MOODY'S
INVESTORS SERVICE

CREDIT OPINION
10 May 2017

Update

Rate this Research

Contacts

Ping Hsieh 212-553-4461
VP-Sr Credit Officer
ping.hsieh@moodys.com

Florence Zeman 212-553-4836
Associate Managing Director
florence.zeman@moodys.com

Iowa Finance Authority

Update: Moody's Upgrades Iowa Finance Authority's Issuer Rating to Aa2; Outlook stable

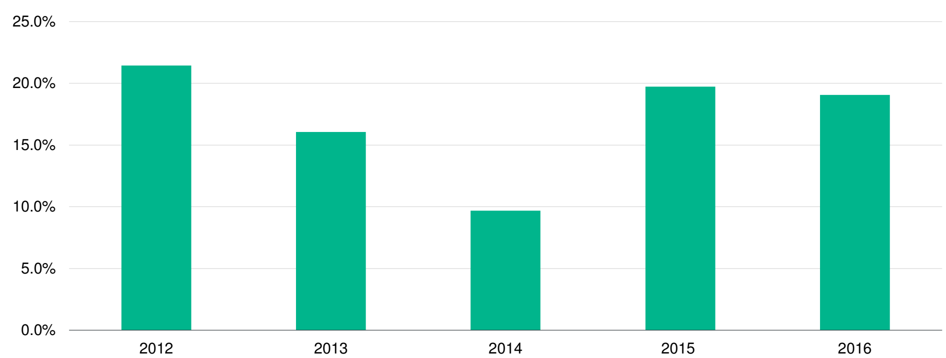
Summary Rating Rationale

Moody's Investors Service has upgraded the issuer rating of Iowa Finance Authority (IFA) to Aa2 from Aa3. The outlook is stable. Outstanding ratings on IFA's general obligation supported Multifamily Housing Bonds (MF 2005 Resolution) have been upgraded to Aa2, with a stable outlook. We have also affirmed the outstanding Aa2 rating in the Multifamily Housing Revenue Bonds program (MF 1978 Resolution) and the VMIG 1 ratings in the MF 2005 Resolution.

This rating action does not affect ratings in the Single Family Mortgage Bond Program (SF 1991 Resolution) and the Single Family Mortgage Revenue Bond Program (SF 2009 Resolution) because these bonds are rated based on respective program's financial strength, the high quality collateral of GNMA, Fannie and Freddie Mac Mortgage-Backed Securities (MBS) and the strength of the liquidity provider.

The upgrade to Aa2 is based on steady growth of IFA's financial position, high quality single family portfolio, profitable bond programs as well as a strong and experienced management. The rating affirmation in the MF 1978 Resolution and MF 2005 Resolution is based on IFA's general obligation and financial strength of the liquidity provider. Our rating analysis only considered IFA's Housing Agency Fund (excluding the Federal and State programs, Iowa Title Guaranty Division and the Agricultural Development Division), and not the State Revolving Fund.

Exhibit 1
Iowa Finance Authority's Margins Rebounded in 2015 and Remained Steady into 2016



Source: HFA audited financial statements

Credit Strengths

» Strong financial performance. IFA's 2016 program asset-to-debt ratio (PADR) was 1.50x. The 5-year average PADR was 1.46x.

» IFA's 2016 margins (net revenues as a % of total revenues) was high at 19%. The 5-year average profitability was 17%.

» High quality collateral in the single family portfolio, consisting of 100% MBS.

» Experienced and capable management team with a proven track record of managing overall risks and administering multifamily programs.

Credit Challenges

» As of December 2016, 27% of IFA's outstanding bonds were variable rate debt; 62% of which were hedged with interest rate swaps from highly rated counterparties.

» Ability to continue originating single family mortgages in uncertain market as well as generate investment returns in the persistent low interest rate environment.

Rating Outlook

The stable outlook is based on IFA's overall financial strength and our expectation that IFA's portfolio characteristics and risk profile will remain consistent with the Aa2 rating level.

Factors that Could Lead to an Upgrade

» Continued growth of IFA's financial strength and significant reduction of variable rate debt.

Factors that Could Lead to a Downgrade

» Substantial erosion of IFA's financial strength and change in management approach resulting in significant deterioration of its risk profile.

Key Indicators

Exhibit 2
Iowa Finance Authority

(Year Ending 06/30)	2016	2015	2014	2013	2012
Total Bonds Outstanding	370,306	359,609	447,796	552,382	712,408
Asset to Debt Ratio	1.50x	1.50x	1.52x	1.36x	1.32x
Margins	19%	20%	10%	16%	21%
Variable Rate Debt as a % of Bonds Outstanding	25%	38%	42%	42%	40%
Swapped Debt as a % of Variable Rate Debt	86%	79%	90%	95%	98%

Source: HFA audited financial statements

Recent Developments

Incorporated in the sections below.

Detailed Rating Considerations

Our rating analysis only considered the general fund plus the single-and-multi-family bond funds of IFA's Housing Agency component. The state revolving fund programs are also excluded from our credit consideration and are not general obligations of IFA.

Loan Portfolio - Mostly single family MBS

IFA financed $248 million of single family mortgage loans in 2016, almost doubled the 2013 level of $129 million. We expect IFA's 2017 single family mortgage origination volume to remain similar to the 2016 level.

As of 6/30/2016, 85% of IFA's mortgage assets were single family MBS which are of the highest quality because they are guaranteed as to the full and timely payments of principal and interest by GNMA, Fannie Mae and Freddie Mac, regardless of the performance of the underlying mortgage loans. Therefore, IFA's single family bond programs are shielded from cash flow disruptions and significant losses from loan defaults, which also minimizes potential draws on IFA's general obligation.

IFA has moved to a dual funding approach in 2015, where IFA finances its FirstHome program with tax-exempt bonds and sell to the secondary market (TBA market) mortgages from the Homes for Iowans program (these mortgages do not meet requirements for tax-exempt bond financing). In 2016, 43% of IFA's single family mortgages were financed with bond proceeds and the remaining 57% with loan sale. Compared to 35%/65% split in 2013, IFA has clearly shifted to rebuilding its balance sheet by retaining more mortgage assets. We expect IFA to reach a 50%/50% bonds vs secondary market sales in 2017.

The remaining 15% of IFA's mortgage assets at 6/30/2016 were mortgage loans made to finance and support multifamily affordable rental housing. At that time, IFA had 54 loans in its multifamily portfolio. One (1) small loan (0.4% of the multifamily portfolio) was FHA risked shared, 13 loans (23.6% of the portfolio) received section 8 subsidy and the remaining 40 were unenhanced. In analyzing IFA's issuer rating, we haircut the multifamily portfolio, loan by loan, against benchmarks based on the loans' insurance provision and debt service coverage required at the Aa2 rating level. Because the portfolio is largely un-enhanced, this resulted in a severe capital charge of 28% of the outstanding multifamily loan amounts to IFA's general obligation. However, IFA's strong financial and liquidity position sufficiently mitigate this risk.

Financial Position and Performance - IFA's Strong Financial Position Provides Robust General Obligation Pledges

IFA's growth in risk-adjusted net assets and profitability has been steady. As of 6/30/2016, IFA's asset-to-debt ratio was very strong at 1.5x with a healthy combined fund balance of $173 million, or approximately 47% of bonds outstanding. On the risk adjusted basis, net assets as % of bonds was 42% at 6/30/2016, with a 5-year average of 34%.

IFA's single family programs have consistently generated good net revenues and high profitability. At 6/30/2016, the profitability for the SF 1991 and 2009 Resolutions were 26% and 19%, respectively. IFA's multifamily programs, despite much smaller in size, garnered even more impressive profitability, averaging 66% in 2016.

IFA's profitability rebounded to 20% in 2015 from 10% in 2014, primarily due to:

» Success in managing TBA sales garnering high premiums; IFA created additional value in its MBS sales by creating specified low balance pools

» Effective restructuring and continuously targeting high-coupon bonds for redemption with prepayments and excess revenues, generating substantial savings

» Carefully balancing interest costs v.s. risks and efficiently managing expenses in the single family resolutions as the programs de-leveraged

» Highly profitable multifamily programs

IFA has been diligently rebuilding its balance sheet since 2015. Between 2008 and 2014, its balance sheet de-leveraged rapidly when the single family portfolio paid off and IFA wasn't able to replace them quickly enough due to difficulties financing mortgage originations with traditional tax-exempt bonds. This has been an HFA sector wide challenge, and not unique to IFA. During that period, IFA's primary tool of financing the single family mortgages was the sale of MBS in the secondary market (TBA market), supplemented by bond issuances under the Treasury's New Issue Bond Program.

If the mortgage rates rise to near 5% level, we expect IFA to make an even more pronounced shift towards financing mortgage loans via the bond market. While this may have a negative effect on IFA's profitability in the near term, it will better position them for a more robust profitability and balance sheet in the longer term.

In 2016, IFA entered into a contract with its master servicer Idaho Housing & Finance Association to provide a $30 million warehousing line to purchase IFA mortgages originated by participating lenders. In addition to the spread, IFA is able to start earning interest on these mortgages sooner, as opposed to waiting untill they are securitized into MBS. We expect this arrangement to positively contribute to IFA's profitability going forward.

LIQUIDITY

As of 6/30/2016, 20% of IFA's assets were cash and cash equivalents. Cash is a natural hedge to the interest rate risks on IFA's variable rate debt because the investment income on cash and cash equivalents rises along with interest rates.

Additionally, we regularly review consolidated cash flows for IFA's single family programs which incorporated stress tests for various prepayment speeds, interest rates, origination scenarios and assumed a portion of the variable bonds become bank bonds. Both programs demonstrated sufficient revenues to meet debt service obligations under all scenarios.

Risk Profile

Variable Rate Debt Risk in the Bond Programs

The SF 1991 Resolution and MF 2005 resolution, with IFA's general obligation pledge, have variable rate debt. Variable rate debt exposes IFA to interest rate, counterparty, liquidity and remarketing risks.

IFA's restructuring effort in the SF 1991 Resolution has already greatly reduced the percentage of variable rate debt in that program to 30% from the 2014 high of 70%. At the end of 2016, 27% of IFA's outstanding debt were variable rate. Of which, about 62% were hedged with swaps. IFA's swap counterparties are all highly rated (see Debt-Related Derivatives section below). Additionally, IFA's has had an interest rate swap policy in place since mid-2013.

Risk from Sales in the Secondary Market

IFA's active use of secondary market financing strategy exposes IFA to interest rate risk and pipeline risk. IFA will incur loss if the prevailing mortgage rate at the time of loan reservation is lower than the rate of the sale in the secondary market. IFA will also have to pay a penalty to counterparties in the secondary market for not being able to fulfill its commitment to deliver in full. To mitigate these risks, IFA changes its lending rates frequently to remain competitive and purchased a pipeline management/hedging software to more effectively monitor its pipeline. IFA's board also approved an interest rate risk management and hedging policy in 2015.

Risk from the Largely Un-enhanced Multifamily Portfolio

The largely un-enhanced multifamily portfolio also brings risks because they have IFA's general obligation pledge. However, IFA actively monitors the financial and physical conditions of the projects on a continuous basis and has seen no delinquencies in its multifamily portfolio in the last couple of years.

We considered IFA's financial strength, high quality swap counterparties combined with strong risk management sufficient to mitigate these risks.

DEBT STRUCTURE

At 12/31/2016, 89% of IFA's outstanding bonds were single family bonds and the remaining 11% multifamily bonds. At the same time, 73% of IFA's outstanding bonds were fixed rate and 27% were variable rate. Although still high, IFA's strong financial and liquidity position serve as a mitigant against variable rate risks.

Because variable rate demand obligations (VRDOs) bondholders have optional tender rights, they are supported by liquidity facilities (SBPAs). At 12/31/2016, Federal Home Loan Bank of Des Moines (Aaa/P-1) provided liquidity support on 100% of the VRDOs in the 1991 Resolution and Wells Fargo Bank, N.A. (Aa1(cr)/P-1(cr)) provided liquidity support for all of the VRDOs in the MF 2005 Resolution.

In the event of a failed remarketing of VRDOs, liquidity providers will purchase unmarketed bonds (Bank Bonds). These Bank Bonds generally have high interest rates and require an accelerated principal amortization. Additionally, liquidity providers can terminate the SBPAs or suspend their obligations without notice and will not be obligated to provide funds under certain circumstances. We consider the likelihood of these events occurring to be remote. Other events of termination become effective only after the liquidity providers give sufficient notice to allow for a tender of bonds before the SBPAs terminate.

DEBT-RELATED DERIVATIVES

IFA intends to keep most of VRDOS hedged and manages its swaps on a portfolio-wide basis. While swap obligations are secured by revenues from pledged assets in respective bond programs, they have IFA's general obligation pledge. IFA may need to make additional payments if certain events occur. As of 12/31/2016, IFA has $67.9 million of swaps outstanding with three counterparties in two different bond programs.

SF 1991 Resolution: As of December 31, 2016, VRDOs in the 1991 Resolution were hedged with swaps from three counterparties. Goldman Sachs Bank USA (Aa3(cr)/P-1(cr)) serves as counterparty for approximately 74% of the program's interest rate swaps. Bank of New York Mellon (Aa1(cr)/P-1(cr)) as the swap provider for 25% of the portfolio, and Royal Bank of Canada (Aa2(cr)/P-1(cr)) as the counterparty for the remaining 1%. Additionally, IFA entered into a forward starting swap with Wells Fargo Bank, N.A. (Aa1(cr)/P-1(cr)) for its 2016 E VRDO.

SF 2009 Resolution: No variable rate bonds and swaps permitted while the program bonds sold to U.S. Treasury are outstanding.

MF 2005 Resolution: Only one swap outstanding with Goldman Sachs Bank USA at the end of 2016, approximately $3.6 million in notional amount or 8% of multifamily bonds outstanding.

PENSIONS AND OPEB

Not a material consideration of this rating action.

Management and Operating Environment - Strong and Seasoned Management Expected to Maintain IFA's Overall Financial Strength

IFA was created in 1975 to undertake initiatives to provide and promote affordable housing within the state of Iowa. IFA's strong and seasoned management team is effective in administering its existing core business and proactively addressing a challenging operating environment since 2008. IFA's Chief Financial Officer, who joined in late 2012, complimented the existing, tenured management team with strong quantitative and financial experience. IFA's management not only fully understands and monitors risks frequently but also maintains a good relationship with the state and other stake holders.

Risk management is an important component of IFA's decision-making process. IFA demonstrates high awareness of new and existing risk initiatives and has instituted formal risk management policies. In recent years, IFA's management has focused on reducing potential financial stress from the SF 1991 Resolution's elevated exposure to variable rate debt, and maintaining significant financial resources as a mitigant. IFA also maintains a strong oversight of their relatively small multifamily portfolio. Management's commitment to repairing balance sheet and fiscal growth is a key credit consideration of IFA's issuer rating.

Legal Security

General obligation of IFA, payable from any available moneys, assets or revenues of IFA.

Use of Proceeds

Not applicable.

Obligor Profile

IFA was created in 1975 and administers housing, water quality, agricultural and economic development programs. IFA issues bonds under its single family and multifamily housing programs, its state revolving fund program, the economic development loan program and the beginning farmer program.

Additionally, IFA has a title guaranty division that provides guarantees of Iowa real estate property titles and facilitates mortgage lenders participation in the secondary market. IFA is also a HUD Section 8 contract administrator within the State of Iowa.

Methodology

The principal methodology used in this rating was U.S. Housing Finance Agency Issuer Rating Methodology published in November 2016. The additional methodology used in the short term rating was Variable Rate Instruments Supported by Conditional Liquidity Facilities published in March 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

REPORT NUMBER 1070203

Contacts

Ping Hsieh 212-553-4461
VP-Sr Credit Officer
ping.hsieh@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454