MOODY'S
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Rating Update: Moody's affirms A3 rating for California Housing Finance Agency's issuer rating and Housing Program Bonds; outlook revised to positive

Global Credit Research - 12 Feb 2015

Approximately $40.390 million in debt affected

CALIFORNIA HOUSING FINANCE AGENCY - ISSUER LONG TERM RATING
State Housing Finance Agencies
CA

NEW YORK, February 12, 2015 --Moody's Investors Service has affirmed the A3 ratings on California Housing Finance Agency's issuer rating and the Housing Program Bonds (HPB - $40.390 million outstanding). The outlook on the issuer and HPB ratings is revised to positive from stable. This action does not affect enhanced ratings on any of the Agency's variable rate demand bonds. No other ratings of the Agency are affected by this action, including the rating on the Multifamily Housing Revenue Bonds III.

SUMMARY RATINGS RATIONALE

Our affirmation of the issuer rating and the Housing Program Bonds, and the change in outlook from stable to positive, is based on the continued improvement in financial performance, improved quality of single family assets and strength of multifamily assets, enhanced performance in stress cash flows and subsiding pressure from variable rate debt and interest rate hedges.

OUTLOOK

The outlook on the Agency's issuer rating and the rating of the Housing Program Bonds is changed from stable to positive based on improved financial performance, three years of profitability and a decreasing risk profile. The positive outlook also reflects the diversity of the Agency's programs and the increase in the Agency's program asset-to-debt ratio to 1.35 in FY 2014 from 1.26 in FY 2013.

WHAT COULD MAKE THE RATING GO UP

Meaningful and sustained reductions in variable rate exposure to mitigate risks associated with expiration of external TCLP liquidity facilities, combined with:

Improved financial performance-- rising asset to debt ratios and improving profitability

Improved liquidity position, with lower potential stress from collateral posting on interest rate swaps

Evidence of a successful return of the single family and multifamily lending programs

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

No material increase in the Agency's risk profile

WHAT COULD MAKE THE RATING GO DOWN

Reversal of trends in financial performance, including lower asset to debt ratios and/or diminished profitability

Higher than anticipated losses from single family loans or decreases in performance of multifamily loans

Weakened liquidity position through collateral posting on interest rate swaps and/or variable rate debt repayment

Weaker performance in cash flows due to expiration of external liquidity facilities

STRENGTHS

Strong financial performance, including increased program asset to debt ratio of 1.35 and a rebound in profitability

Asset quality: satisfactory single family loan performance, and continued strong performance of multifamily projects

Federal resources, including external liquidity facilities for variable rate bonds, low-cost financing for bond debt and funds for mortgage relief, have helped to diminish key risks

Management has demonstrated ability to be proactive in addressing financial risks

CHALLENGES

High levels of variable rate debt bring interest rate risk and potential cash flow stress due to expiration of external liquidity facilities (provided by federal TCLP program) at the end of 2015

Swap collateral posting poses potential stresses on liquidity, although the severity is diminishing

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

DETAILED RATING RATIONALE

LOAN PORTFOLIO: Portfolio Performance Improves as Single Family Delinquencies Decline

CalHFA maintains a large loan portfolio, primarily comprised of single family mortgage loans. The Agency's largest program is the Home Mortgage Revenue Bonds (HMRB) with $2.335 billion in bonds outstanding and 15,967 loans as of 6/30/14. 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, Ba1 positive). 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%. Serious delinquencies (loans 90+ days delinquent plus loans in foreclosure) for HMRB 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.

The Agency also has 2 other single family programs: Residential Mortgage Revenue Bonds MBS (RMRB MBS) and the Residential Mortgage Revenue Bonds 2009 A-5 (RMRB 2009 A-5). RMRB MBS (Aaa/stable) has approximately $175 million outstanding; the security is provided by GNMA mortgage backed securities. RMRB 2009 A-5 (A2/positive) has approximately $327 million outstanding. The single family loans are backed by insurance from FHA (38%), mortgage backed securities (9%), private mortgage insurance (PMI) (18%) and 35% are uninsured but have loan to value ratios below 80%. The PMI loans benefit from reinsurance provided by Genworth Mortgage Insurance Corporation (GMICO, Ba1/positive).

The improved performance of single family loans benefits the Agency as a whole, as the single family lending has been the Agency's largest activity and is a key driver of profitability and fund balances.

In addition, the Agency's portfolio of approximately 475 multifamily mortgage loans continues to demonstrate strong performance and is a source of credit strength. Agency data demonstrates project occupancy averaging 96-98%, and portfolio average debt service coverage is approximately 1.51x. Delinquencies have been minimal. The multifamily bond programs provided 14% of the Agency's operating revenues in FY14 and were highly profitable, with total net revenues of 31% of total revenues.

FINANCIAL POSITION AND PERFORMANCE: Growth in Asset to Debt Ratio Realized for FY 2014

Despite several years of severe stress from the combined effects of single family mortgage losses and high levels of variable rate debt, CalHFA's balance sheet has remained stable, and profitability has rebounded. Assets and liabilities have declined significantly since 2008 as the Agency has reduced new single family lending activity. However, the adjusted combined fund balance was $1.029 billion at 6/30/14, stable from $1.017 billion at 6/30/13, with the ratio of assets to debt increasing from 1.262 to 1.355. Total net revenues as a % of total revenues declined to 9.8% at 6/30/14 from 12.06% at 6/30/13.

Improved performance of HMRB is a factor in our assessment of the Agency's issuer rating. Although the HMRB Bonds are not a general obligation of CalHFA, HMRB is CalHFA's largest activity by volume (accounting for $2.335 billion of the Agency's total bonds outstanding of $3.6 billion) and thus is a key driver of the Agency's fund balances and profitability. The practice of reimbursing swap payments from HMRB to the Operating Account provides another key linkage; if HMRB's net revenues declined, decreased swap reimbursements could impact general fund liquidity.

Liquidity: Cash flow projections on all of the Agency's programs demonstrate that the program exhibits sufficient liquidity to meet all debt service obligations.

RISK PROFILE: Risk Profile Improves as Variable Rate Debt Decreases

CalHFA is highly sensitive to a variety of risks including rollover and counterparty risk as a result of its variable rate debt profile. Variable rate debt accounts for 42% of CalHFA's outstanding debt as of 6/30/14 (25% are variable rate demand bonds, and 17% are variable rate bonds with no tender), all concentrated in HMRB and in the Multifamily III (MF III) program. Ninety percent of CalHFA's variable rate demand bonds benefit from liquidity and credit support provided by the GSEs (Fannie Mae and Freddie Mac) backed by the US Treasury (TCLP).

The TCLP facilities expire at the end of 2015. If the facilities expire and CalHFA has not replaced the facilities or redeemed/refinanced the VRDBs, the bonds will be subject to mandatory tender and become bank bonds at elevated interest rates and must be repaid by 12/23/22 (no term-out before that date).

Debt Structure: The total outstanding debt for CalHFA as of June 30, 2014 is $3,590,525,000, of which $2,082,215,000 is fixed rate, and $1,508,310,000 is variable rate.

Debt-Related Derivatives:

CalHFA's large portfolio of interest rate swaps poses potential liquidity challenges. Approximately 100% of CalHFA's variable rate bonds are hedged with interest rate swaps, used as hedges for HMRB and MFIII Bonds. The swaps are diversified among 11 counterparties.

The Agency has steadily reduced its swap exposure by exercising par termination options purchased at swap inception; the notional amount of swaps has declined from $3.43 billion at 6/30/10 to $1.44 billion at 12/31/14.

Cash Flow Projections Demonstrate Ability to Withstand Stresses

Moody's has reviewed cash flow projections for both single family and multifamily programs, demonstrating the ability of all indentures to withstand stresses in line with the rating assigned. The cash flows, prepared in accordance with Moody's methodology, include high (3-year average life) and low (30%) prepayment speeds in both high and low interest rate environments as well as Bank Bond scenarios.

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

MANAGEMENT AND OPERATING ENVIRONMENT: Management Actions Improve 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.

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 reopened its mortgage origination business through loan sales to the secondary market and increased focus on multifamily loans.

Federal Programs Have Provided Important Support

CalHFA has fully utilized the federal government programs established in 2009-10 to assist HFAs in addressing the mortgage crisis. CalHFA used substantially all of its allocation under the NIBP program, under which the US Treasury provided funds to purchase bonds from HFAs at favorable rates, as a key source of refinancing, which has served to reduce VRDB exposure. The TCLP program provides liquidity support for 90% of the Agency's VRDBs on terms more favorable than those that would likely be available to the Agency from private sector providers. The Hardest Hit Funds are contributing to single family loss mitigation.

HOUSING PROGRAM BONDS RATING AFFIRMED BASED ON THE ISSUER RATING

We are also affirming the rating on the Housing Program Bonds at A3 based on the Agency's general obligation. The assets of the HPB program include a mix of strong multifamily projects and single family downpayment assistance loans; the multifamily loans generate cash flow to support the uncertain repayment schedule of the down payment assistance loans. Performance of the HPB indenture improved significantly in FY13 after a bond redemption which redeemed all remaining variable rate debt. The adjusted asset to debt ratio has increased to 1.66 in FY 14.

KEY STATISTICS:

--Total bonds outstanding: $3,590,525,000 (as of 6/30/14)

--Asset-to-Debt Ratio: 1.355x

--Profitability: (net operating revenue s a percent of total revenue): 9.79%

--Net loans receivable: $3,814,611,000 (as of 6/30/14)

OBLIGOR PROFILE

CalHFA is an agency of the State of California, created in 1975. The Agency is governed by a Board of Directors with 11 voting members. The Agency shares certain functions with the State's housing department, but has independent authority as to its bonds and housing loan programs.

The Agency's primary activities are the financing of single family mortgage loans to low and moderate income borrowers and the financing of loans to developers of affordable apartment developments. The Agency also administers certain programs separately funded by the State.

USE OF PROCEEDS: Not applicable.

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was U.S. Housing Finance Agency Issuer Rating Methodology published in May 2014. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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.

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