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CREDIT OPINION
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Texas Dept. of Housing & Community Affairs - Single Family Mortgage Rev. Bonds

Update to credit analysis

Summary

We expect the Texas Department of Housing and Community Affairs' ("TDHCA") Single Family Mortgage Revenue Bond program (Aaa Stable for the Senior Lien Bonds and Aa2 for the Junior Lien Bonds) to continue to perform at a high level given that 100% of the portfolio is comprised of GNMA, FNMA, and Freddie Mac mortgage-backed securities ("MBS"), and the program's strong financial position as reflected by a program asset-to-debt ratio ("PADR") of 1.22x as of the August 31, 2019 audit. The ratings also take into account the program's variable rate debt, which comprised 12% of total program outstanding bonds as of December 31, 2019 and that 100% of the liquidity on the variable rate bonds is provided by the Texas Comptroller of Public Accounts (State of Texas general obligation rating of Aaa with a stable outlook).

Credit strengths

» A strong loan portfolio comprised of GNMA, FNMA, and Freddie Mac MBSs.

» Strong financial position with a PADR of 1.22x as of August 31, 2019.

» 100% of liquidity for variable rate debt is provided by the Texas Comptroller of Public Accounts; the agreements have favorable terms, including no term-out provisions.

Credit challenges

» The proportion of variable rate debt, though declining, is still 12% of debt outstanding as of December 31, 2019.

» Liquidity facilities provided by the State Comptroller expire on August 31, 2021; extension provisions are typically of short duration.

Rating outlook

The outlook is stable, based on the program's solid financial position, strong mortgage portfolio, and variable rate debt position.

Factors that could lead to an upgrade

» Not applicable.

Factors that could lead to a downgrade

» Replacement of the State Comptroller-provided liquidity with a low rated provider or an agreement containing terms which are too onerous to withstand Moody's cash flow tests.

» A severe decline in the financial performance of the program that causes the PADR to drop.

Key indicators

Exhibit 1

(Year Ending 08/31)	2015	2016	2017	2018	2019
Total Bonds Outstanding	347,390	337,150	374,800	340,008	611,924
Asset to Debt Ratio	1.31	1.20	1.23	1.28	1.22
Margins	31.0%	21.5%	-3.7%	41.4%	30.3%
Variable Rate Debt as a % of Bonds Outstanding	58.2%	42.0%	28.5%	26.3%	12.5%
Swapped Debt as a % of Variable Rate Debt	93.4%	91.0%	95.6%	95.7%	93.4%

Source: Moody's Investors Service.

Profile

The Single Family Mortgage Revenue Bond Program was established in 1980. This indenture is TDHCA's initial single family financing program under which they continue to issue. The proceeds of bonds issued under this indenture are used to finance affordable residential housing to low and moderate income persons in the State of Texas. All the bonds under the indenture are secured equally by all of the mortgage loans.

Detailed credit considerations

Loan portfolio: portfolio comprised of highly-rated MBS

We expect loan performance to remain strong given the portfolio's composition. As of December 31, 2019, the portfolio is 100% secured by Aaa-quality GNMA, FNMA and Freddie Mac MBSs. The program also has down payment assistance loans, which have been growing over the past few years, but we do not incorporate these in our analysis.

Financial position and performance: strong PADR supports Aaa rating

Financial performance remains strong and is expected to remain strong even as ratios decline due to bond issuance. Because of increased bond issuance in fiscal year 2019, the program's asset-to-debt ratio decreased to 1.22x, as of August 31, 2019, from 1.28x at the end of the previous fiscal year. This trend may continue in fiscal year 2020, since the department plans to issue additional debt during the year. We expect this decrease in PADR to be short-term, however, and is not viewed as a negative credit development.

The program's profitability (net revenues as a percentage of gross revenues) was a strong 30% at August 31, 2019. Despite a slight 3.66% decline in profitability in fiscal year 2017, five-year average profitability was strong at 24%.

LIQUIDITY

Standalone cash flows as well as consolidated cash flows based on the August 31, 2019 audit were run and included 15%, 100%, and 3-year average life prepayment scenarios under a variety of stressful assumptions. Cash flow projections demonstrate that the program exhibits sufficient liquidity to meet all debt service obligations.

Legal framework, covenants, and debt structure: variable rate debt and liquidity renewal risk are key challenges

DEBT STRUCTURE

The total outstanding debt for the Single Family Mortgage Revenue Bond Program as of December 31, 2019 is $582,879,000, of which $512,619,000 is fixed rate, and $70,260,000 is variable rate.

DEBT-RELATED DERIVATIVES

Of the $72.26 million variable rate bods in the Single Family Mortgage Revenue Bond Program as of December 31, 2019, $62.38 million is swapped to a fixed rate under four swap agreements, one with Goldman Sachs Bank USA (Aa3 (cr)/P-1 (cr), one with The Bank of New York Mellon (Aa2 (cr)/P-1 (cr) and two with JPMorgan Chase Bank, N.A. (Aa1 (cr)/P-1 (cr).

Variable rate bonds may expose a program to additional risks including that of bondholder tenders resulting in unremarketed bonds being purchased by the liquidity provider ("Bank Bonds"). Bank Bonds may have higher interest rates than the bonds in the primary market and may require a more rapid bond principal amortization. We believe that the program is well positioned to tolerate this risk without impairing the financial condition of the program. The program's strong financial position, with a 1.22x PADR as of 8/31/19, provides it with sufficient resources and liquidity to cover higher interest costs and a certain amount of rapid principal amortization.

100% of variable rate debt liquidity support is provided through liquidity agreements with the Texas Comptroller of Public Accounts (State of Texas general obligation rating of Aaa with a stable outlook). The liquidity agreements contain favorable terms that benefit TDHCA. A lack of term-out provisions is especially favorable for the Single Family Indenture because it limits financial stress in the event of a failed remarketing and limits the stress to the program under Moody's Bank Bond stress cash flow scenarios. While each of the Comptroller-provided liquidity agreements has an expiration date of August 31, 2021, they include provisions to extend the facilities for a term of not less than 90 days or more than two years, at the Comptroller's sole discretion.

ESG considerations

Environmental considerations are not a material rating factor for the Single Family Mortgage Revenue Bonds program. While the program contains loans to properties that have moderate exposure to environmental risks including flooding and hurricanes, the program has low credit risk from these events because 100% of the program's portfolio consists of GNMA, FNMA and Freddie Mac MBS.

Social considerations are not material to the program. Program bonds are secured by MBS and the repayment of principal and interest on the underlying mortgage loans is guaranteed by government sponsored enterprises.

Governance is a material factor for the entire state housing finance agencies sector. For TDHCA, we view the management team as effective in managing its existing core business and fully dedicated to fulfilling its mission. The management staff have demonstrated a focus on reducing financial stress and competence in making decisions that have proven to reduce risk and improve financial and operational results.

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