Iowa Finance Authority; General Obligation

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Credit Profile		
Iowa Fin Auth ICR		
Long Term Rating	AA+/Stable	Upgraded
Iowa Fin Auth var rate multifam hsg		
Long Term Rating	AA+/A-1/Stable	Upgraded
Iowa Fin Auth GO		
Long Term Rating	AA+/Stable	Upgraded
Iowa Fin Auth GO		
Long Term Rating	AA+/A-1/Stable	Upgraded
Iowa Fin Auth GO		
Long Term Rating	AA+/Stable	Upgraded

Rationale

S&P Global Ratings raised its issuer credit rating (ICR) on the Iowa Finance Authority (IFA or the authority) to 'AA+' from 'AA'. At the same time, S&P Global Ratings also raised its long-term rating on the authority's Multifamily Housing Bond Resolution debt to 'AA+' from 'AA' and its dual rating on the debt to 'AA+/A-1' from 'AA/A-1'.The outlook is stable.

The rating reflects our opinion of the authority's following strengths:

- Total equity over total assets of 36.66%, a seven-percentage-point increase over the past five years, that is well in line with 'AA+' rated peers and demonstrates increasing solid performance and sufficient financial resources available to support the authority's GO pledge;
- High-quality and low-risk asset base consisting primarily of 'AA+' rated mortgage-backed securities (MBS), coupled with very low whole loan delinquencies;
- Efficient operations, as demonstrated by a five-year average return on average assets of 1.04%, indicating the organization's financial acumen and ability to generate sufficient revenues to continue operations; and
- A track record of strong senior management, that has continued to strategically plan and implement growth through well-embedded, formalized practices and policies amid top leadership changes.

Partially offsetting these strengths, in our view, is the authority's net income, which declined in 2018 after increasing in 2017. While IFA's profitability metrics have shown signs of volatility due to changes in net grant income, interest income from program assets, loans, and MBS, as well as interest income on investments increased 5.92% in 2018 after falling for two consecutive years.

IFA has demonstrated solid financial strength, the ability to implement strategic objectives, and continued net equity growth over the past five years. The authority increased its asset base for two consecutive fiscal years by shifting some of its single-family loan originations from the to-be-announced market to bond financing. In 2018, IFA issued two new bond series totaling $111.06 million to purchase MBS and to refund prior bonds. This led to a 13.8%, or $69.46 million, increase in low-risk, high-quality program assets, consisting of securitized MBS with enhancement from Fannie Mae, Freddie Mac, or Ginnie Mae. IFA's capital-adequacy ratios reflect a low-risk profile consistent with its current rating and solidly in line with those of other 'AA+' rated housing finance agencies (HFAs).

Outlook

The stable outlook reflects our view of the stable quality of IFA's overall financial position given its high-quality portfolio, which is mostly composed of MBS. The outlook also reflects our view of IFA's management and its strategy of increasing high-quality assets on its balance sheet. S&P Global Ratings believes IFA's continued low-risk asset base and high capital-adequacy ratios create solid credit stability. Through our peer analysis, we assess an organization's equity ratios in both absolute terms and relative to other rated HFAs. IFA's equity levels are very strong when compared with other 'AA+' rated peers, despite volatile profitability related to governmental grant income.

Upside scenario

Should IFA's key ratios outperform those of its 'AA+' rated peers, combined with stable profitability, we could revise the outlook or raise the rating. We would view continued improvement in equity along with continued strong asset quality and liquidity levels as positive factors.

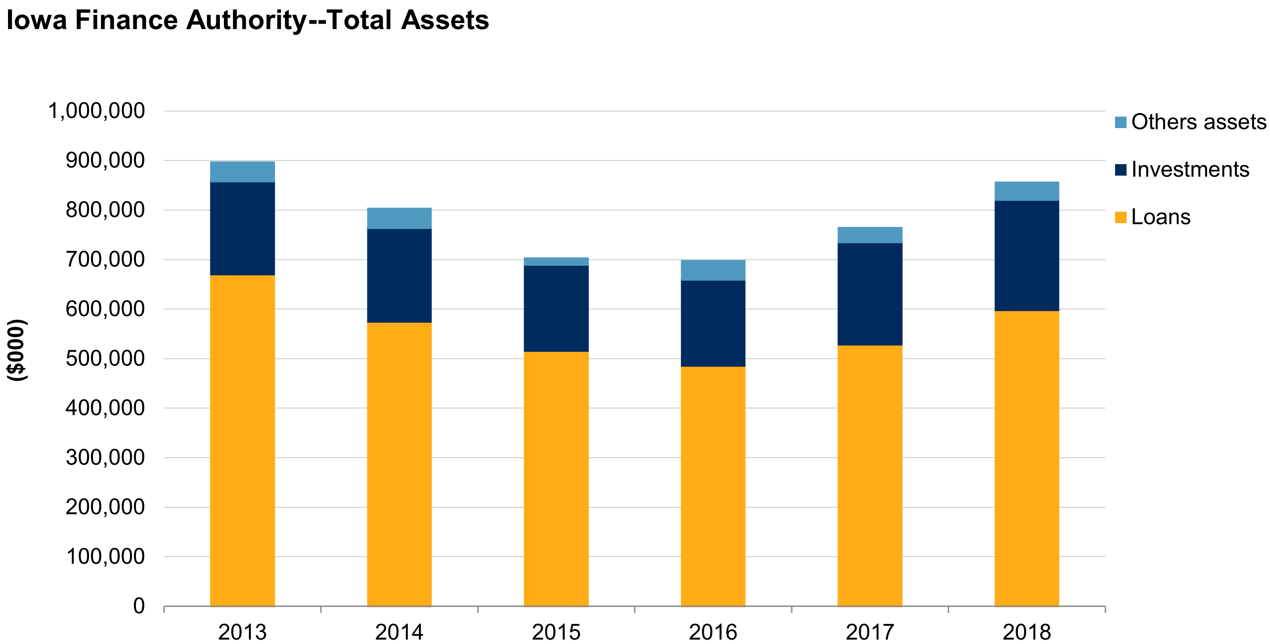
Downside scenario

Although we view it as unlikely during the outlook period, if net income becomes more volatile, financial ratios deteriorate, or the authority's asset and debt profiles become higher-risk due to a material increase in variable-rate debt or increased non-performing assets (NPAs), we could revise the outlook or lower the rating.

Asset Quality

IFA's total assets grew by 11.81 %, or $91.1 million, in fiscal 2018, after steadily decreasing from 2011-2016. The authority originated more single-family loans in fiscal 2017 (2,300) than in any year since 2008. In 2018, IFA originated slightly less, totaling 2,058 loans. Total cash, cash equivalents, and investments grew by 13.9%, or $25.4 million; and total MBS increased 17.9%, or almost $73 million, in 2018. The assets and other financial information S&P Global Ratings used for this analysis exclude the state revolving fund that IFA administers as well as any conduit bond issues, which have no recourse to the authority.

Chart 1



Source: S&P Global Ratings; Iowa Finance Authority.

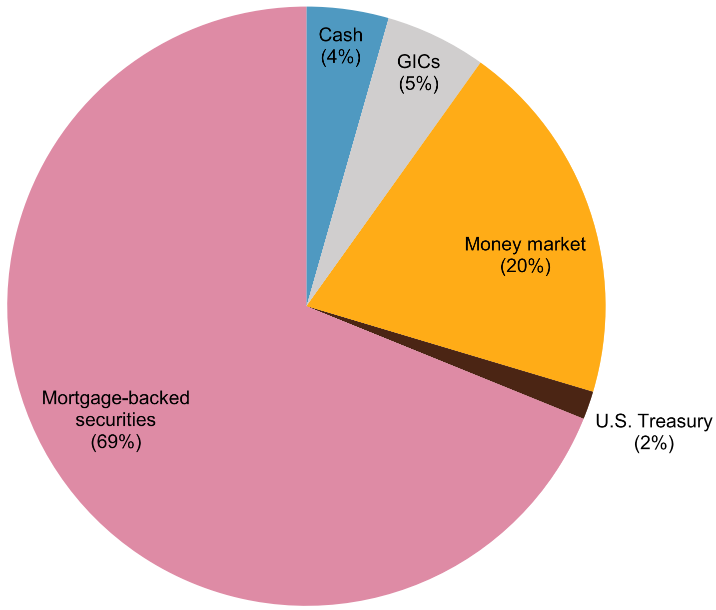
As of June 30, 2018, IFA's loan portfolio consisted of Ginnie Mae, Fannie Mae, and Freddie Mac MBS (80%), as well as multi- and single-family mortgage loans (20%). The proportion of MBS remains high in comparison with most HFAs. Approximately 69% of the authority's asset portfolio consists of 'AA+' rated MBS. We view increased MBS as a positive asset factor due to high credit quality.

We believe that IFA's loan portfolio poses an extremely low risk, due to the authority's conservative approach to collateral: 80% of its loans are backed by Ginnie Mae, Fannie Mae, and Freddie Mac MBS. As MBS guarantees payment on the underlying loans, no reserves are required. However, for the remaining loans, IFA has sufficient equity to cover credit losses. In our opinion, these loans are performing well and have sufficient excess assets to cover any potential credit shortfall or liquidity issues.

Reported delinquencies (NPAs) as of June 30, 2018 were $10.72 million, or a very low 1.79% of total loans and MBS. This fell from a 2017 high of 2.11%. While this ratio has increased from a 2014 low of 0.45%, it is important to note it results from IFA adopting a more conservative practice of including impaired loans in this calculation.

Chart 2

Iowa Finance Authority -- Investment Portfolio As Of Fiscal 2018



Source: Iowa Finance Authority.

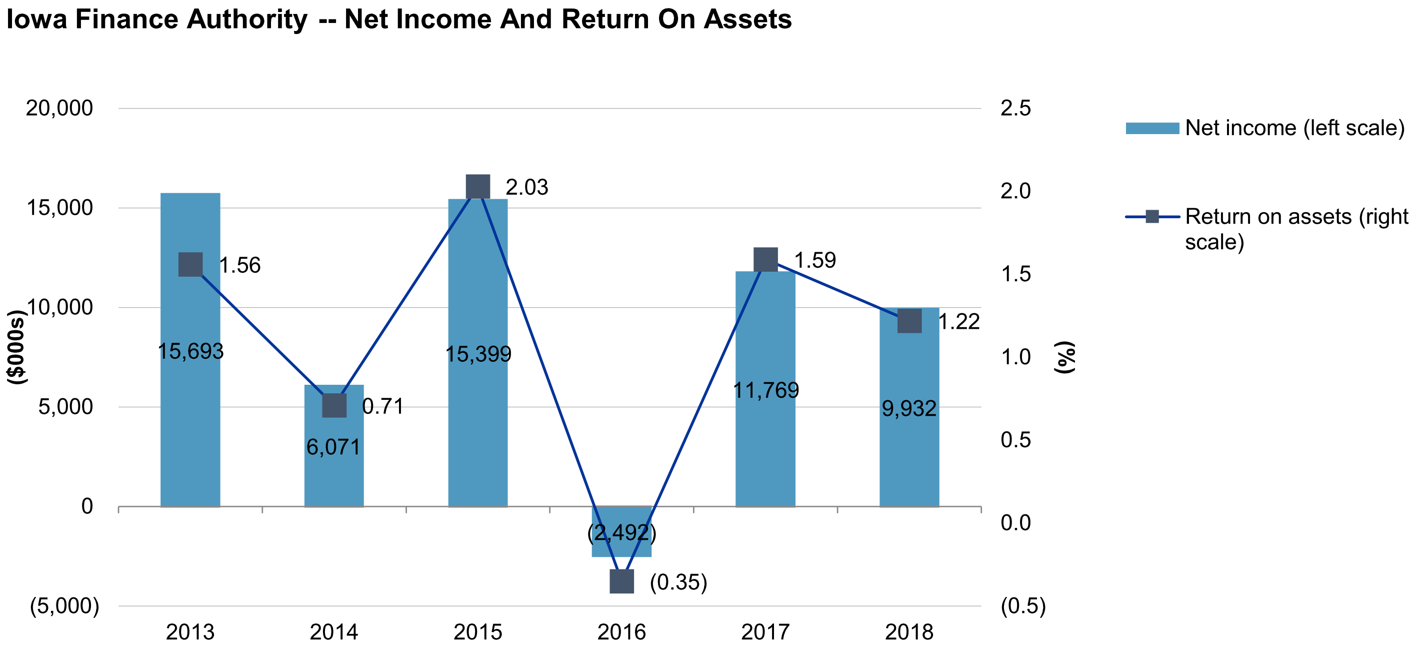
Investments

IFA's investments, in our view, are of high credit quality and provide sufficient liquidity. Management takes what we consider a conservative approach to the oversight and monitoring of the authority's investments. IFA's non-MBS investments and cash or cash equivalents total $219.6 million, primarily composed of short-term cash or cash equivalents, including highly rated money market funds. Its longer-term investment portfolio contains 99% government or agency securities. IFA's investments provided 3.88% of total revenues in 2018, a 1% uptick from 2016.

Earnings Quality And Financial Strength

The authority's total revenues stood at $125.04 million in 2018, down 3.0% from 2017 on the heels of a 70% jump in 2016. Income from loans and MBS increased 5.9% ($1.18 million) from 2017 after a steady decline over the past six years. The growth in income from loans and MBS is due to an increase in MBS being held on the balance sheet. Much of the authority's revenue within the past three years stems from a significant increase in grant income to $85.1 million and $81.5 million in 2017 and 2018, respectively. This is more than offset by an accompanying increase in grant-related expenses during the same time. The authority's net income was $9.9 million in 2018, a 15.6% decline from 2017 after a 2016 drop into negative territory. The volatility of the authority's net income reflects lower grant funding and timing differences between grant income and grant expense.

Chart 3



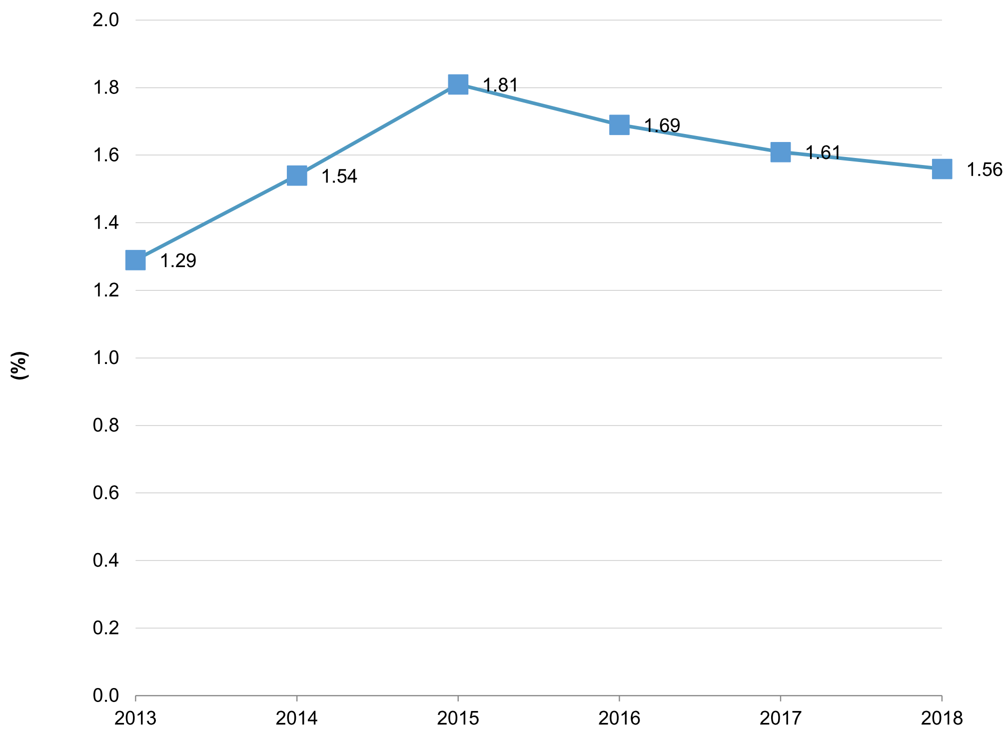
Source: S&P Global Ratings; Iowa Finance Authority.

Profitability

IFA's profitability measured by return on assets was 1.22% in 2018, with a five-year average of 1.04%. Net interest margin declined slightly to 1.56% in 2018 from 1.61% in 2017, yet still contributed to a general upward trend in earnings from 0.78% in fiscal 2011. Although profitability is volatile due to grant income funding and timing differences between grant income and grant expense, we do not view the volatility as a significant risk. As detailed in table 2, the five-year average of the authority's profitability ratios are in line with 'AA+'- or higher-rated HFAs despite reporting negative net income during 2016. We will monitor the trend in grant income for any significant changes during the two-year outlook period.

Chart 4

Iowa Finance Authority -- Net Interest Margin



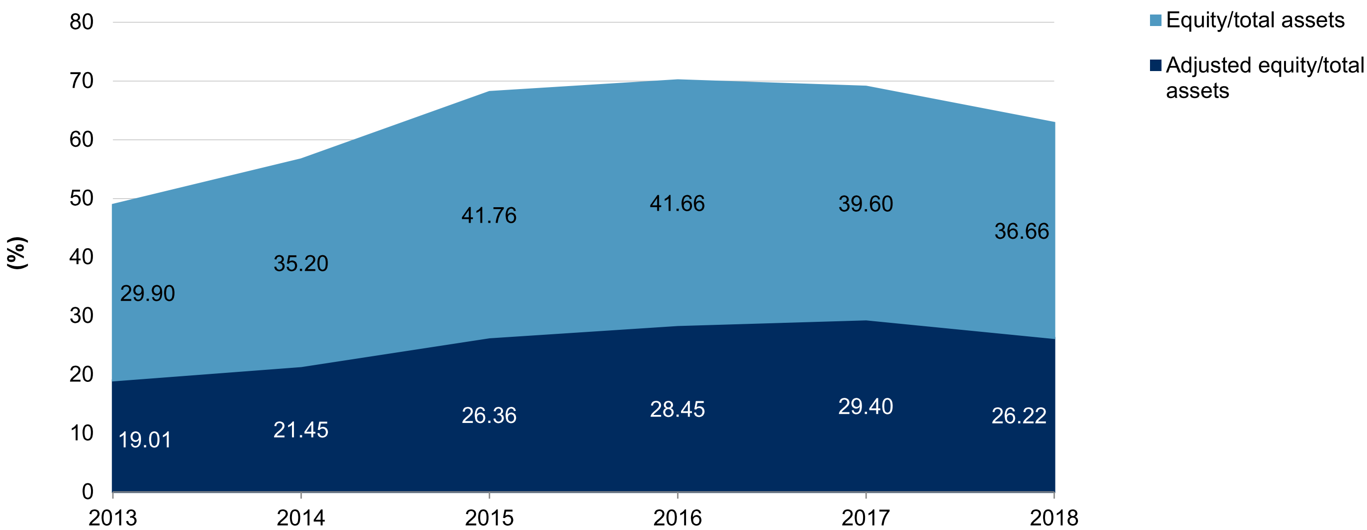
Source: S&P Global Ratings; Iowa Finance Authority.

Equity

Equity was 36.66% of assets in 2018, down for the third year in a row, from 39.60% in 2017, 41.92% in 2016, and 42.46% in 2015, reversing what had been a positive trend from 31% in 2013. IFA's five-year average equity-to-asset ratio of 38.98% remains stronger than those of many 'AA+' rated HFAs. In our view, the decline in the authority's equity base is low-risk since the majority of assets being held are high-quality MBS.

Chart 5

Iowa Finance Authority -- Equity/Total Assets Versus Adjusted Equity/Total Assets



Source: S&P Global Ratings; Iowa Finance Authority.

Debt

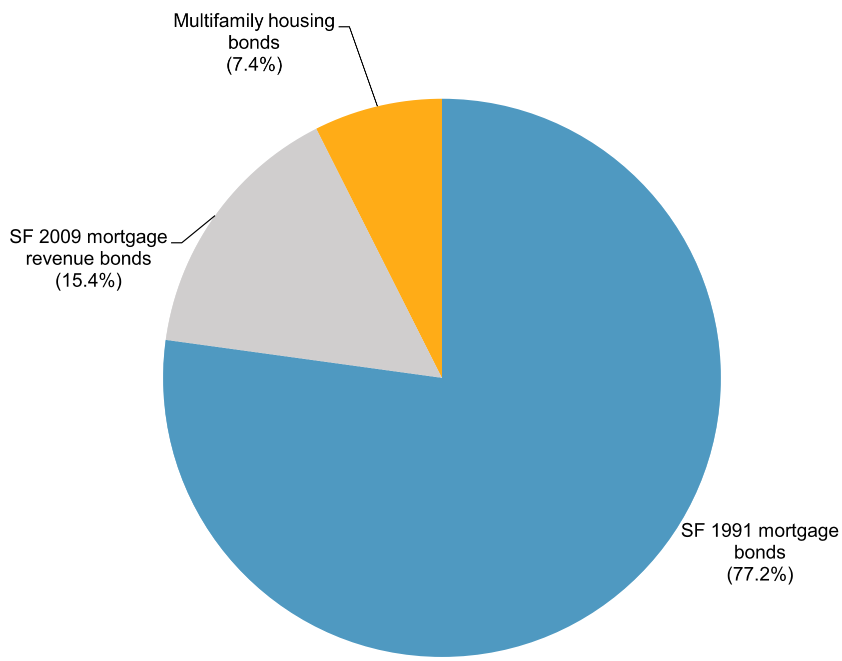
As of June 30, 2018, IFA's debt outstanding totaled $513.255 million, turning around what had been a steady decrease from 2010-2016. Debt increased $81.3 million, or 18.8%, from the preceding year. The authority had $475 million of single-family bonds (92.5%) and $38 million of multifamily GO bonds (7.4%) outstanding.

The authority has single-family bonds outstanding under two master indentures. The Single-Family Mortgage Bond Resolution was adopted in 1991 and is rated 'AAA', reflecting our opinion of the extremely high quality of IFA's pledged collateral, which consists of Ginnie Mae, Fannie Mae, and Freddie Mac MBS; the strong credit quality of investments; and cash-flow sufficiency. The 1991 indenture accounts for 83% of the authority's total single-family bonds outstanding and 77% of total housing authority debt. The remaining single-family bonds are issued under the Single-Family Mortgage Revenue Bond Resolution adopted in 2009 and are also backed by MBS. The authority has issued multifamily GO bonds under two master indentures, which were adopted in 1978 and 2005.

IFA has continued to take action to mitigate the effects of variable-rate counterparty exposure. At the end of June 2018, $122.73 million, or 23.9%, of IFA's total debt outstanding was issued at variable interest rates, with liquidity provided by Federal Home Loan Bank Des Moines (AA+/Stable/A-1+) and Wells Fargo Bank N.A. (A+/Stable/A-1). The authority has hedged a prudent amount, 86.24%, of its floating-rate exposure through interest rate swaps and caps entered into with The Bank of New York Mellon (AA-/Stable/A-1+), Royal Bank of Canada (AA-/Stable/A-1+), Goldman Sachs Bank USA (A+/Stable/A-1), and Wells Fargo. As of June 30, 2018, the total derivative notional amount is $99.7 million.

Chart 6

Iowa Finance Authority -- Debt Summary As Of June 30, 2018



Source: Iowa Finance Authority.

Management

A nine-member board of directors, appointed by the governor of Iowa, governs IFA. Board members are from the banking, business, and government sectors. A new executive director was appointed in January 2019 who will continue leading the Iowa Economic Development Authority in conjunction with IFA. IFA's strong senior management team has remained stable throughout the leadership changes. IFA has had a strong relationship with the state. A tangible sign of this strong relationship is IFA's consistent role in providing grant funding and associated responsibilities. The state has periodically asked IFA to handle nonhousing-related activities over the years, including serving as one of the state's primary bond-issuing authorities. In addition to its active single-family program, IFA manages numerous housing development and rehabilitation ventures meant to provide affordable housing and improve existing housing stock. IFA also administers several federal housing programs, thereby strengthening its legislative mandate.

The authority also administers, in partnership with the Iowa Department of Natural Resources, the state revolving fund

(SRF), which issues tax-exempt bonds to finance wastewater and drinking water facilities. SRF bonds are rated 'AAA' based on the large size and diversity of SRF's loan portfolios, program coverage and reserves, structural features, and management team with a proven track record. Our analysis of the ICR on IFA excludes SRF activities because its funds are legally obligated to the program and do not contribute to IFA's finances.

IFA's Title Guaranty Division (TGD) was established in 1985 to guarantee title to property in Iowa. We consider the TGD when evaluating the ICR on IFA, because surplus funds from TGD, in accordance with state code, are available to support IFA's affordable housing activities. We believe risk associated with the title guaranty to the ICR is minimal, as adequate reserves and reinsurance are in place to cover potential claims.

Economy

According to IHS Global Insight, Iowa's overall economic performance continues to lag the national average. The state's economy is heavily based on agriculture and manufacturing. The share of Iowa's gross state product (GSP) represented by the agriculture sector has steadily declined to a mere 4.0% in 2017 from 8.8% in 2013. The major agricultural products are corn, soybeans, and hogs. Year after year, corn and soybeans have hit record yields. Output increasing faster than demand has led to low commodity prices, resulting in agriculture's share of GSP declining continuously. Despite the pressure, Iowa still ranks in the top five for agricultural output across the U.S. and is first in pork export value and corn export value.

In addition to agriculture, Iowa has a relatively high concentration of manufacturing jobs--13.7% of nonfarm employment, compared with the country's 8.7% average. Improved agricultural performance in 2018 has increased employment in the state's manufacturing sector because a significant portion of the sector is tied to farm machinery manufacturing. When commodity prices are low and farm income weakened, the manufacturing sector suffers. After 2019, manufacturing gains are expected to slow.

Payroll growth increased by 1.0% in 2018, a large increase from 0.1% in 2017 but still behind the national average of 1.7% for the same period. This was mainly because of a major increase in construction hiring. IHS Global Insight forecasts payroll growth will be 1.7% in 2019 and nonfarm industry will be the key component. Construction employment will provide a steady boost over that period, as the housing market continues to pick up steam, and professional and business services will provide healthy average growth of about 2.4% each year.

Iowa's population growth has averaged 0.4% and is forecasted to remain at about the same level in 2019, below the national average of 0.7%. It is projected to remain stable and maintain the same pace of average annual growth through 2022. The unemployment rate decreased to 2.5% in 2018 from 3.8% in 2015 and is projected to remain fairly stable at 3.0% through 2022.

On the housing front, the state has maintained a slow, but steady, pace over the past few years. Average home prices and housing starts have already reached their pre-recession levels. It is expected that construction employment will provide a steady boost as the housing market picks up steam. The average home price increased to $174,027 by the end of 2018 from $159,542 in 2015 and is projected to reach $186,439 by the end of 2021, resulting in 1.3% annual average growth in 2019-2022. Housing starts have displayed a negative trend since peaking in 2016 at 13,489 units, declining to 11,025 units in 2018. In terms of composition, single-family units made up 73% and the remaining 27% were multifamily units in 2018.

For the third quarter of 2017, the total foreclosure rate was 0.7%, compared with the national average of 1.0%. According to Mortgage Bankers Association, 0.5% of conventional loans (compared with 0.9% nationally) and 1.8% of FHA loans (compared with 1.6% nationally) entered foreclosure during that period. With these rates, Iowa ranked 30th in the U.S. for total loans in foreclosure.

Table 1

Iowa Finance Authority -- Financial Ratios

	--Fiscal year ended June 30--					--Five-year average--
	2014	**2015**	**2016**	**2017**	**2018**	**2014-2018**
Leverage (%)						
Total equity/total assets	35.20	41.76	41.66	39.60	36.66	38.98
Adjusted equity/total assets	21.45	26.36	28.45	29.40	26.22	26.37
Total equity + reserves/total loans	55.15	76.91	83.05	78.30	70.99	72.88
Total equity/total debt	63.68	81.88	79.37	70.67	61.56	71.43
Adjusted equity/total debt	31.15	51.67	54.20	52.46	44.02	48.23
Profitability (%)						
Return on average assets	0.71	2.03	(0.35)	1.59	1.22	1.04
Return on assets before loan loss provisions and extraordinary items	0.79	1.57	0.34	1.56	1.20	1.09
Return on average equity	2.18	5.32	(0.85)	3.93	3.20	2.75
Net interest margin (loans + investments)	1.54	1.81	1.69	1.61	1.56	1.64
Net interest margin (loans)	1.99	1.64	1.57	1.48	1.29	1.59
Asset quality (%)						
NPAs/total loans + REO	0.45	0.81	2.07	2.11	1.79	1.45
Net charge-offs/average NPAs	(177.83)	(1,589.57)	(80.54)	17.43	3.86	(365.33)
Loan loss reserves/total loans	5.67	19.75	22.55	20.54	18.15	17.33
Loan loss reserves/NPAs	1,262.37	2,450.35	1,088.69	974.10	1,012.08	1,357.53
Net charge-offs/average loans	(1.34)	(13.50)	(0.54)	0.24	0.07	N/A
Liquidity (%)						
Total loans/total assets	18.01	20.76	16.66	15.72	13.67	16.96
Short-term investments/total assets	21.25	22.04	22.33	25.52	25.17	23.26
Long-term investments/total assets	2.09	2.59	2.26	1.25	0.65	1.77
Total investments/total assets	23.34	24.63	24.59	26.77	25.82	25.03
Other assets/total assets	5.51	2.30	6.55	4.67	4.81	4.77

N/A--Not applicable. NPA--Nonperforming asset. REO--Real estate owned.

Table 2

Iowa Finance Authority -- Peer Comparison

	Iowa Finance Authority 2014-2018	Iowa Finance Authority 2013-2017	--2013-2017-- All AA rated entities	All AA- rated entities	All A+ rated entities	All rated entities
Leverage (%)						
Total equity/total assets	38.98	37.63	28.05	19.16	21.80	26.92
Adjusted equity/total assets	26.37	24.93	21.41	13.73	13.40	20.38
Total equity and reserves/total loans	72.88	67.52	44.14	36.97	36.32	45.06
Profitability (%)						
Return on average assets	1.04	1.11	0.97	1.07	1.41	1.09
Return on assets before loan loss provision and extraordinary item	1.09	1.22	1.14	1.18	1.32	1.20
Net interest margin	1.64	1.59	1.26	1.25	1.58	1.41
Asset Quality (%)						
NPAs/total loans and real estate owned	1.45	1.29	3.14	4.10	3.57	3.31
Loan loss reserves/total loans	17.33	14.42	4.30	2.98	2.03	3.67
Loan loss reserves/NPAs	1357.53	1226.78	144.39	208.41	79.08	210.07
Liquidity (%)						
Total loans/total assets	16.96	17.22	70.23	63.74	62.75	66.62

NPAs--Nonperforming assets.

Table 3

Iowa Finance Authority -- Five-Year Trend Analysis

($000s)	2013	2014	2015	2016	2017	2018
Total assets	911,220	808,087	706,135	705,517	770,853	861,907
% change	(17.5)	(11.3)	(12.6)	(0.1)	9.3	11.8
Total debt	556,245	446,710	360,159	370,307	431,956	513,255
% change	(22.0)	(19.7)	(19.4)	2.8	16.6	18.8
Total equity	272,482	284,483	294,908	293,912	305,275	315,971
% change	(24.4)	(18.0)	(21.5)	0.1	13.1	17.3
Revenues	100,983	80,705	73,252	124,904	128,948	125,044
% change	(31.9)	(20.1)	(9.2)	70.5	3.2	(3.0)
Net income	15,693	6,071	15,399	(2,492)	11,769	9,932
% change	(33.2)	(61.3)	153.6	(116.2)	(572.3)	(15.6)
Total loans and mortgage-backed securities	670,520	575,006	515,959	485,766	528,473	597,937
% change	(13.7)	(14.2)	(10.3)	(5.9)	8.8	13.1
Nonperforming assets	3,050	4,690	4,632	3,371	7,110	10,602
% change	76.6	53.8	(1.2)	(27.2)	110.9	49.1
Loan loss reserves	23,939	32,607	101,910	109,533	108,534	108,519
% change	5.5	36.2	212.5	7.5	(0.9)	(0.0)

Jessica Pabst and Prasad Patil contributed research to this report.