S&P Global
Ratings

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Missouri Housing Development Commission; General Obligation

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Missouri Housing Development Commission; General Obligation

Credit Profile		
Missouri Hsg Dev Com ICR		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'AA+' issuer credit rating (ICR) on Missouri Housing Development Commission (MHDC). The outlook is stable.

The affirmation reflects our view of the following strengths:

- Increasing equity balances providing further resources to sustain operations in difficult circumstances and fund programs;
- Low-risk profile of MHDC's high-quality asset base as evidenced by investments held primarily in U.S. government agency securities and money market funds with high investment-grade ratings and an investment policy that emphasizes preservation of principal;
- Very low-risk debt profile with no variable-rate debt and minimal general obligation (GO) exposure;
- Very strong management team, with strong legislative support and formalized financial policies; and
- Strong profitability as shown by a three-year average return on assets above 1.0x

Partially offsetting the above strengths is, in our opinion, the decreased income from loans due to lower loan originations during the five years between fiscal 2012 and 2016.

MHDC is a self-supporting entity that does not draw upon the general taxing authority of the state. The commission secures resources through the sale of tax-exempt and taxable bonds and notes and through the sale of mortgage assets, for the purpose of financing owner-occupied residential mortgage loans for lower- and moderate-income residents of Missouri. Additionally, MHDC provides construction and long-term financing for rental developments to be occupied by lower and moderate-income persons. MHDC operates in way to be financially successful while fulfilling its social mission of providing such housing opportunities within the state.

MHDC has been successful in managing income volatility by being risk adverse and controlling expenses during times of decreased or uncertain revenues. MHDC's adjusted net income, which excludes the net change in fair value of investments and federal program revenues and expenses, increased 11.91% to $16.98 million in 2016, from $15.17 million in 2015. The increase was due to MHDC's prudent debt management, reducing interest expense by 4.4% while at the same time increasing revenue slightly by 1.04%. Net income across all housing finance agencies (HFAs) has been more volatile in the years since the financial crisis due to market conditions and low interest rates, which have affected investment and loan income.

While fiscal 2016 adjusted total assets are still 13.3% below fiscal 2012's level, the 6.9% increase between fiscal 2015 and 2016 indicates financial improvement and stability as income-producing asset balances return to prerecession levels. During fiscal 2016, MHDC's mortgage investment purchases and originations totaled $259.1 million compared with $162.1 million in fiscal 2015. Mortgage investments comprise 71.6% of MHDC's total assets, and 63.5% of those mortgage investments are Ginnie Mae, Fannie Mae, and Freddie Mac mortgage-backed (MBS) securities. Additionally, MHDC's low nonperforming asset (NPA) levels lend to the commission's very strong asset quality. The five-year NPA to total loans plus real estate owned ratio of 0.24% is far lower than the 3.31% five-year average of 'AA+' rated peers.

MHDC has a very strong five-year equity-to-asset average ratio of 37.9%, compared with an average of 30.5% for 'AA+' rated peers. This indicates that MHDC is well positioned to cover potential losses or income volatility due to market conditions. As of June 30, 2016, MHDC had $888.9 million in outstanding bonds and notes payable, excluding conduit debt, compared to $815.7 million in the previous year. While outstanding debt in the multifamily programs decreased, overall debt increased due to new debt issuances of multifamily housing refunding revenue bonds and single-family mortgage revenue bonds exceeding principal payments and redemptions.

Outlook

The stable outlook reflects our opinion that MHDC will continue its conservative approach to managing risk, continue to benefit from strong legislative support through aligned strategic goals, and sustain financial strength and stability. In our view, the commission is well positioned given that its strong loss reserves, increasing equity base, and strong profitability provide a solid cushion against market volatility.

Downside scenario

While we do not anticipate key financial ratios deteriorating due to negative financial performance, we could lower the rating if such a trend materializes. Further, if MHDC's asset and debt portfolios show increased risk due to less conservative investment choices or the use of variable-rate debt, we could take a negative rating action.

Upside scenario

Conversely, if MHDC is able to boost its profitability, keep NPA low, further increase its equity positions, and improve its asset base to levels comparable to those of higher-rated peers, we could raise the rating.

Earnings Quality And Financial Strength

The principal areas of analysis when assessing an entity's earnings quality, and financial strength are leverage, profitability, liquidity, and asset quality. Each component as it pertains to our analysis of MHDC is discussed below.

Leverage

The highest emphasis of our analysis is placed on leverage as it gives an indication of the resources available to sustain operations in difficult circumstances or fund programs that further the mission of expanding housing affordability. Leverage ratios measure financial resources available to support MHDC's operations and its GO pledge.

The primary leverage ratio is total equity to total assets. As of June 30, 2016, total equity to total assets ratio was 40.41%, up from 31% in 2012. MHDC has been able to increase its equity base even while earning assets have declined between 2012 and 2016. Adjusted equity was $703 million, up from $622 million in fiscal 2012. MHDC has been very successful in managing expenses during the economic downturn, which has, in effect, bolstered its equity base and kept the leverage ratio above that of 'AA+' rated peers whose five-year average is 30.48%.

The secondary leverage ratio is total equity and reserves to total loans. As of June 30, 2016, total equity and reserves to total loans was 59.84%, up from 45.85% in 2012. Again, MHDC's ability to build its equity base while the market recovered from the economic downturn, coupled with strong loan loss reserves, has put it in a solid position relative to 'AA+' rated peers whose five-year average ratio is 48.01%. MHDC has maintained its loan loss reserves over the years even when the loan base shrank. As of June 30, 2016, loan loss reserves totaled $42.6 million, against a loan balance, excluding conduit debt loans, of $1.25 billion. In 2012, loan loss reserves equaled $44.2 million, with a loan balance, excluding conduit debt loans, of $1.45 billion. The commission's priority to maintain well-funded reserves indicates the strength of its equity base.

The capital adequacy leverage ratio (adjusted unrestricted assets to adjusted debt), is used as part of an entity's risk profile assessment. MHDC's adjusted assets were 46.08% of adjusted debt as of June 30, 2016. Investment-grade HFAs are expected to maintain a 4% ratio, so in our opinion, MHDC is very well capitalized to cover potential losses in its generally low-risk portfolio.

Profitability

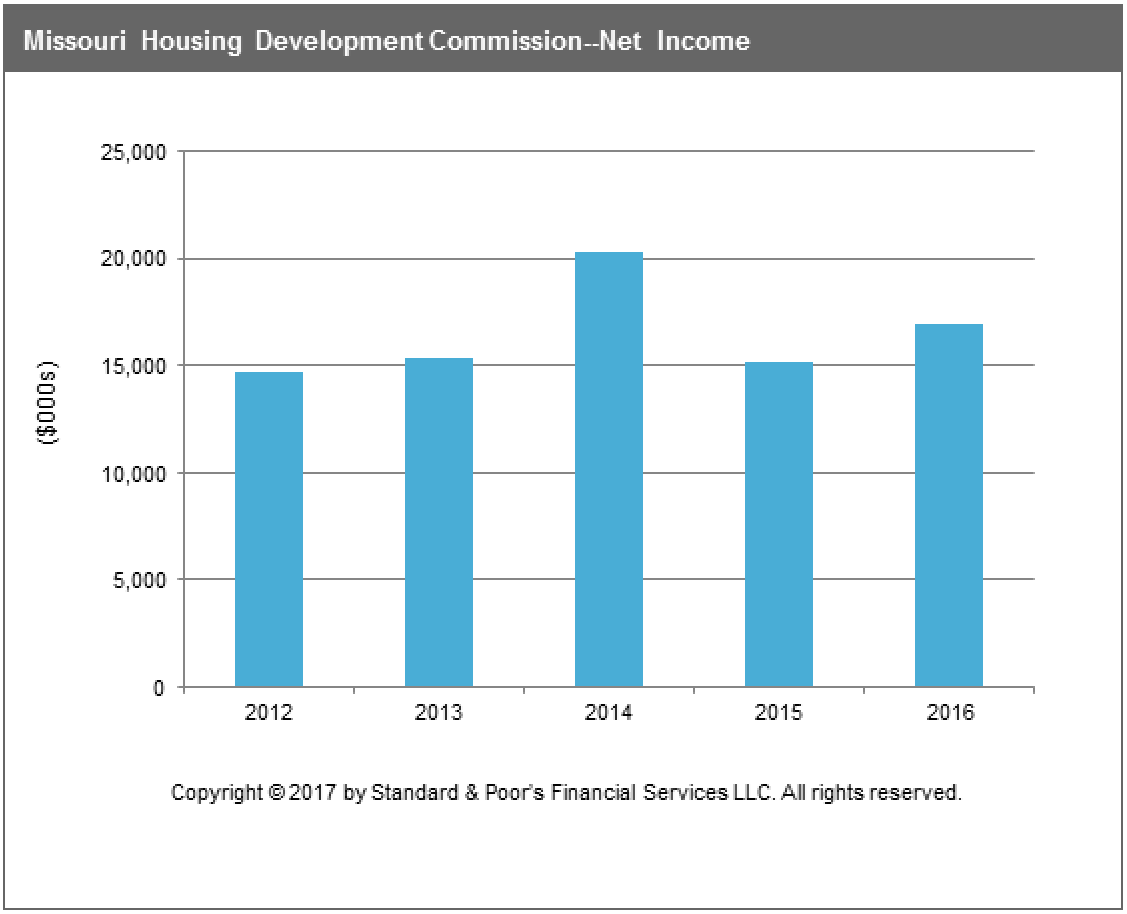
We assess an entity's profitability ratios to measure operating efficiency it is operating and indicate future financial strength as earnings become equity.

The primary profitability ratio is return on average assets. MHDC's return on average assets increased to 1.01x in fiscal 2016 from 0.70x in 2012. As of June 30, 2016, total revenue was $66.4 million, down from $98.3 million in 2012, a 32.4% reduction over the five-year period. However, because MHDC has been able to reduce expenses to $49.4 million in 2016 from $83.5 million in 2012, it achieved a 15.3% increase in net income. The primary reduction in expenses reflected a drop in interest expense for bonds of 51.4% to $27.8 million from $57.2 million.

The secondary profitability ratio is net interest margin, which improved to 1.47% in 2016 from 1.05% in 2012. Again, this reflects MHDC's ability to manage interest expense for bonds while its income from loans was declining. MHDC's five-year average net interest margin of 1.25% is slightly lower than its 'AA+' rated peers' average 1.60%, but is still better than the average of 1.19% for all HFAs in the same five-year period.

Net income rose 11.9% to $16.9 million in 2016, from $15.2 million in fiscal 2015; net income improved 15.3% between fiscal 2012 and 2016. We believe that as MHDC loan origination increases, resulting in higher interest income, net income and profitability ratios will also improve.

Chart 1



Liquidity

We use ratios to measure an entity's liquidity to cover short-term financial needs. And while desirable, high liquidity is often at odds with HFAs' mission of providing access to loans, and also reduces profitability. For those reason, we place lowest weight on liquidity ratios in our analysis.

The primary liquidity ratio is total loans to total assets, which tends to be the most stable across all HFAs. As of June 30, 2016, MHDC's total loans to total assets was 71.62%. As expected, the ratio has remained relatively strong and stable with a five-year average of 70.2% and 72.42% in 2012. MHDC's adjusted liquid assets to total mortgages ratio was 23.41% as of June 30, 2016, and far exceeds our criteria benchmark of liquid assets of 2% of total loans outstanding, reflecting MHDC's overall low-risk profile.

Asset quality

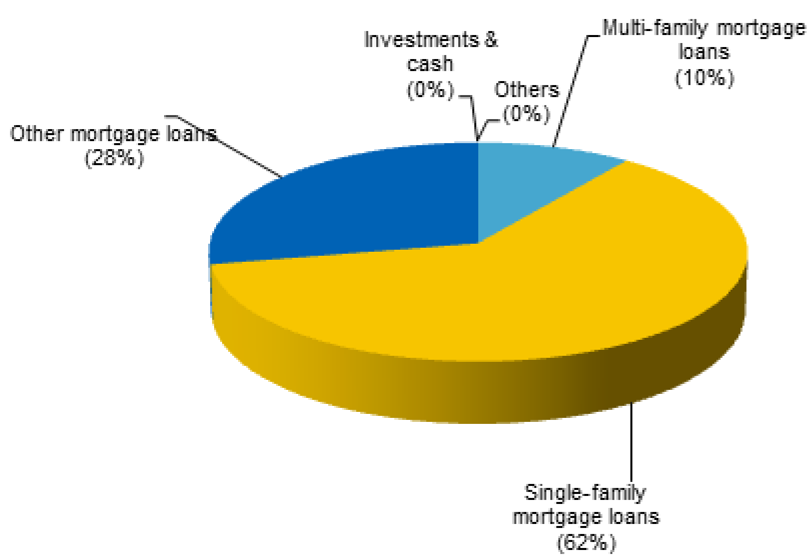
Assessing asset quality is a way to measure how an entity's mortgage loan portfolio has performed and how conservatively it reserves against potential losses. The key indicator of asset quality is the NPA ratio (NPAs to total loans and real estate owned). MHDC's NPA ratio was 0.37% in 2016, and averaged 0.24% during 2012 through 2016. These ratios compare quite favorably with other 'AA+' rated HFAs whose five-year average is 3.31%. Additionally, MHDC had very strong loan loss reserves of 3.42% of total loans in 2016, compared with 2.57% for 'AA+' rated peers.

These performance measures indicate that MHDC's mortgage loan portfolio is both low-risk and high performing.

The low-risk characteristics of MHDC's asset base can be primarily attributed to its conservative approach to credit enhancement and insurance for mortgage loans. Mortgage investments, excluding those funded by conduit debt, comprise 71.6% of adjusted total assets in fiscal 2016. As of June 30, 2016, over 99% of MHDC's single-family homeownership loans were enhanced by Ginnie Mae, Fannie Mae, or Freddie Mac mortgage-based securities and 100% of multifamily rental loans were backed by FHA insurance, including 50% risk-share loans where MHDC is responsible for 50% of losses associated with related loans. Excluding loans funded by conduit debt, single-family homeownership loans comprise 61.9% of MHDC's total loan portfolio, followed by multifamily rental loans at 10.5%, and operating fund loans, 27.6%. As mentioned, we believe MHDC to be well positioned to handle potential losses in the event of adverse market conditions given its loan loss reserve of $42.6 million, or 3.42% of total loans outstanding.

Chart 2

Asset Portfolio As Of June 30, 2016



As of June 30, 2016, MHDC's total adjusted assets were approximately $1.74 billion, up 6.85% from a year earlier. The increase in 2016 primarily reflects an increase in single-family mortgage investments for which new production exceeded loan paydowns and prepayments. While still 13.3% below the adjusted total asset high of $2.01 billion in 2012, 2016 marks the first year the asset base has grown since 2012. The several years of asset base decreases can be attributed to the low interest-rate environment, which made it difficult for HFAs to use the tax-exempt bond market to finance mortgage loans, primarily in the single-family market. As interest rates rise and market conditions stabilize, we anticipate continued improvement in loan origination and an increasing asset base.

MHDC's investment portfolio totaled $488.2 million as of June 30, 2016, compared with $497.9 million in fiscal 2015 and $550.9 million in 2012. The 11.38% decrease since 2012 is primarily attributed to a decrease in investments in money market funds and guaranteed investment contracts. MHDC's investment policy is, in our opinion, conservative and risk-adverse as it emphasizes preservation of principal. Therefore, in accordance with its policy MHDC's investments are held in high-quality, low-risk investments as follows:

- 74.63% in U.S. government securities,
- 17.10% in money market funds,
- 8.04% in cash and temporary investments,
- 0.23% in guaranteed investment contracts (GICs) and FHLB daily time deposits.

Chart 3

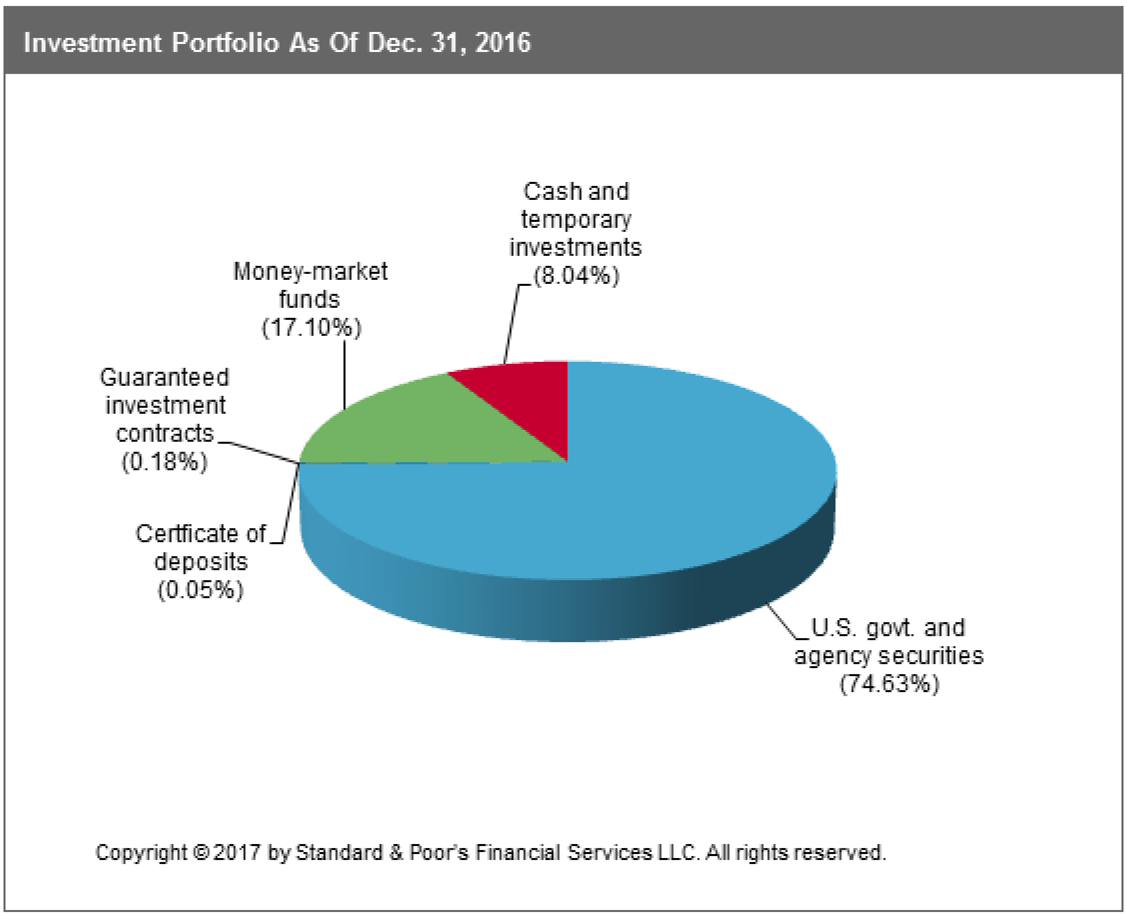
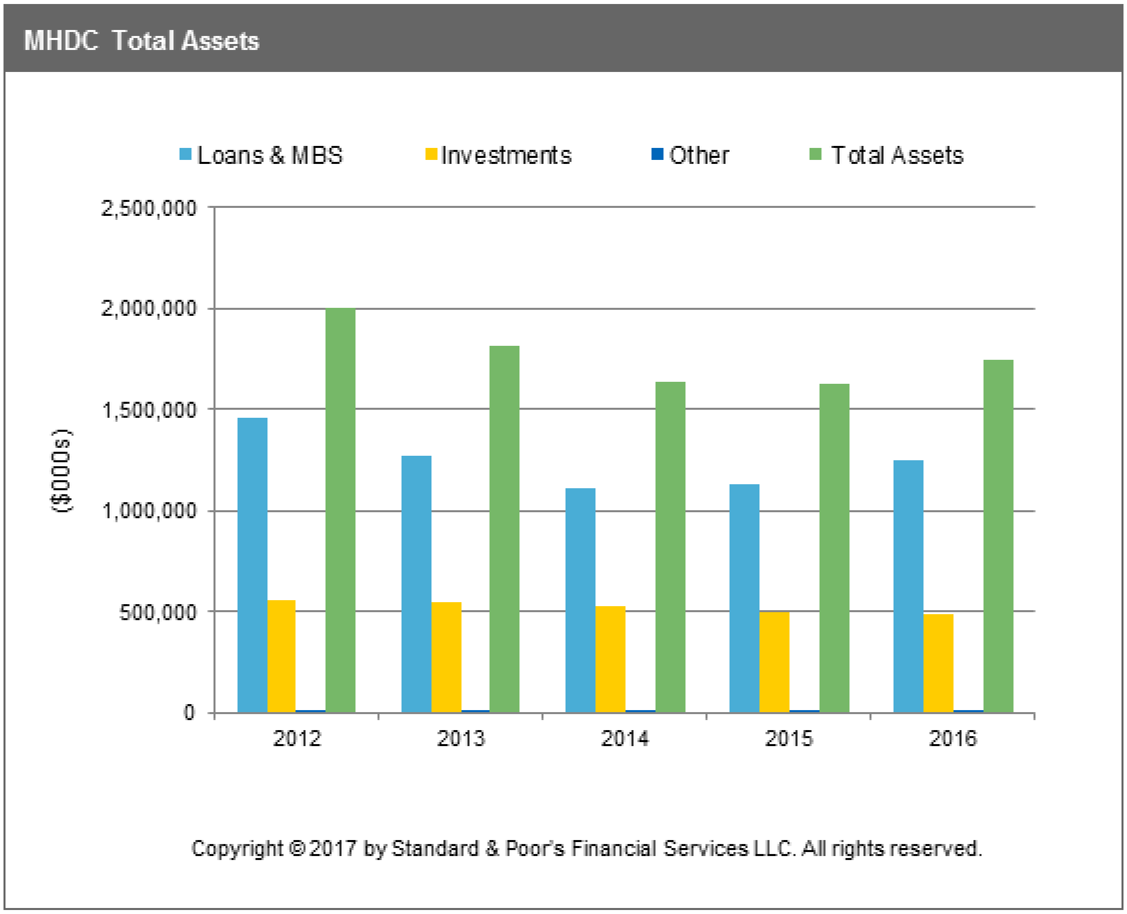


Chart 4



MHDC's growing equity base complements the overall strength and low-risk character of its asset portfolio. Based on our discussions with management in June 2017, we believe that management's conservative and attentive approach to oversight and monitoring of the loan portfolio will further help strengthen the asset base.

Overall, we consider MHDC's earnings quality and financial strength measures commensurate with our 'AA+' rating. We believe the rating continues to reflect our view of MHDC's:

- Overall financial strength;
- High-quality loan and investment portfolios;
- Continuing state support for its essential core mission; and
- Strong management team that has been prudent in its debt management, conservative in its financial practices, and insightful in its approach to risk management. This has enabled the commission to be successful in its goal of financing affordable housing in Missouri.

Table 1

Financial Ratio Analysis						
	2012	**2013**	**2014**	**2015**	**2016**	**Five-Year Average**
Leverage (%)						
Total equity/total assets	31.00	35.41	40.95	41.52	40.41	37.86

Table 1

Financial Ratio Analysis (cont.)						
	2012	**2013**	**2014**	**2015**	**2016**	**Five-Year Average**
Total equity and reserves/total loans	45.85	54.22	64.12	63.76	59.84	57.56
Profitability (%)						
Return on average assets	0.70	0.80	1.18	0.93	1.01	0.92
Return on assets before loan loss provision and extraordinary item	0.73	0.84	1.24	0.93	0.98	0.94
Net interest margin	1.05	1.06	1.27	1.40	1.47	1.25
Liquidity (%)						
Total loans/total assets	72.42	69.72	67.97	69.25	71.62	70.20
Asset quality (%)						
NPAs/total loans and real estate owned	0.01	0.24	0.27	0.29	0.37	0.24
Loan loss reserves/total loans	3.04	3.43	3.88	3.81	3.42	3.52
Loan loss reserves/NPAs	28,637.74	1,437.92	1,432.35	1,300.90	921.49	6,746.08

Table 2

Comparison Of Five-Year Average Financial Ratios				
	2012-2016	**2011-2015**		
	MHDC	**All 'AA' HFAs**	**All 'AA+' HFAs**	**All HFAs**
Leverage (%)				
Total equity/total assets	37.86	24.36	30.48	22.66
Total equity and reserves/total loans	57.56	36.85	48.01	36.57
Profitability (%)				
Return on average assets	0.92	1.00	0.69	0.77
Return on assets before loan loss provision and extraordinary item	0.94	1.31	0.82	0.98
Net interest margin	1.25	1.09	1.60	1.19
Liquidity (%)				
Total loans/total assets	70.20	71.58	68.36	70.67
Asset quality (%)				
NPAs/total loans and real estate owned	0.24	3.45	3.31	3.62
Loan loss reserves/total loans	3.52	4.68	2.57	3.45
Loan loss reserves/NPAs	6,746.08	242.32	3,549.62	722.21

Debt

As of June 30, 2016 MHDC's debt, excluding conduit debt, totaled $888.9 million, up approximately 9% from 2015 ($815.7 million). The increase is attributed to new issuances in amounts greater than principal payments and redemptions during the fiscal period. The new debt issued included one series of multifamily housing refunding revenue bonds, totaling $13.7 million, and three single-family mortgage revenue bond series totaling $205.4 million. Net proceeds of the bond issues were used to provide financing for multifamily bond-financed housing projects, under the multifamily program or for homeownership residential housing units, under the First Place Homeownership program.

All of MHDC's debt is issued at a fixed rate and there are no variable-rate debt obligations. The absence of variable-rate debt insulates MHDC from potential volatility in short-term municipal bond rates and results in a lower-risk debt profile. Additionally, because MHDC does not rely on variable-rate issuance it avoids many of the associated costs, such as increased liquidity fees.

Nearly 80% of MHDC's bonds are issued under its single-family homeownership loan programs. S&P Global Ratings rates these bonds 'AA+' due to the extremely high-quality mortgages receiving Ginnie Mae, Fannie Mae, and Freddie Mac MBS enhancement, as well as the investments' strong credit quality and cash flow sufficiency.

We rate MHDC's multifamily rental bonds 'AA+', which reflects the FHA insurance coverage on the underlying mortgage loans, the investments' credit quality, and cash flow sufficiency.

MHDC has a very limited amount of GO debt. As of June 30, 2016 MHDC had $10.5 million of GO debt outstanding, down slightly from $13.6 million in fiscal 2015.

As of June 30, 2016, MHDC had $72.15 million of conduit debt outstanding. The proceeds of the conduit debt bond issues are used to provide financing for multifamily rental housing projects. These bonds are limited obligation debt, payable solely from and secured by a loan agreement between the commission and the borrower. For this reason, we do not include outstanding conduit debt, or related loans, in our analysis of MHDC.

Chart 5

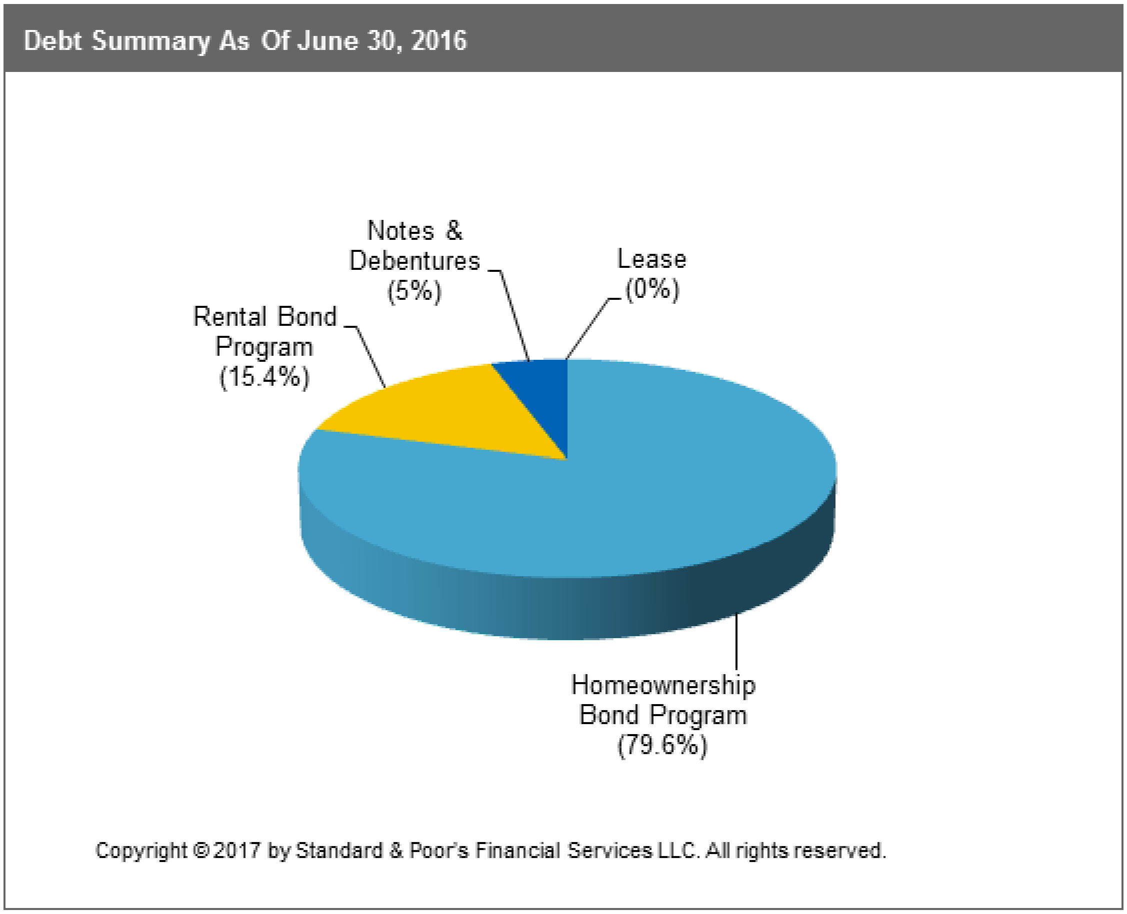


Table 3

Trend Analysis					
	2012	**2013**	**2014**	**2015**	**2016**
Total assets ($000s)	2,006,388	1,812,503	1,634,660	1,628,201	1,739,721
% change	(8.51)	(9.66)	(9.81)	(0.40)	6.85
Total debt ($000s)	1,258,372	1,041,677	840,645	815,712	888,929
% change	(14.24)	(17.22)	(19.30)	(2.97)	8.98
Total equity ($000s)	621,990	641,885	669,330	675,984	703,077
% change	5.03	3.20	4.28	0.99	4.01
Revenues ($000s)	98,245	83,695	74,193	65,718	66,402
% change	(4.09)	(14.81)	(11.35)	(11.42)	1.04
Net income ($000s)	14,731	15,313	20,272	15,174	16,981
% change	57.57	3.95	32.38	(25.15)	11.91
Total loans & MBS($000s)	1,453,037	1,263,683	1,111,153	1,127,574	1,246,043
% change	(10.76)	(13.03)	(12.07)	1.48	10.51
NPAs ($000s)	154	3,013	3,009	3,303	4,623
% change	30.30	1,856.49	(0.13)	9.77	39.96
Loan loss reserves ($000s)	44,172	43,322	43,094	42,965	42,598

Table 3

Trend Analysis (cont.)	2012	2013	2014	2015	2016
% change	(0.43)	(1.92)	(0.53)	(0.30)	(0.85)

Management

MHDC is governed by a 10-member board of directors that includes the following elected state of Missouri officials: governor, lieutenant governor, state treasurer, and attorney general. The remaining six board members are appointed by the governor with the advice and consent of the state senate. Four elected officials joined the board this year. MHDC has spent much time and effort to educate the new and current board members about its mission and priorities and fully expects the beneficial and successful relationship between MHDC and the governing board to continue.

Based on discussions with MHDC throughout the year, and specifically at our management meeting in Kansas City on June 28, 2017, we believe management has an ongoing commitment to leverage public and private resources and increase financial strength. Management has a formalized five-year rolling strategic plan that is updated annually. The goal of the strategic plan is to "analyze financial impacts of current and proposed programs to assess long-term sustainability." We believe the experienced, stable, senior staff is well suited and capable of continuing to be financially successful while serving their social purpose through programmatic operations.

MHDC continues to actively seek new ways to increase housing stock statewide, coupled with attempts to preserve older housing communities through rehabilitation. One effort to continue to provide for the citizens of Missouri is MHDC's participation in the To-Be-Announced (TBA) market as an additional source of funding to provide mortgage financing for homebuyers including previous homebuyers. MHDC began participating in the TBA market in fiscal 2017.

In addition to its homeownership and rental programs, the commission continues to strengthen its legislative mandate through various activities and programs such as: homelessness prevention; administering the federal and Missouri Low-Income Housing Tax Credit (LIHTC) programs; the Down Payment Assistance Home Repair Opportunity and First Place Loan programs; disaster assistance; and advisory, consultative, training and educational services to nonprofit housing organizations. MHDC administers the Project-Based Section 8 program in the state through a contract with U.S. Dept. of Housing and Urban Development (HUD) that provides over $143 million in pass-through housing assistance payment revenue and expense activity annually. HUD is expected to competitively bid for this program administration sometime after the current contract expires (Dec. 31, 2017). At that time, management will evaluate whether to submit a proposal for the bid. We believe the commission has the resources and experience to effectively carry out its responsibilities associated with these programs.

Finally, we expect the favorable relationship and support from the state to continue as the state has never in the past attempted to appropriate any of the commission's fund balances for alternative purposes, or required it to assume responsibility for any programs that would impair its financial strength and such actions by the state are not anticipated in the future.

Economy

According to IHS Global Insight, Missouri ended March 2017 with moderate employment growth of 1.4% from a year earlier, a weaker pace compared with the end of 2016 and below the national payroll growth rate of 1.6%. The leisure and hospitality services sector experienced solid growth of 3.2% with the addition nearly 10,000 jobs to meet demand in the expanding tourism and convention business. St. Louis and Kansas City are continuing their efforts to attract corporate offices and start-up enterprises; this has resulted in a 2.8% employment increase in office-related businesses. The information sector witnessed cutbacks with a 4.1% drop in employment in March 2017. The growth in the manufacturing was mixed, with employment in durable goods up 1% while nondurables had a job loss of 1.1%.

As of March 2017, the unemployment rate in the state decreased 0.5 percentage point from December 2016, to 3.9%, compared with the national rate of 4.5%. As of 2016, Missouri was the 18th largest state by population. From 2015 to 2016, the state's population increased by 0.3% to 6.1 million, behind the national growth rate of 0.8%, making it the 31st fastest growing state. The below-average rate of population growth and higher-education attainment is considered a weakness and could be an impediment to economic development in the state.

Over the long term, economic growth is expected to lag the national average. Job growth in Missouri will decelerate modestly over the near term, with payrolls growing at 0.8% in the second quarter of 2018, below the national rate of 1.4%, according to IHS Global Insight. The professional and business services sector is projected to experience the most sustainable growth as employment will grow by nearly 2% on average per year, well above the projected growth in other services sector.

The housing market in Missouri has seen notable improvement in recent years but is still substantially behind prerecession peaks as measured through housing starts and construction activity. That being said, while home prices in Missouri did decline during the recession, existing home prices have recovered quite well and are on pace with the economy and overall housing market. After falling approximately 16% during the recession, the median price of an existing single-family home was around $154,000 in the fourth quarter of 2016--above the prerecession peak. The new-home market is doing, with a median price of around $275,000 at the end of 2016.

Overall strengths of the state include Missouri's moderate cost of living and favorable tax policies, which have attracted a large number of corporate headquarters. Ten Fortune 500 companies, along with the presence of several key players in the food manufacturing business, such as Purina and Anheuser-Busch InBev, are headquartered in Missouri, adding to the strength and recovery of the economy.