MOODY'S
INVESTORS SERVICE

Rating Update: Moody's upgrades rating for California Housing Finance Agency's Home Mortgage Revenue Bonds to A3 from Baa2, outlook revised to stable

Global Credit Research - 12 Feb 2015

Approximately $2.335 billion in debt affected

CALIFORNIA HOUSING FINANCE AGENCY - HOME MORTGAGE REVENUE BONDS
State Housing Finance Agencies
CA

NEW YORK, February 12, 2015 --Moody's Investors Service upgraded the long-term underlying rating on California Housing Finance Agency's Home Mortgage Revenue Bonds (HMRB- $2.335 billion outstanding at 6/30/14) to A3 from Baa2. The outlook on the rating is revised to stable from positive. In addition, we have affirmed the Aaa/VMIG 1 enhanced ratings on the HMRB's variable rate demand bonds.

SUMMARY RATING RATIONALE

Today, Moody's Investors Service upgraded the long-term underlying rating of CalHFA's HMRB to A3 from Baa2 and revised the outlook to stable from positive based on the significant improvement in the program's financial performance as demonstrated by an adjusted program asset-to-debt ratio (PADR) of 1.12, a notable decrease in the overall delinquencies for the underlying single family loans, and the ability of the cash flows to completely sustain all stress runs. This program, while not a general obligation of CalHFA, represents the largest standalone program of CalHFA. However, the program has experienced significant runoff since 2008, and there is no expectation of additional issuance under this program.

The A3 rating reflects the program's solid financial performance demonstrated by increased balance sheet strength and profitability, satisfactory loan performance with relatively low single family mortgage loan delinquencies and foreclosures, and improved cash flow projections under all stress runs. The seasoning of the loans further supports the rating and provides cushion in the event of a potential downturn.

OUTLOOK

The outlook is revised from positive to stable based on favorable trends in loan performance, an improving state economy, and strong management which offsets the continued high level of variable rate debt. The outlook also reflects further improvement in the PADR.

WHAT COULD MAKE THE RATING GO UP

Substantial and sustained decline of % of VRDBs which are subject to liquidity expiration or early redemption, through facility replacement/extension or repayment/refinancing of bonds, demonstrating improvement in cash flow projections, combined with:

A continuation of the current trend of improved financial performance, including growth of PADR and profitability

The complex debt structure and high % of variable rate demand bonds (VRDBs) continue to constrain further upward movement of the rating. Significant progress must be made on reducing the amount of VRDBs and/or successfully replacing existing liquidity facilities with new facilities with favorable terms

WHAT COULD MAKE THE RATING GO DOWN

A reversal of the trend in financial performance, including reduced PADR and/or profitability

A decline in mortgage loan performance, through increased delinquencies or foreclosures leading to increasing losses

Increased risk of VRDBs subject to liquidity expiration/early redemption as expiration date for TCLP facilities approaches, pointing to increased stress in cash flow projections

STRENGTHS

Solid financial performance as indicated by an adjusted program asset- to- debt ratio (PADR) of 1.12 and profitability of 3.95% through the recent period of deleveraging

Mortgage insurance mitigates loan losses: FHA insurance on 28% of loans, Genworth Mortgage Insurance Corporation reinsurance on 33% of loans (GMICO, Ba1, positive)

Satisfactory loan asset performance due to decreases in loan delinquencies/foreclosures to 4% (as of December 31, 2014) and reduced losses on foreclosed loans

Federal resources, including external liquidity support for variable rate bonds and funds for mortgage loss relief, bolster HMRB performance

CalHFA (Long term issuer rating A3/positive) support as net swap payments are paid by the Agency subject to reimbursement by HMRB

Strong management actions continue to improve program performance

CHALLENGES

External liquidity facilities on VRDBs through TCLP scheduled to expire on 12/23/15; if not extended or replaced, will result in higher interest rates on the bonds and accelerated repayment of bonds by 12/23/22, reducing the program's financial performance

GMICO reinsurance policies became subject to rollover on the 10th anniversary of each vintage (subject to reimbursement of accumulated reserves) reducing benefit of mortgage insurance

Unhedged portion of variable rate debt causes stress in rising interest rate cash flow scenarios

RECENT DEVELOPMENTS: Recent developments are incorporated in the Detailed Rating Rationale.

DETAILED RATING RATIONALE

LOAN PORTFOLIO: Portfolio Performance Improves as Delinquencies Decline

Improvements in performance of the mortgage loan portfolio (15,967 loans at 6/30/14) are particularly significant to HMRB because the HMRB bonds are limited obligations of the Agency secured by the mortgages and other assets pledged under the bond indenture. Serious delinquencies (loans 90+ days delinquent plus loans in foreclosure) continued to show significant improvement, declining from 6.16% at 12/31/13 to 4.95% at 12/31/14, pointing to reduced levels of losses from missed payments and foreclosure. Improvements in California housing market are reflected in smaller losses to CalHFA on sales of REOs.

Delinquency levels, although much improved, remain slightly elevated compared to California state-wide benchmarks. Mortgage Banker's Association Q3'14 seriously delinquency levels for all loans in California was 2.57% (3.53% for FHA fixed rate loans). Thus we expect continued losses going forward, albeit at reduced levels.

Mortgage insurance continues to mitigate losses. At 6/30/14, 28% of HMRB loans have FHA insurance, which significantly reduces any exposure to the program. An additional 33% of the loans benefit from private mortgage insurance that continues to be reinsured by Genworth Mortgage Insurance Corporation (GMICO). However, the GMICO policies expire on the 10th anniversary of each covered vintage, and CalHFA has opted not to renew for the 2003, 2004 and 2005 vintages. The portfolio also contains 26% of uninsured loans with loan-to-values (LTVs) below 80% and 9.5% uninsured loans with LTVs above 80%.

Proactive improvements to single family asset management by CalHFA have contributed to improved performance. Federal funds paid to CalHFA from the Hardest Hit Fund (HHF) through December 31, 2014 total$36 million.

FINANCIAL POSITION AND PERFORMANCE: Growth in Financial Performance Realized for FY 2014

Increases in overcollateralization and stable profitability are important factors in the rating upgrade. Although HMRB's fund balance has declined since 6/30/09, reflecting losses absorbed from mortgage loan delinquencies and foreclosures, the program has demonstrated strengthening overcollateralization through the period of deleveraging. The adjusted asset to debt ratio (PADR), a key metric in our comparative assessment of single family programs, increased from 1.088 at 6/30/13 to 1.12 at 6/30/14.

Profitability as shown in the financial statements remains elevated because the Agency accounts for payments on the interest swaps hedging HMRB debt from its Operating Account, and then reimburses the Operating Account from HMRB. Adjusted to cover the swap payments, HMRB's adjusted profitability (net revenues as a % of total revenue) for FY14 was approximately 4%, a decrease from 6.03% in FY13.

Liquidity: Cash flow projections demonstrate that the program exhibits sufficient liquidity to meet all debt service obligations.

LEGAL FRAMEWORK, COVENANTS AND DEBT STRUCTURE: Stress From Variable Rate Debt is Significant But Reduced

Debt Structure: The total outstanding debt for HMRB as of June 30, 2014 is $2,335,370,000 of which $1,084,270,000 is fixed rate, and $1,251,100,000 is variable rate.

Debt-Related Derivatives:

HMRB's high level of variable rate debt is a source of potential stress primarily from potential expiration of external liquidity facilities and from interest rate risk. 53.58% of HMRB bonds (as of 6/30/14) were variable rate (including 31.89% VRDBs and 21.69% with no tender option). All of the VRDBs ($744.670 million of bonds) benefit from credit and liquidity facilities under the federal TCLP program which currently expire on 12/23/15. If the facilities are not renewed or replaced by that date, remaining VRDBs will become bank bonds bearing interest at elevated rates, and must be repaid in full by 12/23/22, which will strain HMRB's cash flows.

Approximately 82% of the variable rate bonds are hedged with interest rate swaps, exposing the unhedged 18% portion to increased costs if interest rates begin to rise. Swap payments are a general obligation of CalHFA and are made from the Agency's general fund, subject to the practice of reimbursing the payments from HMRB. The Agency pledge insulates HMRB from collateral posting and counterparty exposure.

We incorporate these risks into our analysis by reviewing cash flow projections that include combinations of low rate and rising-interest rate scenarios as well as high and low prepayment speeds. Additional stress scenarios combine loan losses with full repayment of bank bonds by the end of 2022. Loan losses were $160 million (7.2% of principal), although we expect our modeled losses to be lower going forward due to improving loan performance. The cash flows were able to sustain all stress scenarios including high interest rates, loan losses and full bank bond repayment with no shortfalls.

Pensions and OPEB: Pensions and OPEB are not a major factor in the methodology.

MANAGEMENT AND GOVERNANCE: Management Actions Improve Program Performance

Since 2008, CalHFA's management has taken effective steps to improve the Agency's finances and demonstrated management focus on reducing financial stress. The Agency has substantially enhanced its single family asset management function and reduced timelines for moving defaulted loans through the pipeline. This trend has continued, with the Agency focusing on purchasing servicing rights from certain servicers to improve overall performance.

The Agency has also worked proactively to improve the Agency's balance sheet to address the combined effect of the mortgage decline and the financial crisis. Actions have included mortgage loan sales, bond purchases at a discount, refinancing of multifamily projects to reduce risk to the Agency, negotiation of more favorable terms for swap collateral posting, refunding to reduce variable rate debt, and exercise of par swap termination options to reduce exposure. The Agency has also reopened its mortgage origination business through loan sales in the secondary market.

KEY STATISTICS:

--Total Bonds Outstanding (as of June 30, 2014): $2,335,370,000

--Asset-to-Debt Ratio (as of June 30, 2014): 1.12

--Net Revenue as % of Total Revenue: 3.95%

--Delinquent Loans 4.95% as of 12/31/14 (single family 90 days+ and loans in foreclosure)

--Variable rate debt as % of bonds outstanding: 54%

--Swapped debt as % of variable rate debt: 82%

OBLIGOR PROFILE

HMRB was CalHFA's single family mortgage finance program from 1982 to 2008 and remains CalHFA's largest obligation by volume (bonds outstanding: $2.335 billion HMRB, $3.6 billion for CalHFA total). HMRB's performance represents a key driver of CalHFA's overall performance. Bond proceeds were used to finance single family mortgages for low and moderate income households in the State of California. All of the bonds under the Indenture are secured equally and ratably by all of the mortgage loans.

HMRB is not a general obligation of CalHFA; however, CalHFA is responsible for payments on interest rate hedges, with reimbursement by HMRB.

LEGAL SECURITY

The bonds are special limited obligations of the Agency, payable solely from the revenues, reserves, assets and properties pledged under the Indenture, including the single family mortgage loans financed under the Indenture and certain reserve accounts. All of the mortgage loans and other assets are pledged to secure all of the bonds, equally and ratably. The bonds are not back by the State of California.

USE OF PROCEEDS: Not applicable.

PRINCIPAL METHODOLOGY

The principal methodology used in the long-term rating was U.S. Housing Finance Agency Single Family Programs published in February 2013. The additional methodology used in the short-term rating was Variable Rate Instruments Supported by Conditional Liquidity Facilities published in May 2013. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

Analysts

Eileen Hawes
Lead Analyst
Public Finance Group
Moody's Investors Service

Ferdinand S. Perrault

Backup Analyst
Public Finance Group
Moody's Investors Service

Florence Zeman
Additional Contact
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
USA