S&P Global Ratings

RatingsDirect®

Illinois Housing Development Authority; General Obligation

Primary Credit Analyst:
Richard E Kubanik, New York + 1 (212) 438 5112; richard.kubanik@spglobal.com

Secondary Contact:
Ki Beom K Park, New York (1) 212-438-8493; kib.park@spglobal.com

Table Of Contents

Illinois Housing Development Authority; General Obligation

Credit Profile		
Illinois Hsg Dev Auth ICR		
Long Term Rating	AA-/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'AA-' issuer credit rating (ICR) on Illinois Housing Development Authority (IHDA). The outlook is stable.

The rating reflects our view of the following credit strengths:

- Strong leverage ratios, as demonstrated by an S&P Global Ratings fiscal 2018 adjusted equity position of $706 million, one of the highest among the 'AA-' rated peer group;
- Solid financial performance, with earnings of $49 million in fiscal 2018 despite limited on-balance-sheet loan portfolio growth; and
- Strong financial management supported by a culture of constant improvement, a good working relationship with the state government and no exposure to the state pension fund or other postemployment benefits (OPEB).

Offsetting these strengths is our view of the following factors:

- A shift in the asset base away from higher-yielding 30-year mortgage loans toward shorter-duration investments; and
- The five-year average nonperforming assets (NPA) ratio of 5.3% remains above those of similarly rated peers at an average of 3.7%.

IHDA's improving equity levels are the result of strong revenue from investment earnings, as total mortgage loans on the balance sheet have declined. Although net income also declined in fiscal 2018, the authority's total equity grew 9% to $706 million, from $660 million in fiscal 2017. The authority's equity-to-total assets were strong, in our opinion, at 34% in fiscal 2018, above the five-year average of 30%.

IHDA's financial strength, rising equity, and strong and proactive management continue to support the 'AA-' rating because excess capital cushions have enabled the authority to preserve its overall financial strength and provide affordable housing for Illinois residents.

Outlook

The stable outlook reflects our view of IHDA's overall financial strength, with strengthening equity and strong leverage ratios. A strong equity position and the preservation of positive net operating income despite reduced on-balance-sheet programmatic activity for both single-family and multifamily make IHDA a strong housing finance agency (HFA), in our opinion, especially when compared with its 'AA-' rated peers.

Upside scenario

Should IHDA demonstrate sustained improvement in its NPAs and continued equity growth while improving its return on average assets, we could revise the outlook to positive or raise the rating.

Downside scenario

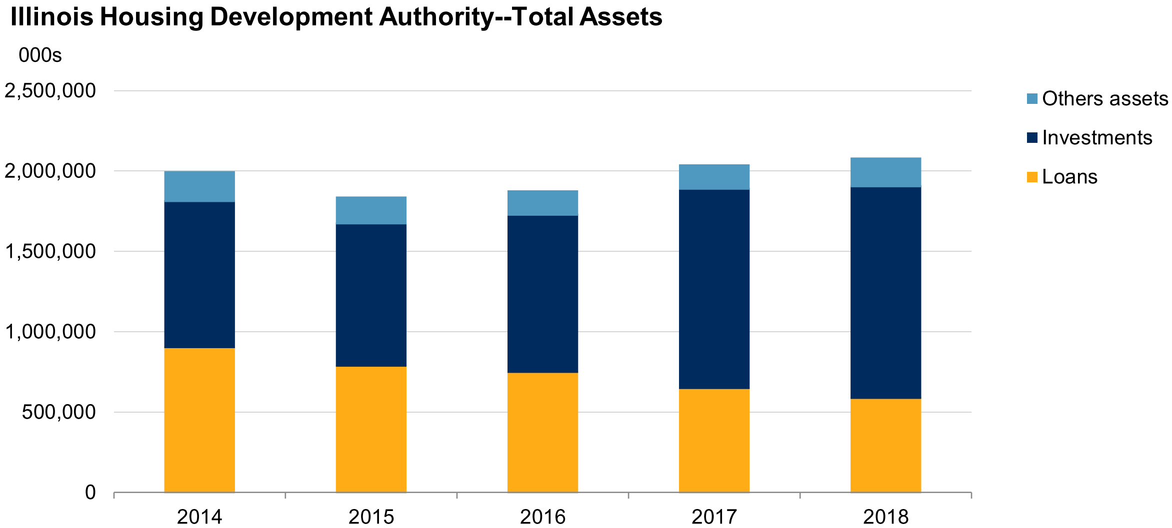
IHDA faces a challenged state economy. The authority has ample reserves but is experiencing diminished investment earnings due to the low interest rate environment. Should the authority experience a prolonged decline in operating income and profitability, we could revise the outlook to negative or lower the ICR.

Asset Quality

In our view, the authority's asset management policy remains strong. IHDA's loan-loss policy includes a ranking system for loans; the authority bases estimated potential losses on these rankings. IHDA's asset quality deteriorated slightly in fiscal 2018, with NPAs significantly increasing to 4% of total loans and real estate-owned from 3.4% in fiscal 2017. However, the authority's loan-loss reserves as a share of NPAs remained strong in fiscal 2018 at 54% (see table 1).

IHDA's asset base experienced its second year of growth, up 2% to $2.08 billion after declining in previous years from fiscal 2013 levels of $2.14 billion. However, we note that loan-origination levels of $45.5 million were half those in fiscal 2017. Mortgage loans, which had represented the majority of IHDA's asset base, have declined about 10% each year over the past five years. Mortgage loans currently represent only about 28% of the authority' asset base, while investments account for 63% of the total. IHDA's loan portfolio consisted of $336 million in multifamily loans (56%), $186 million (31%) in single-family loans, and $78 million in other loans (13%) in 2018.

Chart 1



Single-Family Loan Portfolio

The bulk of IHDA's single-family loans are contained in its homeowner mortgage revenue bonds (HMRB) resolution, although this portfolio has declined in size with higher-rate loans prepaying steadily. In addition, IHDA has decided to originate more mortgage-backed security (MBS) single-family loans, because the market for these loans has been more advantageous in recent years. IHDA reported an average home purchase price of $130,000 in fiscal 2018, with average loan amounts at $123,000. A typical IHDA borrower is 35 years old, holds a 702 FICO score and makes about $59,000 with a debt-to-income ratio of 33%.

As of Sept. 30, 2018, the HMRB loan portfolio consisted of $178 million in whole loans (50%), $119 million in Ginnie Mae MBS (33%), and $58 million in Fannie Mae MBS (16%). The whole loans are predominantly insured through private mortgage insurance (67%), followed by uninsured (26%), Rural Development (6%), and Federal Housing Administration (less than 1%). The portfolio is well seasoned, with over half of the whole loans origination in 2004 or earlier and the vast majority has a loan-to-value below 80%.

The breakdown of private mortgage principal outstanding by insurance type on primary loans is as follows:

- Mortgage Guaranty Insurance Co. (50%)
- United Guaranty Residential Insurance Co. (27%)
- Radian (12%)
- Republic Mortgage Insurance Co. (6%)
- Genworth Mortgage Insurance Co. (3%)
- PMI Mortgage Insurance Co. (2%)

Delinquencies of 60 days or more and loans in foreclosure (as a percentage of loans outstanding) continued to improve, decreasing to 4.3% in the third quarter of 2018, compared with 4.5% and 5.4% in the third quarters of 2017 and 2016, respectively. We believe management has provided strong oversight in IHDA's functional areas, including financial risk management as it pertains to managing debt and investments, and asset management as it pertains to loan underwriting and loan servicing. Dovenmuehle Mortgage Inc. is the whole-loan servicer, and U.S. Bank services IHDA's MBS portfolio.

Furthermore, we believe the current team has remained proactive in guiding the authority during difficult market conditions and helping it fulfill its mission. The 'AA' HMRB program rating reflects the credit quality of pledged single-family mortgage loans and investments appropriate for the rating, an ability to absorb forecast loan losses, and cash flow sufficiency. HMRB cash flows indicate that asset-to-liability parity is approximately 123% as of a June 30, 2018 basis date, which is in-line with 2017 levels. We assume a conservative credit for recovery in our loss coverage assumptions for various mortgage insurers and write-off forgivable second loans. The resulting loss reserve assumption, based on the whole loan characteristics and performance, is about 4.3% ($7 million). When we assess the reserves on the loan assets, the HMRB bond program has excesses of about $53 million.

Multifamily Loan Portfolio

The bulk of IHDA's multifamily portfolio is concentrated under its housing bond resolution, consisting of seasoned loans (June 30, 2018 portfolio average loan to value of approximately 69%) predominantly subsidized by government insurance. We believe federal subsidies and guarantees, coupled with strong underwriting, contribute to a risk profile for the program that we consider low to moderate. Approvals for multifamily projects did experience delays during the recent partial government shutdown but IHDA reports that conditions have returned to normal.

As of June 30, 2018, IHDA maintained approximately 69 loans under the housing bond program. Developments encompassed the following program types (listed by mortgage balance percentage):

- Unassisted conventional financings: 81%
- Section 8 or Section 236: 12%
- FHA Risk Share: 7%

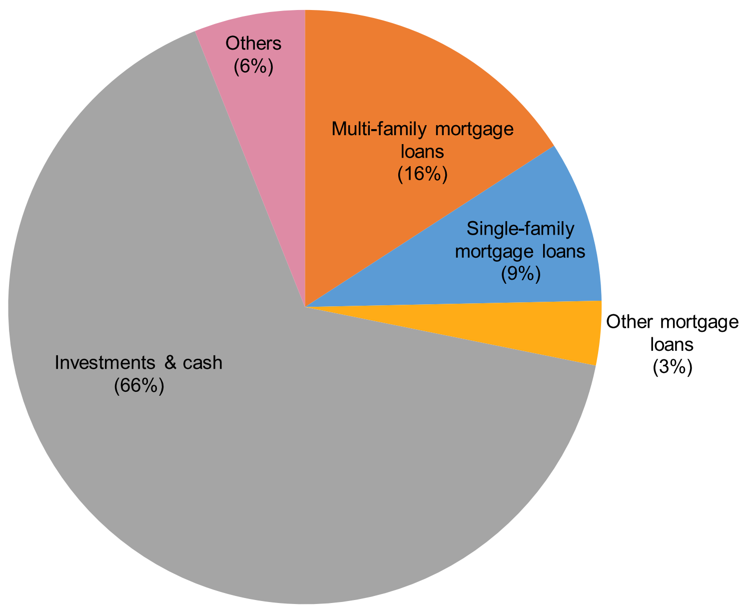
The quality of the pledged collateral and IHDA's general obligation pledge back the housing bond resolution; the resolution contains well-seasoned, federally subsidized mortgages. To the extent available equity is insufficient to account for our assessment of portfolio risk, a capital charge is assessed to the authority's administrative fund. Consolidated cash flows, assuming no prepayments with a July 1, 2018 basis date, indicate equity totaled $193 million, approximately equal to a 190% asset-to-liability ratio. We believe the mortgage portfolio, while paying down, is performing well overall, with approximately 1.39x in average debt service coverage. Occupancy for IHDA developments averaged approximately 97% in fiscal 2018. As of June 30, 2018, multifamily loans under the housing bond program totaled $240 million, and the authority had four mortgage loans delinquent for 60 days or more.

Investments

IHDA's portfolio is predominantly invested in U.S. government and agency obligations, and we believe it is of high credit quality and provides strong liquidity support, as 25% of investments have a duration of one year or less. As of June 30, 2018, the authority's investment portfolio grew to $1.3 billion, or 63% of the total asset base.

Chart 2

Illinois Housing Development Authority--Investment Portfolio

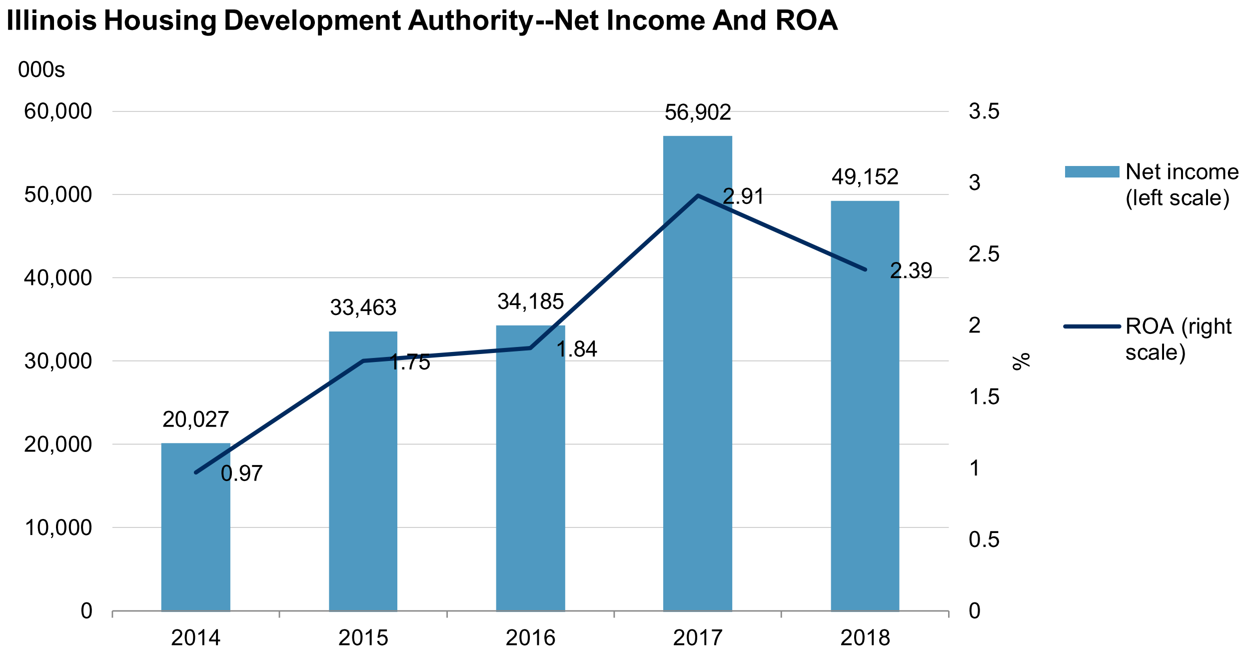


As of June 30, 2018

Earnings Quality And Financial Strength

The authority's financial position remains strong. Total revenue was $119 million in fiscal 2018, slightly below fiscal 2017 levels of $123 million. At $50 million, investment income is the largest component, followed by other income, which includes strong to-be-announced (TBA) sales of $24 million, and mortgage income of $30 million. IHDA's net income fell in fiscal 2018 to $49 million, as lower investment income, higher salaries and benefits, and increased estimated losses brought levels down from $57 million in 2017.

Chart 3



Net interest margin, a key measure of profitability, was 2.6% in 2018, down from 2.9% in 2017 but remains above peers. As mortgages prepaid, funds have been placed in investments instead of new mortgages. In addition, return on average assets also fell in 2018 to $2.4 million from $2.9 million but remained above the five-year average.

IHDA's improving equity, driven by growing investments, further exemplifies its strong financial strength and comfortable leverage measures. Its total equity increased to $706 million in fiscal 2018, up 6% from $660 million in fiscal 2017. The authority's equity-to-total assets were strong at 34% in fiscal 2018, similar to previous years. After applying our capital-adequacy adjustments for potential losses, IHDA's capital adequacy has sufficient available funds, in our view, to support the various bond programs' risk. The ratio of unrestricted assets to adjusted equity is 26%.

Debt

We believe IHDA has maintained a relatively low-risk debt profile. As of June 30, 2018, the authority's total debt outstanding was $1.16 billion, which was similar to the prior year. The authority was active in both single-family indentures with MBS originations and simultaneously managed a TBA platform that earned $24 million on volume of $472 million, which is a better yield that the prior year's $28 million in earnings from $644 million of volume. Multifamily activity was primarily driven by conduit issuance, which is reported in the notes of IHDA's financial statements and does not constitute a credit risk to the authority.

Of the total debt, about 57% relates to single-family bonds, while 36% relates to multifamily bonds (see chart 4). As of

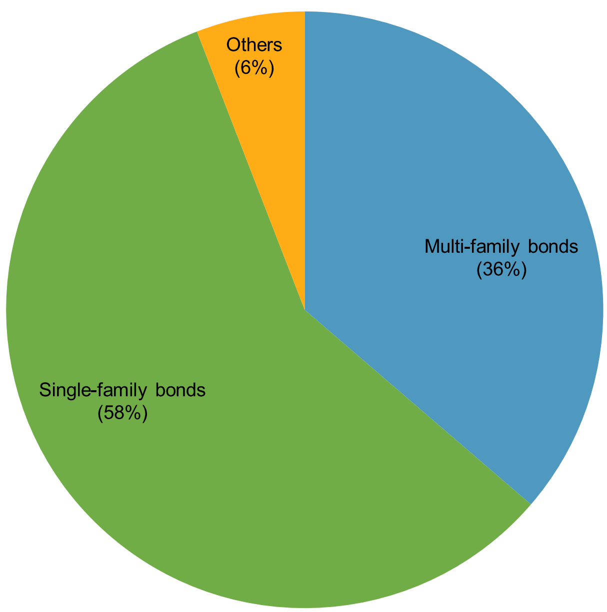
June 30, 2018, approximately $163 million, or 14%, of IHDA's bonds outstanding were variable rate. While not a large total percentage and quite manageable given IHDA's liquidity position, the majority is unhedged. The increase in interest expense for unhedged variable-rate debt was noticeable, as the fiscal 2018 interest rate range was 1.55%-2.07% compared with 0.42%-0.75% in the prior year.

IHDA has entered interest rate caps to hedge a small portion of the variable interest rate exposure associated with its variable interest rate bond program. Use of interest-rate swaps and hedging instruments exposes IHDA to a series of risks, including termination, counterparty, amortization, basis, and tax risk. In our opinion, IHDA's hedged variable-rate debt portfolio is a low risk to the authority, as it reflects:

- A moderate degree of involuntary termination risk under the swap due to a narrow ratings trigger spread;
- A low-to-moderate degree of counterparty risk given the ratings on related counterparties;
- Strong management oversight, with a written financial management plan that requires periodic review of all hedging agreements; and
- The modeling of S&P Global Ratings' stressed interest rate risk assumptions into consolidated cash flow simulations in the housing bond program and new issue bond program.

Chart 4

Illinois Housing Development Authority--Debt Summary



As of June 30, 2018

Management And Legislative Mandate

IHDA was created in 1967. The authority is led by a nine-member board of directors appointed to four-year terms by the governor with the state senate's advice and consent. The board members are well versed in community development, public finance, and affordable housing construction. The board is aided by a 300-person staff headed by an executive director with 25 years of industry experience. In 2017, IHDA added a chief technology officer position to focus on maintaining a strong and secure infrastructure. The authority has a cyber-insurance policy and regularly tests network vulnerabilities. Unique to IHDA, is a culture of operational excellence with a senior team leader reporting directly to the executive director on best practices and process improvement.

Full-time employees may set aside earnings in a defined-contribution plan. In addition, IHDA participates in a 6% employer contribution plan, with employees being 100% vested on the first day of such contribution. The authority does not offer additional other postemployment benefits beyond unused vacation days and carry-forward sick leave.

In our view, IHDA's management is strong and contributes to the authority's credit strength. We believe the team has provided strong oversight in all authority functions, including financial risk management pertaining to debt and investments, and asset management relating to loan underwriting and loan servicing. Furthermore, we believe the team remains proactive in guiding the authority through difficult market conditions and helping to fulfill its mission. Despite the state's fiscal issues, we believe IHDA's relationship with the state government remains strong. Furthermore, we are unaware of any state proposals that could affect the authority's financial strength.

IHDA maintains a presence in affordable housing statewide by acting as administrator for the Rental Housing Support Program, which awards funds to local agencies that make rental units affordable to households earning less than 30% of area median income. In addition, the authority oversees and administers the state's Affordable Housing Trust Fund. IHDA also administers the Illinois Affordable Housing Tax Credit program, and it allocates federal low-income housing tax credits and federal HOME Investment Partnerships Program funds.

In addition, the authority administers the Hardest Hit Fund (part of the governmental activities, which is not included in this analysis). During fiscal 2018, the fund provided $35 million of down payment assistance to over 4,632 first-time homebuyers, and provided $40 million in direct mortgage assistance that enabled 3,268 households, many of which were seniors, with reverse mortgages and overdue tax and insurance payments to avoid foreclosure. IHDA is one of only two state HFAs to launch an I-Refi program that enables homeowners with declining property values to write down the balance of their first mortgage and refinance into a smaller, more affordable loan.

Economy

Although diverse, Illinois' economic growth is sluggish and unemployment remains over 4%. Chicago and its suburbs dominate the state's economy, with a labor force of 4.9 million. Chicago is the finance and insurance hub of the Midwest, and is the region's main transportation, distribution, health care, and education center. Outside the Chicago metro area, the state's economic structure is dramatically different. Farming and food processing, government, and resident-driven services bolster business activity in southern Illinois. The western part of the state is closely tied to transportation and distribution centers served by the Mississippi River. Located along the river's eastern bank, the Illinois portion of the St. Louis metropolitan area forms the state's second-largest commercial center. The Moline and Peoria metropolitan areas have high concentrations of farm, construction, and heavy-equipment manufacturing.

The state severely lags behind national payroll growth, with many sectors in the negative, including retail trade, information, and other services. An increase in competition from online shopping combined with Illinois' declining population, negatively affected traditional brick-and-mortar stores. Manufacturing and construction remain the state's bright spots. Manufacturing expanded 2% in 2018 and was the state's second-largest job creator, following the public sector. Construction sector was the fastest-growing sector, adding jobs at a rate of 4%, driven by a steady stream of new-home construction.

The state's real estate market remains weak but is slowly improving. The average real price of existing single-family units has bounced back as prices gradually rose over 2013-2017. Given the lackluster movement in existing home sales, many buyers are hesitant to pay higher prices, especially considering that Illinois is ranked 12th in the country for total loans in foreclosure. While new-home construction has been increasing, homebuilding is nowhere near the previous levels at the height of the boom. A healing labor market will eventually aid the real estate sector's recovery, as higher employment levels will correlate to increased demand for housing. This should, in turn, drive up sales and prices, along with starts and construction employment. We expect prices and existing home sales to increase in 2018; housing starts are expected to decline in 2018 before recovering in 2019.

Table 1

Illinois Housing Development Authority--Financial Ratio Analysis

	2014	2015	2016	2017	2018	Five-year average
Leverage						
Total equity/total assets	24.48%	29.88%	32.05%	32.42%	33.97%	30.56%
Adjusted equity/total assets	16.94%	22.10%	24.18%	24.66%	25.70%	22.72%
Total equity and reserves/total loans	57.57%	71.67%	81.67%	103.28%	122.48%	87.34%
Profitability						
Return on average assets	0.97%	1.75%	1.84%	2.91%	2.39%	1.97%
Return on assets before loan loss provision and extraordinary item	1.17%	1.68%	1.62%	2.84%	2.48%	1.96%
Net interest margin	1.37%	2.41%	1.90%	2.87%	2.64%	2.24%
Asset Quality						
NPAs/total loans and real estate owned	9.58%	4.78%	4.49%	3.37%	4.06%	5.25%
Loan loss reserves/total loans	3.43%	2.12%	1.69%	1.73%	2.21%	2.24%
Loan loss reserves/NPAs	35.20%	44.15%	37.57%	51.12%	54.41%	44.49%
Liquidity						
Total loans/total assets	45.22%	42.97%	40.07%	31.92%	28.24%	37.68%

Table 2

Illinois Housing Development Authority--Peer Comparison						
	Illinois Housing Development Authority 2014-2018	**Illinois Housing Development Authority 2013-2017**	**All 'AA' rated entities**	**All 'AA-' rated entities**	**All 'A+' rated entities**	**All rated entities**
			2013-2017			
Leverage (%)						
Total equity/total assets	30.56	28.13	29.18	17.37	21.80	27.39
Adjusted equity/total assets	22.72	19.95	21.75	12.48	13.40	20.58
Total equity and reserves/total loans	87.34	73.05	46.80	29.76	36.32	44.84
Profitability (%)						
Return on average assets	1.97	1.83	0.98	0.91	1.41	1.06
Return on assets before loan loss provision and extraordinary item	1.96	1.72	1.15	1.07	1.32	1.18
Net interest margin	2.24	1.88	1.30	1.13	1.58	1.40
Asset Quality (%)						
NPAs/total loans and real estate owned	5.25	6.14	2.91	3.69	3.57	3.08
Loan loss reserves/total loans	2.24	2.37	5.42	3.10	2.03	4.22
Loan loss reserves/NPAs	44.49	40.31	275.84	242.02	79.08	269.32
Liquidity (%)						
Total loans/total assets	37.68	41.10	70.37	68.27	62.75	68.00

Table 3

Illinois Housing Development Authority--Five-Year Trend Analysis					
	2014	**2015**	**2016**	**2017**	**2018**
Total assets (000)	1,995,624	1,835,692	1,875,339	2,036,706	2,079,795
% change	(6.84)	(8.01)	2.16	8.60	2.12
Total debt (000)	1,282,076	1,083,982	1,080,341	1,147,673	1,164,425
% change	(11.39)	(15.45)	(0.34)	6.23	1.46
Total equity (000)	488,524	548,566	600,975	660,250	706,435
% change	4.47	12.29	9.55	9.86	7
Revenues (000)	107,606	110,240	101,751	123,088	118,679
% change	2.16	2.45	(7.70)	20.97	(3.58)
Net income (000)	20,027	33,463	34,185	56,902	49,152
% change	(44.07)	67.09	2.16	66.45	(13.62)
Total loans (000)	902,364	788,803	751,376	650,118	587,385
% change	(7.09)	(12.58)	(4.74)	(13.48)	(9.65)
Nonperforming assets (000)	87,967	37,915	33,809	21,942	23,910
% change	4.79	(56.90)	(10.83)	(35.10)	8.97
Loan loss reserves (000)	30,966	16,738	12,700	11,216	13,010
% change	9.96	(45.95)	(24.12)	(11.69)	16