

MR. HSU: I think it's -- it's adequate for now. And to be fair, the warehouse lines that we used to have in the aggregate was much higher than this. I want to say that we had almost half-a-billion-dollar warehouse line at some point. We had two sources, one from the State and one from a private bank. And together, combined at its peak, we probably had close to $450 million.

So at the moment, the originations that we have out of multi-family, I think at some point -- we talked to the Board about this last year -- we're able to warehouse those loans with internal resources. Where this I think really -- where I see this coming into play in sort of a viable fashion is this idea that if we are starting to get a lot of MBSs delivered on a monthly basis. At the January Board meeting I had mentioned that our threshold is roughly about $20 million a month. Once we start seeing that number getting close and we are contemplating issuing bonds, we probably should engage in a serious discussion with -- the people that we have started some conversation with is the Federal Loan Bank of San Francisco. We should probably sort of consummate that transaction of saying, okay, well, we would like to get this warehouse line from you so that we can warehouse these MBSs.

So we like to think that at some point we're going to blow through that number, but at the moment I think that's enough.

MS. CAPPIO: But, Tim, if we did, we'd come back to the Board.

MR. HSU: Oh, yeah. And that would be a very happy day.

MS. CAPPIO: Exactly.

MR. HSU: For everyone.

CHAIRPERSON JACOBS: We're optimistic.

Any other questions?

We've got, what's this, 14-01, I believe.

MR. HUNTER: I move adoption of Resolution 14-01.

CHAIRPERSON JACOBS: Great.

MS. SOTELO: I'll second.

CHAIRPERSON JACOBS: JoJo.

MS. OJIMA: Ms. Sotelo was the second?

MS. SOTELO: Yes.

MS. OJIMA: Thank you.

Ms. Caballero.

MS. CABALLERO: Aye.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Ms. Patterson.

MS. PATTERSON: Aye.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: Resolution 14-01 has been approved.

MR. HSU: Thank you.

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Item 5. Discussion, recommendation and possible action regarding the adoption of a resolution authorizing the Agency's multifamily bond indentures, the issuance of multifamily bonds, short term credit facilities for multifamily purposes, and related financial agreements and contracts for services. (Resolution 14-02)

CHAIRPERSON JACOBS: Tim, you're up. Item No. 5.

MR. HSU: Yes. Let's try this again.

So agenda item 5 is the multi-family financing resolution. And the multi-family resolution is structured much the same way as the single-family resolution. It has three sections. Section one deals with the debt management bonds or refunding bonds, again, to continue -- to continue to restructure or deleverage our balance sheet. Section two deals with new money bonds. And section three deals with all the related documents to do one and two.

A couple of things I highlight here is that -- is sort of the differences with the single family. In the multi-family side, there's this sort of whole idea of conduit transactions versus nonconduit transactions. So for the nonconduit transactions, which is the loans that -- for example, that we brought to the Board back in November, those transactions we have in the resolution stipulated that we would at least get the FHA risk share insurance on these loans and that throughout the single- and multi-family resolutions we have stipulations that they ought to be fixed-rate bonds and we're not going to use any more swaps.

On the conduit side of the equation for multi-family where the Agency is not putting our own credit on the transactions, there the structure of the transaction could be more flexible because we're not using our own credit to box up those transactions.

I would also note one more thing, which is that this is a little bit subtle, but we also reintroduced Multi-Family III. As we talked about, Multi-Family III was upgraded by S&P by four notches back in December, and now it's on watch for upgrade with Moody's. Last year when we passed the financing resolution for multi-family, we did not include Multi-Family III as part of the list of indentures that could be issuing new bonds for new deals. With these upgrades that we've gotten recently, we have reintroduced Multi-Family III back into the list of indentures that could fund new deals.

That's for a couple reasons. One is that the indenture is very, very strong and that if we use these legacy indentures, it could be more capital efficient because there's a lot of capital sitting inside these indentures already. We don't have to pluck out money from, let's say, unencumbered sources to put it into this place that we can't really touch for the next 30 years. It's more capitally -- it's more capital efficient to use old, big, large indentures like that. So that's one.

And two is that we are trying to get people to focus on the strength of this credit. And when we sell bonds, the capital markets tend to pay attention because of the disclosure documents and because there's a need to market bonds. Getting people to focus on Multi-Family III will also highlight the strength and then increase -- or let's say improve -- the options that we will have next year as we exit TCLP because some of these credits that we have that have had TCLP on them, they haven't gone into the marketplace for quite some time.

And then sometimes they're sort of sitting there out of sight, out of mind kind of thing. People are not really paying attention to these credits, and we need to start -- although the end of next year is not all that far away, we need to start sort of changing these narratives in the mind of investors so that we can get people perhaps to come to the table to help us replace TCLP next year.

So those are sort of the thinkings that we had in reintroducing Multi-Family III back into the equation of the new money bonds under this resolution.

CHAIRPERSON JACOBS: Does anyone have any questions?

Does anyone --

MS. PATTERSON: I move Resolution 14-02.

CHAIRPERSON JACOBS: Great. Second?

MR. HUNTER: I'll second.

CHAIRPERSON JACOBS: Okay. JoJo, is that the list?

MS. OJIMA: It is.

Ms. Caballero.

MS. CABALLERO: Aye.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Ms. Patterson.

MS. PATTERSON: Aye.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: Resolution 14-02 has been approved.

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Item 6. Discussion, recommendation and possible action regarding the adoption of a resolution authorizing applications to the California Debt Limit Allocation Committee for private activity bond allocations for the Agency's homeownership and multifamily programs. (Resolution 14-03)

CHAIRPERSON JACOBS: Great. Let's move on to CDLAC.

MR. HSU: All right. Two for two. Let's try for the last one here. So the last related resolution is asking the Board to authorize the staff to apply for private activity volume cap at CDLAC.

So on the single-family side, we have requested a $250 million authority, and on the multi-family side we have also requested for a $250 million authority. We currently have -- I believe we currently have $450 million of carryover volume cap for single family. It's not clear at the moment if we'll use that single-family volume cap. My -- as Matt said earlier about being optimistic and hopeful, I'm hopeful that as the origination picks up, that we could transition to this idea of warehousing MBSs, issuing bonds and rebuilding our balance sheet. I'm -- sorry? What happened? There we go. I'm hopeful that we can make that transition sometime later this year, perhaps in the fourth quarter. But it's -- it's -- there's some time between now and then.

On the multi-family side, that's -- that's -- if we can get to that number, that would be fantastic, but I think these are -- for the moment I would venture to say that these, both of these numbers, are a little bit on the higher side. And we tend to ask for the authority for a high number and perhaps at a later point if we deem that is too much, we apply for something less.

CHAIRPERSON JACOBS: Dalila.

MS. SOTELO: If you were finished, Tim, I just had a question about that. On the multi-family side, I think the $250 million is appropriate. I think that if we market it aggressively and we're out there and talking to folks about it, I think that it's a good product.

I'm a little concerned about the single family and wanted to talk with you about what are the downsides of asking for such a large amount and not being able to utilize it. Does it have expiration, or does it have, you know, any negativity in terms of perception on the CDLAC side if we ask for so much authority and not use it?

MR. HSU: I think that's a real risk. I think that if we ask for volume cap and not use it, it doesn't reflect well on the Agency. The single-family volume cap for the Agency, we do get to carry over for three years, so we do have some time to complete its use, if we don't end up using it all next year.

One of the things that we have been doing with some of the old volume cap that we haven't gotten around to use is that we turn them into MCCs. So there's sort of like a second life, if you will, of these volume cap if we don't use them for MRBs. And I think that -- if I'm not mistaken, that if we request for the volume cap and we don't use it and we don't use 80 percent of what we request for, I believe there is a small penalty. I don't quite remember what it was.

MS. PATTERSON: Would it be more realistic to reduce that number somewhat so that we don't run the risk of having a penalty? Or do you assume that we're going to use at least 80 percent?

MR. HSU: Well, I think that if we don't get some visibility -- we tend to apply -- unlike other agencies, for example, we tend to apply for these volume caps, especially the single-family side, at the very last CDLAC meeting of the year, in the December meeting. So by that time we should have much better visibility on what is going on in terms of our origination on the single-family side. And if we are not getting the kind of traction that we are hoping for, maybe we wouldn't apply for it. It's possible.

CHAIRPERSON JACOBS: I guess one of the questions I've got on the single family is the debt to income gap that we're hopefully closing later on in the meeting maybe. Is that going to shift the needle enough to make this a more realistic number?

MR. HSU: I don't want to steal the thunder because there's a lot of good things they're going to tell you about, but I think that there are many changes that are coming that we're hoping that will really sort of give the program a kick in the butt and get going. And the DTI is going to matter, but I think that one of the things they will talk to you about is the conventional product that we're hoping to launch in May. The marketplace, here in California especially, has really changed to a conventional product versus an FHA product, and what we have right now is just an FHA product.

So that, I think, if it were to -- if it gains traction, coupled with all the stuff that we're offering on our menu already, I think it's -- it's going to be fairly powerful.

MS. CABALLERO: So did I understand that although the resolution is $250 million, that you won't apply for it until December?

MR. HSU: On the single-family side, we don't apply until December; that's correct.

MS. CABALLERO: So that might appropriately be up to 250, but you might come back and advise us that you're going to ask for less during the year?

MR. HSU: We could do that if the Board chooses. Traditionally we -- if we apply for less, we -- traditionally we haven't brought that back to the Board, but if you wish, we could advise you that we're going to apply for less.

MS. CABALLERO: I guess I'm just thinking I'm hearing some hesitation. I'm hearing some optimism from you and that the meeting between the two is just to let us know if it ends up being less than 250. Frankly, I'm happy with the 250. I'm interested in seeing what the market is going to do. And if you're optimistic, I want to be optimistic too, but I'm hearing some concerns, so it might just be good to bring it back, rather than to spend all the agonizing time, you know, is it 250, is it 230, is it 220?

MS. PATTERSON: I'm comfortable with the 250, but just letting us know if you apply for less.

MR. HSU: Okay.

MS. PATTERSON: I don't need you to bring anything, just a disclosure to the Board --

MS. CABALLERO: Yes. That's what I'm thinking.

MS. PATTERSON: -- that that's what you're doing.

MS. SOTELO: I think it's just a correlation between the programs and the amount that we're asking for. I like the MCC product. I think it's really good. I think that it's -- it's not very well-advertised, so if from a programmatic standpoint you can put that into, you know, your programs and get people involved in that, then we'll have a backstop to actually spend it within three years if we don't use the full 80 percent.

MR. HSU: So I think if the timing works out, we can try to give the Board an update at the November Board meeting, if the timing works out. If not, clearly the September Board meeting. Yeah, we can do that. That's not an issue.

CHAIRPERSON JACOBS: Great.

MS. SOTELO: So with that, I move approval of Resolution 14-03.

CHAIRPERSON JACOBS: Do we have a second?

MR. HUNTER: I'll second.

MS. OJIMA: Ms. Caballero.

MS. CABALLERO: Aye.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Ms. Patterson.

MS. PATTERSON: Aye.

MS. OJIMA: Thank you.

Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: Resolution 14-03 has been approved.

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Item 7. Presentation and continuing discussion of new

financing strategies, including hedging loan commitments.

CHAIRPERSON JACOBS: All right. Item 7, the hedging discussion.

MR. HSU: So Matt, I believe the last -- at the January Board meeting, you kicked this off by saying now for the fun stuff, so I'm going to pass the baton to Tony to talk about the fun stuff. It is -- it is interesting stuff.

So as I mentioned earlier, that the Board had expressed concerns and questions at the January Board meeting, so we feel that it's the right thing to do to continue the dialogue. This presentation is a response to the Secretary's request about having a more in-depth discussion about risks. Along the way we have refined the policy to address Janet's concern about a maximum loss allowance and also, I believe, Dalila's concern about certain operational risks. So we have a very in-depth discussion here on risk that Tony's going to present.

The one last thing I would say is that what we've doing here is very different than what we used to do. What we used to do is getting very, very long-dated swaps to hedge variable-rate bonds for a very long period of time, up to 30 and, for the multi-family program, sometimes 40 years. What we're doing here is we are trying to protect our interest-rate risk on our loan commitments, which tends to be a much shorter time, 60 days or so.

So anyway, without further ado, Tony is going to walk you through the risks.

MR. SERTICH: Good morning, Board. As Tim mentioned, my name is Tony Sertich. I'm the financing risk manager at the Agency. I work in the department -- I mean the Division of Financing. And I just wanted to walk you through some of the risks involved of any hedging program that may exist within the Agency.

As Tim mentioned, what we're proposing now is very different than what we did ten years ago or five years ago with our long-dated hedge swaps, hedging our variable-rate bonds. Today we're doing short-dated hedges to reduce the interest-rate risk on our loan commitments.

The master hedge policy draft that was put together was in the Board package, I don't know if you've been able to review it or not. If you have, please feel free to ask any questions as I'm going through this presentation. I want this to be more of a conversation because I know that it can be pretty full of jargon and stuff, so I want to be able to make sure everyone's understanding as we go through this what we're talking about.

So the master hedge policy was developed to establish guidelines for the use of any financial derivatives that we have going forward. The general purpose of all these hedges is to reduce our interest-rate risk to the Agency on the loan commitments, not on variable-rate bonds. We don't plan on doing that, and it's not part of the hedge policy, and so we wouldn't have approval to do that. It's only for short-term loan commitments.

On the single-family side, the hedge policy talks specifically about up to 180 days, hedges set up within 180 days, and on the multi-family side within 36 months. And the hedges, as I said, the hedge policy will help manage many of the risks inherent in using financial derivatives.

And I'll go -- that's what I'm going to go through now, is the different risks that are inherent in the derivatives.

The single-family hedge bond we're proposing would look something like this. I don't know if this is -- so CalHFA sort of sits in the middle here. And traditionally what we've done is we've provided a rate lock to a mortgage borrower. It could be for 30 days.

It could be for 90 days. It just depended on the program we're running. What we then would do was we would then sell bonds to finance that loan.

In the current environment what we're doing instead is we're selling the -- we're securitizing and selling an MBS to an investor at a given rate. However, when we sell the MBS, there's a timing difference between the lock and the -- and the sale. So that could be 30 days. It could be 90 days, something like that.

The hedge, then, would come into play over here where we would lock in a rate when we lock the rate to the borrower. And what we receive from the MBS investor as a sales price would then be passed back through to the hedge provider so that we're taking the interest-rate risk from the time that we lock the rate until the time that we sell the MBS out of the equation and locked a fixed income to the Agency.

The hedge itself, if done perfectly, would eliminate all interest-rate risk. However, it's very difficult to do the perfect hedge, and that's what I'll walk you through, all the risks tied to that.

As I said, if this hedge is not here, we need to take all of the interest-rate risk from the time that we locked the rate to the time we sold the MBS. If rates rose during that time, the MBS prices would decrease, and if rates fell, the MBS prices would increase. So if -- when rates rose, we would lose money, and when rates rise -- when they fall, the Agency would make more money.

However, we're not in the business of taking interest-rate gambles. We're trying to lock in specific income to the Agency up-front and make it as clean as possible.

So as we walk -- the first risk I want to talk about is what's known as counterparty risk. What if the hedge provider does not meet its obligations to us? There's multiple reasons that this could happen, actually. One is that the hedge provider, as Lehman Brothers did, would -- just goes away. We did have interest-rate swaps with Lehman Brothers, but we were able to work that out because -- so they weren't able to continue to pay on the swap, but we had termination provisions and replacement provisions in those documents, and we were able to replace the swap. So we plan on putting those into any hedges we do in the future as well, is termination, replacement provisions upon credit events so if one of our hedge providers gets downgraded to some low rating, we can terminate the swap at market, meaning we settle up -- if they owe us money or we owe them money, we would settle that up and replace it with a new counterparty without any cash actually being exchanged.

The only reason we wouldn't be able to replace is if, A, CalHFA's rating was too low for someone else to accept it, so no one wants to take our credit anymore, or if the market just fell apart completely and no one was doing these hedges anymore. So those are two sort of -- you know, the CalHFA rating was -- could have been a problem in the past. We don't see that as a problem going forward. But the market problem has never really -- that's sort of an outside risk that, being in this business, we think we're willing to accept.

Another way that we'll try to mitigate this risk is by making sure we diversify our hedge portfolio amongst many different hedge providers. We won't throw all of our eggs in one basket, and we will spread it out amongst many different hedge providers.

MS. CABALLERO: Could I ask a question?

CHAIRPERSON JACOBS: Yes.

MS. CABALLERO: Could I ask a question?

MR. SERTICH: Sure.

MS. CABALLERO: So in reality, hedge providers don't fail to meet their obligations very often; am I right about that?

MR. SERTICH: No, we've never -- that's a very rare occurrence, correct.

MS. CABALLERO: Okay. Because I mean it just seems to me that I understood it better before we started this discussion, because I've spent some time talking with staff just because there's money to be made in hedging.

MR. SERTICH: Correct.

MS. CABALLERO: And so because of that opportunity -- right now we're contracting with someone that does the work for us.

MR. SERTICH: Correct.

MS. CABALLERO: But the idea would be to bring that in-house --

MR. SERTICH: Correct.

MS. CABALLERO: -- and potentially make the money that we're paying to someone else.

MR. SERTICH: Correct. You make it and pass it along.

MS. CABALLERO: Okay.

MR. SERTICH: Let me rephrase my answer. The hedge providers that we plan on dealing with, which are highly rated hedge providers, we don't expect to -- them to have failures. And with the contracts that we enter with them, with the termination provisions and such, we would expect to eliminate or to mitigate most of those risks.

MS. CABALLERO: Okay. I just wanted to make sure I understood it correctly.

CHAIRPERSON JACOBS: In this section, please interject if anyone --

MR. SERTICH: Yes, please, at any time if you just get my attention, I'm more than willing to --

CHAIRPERSON JACOBS: I think the long-term capital management did fail on the hedge obligations. This is back many years ago. I think the ratings that we're looking for of counterparties wouldn't -- that wouldn't be --

MR. SERTICH: There was a hedge fund really.

CHAIRPERSON JACOBS: We wouldn't be in that situation, I think.

MS. CABALLERO: Doing that.

MR. SERTICH: We are trying to put as many safeguards in place to prevent that from happening, is the goal here with the hedge policy that we've put in place.

CHAIRPERSON JACOBS: In terms of the sizing of this, and maybe it's covered further in here, but is this adjusting daily, weekly? How often are we in the market?

MR. SERTICH: It would really depend on the volume we have. I mean, if we're talking about the -- you know, the $250 million of single family, you know, or 300 million, it would probably not be daily, but it would be fairly -- it would be often, probably at least weekly. It really depends on the volume that we're getting on the single-family side, but we're sort of truing up our balances on a regular basis.

CHAIRPERSON JACOBS: And is this an additional staff person who's a specialist, former trader, doing this, or is this existing people?

MR. SERTICH: This would be existing staff. We think we have the expertise in-house to do this at this point.

So the next large risk which is a real risk is -- is the risk that what we hedge does not actually -- is not the same amount as the amount of loans that have come through -- come through the pipeline. So a big reason for this would be single-family loan fallout. We may reserve a hundred thousand dollars or, say, a million dollars of loans. We expect 700,000 of those dollars of loans to come through, but only $500,000 comes through or maybe $900,000 comes through. And so we're not completely hedged on that interest rate. The over or under hedge -- hedged amount is -- is -- is -- has interest-rate risk on it.

So let's take an example. Let's say we had -- we had hedged for $700,000 of loans to come through that we can sell, but only $500,000 of loans came through to sell. We would then have $200,000 of extra hedge, and we would have to settle on that amount. We would have to settle with the hedge provider on that extra $200,000 without an offsetting loan. So if rates went down, we would then have to pay the hedge provider on $200,000 of --

CHAIRPERSON JACOBS: Historically how much volatility is there in the rate of dropouts on the single families?

MR. SERTICH: When we ran our own loan program, we would monitor that because we would -- not for hedging purposes, but we would need to know how many bonds to issue, and so we would monitor it for that purpose. The risk on that is in general CalHFA historically has not been very volatile, especially with regard to rates movements, because we've been through the market on rates, so that's a big reason loans would fall out. If -- for example, if you had a -- if you went to a mortgage, got a mortgage locked at 5 percent, but then two weeks later you can go relock a new one at 4 and half percent, you would say, "I don't need that

5-percent loan anymore." Traditionally CalHFA's been through the market, so if the general market rate was 5 percent, we might already be at 4 and a half percent, so we had a lot more room.

In the current market, we're -- we're not as rate sensitive as the general marketplace because a lot of our program is based on the extra downpayment assistance that we give to the borrowers. So we're not exactly sure how volatile, but my guess is, you know, this 20-percent volatility, like I said, is probably on the very high end of the volatility that we would experience.

CHAIRPERSON JACOBS: The concern I've got is with the conventional product, you know, for obvious reasons.

MR. SERTICH: Yes. And it would still be the same thing. The conventional product, we would have more downpayment assistance so that should reduce the people's ability to drop out and go get another loan because they can't get the extra downpayment assistance.

CHAIRPERSON JACOBS: With the current program where there's a third party taking the hedge and someone drops out -- let's say rates drop dramatically and everybody drops out. Under the current scenario, who bears that?

MR. SERTICH: The third party bears all of the risk.

CHAIRPERSON JACOBS: All of that risk.

MR. SERTICH: So we are paying them three-quarters of a point on every loan that comes through to bear that risk plus do the administrative work for the hedges. So it's a large -- it's a large chunk that they're getting. And we -- we would take that in-house, so that would be a risk buffer that we would have to manage some of these risks. And that's one thing that I know Ms. Falk had a question about, how we deal with the -- we factor that into the equation of how much we'd be willing to do.

CHAIRPERSON JACOBS: Okay.

MR. SERTICH: But I do think that is -- this is the one risk that requires the most day-to-day management of the -- of the hedging program, is making sure that we have the proper amount of hedges out there. And it's something that we can roll forward. If we get a little over hedged or under hedged and the loans keep coming in, we just keep balancing that out over time so that it's not -- it's not like all of a sudden we get one loan, and that's the only loan we're going to get for a month. If that was the case, it would be a much more difficult thing to manage.

On the multi-family side, that would be the case. And the -- the one thing that we're going to do on the multi-family side to prevent loans from falling out is we're going to make the borrowers put a lot up-front, a big deposit up-front, so that they make sure they actually come through with the loan when it's -- when the time comes.

CHAIRPERSON JACOBS: Now, I'm personally not really concerned about the multi-family or the traditional CalHFA products. It's the conventional loan I'm kind of a little -- a little nervous on it.

MR. SERTICH: Yeah, and I think that we've -- you know, it's really monitoring on a daily basis. Even if we're not hedging on a daily basis, it's looking at the reservations daily or multiple times per day, following the market rates, because that will affect things. Not as much as I said on a general -- general hedging program, but it will affect our fallout. Watching the fallout regularly, we get reports daily from our data staff.

CHAIRPERSON JACOBS: Sorry to keep --

MR. SERTICH: No, no, please.

CHAIRPERSON JACOBS: Just one thought maybe on the -- I know we don't have a lot of alternatives in the downpayment assistance pools and all of that. On the conventional product, are there more third-party facilitators who are out there in the market or --

MR. SERTICH: There are some third-party facilitators out there. We've talked to multiple -- I mean, there's not -- it's not a huge universe, but there are a few. So your suggestion would be to talk to others?

CHAIRPERSON JACOBS: Yeah, I don't know. Just on the conventional product, we may want to look at how we take it to market. On the other hand, we have to evaluate the risk versus the savings.

MR. SERTICH: Yeah.

CHAIRPERSON JACOBS: And the savings is substantial.

MR. SERTICH: That's sort of what -- you know, that's why we're bringing this to you to have continue to have the conversation, because it is a risk. We think that with the hedge policy we've put in place, we've tried to put parameters around those risks to limit the risk as much as possible, but we know -- but, you know, again, as you just reiterate, and reiterate that it's not the same level of risk that we took --

CHAIRPERSON JACOBS: Not at all.

MR. SERTICH: -- with the interest-rate swaps on the long-term bonds. Those were 30-, 35-year risks.

This would be a much shorter period and much more contained risk, much smaller dollar amount as well.

MR. HUNTER: And so just -- I'm a little bit confused here, but to make sure I understand this, when you're actually doing these hedges, are you doing transaction by transaction, so like individual loan by individual loan, or are you grouping these loans?

MR. SERTICH: It would be grouped, for sure. And it's -- like I said, because of the fallout, you know, we don't expect every loan to come through. We expect some percentage of the loans to come through, which would change, depending on how the loans look.

MR. HUNTER: So that's where your scenario was $700,000 may represent five loans, and one of them falls out.

MR. SERTICH: Correct. Yeah, if there's a million dollars and we have -- expect to say --

MR. HUNTER: Right.

MR. SERTICH: Traditionally we've had between 25 and 35 percent of our single-family reservations fall out. So that's where I get the 70 percent.

MS. SOTELO: I think there's a programmatic control of volume. I mean, there's obviously the marketplace.

MR. SERTICH: Yes, right.

MS. SOTELO: And that's what the hedge is about, understanding the market and hedging against that. But for me, my perception is that from a programmatic standpoint, if you have the right product, you know, the market will do what it's going to do. But if you have the right program where you're, you know -- where you're more user friendly, where you can close quicker, where you can really have a product that people like and there's a competitive advantage, not necessarily just on the interest rate, but the actual program itself, you know, it's kind of something where I think operationally and programmatically we can maintain the volume as opposed to, you know, expecting the 35-percent fall-off rate.

MR. SERTICH: Oh, no, I agree. The fallout rate is going to be there, sort of no matter -- I mean, it's --

MS. SOTELO: It will be --

MR. SERTICH: -- something that will affect --

MS. SOTELO: -- the market, right?

MR. SERTICH: Yeah, I mean, it's just the general single-family marketplace. There's always going to be some fallout. Whether it's 35 percent or 15 percent, I think there could be some controls there. I mean, more efficiencies, closing quicker, things like that, we should reduce that.

MS. SOTELO: And from a paperwork standpoint making it easier for single-family loans to close and go forward. So for me, there's an upside on the profitability of, you know, turning this in-house as opposed to giving it to a third party. Then my hope is that we have more control of it on the staff side and that programmatic control can, you know, incentivize our buyer by the potential upside of it.

MR. SERTICH: Yeah. I mean, we would still be working with outside master servicers to run this program as well, which is -- a lot of the underwriting and stuff runs through them, so that we wouldn't be able to bring all of that in-house additionally, so -- but -- but I think the more control we have over the program, you're right, the more we can tweak and adjust things. But that's -- we'll never have full control over any of that because we're still working with outside lenders. We're still working with different outside parties that -- that will control a large part of the process.

MS. SOTELO: Would we be able to bifurcate -- just addressing Matt's concern about the conventional product, would we be able to bifurcate or treat it separately, the conventional product?

CHAIRPERSON JACOBS: Well, in the conventional part, there are more hedging counterparties, whereas on the -- on the downpayment assistance product, there aren't.

MR. SERTICH: Oh, yeah, we're not hedging anything on the downpayment assistance. We have the conventional. We have the FHA.

CHAIRPERSON JACOBS: Okay. So it's just the FHA that's --

MR. SERTICH: Both of them will have the downpayment assistance benefit versus the marketplace in different ways.

CHAIRPERSON JACOBS: Even on the conventional?

MR. SERTICH: Yes, there's a special --

CHAIRPERSON JACOBS: Oh. That reduces the dropout risk even more.

MR. SERTICH: Yeah. That's what I was going to --

CHAIRPERSON JACOBS: I think it's the blue moon event that where for some reason the federal government does something and rates drop two points.

MR. SERTICH: Yeah, exactly.

CHAIRPERSON JACOBS: And then we have everyone drops out --

MR. SERTICH: Yeah, the --

CHAIRPERSON JACOBS: -- what the total exposure is there.

MR. SERTICH: Yeah, and I think if we're rolling these forward -- if we're rolling these out there every 60 days or so, if our -- our total exposure should be limited to that amount. I mean, that's the good thing about having a shorter duration of --

MS. SOTELO: Because you're adjusting it every 60 days.

MR. SERTICH: Well, because the loans are closing every 60 days, so we're not --

MS. SOTELO: You can adjust.

MR. SERTICH: -- out the total amount of this hedge. You know, if we -- excuse me. If we do -- you know, if we got to the point where we're doing a billion dollars of loans every year and we have this outstanding for 60 days, that's, you know, $150 million of notional amount on the swaps on the market value. I don't know what it would be, but it's not going to be --

CHAIRPERSON JACOBS: It's not going to be --

MR. SERTICH: It's going to be some ratio, some small percentage or some percentage of that.

CHAIRPERSON JACOBS: Continue with the presentation, sorry.

MS. CABALLERO: This is the reason for the agenda item.

MR. SERTICH: Yeah, no doubt. I want this to be as conversational as possible, so please continue to ask questions. This is helpful.

MS. PATTERSON: So we had talked about our various different single-family products and whether we would be hedging on all of those single family or we would cherry pick, basically.

MR. SERTICH: Yeah, I think that was what came up last time, yes.

MS. PATTERSON: Last time we kind of talked about that.

MR. SERTICH: Okay, yeah.

MS. PATTERSON: So that's something you're still looking at like --

MR. SERTICH: I think from what we've thought about is -- from our point of view is if we're going to hedge -- so really there's two products that we'd be looking to hedge. It would be the conventional Fannie Mae program, or it would be the FHA Fannie Mae program.

MS. PATTERSON: And they both have downpayment assistance.

MR. SERTICH: They both have extra downpayment assistance -- or higher LTV ratios than the general marketplace can offer.

MS. PATTERSON: Got it, okay.

MR. SERTICH: Excuse me. So we were thinking that they're very similar. If we're going to bring one in-house, we'll bring both in-house, but by no means do we have to do that, because I think the other thing we were talking about last time is there's a possibility of other small niche programs, like the energy efficient mortgage or things like that, where it might make more sense too to let someone else take that off. So there are other small programs, but the two large programs, which is the --

MS. PATTERSON: Got it, okay.

MR. SERTICH: -- FHA or the conventional --

MS. PATTERSON: Okay.

MR. SERTICH: -- we were thinking of bringing both of those in-house.

The -- the next risk, which is not quite as big as the size risk but it is a significant hurdle to manage, to get exactly right -- this is another thing that we're -- the extra savings would help cover is the timing risk. The duration of the hedge that we enter has to be a fixed rate when we first enter it. And the closing and sale of the MBS may not always exactly meet that duration.

So if we entered into a hedge assuming the sale of the MBS would be 75 days out but it actually took a hundred days to settle the MBS, we have 25 days of rate risk we're taking there. Vice versa, if it only took 50 days to sell the MBS, then we're over hedged extra for the 25 days. Again, we can roll that rate. We can roll that hedge as new loans come on, but that is another risk that we would have to cover.

One of the basic controls on this is that both our single-family and multi-family programs would have very hard deadlines about when the rate locks would expire, so you can only lock it for 60 or 90 days or something like that or two years for a multi-family loan or something like that. So that would be -- the general TBA program has a -- our current TBA program has a 60-day rate lock with one 30-day extension available at a cost, at an extra cost.

CHAIRPERSON JACOBS: How would we be adjusting our financials to reflect the -- again, the blue moon scenario, just as an exposure, just if interest rates nationally fell to zero? What would be our -- I mean, how do we have to reflect that on our books?

MR. SERTICH: GASB has very clear rules about the financial -- how to address hedges in the financials. So it's -- currently we're not addressing it for a sort of risk adjusted. So we're not looking at worst case scenario on our financials; we're looking at actual market values. What we do internally is look at -- and you've seen this on some of the presentations that Tim has given, is what happens if we get downgraded and rates drop by a point, what -- what does our market value look like on our swaps?

CHAIRPERSON JACOBS: Right.

MR. SERTICH: So we do look at that internally, but it's not something that GASB asks for or wants to see on the financial statements.

The last major risk that I wanted to go over is what's known as basis risk. And this is the risk that what we're trading on the hedge -- so if we're trading, you know, prices of MBSs -- doesn't tie to the changes in prices of MBSs in actuality. This shouldn't happen on the TBA program because we're trading very clean. It's a very liquid market. The prices are out there for everyone to see.

This happened a lot on our old interest-rate swaps. It's actually still a part of our -- it was part of our -- the interest-rate swap report that you guys would get on a -- every Board meeting, what we call basis mismatch calculation. If we -- our bonds may be tied to -- they're not really tied to an index, but they follow generally an index of tax-exempt variable-rate bonds. But our swaps may be tied to taxable -- some percentage of a taxable index or something like that. So the -- there was a difference between what we received and what we were paying, just inherent in the calculations. We tried to limit that as much as possible.

The TBA single-family hedging program we're talking about should not have that risk.

The multi-family long-term -- not long-term, but the multi-family forward rate lock would have some of that risk because there's no CalHFA fixed-rate bond index. You know, we issue fixed-rate bonds. Who knows what it's going to be?

We could buy a forward rate lock from a bank probably on our fixed-rate bonds, but that would be outrageously expensive and make us uncompetitive probably, so that's a risk that we would -- if we're going to put a hedge together on the multifamily side, that's a risk we would have to be willing to take, that the hedge does not completely cover the interest-rate risk we're taking.

The other risks that the hedging policy considers and tries to put parameters around are the administrative burden of managing the hedge. So from an accounting perspective, from a financing perspective, from a legal perspective, does the Agency have the means to manage any hedge correctly? We would not enter into a hedge if we thought that it would place some undue burden on some part of the Agency. And I don't think anything that we're considering at this point has met that.

CHAIRPERSON JACOBS: I think the other risk that's not talked about is headline risk, that the Agency doing a different kind of derivatives got into trouble before, which I think maybe part of this is just a communication when you do this, that this is different and here's why we're doing it. It saves money, and there are reasons for it, so just getting in front of that headline.

MR. SERTICH: Yeah, and that's something that we definitely want to, you know, make sure that everyone's comfortable with before we move forward. I guess from a financing point of view we think about the numbers risk, but you're right, there's always headline, reputation risk on that side of the things as well.

MS. CAPPIO: Well, and somewhat editorially, the Governor's Office gives me a wide degree of latitude and only cares if the news is bad. So I mean, we have to -- we have to balance that out, I think, and we will.

MR. SERTICH: Yes, for sure.

MS. CAPPIO: We have to move forward, and we will do so in a balanced way.

MR. SERTICH: One of the basic precepts of the hedging policy -- hedge policy is that we're not going to take any risk that the Agency cannot afford if things go completely wrong. If they go as bad as possible, we wouldn't take that risk. We would still, you know -- if things go as bad as possible and the Agency couldn't handle it, we're not going to take that risk.

MS. SOTELO: And, Claudia, the good news is that we as a Board will acknowledge the good stuff as well as, you know, the horrible wrong things.

MS. CAPPIO: I guess the curious timing issue is it's election year, so I'm going to be doubly careful.

MS. PATTERSON: So one of the reasons why we're looking at this whole thing is for cost savings, being more competitive and potentially passing those savings on in the form of perhaps a lower interest rate to some of our borrowers.

MS. CAPPIO: That's right.

MS. PATTERSON: So -- and it's not part of hedging, but one of the things that costs a lot is that we don't do any direct lending. And so I want to throw that out there for staff to consider, maybe a small direct lending program getting authority that goes in conjunction with on the single-family side. I don't know, but some of these things to explore if you really are trying to do what others aren't doing in the market and you want to limit it to a targeted geographic area and you're really trying to get down to helping homeownership in certain communities, what tools do you have in your toolbox to make that happen?

As I understand, this is one of the tools. I'm getting much more comfortable with where you're going with this. I'd like to offer that staff consider thinking about those things. And I want, don't want to be taboo in an election year, but I do think that if we are a bank and we're lending and we want to lend with a purpose, that we do look at some of the tools in the toolbox and perhaps a direct lending -- small direct lending program.

MS. CABALLERO: To that end, I think it might be really interesting to see if there's a way to do that in conjunction with a program that is focused on an educational -- because part of the reason that people can't afford these loans is because they're not making enough money. But if you can infuse a community through an economic development program where they can get training, it then gets them the better jobs. Then they can afford the loans -- better afford the loans. So, you know, I tend to think of it in terms of what you can do in a community. Very difficult to put the two together, but I just think it would be very interesting to see a pilot project.

MS. SOTELO: And maybe the pilot project happens from an industry base.

MS. CABALLERO: That's exactly what I was thinking. Either industry or from labor, because they've got really good programs, apprenticeship programs, where you come out as a journey -- journeyperson, and you're actually earning pretty good money so you have the ability to do loans in a neighborhood, maybe, that may be very challenging otherwise.

MS. SOTELO: And then you have the wraparound concept of credit counseling plus loan product. That's a great idea.

CHAIRPERSON JACOBS: Certainly in partnership with our sister agency it's something we've got.

MR. SERTICH: Yeah, these all -- a lot of these things have been discussed before. It's just --

CHAIRPERSON JACOBS: I still think the public markets would buy those ventures as well. Maybe those can be pooled and sold the same way anyways.

MR. OKIKAWA: Hi, I don't want to interrupt.

CHAIRPERSON JACOBS: We want to get you through here, but go ahead.

MR. OKIKAWA: I just wanted to make a few comments about the direct lending. One of the things that prohibits us currently from direct lending is we can't do it on a first mortgage, you know. We can on seconds. One of the things we'd love to explore is see how we can actually do these types of programs, but it also involves truth in lending, all those sort of things.

MS. PATTERSON: There's more administrative work --

MR. OKIKAWA: Right.

MS. PATTERSON: -- that goes into a direct lending program.

MR. OKIKAWA: There's a lot more. But we'd love to address some of these things.

MS. SOTELO: Small targeted pilot --

MR. OKIKAWA: Yeah, small.

MS. SOTELO: -- program. Pilot.

MR. OKIKAWA: Pilot.

MS. SOTELO: Yes, small, little authority in conjunction with other things in a particular community.

MR. OKIKAWA: Yeah, we'd like to explore that.

MS. SOTELO: Like NHS or someone that already does lending but you can partner up with.

MR. OKIKAWA: Uh-huh, yes.

MS. SOTELO: Because it costs a lot of money. Someone else is doing the work and then we're buying that, and if you could cut through the middle man, that's savings, actual savings, for the borrowers.

MR. OKIKAWA: Correct.

MS. SOTELO: So, Claudia, would it be appropriate to ask for a report back on maybe some creative ideas from staff about that for our next meeting?

MS. CAPPIO: Sure. If not the next meeting, then the July meeting, but we'll take it to heart and explore it.

CHAIRPERSON JACOBS: And I think we should be moving forward with the hedge discussion, and I would think for the next meeting we would like, you know, with some -- some adjustments based on the discussion today a resolution in there to start looking at to approve it, frankly, just with those tweaks we discussed and establishing clearly in here the limits.

MR. SERTICH: Yes. Okay. There was just one other thing I wanted to cover on the next page, is that we have put sort of a -- in the hedge policy there's discussion of the maximum risk that the Agency is willing to take on these -- on any hedges that we do.

As I said, you know, CalHFA won't enter into anything that we don't have sufficient capacity to terminate at market rates.

Also, the short-term nature of the hedges will limit the risk. We talked about the single family being, you know, 60 to 90 days on average.

And also, there's a formula in here talking about the cumulative losses from the single-family TBA hedging program won't -- we won't let it exceed the savings from running the program in-house. So once that happens, I think it talks about on a six-month basis, then we would -- we would just stop doing the hedging program, stop the TBA program in general.

CHAIRPERSON JACOBS: I know this is a little late for it, but one of the -- if we could put into our agreements with the counterparties we work with fat finger clauses just to eliminate that risk completely.

MR. SERTICH: Yeah, we have -- we could re-do some of that stuff.

CHAIRPERSON JACOBS: Okay.

MR. SERTICH: And then on the multi-family side, an initial hedging program is designed with only up-front costs, so it's really -- where a lot of that is going to be paid for by the borrower, like I said, so that they're sort of -- have a lot of skin in the game and they'll follow through and then without ongoing costs or risk so that we're really buying the option up-front for them as opposed to taking a real hedge.

And then we plan -- as we did with our old interest-rate swaps, probably even in more detail -- reporting on all the hedges on a regular basis to the Board, to the rating agencies, and through our disclosure documents to the general public and investors.

And if there's any more questions now, I'm willing to take them. If not --

MS. CAPPIO: Now or later.

MR. SERTICH: Now or later, yes. And Tim is always available as well.

CHAIRPERSON JACOBS: I just have to say it was a really great effort to answer the Board's questions, just based on our discussion last time. I think it was a really, really helpful presentation.

MR. SERTICH: Thanks.

MS. SOTELO: Thank you very much.

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Item 8. Discussion, recommendation and possible action to increase the Debt To Income Ratio on Single Family Loan Products from 43% to 45%. (Resolution 14-04)

CHAIRPERSON JACOBS: All right. Let's call up Ken for moving this little needle, debt to income.

MR. GIEBEL: Good morning. Happy St. Patrick's Day.

We're here to talk to you about one thing today. I know we're going to wind up talking about a lot of things. But when -- and I'm going to talk to you about the recommendation and the benefits, and Sheryl is going to talk to you about background on this. This was -- we're going backwards a little bit. We're going to start how we started at 43 and why we're recommending 45 today on the DTIs, and while you think it's only a couple of points, we'll show you the impact it has.

I just want to make one other comment because there's been a lot of discussion about interest rates. On our FHA products, we have a very, very good interest rate. We were told on Thursday by our hedger that we have the best interest rate on an FHA of any HFA in the country.

So today it's not all about interest rates, because they're so low. It's about the overlays. And we have a lot of overlays. This is one of them, and this a big one. So that's why we brought it to you. We want to try to get it approved with your approval before we introduce in mid-May the conventional and the energy efficient products. We think it will make a big difference, and it will be very helpful to us. In the long run it will make us competitive.

Okay. With that, I'm going to turn this over to Sheryl to give you a little background.

MS. ANGST: In response to the anticipated 2014 qualified mortgage definition by the Consumer Financial Protection Bureau, we presented to the Board in the May meeting to have a flat DTI of 43 across the board on all our lending programs, which was approved.

As a result of this 43 percent, since -- since -- well, it started July 1, we basically reduced the amount of volume on our CHDAPs by 57 percent, and we figure based on our production, 1,772 borrowers did not receive financing on the CHDAP program.

October of 2013, CFPB final ruling exempted FHAs, Fannie Mae, Freddie Mac and housing and nonprofits from the 43 DTI.

MR. GIEBEL: And we'll just give you a little more background on the CHDAPs.

CHAIRPERSON JACOBS: Some of the acronyms --

MS. ANGST: Oh, I'm sorry.

CHAIRPERSON JACOBS: -- it would help if --

MS. CABALLERO: I apologize, but I've got to go back to our staff report to figure out --

MS. ANGST: I can --

(Court reporter interrupts for clarification of the record.)

CHAIRPERSON JACOBS: Sorry. There was just a question about some of the acronyms.

MS. ANGST: Okay.

CHAIRPERSON JACOBS: And so we'll ask staff for a little bit of help with that.

MS. ANGST: QM is qualified mortgage. CFPB is the Consumer Financial Protection Bureau.

MR. GIEBEL: The federal --

MS. ANGST: DTI is debt to income ratio. CHDAP is the California Housing Assistance Homebuyer --

CHAIRPERSON JACOBS: Downpayment Assistance.

MS. ANGST: Exactly.

MR. GIEBEL: That's a bond-funded program, a couple of bonds.

MS. CABALLERO: Thank you.

MR. GIEBEL: Okay.

MS. ANGST: So we did a little bit of research, and in the three months prior to us changing the DTI to 45, our average DTI was actually 44.6 percent. And then we did a sampling of 320 loans. And during that time frame, we had -- that basically under -- less than 43 percent was 40 percent of the value, between 43 and 45 was 10 percent of the value, and then over 45 percent DTI was 50 percent of our total loans. The CHDAP loan since 2009 -- and this is before we actually had a DTI restriction -- was 27 out of 15,785 or 17 percent.

MR. GIEBEL: Point --

MS. ANGST: Excuse me, .17 percent.

MR. GIEBEL: -- 17 --

(Court reporter interrupts for clarification of the record.)

MS. ANGST: .17 percent.

And then we also spoke to Genworth Mortgage Insurance Company. Basically there's been no increase in their default rate between -- with a DTI between 41 and 45 percent. And that was based on their 2010 and '11 book of business.

MR. GIEBEL: So from a benefits standpoint, immediately, at least on the CHDAP side, that's providing that 3 percent downpayment assistance for someone's -- anyone's first. It should go up by 10 percent, easily. And we are expecting with the business we have right now, the FHA loans, we should go up somewhere between 5 and 10.

Here are some of the other guidelines with overlays that we're dealing with people that we will deal with currently on the FHA, but we'll also deal with on the conventional products. U.S. Bank is our master servicer. They have a 45 percent max DTI. Fannie and Genworth, 45 percent manual underwriting. HFAs are pretty much 45 percent across the board on DTIs.

And the other thing that you'll see is this number is a little low based on something I saw the other day, and I know we presented this back on our original presentation, but in the areas we do business, which is about eight counties in the state, on CHDAPs, for example, it's still about 26 percent cheaper in these targeted markets to purchase than to rent. And I just saw a number the other day from Di that that number is escalating quickly, especially in the coastal communities of California. It's like 38 percent.

So anyway, these are some of the immediate benefits we see for moving those two percentage points.

Any questions you might have? Yes.

MS. PATTERSON: So there are no limitations to going higher than 45 percent?

MR. GIEBEL: No, but that seems to be the industry standard. We know -- correct me, help me here. We know some of the HFAs for higher FICOs are going to 50. Over 700, I think Genworth will permit over 720, maybe a little higher DTI.

MS. PATTERSON: And the risk of having a higher

DTI is that you have a higher risk of default?

MR. GIEBEL: Yes. But as -- if we go backwards and look at when we didn't have any DTIs, the seven -- you know, the less than one quarter of one percent doesn't seem to be an issue.

CHAIRPERSON JACOBS: I guess the 50, maybe it's ambitious for right now, but certainly for certain borrower types, seniors on a fixed income where it's known what that's going to be, firefighters, police officers, school teachers, it may be worth looking at that in the future.

MR. GIEBEL: We can look at it, and it's not an issue. Where it would really be effective would be on the CHDAPs, because with our overlays from our master servicer and our MI provider, we're going to be at 45, okay, on the conventional. Fannie would be the same.

MR. HUNTER: When you're talking about this number, debt to income, you're talking about total debt, not just --

MR. GIEBEL: Yes.

MR. HUNTER: -- the percentage --

MR. GIEBEL: Back end.

MR. HUNTER: So when you talk about only having, you know, less than a quarter of a percent default rate, I just wonder if there -- what the variables are in terms of, well, if your maximum -- if your 45 percent consists of 40 percent housing costs and only 5 percent other costs, as compared to, you know, we were using other kinds of limits to say, well, your housing debt could only be 33 percent, and then you don't have a lot of other debt in addition to that. I just -- it seems to me it's kind of a fluid --

MR. GIEBEL: Yes, it's basically the end looking at all the debt. So if it's a student loan or your car loan or your credit card loan, plus your house payment, that's what they're -- that's what everyone's writing to these days.

Now, the market, conventional market, is still at 43 per the rules of the qualified mortgage. These exemptions are only for the people, the organizations, that are listed. So that's why first-time homebuyers are having a tough time in the marketplace. Traditionally that's about a third, a little over a third, 35 percent of mortgages, and it's below 30 now. And besides the supply issue, it's the underwriting requirements for the conventional people. And people like Wells Fargo do have some specialty products they're putting out there where they're giving them downpayment assistance, which is a considerable amount of money, but they're very high FICOs -- I mean very high DTIs.

CHAIRPERSON JACOBS: I think another point just to keep in mind is our buyers are getting homeowner education, and it's a fairly robust process.

MR. GIEBEL: Yes.

CHAIRPERSON JACOBS: I guess going forward, monitor this and keep us apprized.

MR. GIEBEL: We will. We will give you an update, especially when we talk about conventional. We want to come back and talk to you about a couple other things in May.

MR. PRINCE: Last Board meeting, we talked about the 12 percent or 13 percent default rate. I know you said it's .17 on the downpayment assistance. I guess I'm concerned as we keep pushing these ratios upwards and I hear the concerns about not being able to get some people into homeownership, but as a renter provider, maybe that's not so bad, I mean, to put people into housing, into homeownership and then have a high default rate, is pretty harmful to the community as well. So I guess that's what I'd like to know, is when you look at the default rates that you've had over the past few years, have you looked at what percentage of that was due to underwriting, pushing people's ratios to start with? I mean, that's a question.

MR. GIEBEL: Right.

MR. PRINCE: So I do have concerns about pushing ratios. On a personal note, I think my wife and I, our ratio is at 15 percent. And I understand my income might be a little bit higher, but I don't believe in pushing ratios like that. I have to tell you the truth.

MR. GIEBEL: Well, when we started, we just started in August with our FHA project. When we reinstituted the CHDAP program in 2009, we've watched those numbers very closely because we don't like eating the four to six thousand dollars ourselves, so we've kept an eye on it. And again, we didn't have any ratios then because we don't underwrite the first. We just look for the compliance: First-time homebuyers, income limits, sales price limits. And that's what we've seen, was the first thing we looked for, is are these loans, you know, having problems, and we haven't seen that.

And we can tell you on the first we have written so far on the FHA loans, the amounts are up slightly and the FICO scores are up. I think they're 6 -- 686 is our average FICO on our FHA products to date.

MR. HUNTER: I think the thing -- part of what I was trying to get at and it's taken me a little while to muddle it through, but, you know, to me one of the problems with this is that it's so -- it's so fluid as to how much risk that number represents.

So, for instance, if somebody's DTI is 45 percent because of a college loan, well, that's a solid indicator that if they got the degree, that their income potential is going to increase, and so getting them into the housing market is a good risk. On the other hand, if a big chunk of that 45 percent is health care costs and you're having long-term health issues, that's someone whose income is likely to decrease rather than to increase, and so you've got to -- it's maybe more problematic.

So I guess part of my concern is that it's a -- you know, from an underwriting perspective, 45 percent for one household it could be a very, very different risk than 45 percent for another household. It's what is in that 45 percent is the big issue.

MS. SOTELO: Well, I see this recommendation as aligning to the marketplace, so I don't necessarily see it as us reevaluating our own risk and what we will or won't do. It's really aligning to what Fannie and Freddie and other housing nonprofits are already doing, so -- so from that side I guess I'm comfortable. The marketplace is there. And, you know, they're -- they're -- we're using their product anyway. To me I'm comfortable with that.

But I do want to be cautious because the next report -- or I don't know if it's going to be a report, but, you know, we had $75.8 million worth of write-offs for subordinate loans this last year, in December 2013, right? So, we had a real impact, not only on the -- because of the foreclosure stuff, but it was a significant impact. So I don't want to necessarily gloss over the fact that, you know, we have a default rate of -- you know, a low default rate on subordinate loans, but the reality is that the default rate on the senior loans have created a loss of $78.8 million.

MR. GIEBEL: Exactly.

MS. SOTELO: So I mean it's a big deal. So I understand the concern, and I understand wanting to not be too aggressive in terms of that. But if we're aligning to the marketplace and maybe you put some staff on programmatic quality controls, like Jonathan is talking about, in terms of evaluating the types of income or the types of debt that the borrower has, that informs you as to whether it should be 41 or 45 percent.

MR. GIEBEL: We have a process in place that we pull every tenth loan and send it through our quality control department.

MS. SOTELO: Okay.

MR. GIEBEL: And we look at it for our compliance, so that they're 43 now, hopefully 45. So we are looking at every tenth loan.

MS. SOTELO: So that maybe programmatically or statistically we can say it's -- you know, it's up to 45 percent, but from a comfort level, you know, we're still at or underwriting or looking at, at least monitoring, you know, where -- you know, whether we're at 41 or 42.

MS. PATTERSON: So are you asking for approval to have your DTI at 45 for all of your single-family products or --

MR. GIEBEL: Yes.

MS. PATTERSON: And these are all ones in which we are going to use a downpayment assistance program with?

MR. GIEBEL: It would be for the current products, which are the Extra Credit Teachers Program, the Downpayment Assistance Program. It would be for the first mortgage FHA program. It would be for CHDAP.

MS. PATTERSON: So those four single-family programs.

MR. GIEBEL: Yes. And then going forward in May it would be the Energy Efficient and the conventional Fannie Mae product.

CHAIRPERSON JACOBS: Any other questions?

MR. HUNTER: I'll move the adoption of Resolution 14-04.

MS. SOTELO: I'll second it.

MS. OJIMA: Thank you.

Ms. Caballero.

MS. CABALLERO: Aye.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Ms. Patterson.

MS. PATTERSON: Aye.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: Resolution 14-04 has been approved.

MR. GIEBEL: Thank you.

MS. ANGST: Thank you.

CHAIRPERSON JACOBS: Thanks, guys.

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Item 9. Review and discuss initial draft of Agency's two-year Strategic Business Plan for Fiscal

Years 2014/2015-2015/2016.

CHAIRPERSON JACOBS: Let's jump to the business plan. And I guess before you start, if people have any particular issues of concern or items that they think should be in this plan that are not addressed as fully in the plan as you think, speak now. Please speak now.

I guess before you jump in I would like to call attention to the fact that MHSA money is running out or has run out, and we should be trying to get more of this money from the Legislature because it's been a great program, created a lot of housing for those in need, and so that would be one comment I'd like to make before we jump in.

Anyone else before Claudia goes to it?

(Court reporter requests break.)

CHAIRPERSON JACOBS: Oh, yes, let's take a five-minute break. That's a great idea.

(Recess taken.)

CHAIRPERSON JACOBS: Sorry for that long five minutes, but let's jump back to the strategic plan.

MS. CAPPIO: Okay. So I just have a little bit of background to begin. At the last meeting, at the January meeting, we reviewed with you the status of the current strategic plan as a basis for moving forward. And before you today is our latest thinking on the draft for the current fiscal year coming up, the '14/15 plan. And we wanted to get early comments and feedback from you because the process moving forward from here is in May you will get the final draft of the plan, and that is -- as we move through the year, you will consider that for action along with the budget for '14 and '15. So we are definitively in the midst of this. This is by no means a finished product. It's a work in progress, and we would appreciate the comments and feedback from you at this time.

I will note that at the last meeting, Tim gave you an old Chinese adage, "Better to be a dog in peaceful times than a man or a woman in chaotic times." And I will safely note that we are not in peaceful times and therefore don't have the ability or choice to be a dog. I think we are men and women in chaotic times, and the exciting part of that is that we are -- we can safely build ourselves on more stable financial ground, thanks to the excellent work of my staff over the last couple years. And with that, it has its own challenges because we're out of survival mode and into oh-oh, how do we need to remake or reform ourselves to be continuing to be relevant and serving the needs of Californians with affordable housing.

So with that, let the discussion begin.

CHAIRPERSON JACOBS: Does anyone want to call attention to a certain part or ask a few questions?

MR. HUNTER: I just would maybe join in asking Tim to go back to sports metaphors. It was really entertaining to go through the minutes and reread all those gems from Tim.

I just would like to note, particularly in the context of this meeting, I'm the only one still here from the years of disaster. We -- there was a time when this Board was really talking very intensively with the staff about focusing all of our energy on number one. And I just wanted to say overall, it's nice that that's now the smallest piece of the work. But I would just encourage staff and the Board to remember that it's still a critical part of the work in the ongoing effort to increase the stability of the capital structure, which is what is enabling us to finally get back into looking at lending and other activities.

So I just wanted to comment, as I looked at the plan overall, that it was really nice to see the number of areas in which we're looking at new initiatives, given the fact we've managed to successfully address many of the financial problems of the organization.

MS. PATTERSON: No. 7 and No. 12, I think are linked, and I know there are ongoing discussions about

12 and the administration and how that works together and 7, dealing with right sizing of the Agency, basically. And I know when you have resources that are diminished, then your workforce is sometimes diminished accordingly or you have a re-shifting because your focus is restricted, so I would like to maybe have some feedback from Jackie on managing through attrition, some of your organizational strategies to kind of right size and reorganize and that your workforce is matching your resources, et cetera.

MS. CAPPIO: Jackie Riley, Director of Administration.

MS. RILEY: Good morning.

We have already been doing some of that, especially in single family. When lending stopped happening, people were reassigned to loan servicing. And as the portfolio went more into runoff mode with REOs and short sales, people have -- from lending and from loan servicing have gone into portfolio management. So we have provided a lot of training for folks, especially of late. We had a big migration to try and do closeout on some things in portfolio management. So people who were used to doing lending are now doing the other side of the operation and vice versa with loan servicing. So we've done some of that.

We've had a few retirements and determined that we're not filling those positions. We're looking now -- because I'm in active budget mode because at the next Board meeting you'll be getting the Agency's budget, looking at establishing some workload standards in the units where we can -- what's the workload; what's the percentage of, you know, employees that are working on certain things -- and trying to come up with kind of a standard and looking at some of it as it relates to also industry. What are the industry standards? What are our standards? How can we improve through work flow or some other things? So we're actively pursuing that.

MS. SOTELO: Is it possible to have a summary of that or an organizational chart or something that shows that when you come back with the budget to marry that up so we can just understand that a little bit better?

MS. RILEY: Okay.

MS. SOTELO: And then I know the budget is such a long process and it's so hard to do, so I commend you for doing it, but maybe we can send the operational stuff, you know, two weeks before the next meeting or maybe three weeks. That way we can have some time to take a look at it. Two weeks would be fine.

MS. RILEY: Okay. Right now we're running still quite a few vacancies, so I don't know because we haven't gone through our internal little budget hearing process with what our divisions are going to be requesting, but I do believe that some of those vacancies are going to be taken off the budget. We just don't need them at this point.

And budget numbers drive a lot of numbers in state government. You get -- you know, you have expenses based on how many employees you have or the size of your budget. It comes out in the wash three years later, but if we don't need them, we don't need to show them. It's kind of like you don't want to be under your budget, but you don't want to be way over your budget, either.

MS. PATTERSON: Right. So I know at the local government level -- and I'm not sure if this happens at the state level -- you may have the position, but you leave the position unfunded. So you have a full-time FTE, but just you don't fund that position so that you --

MS. RILEY: The way the Agency has done its budgeting is that -- and it's kind of based on state government budgeting. You have something called -- it's called a 7A inside of state government. It lists all of your positions. And so for us, we will show -- if we're not going to fill it, it would stay on there for two years. It will be a zero, zero, and then it goes away.

MS. PATTERSON: Okay.

MS. RILEY: So, yeah, you aren't funding it. It's still there. It was filled this year. We're not anticipating, you know, filling it. It was only filled for .5 or something like that.

MS. PATTERSON: Okay.

MS. RILEY: They would be not -- it would essentially be unfunded. But after that time, the Agency also -- because we come to the Board and request additional positions. I mean back when we needed that, we had the ability to come and request from the Board: We have this program, and we need two more positions that aren't showing up in our budget. So we have the ability to create positions also.

MS. PATTERSON: Oh, okay.

MS. RILEY: So if there's -- I mean, you know, if lending took off and was going gangbusters and we didn't have enough positions and we needed more, we could come to the budget anytime -- I mean come to the Board anytime during --

MS. PATTERSON: And ask for position.

MS. RILEY: -- the year and ask for, you know, that much more money to fund those positions.

MS. PATTERSON: Okay. Well, I'm going to parrot what Dalila was saying, kind of some of the strategies that you're using --

MS. RILEY: Okay.

MS. PATTERSON: -- to deal with the workforce operationally and hear some of the strategies that we employ to make sure that our workforce is aligning with our resources.

MS. RILEY: Okay. And you know we are a civil service organization, so some of it, too, is, you know, really getting our heads and minds around some -- how can I say -- lower performing employees and trying to work on that performance.

MS. PATTERSON: Okay.

MS. RILEY: So they're fully performing and if not, then maybe they don't -- you know, there could be some consequences.

MS. PATTERSON: Okay.

MS. RILEY: So it's kind of all fronts, right at this moment.

MS. PATTERSON: Okay. Thank you.

CHAIRPERSON JACOBS: I've got a question on the Agency integration, you know, with HCD. I'm sort of -- can we get a quick update?

MS. CAPPIO: Sure. It's still in process. We are moving ahead, and I've had internal meetings at

Agency to bring them fully up-to-date. We've had an additional meeting of the Governor's Office, and we have a Governor's Office meeting yet to be scheduled to fill them in on our latest thinking. So it's still very much a work in progress, but we'll keep you posted. I would hope that we would have that resolved sometime in the next couple of months because we really need to move forward in strengthening both HCD and CalHFA. There's vacant positions, exempt positions, open simply because we don't know the final organization, and we would like to get those filled or let those go in an effort to have the strongest executive team we can.

MS. RILEY: And the May budget for the Board will not include any HCD positions or any discussion regarding that. It will just strictly be CalHFA.

MS. SOTELO: So, Matt, I had a general question, just stepping back a little bit on the business plan, and I'm not sure whether -- maybe this exercise was done sometime last year, Claudia, but when I look at a business plan, I look at really what are we trying to achieve, what's the big -- what's the big picture, what are the major milestones that we're trying to hit and are those achievable and realistic goals? I see a lot of strategies and action items, and I appreciate that, and I think that's good. But can you step back for a moment and just kind of give us a bigger picture? Obviously the last two years have all been about risk management and stabilization, but what do you see for the next year, and how do we -- how do we articulate that in your business plan?

MS. CAPPIO: Well, I guess the key -- the three keys for me are to be in the best position we can be at the end of 2015 when the U.S. Treasury unwinds its credit, right, so we are currently in a temporary liquidity buttress or strengthening position because of the U.S. Treasury. They're going to end that. They have indicated there's not going to be an extension to that. And there's going to be -- as much as we would aspire to have that be zero, I think there's likely going to be a little bit left over, and we have to be in the strongest position we can to have the private market take over -- take that over, again, so that we can be financially stable.

Second and third are the -- are our ability to reformulate ourselves for the new market, both in single family and multiple family. The interest rate continues to be depressed, and we have to figure out how to be relevant, strategic and get the money out to people who need it the most in order to meet California's affordable housing needs. We've been thwarted in that the last couple years not only because of the interest rates but also because of our financial position. Now we're at that stable point, and we've got to go forth and figure that out. That's a really wild thing to do. I mean, so much is new and unformed, and we have to find our niches and go for it.

I guess related to that is that we're spending 40 million, plus or minus, on keeping ourselves afloat each year, keeping business operating. We've got to figure out a new series of revenue streams in order to sustain ourselves. It's not going to be the way it was in the first 35 years of this Agency's life. It's not going to be strictly from tax-exempt bonds. It's going to be other revenue streams we have to employ in order to keep ourselves in business because we don't rely on any other source of funding from the State.

And then lastly is what we've been dealing with, the reorg of the Governor. How can we build a platform with HCD to be as efficient and effective as possible on delivering programs and services to the people of this state, again to make sure that we serve the people that we're in business to do?

So that, in a nutshell, is what we've been focused on.

MS. SOTELO: I appreciate that.

MS. PATTERSON: That's a really good kind of overview. I really appreciate that. I would like that -- you listed it as No. 4, but it actually kind of runs through what you're doing with No. 2 and 3.

MS. CAPPIO: Yeah. That's right.

MS. PATTERSON: So I don't want those conversations -- we as government have always worked in kind of silence. And so while you're having the conversation over here about reorg, I don't want them not to be considering your -- what our -- what is CalHFA going forward and what -- how do you deal with your operations separately and apart from. I would like to make sure that those conversations kind of run throughout so that you're all talking the same page and going the same direction, because they're all related. And the whole point, I believe, in the Governor wanting to have a reorg was so that you could get some efficiencies.

MS. CAPPIO: Yeah, absolutely.

MS. PATTERSON: That was the whole reason why. And so when you're talking about what are you in this new market, what are you going to become, how do you sustain yourselves with the $40 million, knowing that you can't -- it's no longer business as usual, and you have this reorg plan that's sitting out there, that was the purpose of the reorg plan. So I would like to make sure that at least the conversations are aligned, and I know under your leadership --

MS. CAPPIO: Well, we are -- I mean there's been some fascinating discussions because we, again, have to maintain our sort of independent authority and be managers of our own ship in order to manage the risk appropriately and yet we are -- we are fulfilling the same mission in a lot of ways, and we have to figure out how to do that in the most collaborative. And in some ways if we can get some consolidation, we will. And there are some keys that, as I've explained before, other than stuff that makes immediate sense, like our leg units are already combined. They're operating. We've had tremendous success with that I think because we're looking at it through different lenses, thus giving the Governor and the Secretary the benefit of both of our perspectives with regard to prospective legislation.

Asset management, 90,000 units between the two agencies, how can we get more efficient in how we manage, inspect, look at the financial risk of some of that -- of some of the pieces of that portfolio, that to me is a tremendous opportunity. So we're beginning to figure that out.

And the multiple family programs is the other key.

MR. PRINCE: So based upon this morning's conversation about certain outcomes with our homeownership efforts, I like 11A, and I just want to stress that one, about really looking at those other outcomes and those other partnerships. We do housing for a purpose and really thinking about how do we measure those outcomes and then thinking about some new collaborations.

I was thinking as people are talking this morning about Scholar House, which is run by the Louisville Housing Authority. They are a Move to Work so they are a little special, but they have a program that targets mothers with children and educations for both. If we could do something like that in California and then have homeownership be at the tail end, I think that that would be a great opportunity. So I like the idea of figuring out those partnerships that might create some new outcomes.

MS. CAPPIO: Yes, this --

MR. PRINCE: And I appreciate everyone who's housed in multi-family in the homeownership are important and them being housed by themselves is really important, but I do believe that I think the taxpayers want to see a little bit more, and so if we can demonstrate that people are doing more, it would be great.

MS. CAPPIO: I -- yeah, I echo that, Preston, simply because we -- I keep saying this: Lending with a purpose. We have to figure that out. In an era of fewer resources, we have to figure out how to use them better and most effectively, so.

And it's -- that's a positive influence that HCD has had on us. It's clear that when you have a stable housing platform, your health outcomes are better, your educational outcomes are better. The more hard analysis and evidence we have of that, the more effectively we'll be able to make our pitch for various programs.

MS. SOTELO: And I think it's important from a Board perspective, at least my Board perspective, is that the business plan lays out your objectives and creates deliverables for the team. And I think that the staff -- I mean the role of the administration is to link those goals and those outcomes to people's performance. So as you're looking at how your team performs and holding accountability throughout the organization, really linking the deliverables that as we the policymaking Board can establish, makes it more transparent, makes it easier to say, well, okay, the goal of the Agency is to, you know, remain relevant and strategic and find its niche, what is the niche? What's the real deliverable in that niche? And then how do we get measured, and how do we perform under that?

So if the goal is to use $250 million of our volume cap for single-family homes, how do we get there, and how do we get there quickly, and how do we perform as a team to get there? So I'd like to see that a little bit in the plan, and when you present it again, along with the budget, maybe make those correlations for us.

MS. CAPPIO: Okay.

MR. HUNTER: I have a very different kind of question. I noticed a couple points where it talked about assessing the ability of CalHFA to become a master servicer, and that confused me a little bit because I thought CalHFA is servicing a part of the portfolio. I mean, is this something different?

MS. CAPPIO: Yes. We are -- we have a robust servicing function currently. The master servicer would be a different category or class of servicer. And if someone could come up briefly and explain -- yeah, Tim, that would be great. I don't want to be in error. I want you to have an accurate representation. It's a -- it's a way -- there are very few master servicers, but we are exploring the possibility of becoming one.

MR. HSU: You're correct, Jonathan, that we are definitely a single-family servicer. The servicing function that we have had traditionally comes from the fact that we were purchasing whole loans from the lenders, like as Tia was saying earlier, that we have a program, there's a lending -- a lender network out there. They make the loans; we buy the loans from them. And then we take these whole loans, and we issue bonds to purchase these whole loans.

The role -- there's no role there for a master servicer. The master servicer's function comes in when you are taking these individual loans, which I refer to as whole loans, and you are making it into a mortgage-backed security, because the master servicer has some responsibilities to someone like Fannie Mae and Ginnie Mae that a servicer does not have.

So, for example, these mortgage-backed securities, part of the reason why investors are buying mortgage-backed securities instead of whole loans is that they're expecting their cash flows on a very routine, scheduled basis. So when you are servicing a mortgage-backed security, it's what's referred to as schedule payments.

So if someone inside a pool -- so as Tony was referring to earlier, so suppose there's $250,000 in a pool, it's four loans, if one of the loans is delinquent, for example, the master servicer actually would come in and make that loan payment on behalf of the delinquent loan and then work with that loan to make the payments current.

It has certainly liquidity risk from that vantage point because it has to front money on a scheduled basis versus actual or actual instead of you're passing through what you actually received. This function has become extremely important as we enter into mortgage-backed securities space because there are not as many players in that space because of all the fallouts from the responsibilities of being a player in that space.

But what we're noticing is that if we were to become a master servicer, it can afford us the kind of flexibilities that Dalila and Tia were talking about in terms of controlling the program, which is something that you guys had asked Tony about as well. Because the master servicers these days, because of their own internal risk controls, are exacting -- exacting and getting their own risk overlays, which makes the programs look like the way they want them to look. We have fewer controls because they are coming in with their risk overlays.

This is a function that's very different. So functionally, this is what it is about, but operationally it's also very different from what we're doing because the master service will get involved with things like delivering loan documents at a very specific deadline on a very specific date. And, frankly, that's not something that we currently are really, really good at doing because when we wire money out, it has to go through the Controller's Office; it has all these things. And then sometimes we can get money out the next day, but that's really kind of not the norm.

Also, there's -- you have to set up a whole department that's -- I think we refer to them as like a delivery department, right, so that kind of delivery function is not one that we have now. But the master servicing could also be a way for us to, if you will, retrofit the servicing functions that we have now into a bigger pipeline, meaning that as our servicing portfolio is sort of declining, if we were to enter into the master servicing space, that would also mean that we would retain the servicing, and then the servicing capacity we built could actually be used in that kind of function.

So it could be good in terms of origination and then be able to control our programs more so that we can do what we want do and also to utilize the capacity we have.

MR. GIEBEL: Jonathan, it would make it what we're doing piecemeal now. So we have a master servicer, U.S. Bank. And then we go to the hedgers, and the hedgers go back. If we did that, it would be seamless from origination through master servicing through hedging and then back, so you have way more control. And master servicers charge you. It's not cheap, but they're doing all the work and taking all the risk, so that's -- ultimately you would look at this as a whole, seamless process on the -- with the TBA model.

CHAIRPERSON JACOBS: I think this is a particularly good idea just because as an Agency, we've been more effective -- when there are troubled loans, we work at getting them stabilized -- than any of the other servicers. So this goes to both the mission of keeping people in their homes, but also ensuring that the bondholders get paid back.

MR. GIEBEL: There is risk involved in it --

CHAIRPERSON JACOBS: Of course there is.

MR. GIEBEL: -- as Tim said, so.

MS. CAPPIO: It's a new notion of labor and delivery, right?

MR. GIEBEL: Yes, it is. It's a whole new ballgame. And typically they are separate units. So the U.S. Bank unit, for example, is in Ohio, and the people we deal with in U.S. Bank are in Chicago. So it's typically a whole separate unit, self-contained unit.

MS. CAPPIO: Dalila, when you were saying what -- how I think what you want is sort of an overlay of how we connect up the business plan with performance measures?

MS. SOTELO: Yes. It's almost the -- the business plan is the articulation of the mission and the vision for the organization, and how does that trickle down to all the departments and how does that trickle down to individuals, right?

MS. CAPPIO: Okay.

MS. SOTELO: And so for me, if you're creating a new market service, right, such as -- such as asset management or, you know, taking all the redevelopment loans or -- you have something in there around that in the business plan. If you're creating a new market, then how does that translate through the department that's going to administer that and then how does that --

MS. CAPPIO: In terms of impact on the

department?

MS. SOTELO: From an operational standpoint --

MS. CAPPIO: Okay.

MS. SOTELO: -- from a cost standpoint, how many new staff people do you need to do that, and then how do you measure whether they're doing their job or not?

MS. CAPPIO: All right.

MS. SOTELO: I think that speaks to Jackie's, you know, comments about the performance and performance standards.

MS. CAPPIO: Okay.

CHAIRPERSON JACOBS: All right, thanks.

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Item 12. Public testimony.

CHAIRPERSON JACOBS: Let's move onto -- actually, before we move onto No. 10, I think we've got a speaker card -- this sort of ties into the next item -- but from Pete Serbantes from HomeStrong USA. And the -- the item he's discussing is how Keep Your Home California has worked from the front lines.

So is Pete -- here he is. Just if you'd come up and just address everyone and sort of explain how things are working on the front lines.

MR. SERBANTES: Just so you know, I'm a Toastmaster, but I'm exerting massive control -- one page.

Good morning, Board of Directors. My name is Pete Serbantes. I am the program director for HomeStrong USA. We are a HUD approved Keep Your Home California program provider as of June 2013. I wanted to let you know that the Keep Your Home California program is working. No, the Keep Your Home California program is not for everyone. Those with true needs that meet the criteria can and have saved their homes.

That being said, I would like to thank you all for the development of this program. How do I know Keep Your Home California is working? Here are some stats that will show how I know. July 1, 2013, through December 31, 2013, HomeStrong USA has completed and -- completed applications and assisted 1,758 families in saving their homes with various Keep Your Home California programs. January 1 through January 31st, HomeStrong USA has completed and assisted 480 families in savings their homes with the various Keep Your Home California programs. I would like to thank those responsible for the management of the program as based on these stats, the program works.

I would further like to state that HomeStrong USA is committed to the Keep Your Home California program and our California homeowners.

And just in, it's so great this modern technology, there's -- the program is such that it can adjust to the needs of California homeowners. There's a new adjustment that just came out this morning that allows for a husband and wife, he's on the title -- let me see. Husband and wife -- it's in essence a reset of the UMA program that allows for more people to save their homes.

I just want to say thank you so much, and I'll give you my number if anybody wants to -- or anybody says it doesn't work. It does work. And I thank you for that. That's all I have to say.

CHAIRPERSON JACOBS: Thank you, Pete.

MR. SERBANTES: Did you have any questions?

Okay, good. Sorry.

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Item 10. Reports: A. Homeownership Loan Portfolio Update

CHAIRPERSON JACOBS: So with that, let's have a discussion of the items 10 through -- Reports 10A and 10B, the homeownership loan portfolio, because we had an update on numbers.

MS. CAPPIO: Yeah, do you -- unless -- these are included as a typical part of the packet, unless you have questions -- unless you want a presentation.

CHAIRPERSON JACOBS: No, I just think based on the last discussion we had on the servicing, I think it is worth a little discussion of just our rates of converting problem loans into stable loans. I think it's very -- I think that's one of the Agency's -- this Agency has done far better than the for-profit banks.

Does anyone have specific numbers for the last -- last period? I mean, it was interesting. We saw a comparison the last time, the last meeting, and we were doing far better.

MS. PATTERSON: Was that during Rhonda's presentation --

CHAIRPERSON JACOBS: Yeah.

MS. PATTERSON: -- where she had taken back a portion of the loans?

MS. CAPPIO: From BofA.

MR. OKIKAWA: So I understand your question to be more about taking back the BofA loans. So I know Tim had worked on this pretty extensively too, but what we did is we boarded -- and I'm trying to remember the actual numbers. We boarded 1500 of those loans, and I think on this report that we have at the back in the homeownership loan portfolio you can see REO, December 31st. That's not exactly current because I looked on those and some of the -- in the page -- on page 206, it talks about Bank of America BAC, where it offers it in two places. It says for CalHFA loan servicing BAC loans -- you're going to make me wear my glasses. So it says here on the CalHFA loan servicing BAC loans, 1,553 loans that were boarded. And then there was another division here, BAC Home Loans Servicing LP for 135.

But since then, those 135 have been taken back in, and boarding being we've taken these 1,500 -- 1,553 loans in our loan servicing, and they're being serviced as all the other loans are being serviced. What's happened now in our portfolio management group, we've developed a system where we have now a single point of contact, SPOCs. And these SPOCs have been dealing with some of these that have been outrageously outstanding, in other words, they haven't been dealt with in three to four years. So we shifted a lot of those into -- straight into foreclosures.

So we're moving these. In terms of dates, in terms of what delinquency dates they are, we're trying to move these through and get the most effective means of processing these. So as it goes into portfolio management and we see these, immediately we have 12 SPOCs, single point of contacts, they make that phone call. And what's really important is that these people have never been talked to before in three or four years.

So the fact that we make this initial contact and try to do some kind of triage as to where these really go, unfortunately the ones that are three to four years, the back payments and everything on those, there's not much you can do on a loan mod.

But when you go through our waterfall, you know, it's -- to how this works, it goes through a waterfall, more or less, and so we're looking at loan modifications and keeping people in their homes.

One of the bigger things that we're proposing here as well, it's in our -- it's in our plan, is about the FHA HAMPs. I think we talked about that last time. And with those FHA HAMPS, currently CalHFA and Guild have been the only two that have been allowed to reduce the interest rates as well as extend the term. We're now offering that out to all our loan servicers, so what that does is it completes their waterfall, because initially right now if they're not qualified under our -- initially if they aren't able to do the interest rate reduction or the extension, then that kind of shuts their waterfall off so they go straight into foreclosure. By adding that and allowing this interest-rate reduction and extension of term, it completes their waterfall so they can go into that as well.

And for us, in terms of the interest rate, interest rates have gone up. We're not looking at that loss that we might have initially looked at, because after six months -- if you do an interest rate reduction, after six months FHA doesn't cover that. And where we're being covered is we're still -- since interest rates are still a little bit higher, we're going to be covered by that sort of protection. So hopefully that's kind of a general -- maybe I'm -- Tia, I'm sorry.

MS. PATTERSON: The foreclosure rate, wasn't that one of the questions you asked, Dalila, last time? Foreclosure rates versus -- it might just be a matter of terminology, but default rate, delinquency rate, foreclosure rate. Of the 1700 loans, or whatever is in our portfolio, what's our foreclosure rate at the, I guess, end of 2013? What percentage of the folks were actually losing their homes? I think that's one of the questions we had.

And then to follow up on that, of these 1700, are these all we're in first position, or is this a mixture of first and either some DPA assistance or we're in something other than first? Our universe is what I'm asking.

MR. HSU: A couple things, Tia. The BofA

transfer, most of the loans transferred on November 1st, and then the second batch transferred on February 1st. In large part, the first batch of the transfers were loans that were not in the middle of some sort of loan modification. And in large part, the second batch were loans that were -- they had kept them back for a couple more months because they were in the middle of working with the borrowers.

The transfer, for now, hasn't helped with the delinquency ratio because as it turns out, after the transfer, despite the notices, many of the payments still went over to BofA so they had to reroute it back to us. So this might not be part of the package, but you can actually -- we do something that we refer to as transition rates analysis. This is something that everybody in the MI industry does. So what it does is it shows new loans that become 30 days delinquent from last month.

If you look at that, and we look at this internally, you'll see that we actually had a couple of spikes after the transfer because these payments went to the wrong directions.

The real benefit from having these loans come in from BofA is that we believe our conversion ratio to tie into KYHC is going to be much higher. We're going to have a greater ability to make sure that all these borrowers are exposed to the benefits of KYHC. So that's one thought -- two thoughts.

So getting to your thought about foreclosure ratio. So what we do is that we -- if there's a lot of interest in this, we can certainly include it in future Board reports. So what we do is that we figure out how many loans have gone into foreclosure in the middle of some year. And then what we do is we take all the loans at the start of the year and all the loans at the end of the year, and we take the average of the two to figure out our foreclosure rate.

So in 2010, our foreclosure rate for conventional loans reached 10 percent. And this past year, in 2013, the conventional loan foreclosure rate was about 2.5 percent. Okay. And for the FHA loans in 2010, similarly we peaked at about 6.4, and now it's about 1.3 or so. So they're significantly lower. And you can certainly see the huge spike around 2010/2011, and it has really fallen off a lot.

Now, to the other question about -- so when we say foreclosure -- so that particular ratio is about foreclosure, okay, only foreclosures. So if they are loans that have gone to short sale, they don't count in our delinquency ratios.

MS. PATTERSON: I'm sorry what?

MR. HSU: Delinquency. So by that we just mean everything that has not gone to foreclosure. It's up. I think I've said this before. So our conventional -- okay, let me start with our -- this is our fixed rate, so our FHA fixed rate only. So we have charts that kind of cut up the loans in different segments, so if you're only looking at FHA fixed rate, that's actually -- right now the total delinquency ratio is 14 percent.

MS. PATTERSON: And that is at the end of 2013?

MR. HSU: That's -- that's right. It's December 2013.

MS. PATTERSON: Okay.

MR. HSU: Okay? And if you were to compare that to the MBA's FHA California fixed rate, we're high. That's only 8 percent. But I think I mentioned previously -- I know I was challenged on this a little bit -- that the MBA ratio, however, does have new vintages. So it includes new loans that were made in 2013, '11, '12, '10, '9, whereas our ratios have the only vintage that we have, which is prior to 2009.

MS. PATTERSON: So comparing those two is like comparing apples to oranges. It's not an apple-to-apple comparison, comparing delinquency rates.

MR. HSU: That's -- yes. I mean, we do have charts that show this, but you're absolutely correct. It's -- it's -- we don't have the benefit of the new originations. So but that vantage point, it doesn't look good.

MS. PATTERSON: So is your FHA -- and I don't -- I'm sorry, I don't have the right chart in front of me -- FHA fixed different than your conventional?

MR. HSU: Yes, so the --

MS. PATTERSON: So the conventional delinquency rate is what?

MR. HSU: It is 1.5 and whereas if you look at the California MBA, that's only 4. But it has -- it suffers from the same issue that the market indices out there. And this is, frankly, an argument we have with the rating agencies too, because if you look at our rating right now, they'll say something like, well, to the degree that your ratios continues to underperform the market ratios, it's hard for us to think about upgrading you.

So we have this argument every year. You are looking at ratios that include these new book years that we don't have. So every year they recognize that issue, and they kind of say, well, that's nice to know, but it's still going to be there.

MS. PATTERSON: Let me see if I can put this in

English so that I can understand it. The market has the ability to continue to make new loans. Because we haven't continued to make new loans at a rate that the market has, our delinquency rate looks higher because they're able to stabilize their delinquency rate because they have the advantage of having new loans coming in?

MR. HSU: That's correct.

MS. PATTERSON: New business.

MR. HSU: So another way to think about it when you relate it to these headlines of Fannie Mae and Freddie Mac now are making noise about breaking away from the federal government because they're making so much money is that they're making money because the new loans they have made in the last three, four years are making oodles of money, right? They're charging higher premiums, and they're not defaulting. That -- that -- that benefit of that book, those book years, which is benefiting the GSEs, for better or worse we have not benefited from that.

MS. PATTERSON: Right. Which is why you're now coming for new strategies to get back lending again.

CHAIRPERSON JACOBS: And beyond that too.

MS. PATTERSON: Tying it all together.

CHAIRPERSON JACOBS: Tia, this goes back to the discussion we had of the private servicers, their motives, and if it goes delinquent and there's insurance, they take the insurance proceeds as quick as you can. Don't worry about keeping the person in the home.

MS. PATTERSON: Exactly. Okay.

MR. HSU: But I mean, if there's a lot of interest, I mean, some of the other things that are worth mentioning sometimes is that probably the reason why we're getting better is some of the things that you guys see in the marketplace, that generally speaking people are seeing a benefit of rising prices in their homes. So as we go into the marketplace and we're dealing with foreclosures and REOs, at the lowest point we were getting -- prior to all the credit enhancements that we have, like the MIs and all these other issues we talked about, prior to all those things coming in, we were getting 45 cents on a dollar back. So if we had a loan that would go into foreclosure and that's a hundred dollar UPB, what we collect back in terms of the principal is 45 cents to the dollar. And now that number is hovering around 70 percent.

MS. PATTERSON: Okay.

MR. HSU: And that's -- that's one segment too. You know, that's conventional foreclosure REOs. It looks a little bit different when you look at FHA. It looks a little bit different when you look at short sales. But that's just one thing too so that you can see that that nadir, that low point, that we reached in about 2011 or so of 45 cents on a dollar, is way behind us.

CHAIRPERSON JACOBS: Any other questions?

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Item 10. Reports: B. Update on Variable Rate Bonds and Interest Rate Swaps.

CHAIRPERSON JACOBS: And we've got one other report. Does anyone have questions about the rate swaps and risk report?

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Item 11. Discussion of other Board matters.

CHAIRPERSON JACOBS: Any other Board matters anyone wants to bring up?

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Item 12. Public testimony.

CHAIRPERSON JACOBS: Any members of the public who wish to speak?

All right. Seeing none, let's adjourn. Thank you, everyone.

(The meeting concluded at 12:30 p.m.)

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REPORTER'S CERTIFICATE

I hereby certify the foregoing proceedings were reported by me at the time and place therein named; that the proceedings were reported by me, a duly certified shorthand reporter and a disinterested person, and was thereafter transcribed into typewriting by computer.

In witness whereof, I have hereunto set my hand this 4th day of April 2014.

Yvonne K. Fenner
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