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RATINGSDIRECT®

August 26, 2009

District of Columbia Housing Finance Agency; General Obligation; Other

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District of Columbia Housing Finance Agency; General Obligation; Other

Credit Profile		
District of Columbia Hsg Fin Agy ICR		
Long Term Rating	A-/Stable	Upgraded
District of Colu Hsg Fin Agy certs of part ser 1998		
Unenhanced Rating	BBB+(SPUR)/Stable	Upgraded
Many issues are enhanced by bond insurance.		

Rationale

Standard & Poor's Ratings Services raised its issuer credit rating (ICR) on District of Columbia Housing Finance Agency (DCHFA) to 'A-' from 'BBB'. In addition, Standard & Poor's raised its underlying rating (SPUR) on the agency's certificates of participation series 1998 to 'BBB+' from 'BBB-'.

The ratings are based on our opinion of the following strengths:

- The very high quality and very low risk profile of its asset base;
- Reasonable financial performance, with sufficient capital adequacy ratios at the 'A-' level;
- Minimal general obligation (GO) debt exposure;
- Active management team in transition that continues to explore opportunities to increase asset base growth; and
- Success in meeting its legislative mandate and maintaining a strong and positive relationship with the district government.

Weaknesses:

- Limited growth due to the district's small geographic area; and
- Low leverage and profitability ratios.

Standard & Poor's believes DCHFA has made improvements in recent years. DCHFA has one of the smallest loan portfolios of all state housing finance agencies (HFAs) with a Standard & Poor's ICR rating, as the district's small geographic area limits the agency's growth. Despite this limitation, DCHFA's loan portfolio has expanded by 10% during the last year. The bulk of its loan portfolio is either insured by government and private mortgage insurance providers or is backed by Ginnie Mae, Fannie Mae, or Freddie Mac mortgage-backed securities (MBS). This resulted in low capital costs and no loan losses in 2008. As of Sept. 30, 2008, DCHFA asset portfolio was $1.35 billion reflecting a small increase of 1% over fiscal 2007. The investment portfolio has decreased to $527 million reflecting a 10% decline over the previous fiscal year. Its financial position is adequate, given its low general obligation (GO) debt exposure and low risk nature of the asset base. Standard & Poor's rated $353 million of DCHFA's debt outstanding as of Sept. 30, 2008. Of DCHFA rated debt, 82% is rated 'AAA' based on the strength of the pledged collaterals. As of Sept. 30, 2008, DCHFA had $1.4 million outstanding in certificates of participations (COPs) that rely on the agency's GO pledge.

In addition Standard & Poor's believes that DCHFA's management team is transitioning effectively into providing

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successful affordable housing programs. The management team reported it has a strong and mutually beneficial working relationship with the district government. Standard & Poor's believes that the agency's management will continue to be proactive and successful in meeting its mission of financing affordable housing for residents of the District of Columbia.

Outlook

The stable outlook reflects Standard & Poor's opinion of the agency's steady asset base and low-risk loan portfolio which is majority guaranteed by government sponsored entities or being FHA insured. Although a decline in the profitability ratios is slightly concerning, Standard & Poor's is closely monitoring the changes in the leverage and profitability ratios that are key to DCHFA's long-term financial strength. Low leverage and profitability ratios are offset by DCHFA's low-risk profile which has created some stability. In addition to these factors, the stable outlook reflects the agency's improving program administration capabilities, strong relationship with the district government, and a strong local economy.

Asset Quality: High Quality Loans And MBS

Standard & Poor's believes that DCHFA's loan portfolio poses an extremely low-risk due to the agency's conservative approach to collateral. As of Sept. 30, 2008, DCHFA's asset base was at its all-time high of $1.35 billion, following a marginal increase of 1% over fiscal 2007 (see chart 1). Its asset portfolio consisted of mortgage loans and MBS (59%), investments (39%) and other assets (2%) (see chart 2). At the end of fiscal 2008, the agency's loan portfolio reached a high of $799 million, following a 10% increase over fiscal 2007. Out of the total loan portfolio, $794 million accounted for mortgage loans while $4.7 million consisted of McKinney Act loans which are restricted to benefit very low-income persons. Roughly 84% of DCHFA's mortgage portfolio consists of multifamily loans and the remaining 16% are single-family loans. Of the entire loan portfolio 46% consisted of Federal Housing Administration (FHA) or private insured mortgages and approximately 34% are Ginnie Mae, Fannie Mae, and Freddie Mac MBS. The balance of 20% is unenhanced.

DCHFA has two 'AAA' rated single-family parity resolutions (1988 and 1996), of which the 1996 resolution is currently active. As of Sept. 30, 2008, the 1996 resolution asset-to-liability was at 101.06% and 135.5% for the 1988 resolution. In fiscal year 2008 the single family loan portfolio increased by 26% over fiscal year 2007. As of Sept. 30, 2008, approximately 99% of the agency's single-family loan portfolio was backed by Ginnie Mae, Fannie Mae, or Freddie Mac MBS. Of the $794 million mortgage loans in DCHFA's portfolio, $131 million are associated with the single family program and are obligations of the agency.

As of Sept. 30, 2008, 21% of DCHFA's multifamily loan portfolio was backed by Ginnie Mae or Fannie Mae MBS. The multifamily loan portfolio increased by 7% over fiscal year 2007. Of the $794 million mortgage loans in DCHFA's portfolio, $663 million of the loans are multifamily conduit issues. Because the loans are conduit issues and the sole obligation of the developers, DCHFA bears no direct or indirect financial risk (unless it's a FHA risk share loan where the agency is responsible to cover 10% of the loss on the mortgage which is 1.5% out of the total loan portfolio). Furthermore DCHFA does not realize any earnings gained from these mortgages except for those associated with issuer fees. Although the conduit issues are of no obligation to the agency Standard & Poor's reviewed the financial ratios including the conduit issues.

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DCHFA participates in the Department of Housing and Urban Development (HUD) Federal Housing Administration (FHA) 90/10 Risk-Share program, where a multifamily project is insured by FHA for 90% of the mortgage while 10% of the mortgage is insured by the agency. In order to participate in this program, the agency deposited $500,000 in a reserve account with Merrill Lynch. With every risk-share project, an FHA placement fee of 1% of the mortgage balance is collected and deposited into the reserve account. As of Sept. 30, 2008, the reserve account had a balance of $1.89 million. Standard & Poor's takes a conservative approach by assessing a 50% loss of the 10% that the agency is responsible to cover. DCHFA has sufficient liquid reserves at $96 million to cover the loss. In fiscal 2008, the agency issued $3.23 million in tax-exempt housing bonds for Fairmont I and II under the risk-sharing program.

The agency's multifamily properties are monitored and managed by DCHFA's compliance and Asset Management Group. Asset managers ensure all procedures and guidelines are compliant with DCHFA's requirements, as well as low income housing credit (LIHTC) regulation and FHA/HUD requirements. The focus of the asset and management group during the monitoring process is to provide long term, quality affordable housing and to protect DCHFA's assets and bondholders investments. The projects are divided into risk sharing and nonrisk sharing where debt service and uncollected rent ratios are monitored during the fiscal year review. In addition to these processes, the agency also has a watch list criteria for the multifamily projects which can be found on DCHFA's website. Standard & Poor's believes this process allows for prudent property management through, detailed information on the monitoring, review and evaluations process.

Standard & Poor's believes that with the proactive approach to providing affordable housing, DCHFA will continue to build its asset base which was at its all-time high of $1.35 billion in fiscal year 2008. In fiscal year 2008 the Agency financed 904 rental units after the closing of $90.53 million in tax-exempt bonds. The total amount of outstanding multi-family bonds from new issuances increased by $35.97 million in the form of newly issued debt and the draws on the existing and newly closed draw-down bonds. During fiscal year 2008, the Agency was able to provide single family mortgages for persons purchasing homes in the District at below national and local conventional rates. The Agency provided over $43.79 million to assist 218 homebuyers purchase homes in the District at very competitive interest rates.

Standard & Poor's believes DCHFA has conservative yet prudent investment guidelines which require investments to be of investment grade, are approved by its board of directors regarding its general fund. Funds from bond issuances are governed by the covenants of the trust indenture, and are normally invested in investment agreements rated 'AA-' or higher. At the end of fiscal 2008, the agency's investment portfolio was $527 million, following a 10% decrease over fiscal year 2007. Declining investment income and interest rate environment has resulted in DCHFA's investment income to dip to an approximate 27% of total revenues in 2008, compared to 30% in 2007. Despite this decrease, the agency's investment portfolio is still above its past five-year average. The agency's investments, as of Sept. 30, 2008, are of high credit quality and provide sufficient liquidity, with 8% in money market funds and 74% in investment agreements (see chart 3).

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Chart 1

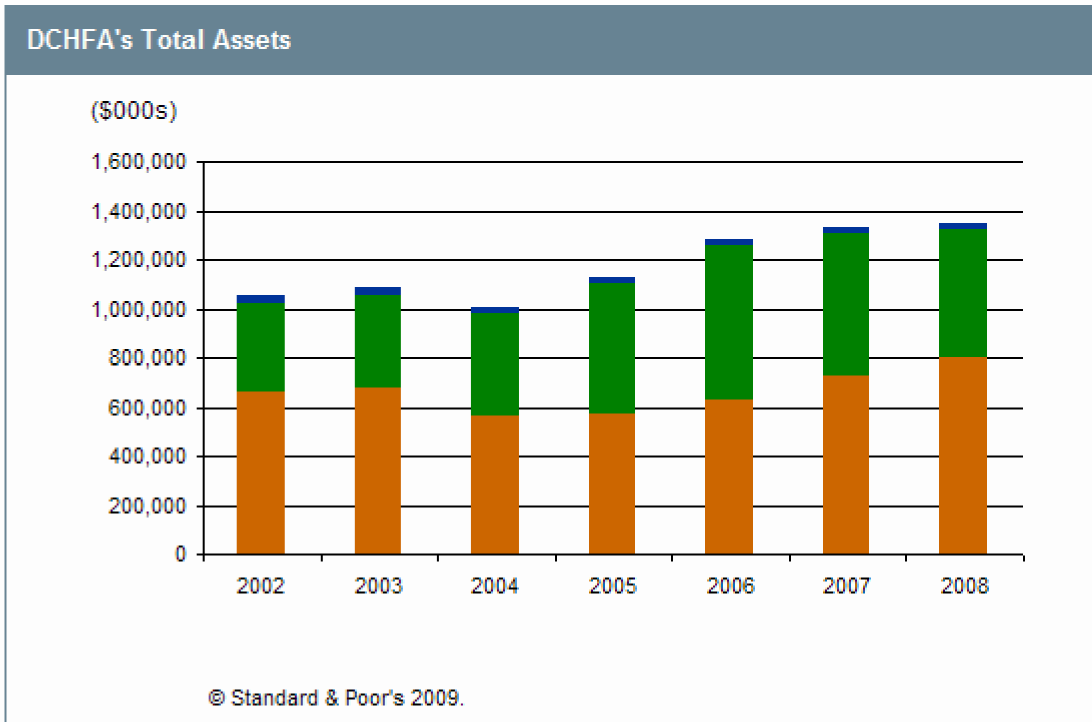

Chart 2

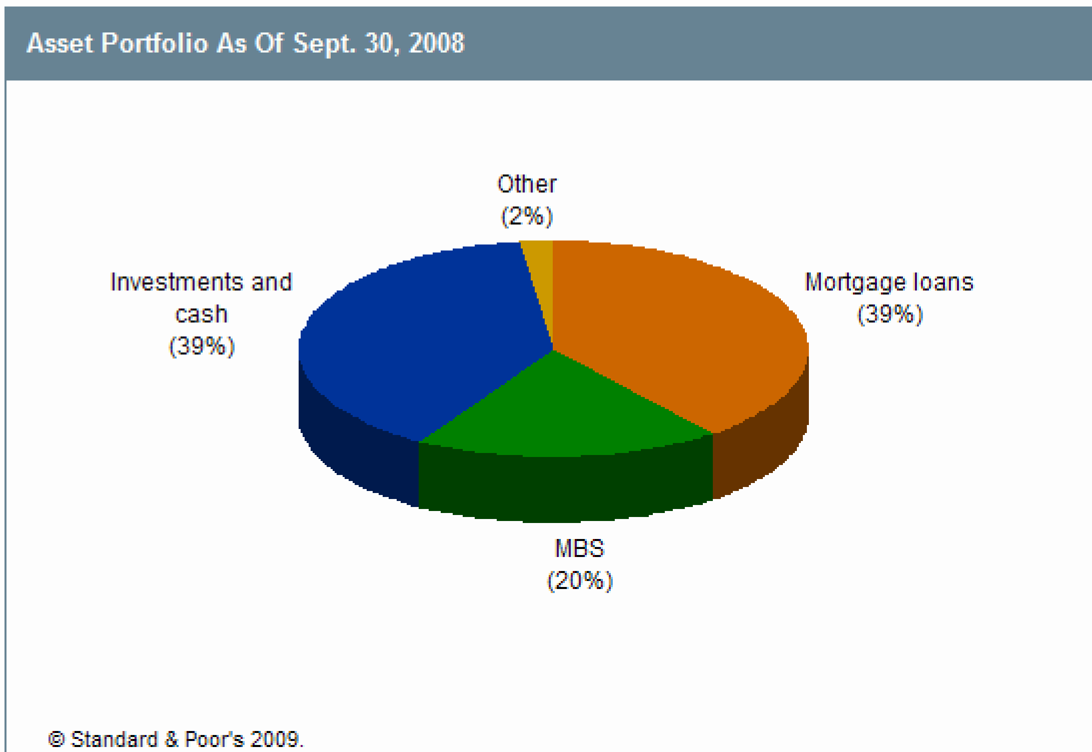

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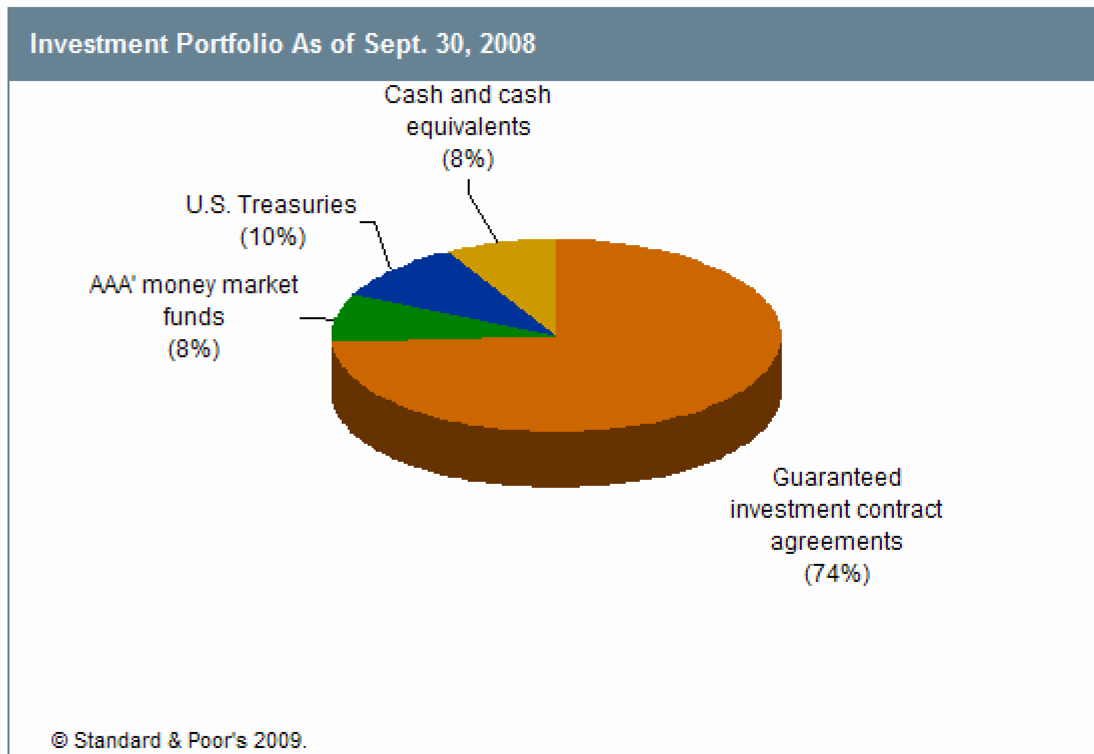
Chart 3



Earnings Quality And Financial Strength

As of Sept. 30, 2008, the agency's total revenues were $81 million, a substantial 16% decline over fiscal year 2007. The decline in the total revenue was due to a 24% drop in investment income attributed to drop in the short term interest rates in the U.S. The agency also saw a decline of 29% in other income derived from fees, service project receipts and other small sources of revenue. The other income also included HUD Section 8 housing assistance receipt which saw a significant decline in 2008 as a result of the agency no longer participating in the section 8 program.

DCHFA saw a decrease in total expenses to $78 million in fiscal year 2008, following an 8% decline over fiscal year 2007. This is due to the agency no longer participating in the Section 8 program. Although the interest expense had increased by 7% due to increased bond issuance, Standard & Poor's believes the increase was somewhat nullified by the substantial decline in the housing assistance payments from the section 8 program. In addition the agency's net income declined to $2.9 million following a 69% decline over fiscal year 2007. DCHFA's profitability, measured by return on average assets (ROA), decreased to 0.22% in 2008 from 0.75% in 2007. The agency's net interest margin (NIM) decreased significantly to 0.01% in 2008 from 0.79% in 2007 (see table 1). Standard & Poor's attributes reductions in return on assets (ROA) and net interest margin (NIM) with drop in investment income which corresponds with recent market conditions as experienced by other housing finance agencies. As exhibited in table 2, the five-year averages of DCHFA's profitability and leverage ratios are lower than the average of other rated housing finances agencies (HFAs) in the 'A' category. However, this is not an area of concern, given the low risk profile of the agency's existing asset base. At the end of fiscal year 2008, DCHFA's equity base was $100 million,

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following a 6% increase over fiscal year 2007. As of Sept. 30, 2008, its equity base represents 7.4% of total assets and 8.6% of total debt (see chart 4).

Although DCHFA's capitalization is lower than that of other HFAs in the 'A' category (see table 2 and table 3), given its zero loan losses, Standard & Poor's assessment of the agency's capital adequacy ratios as sufficient at the 'A-' level. After adjusting for potential losses, the agency's unrestricted equity, as a percentage of debt, was 16.7% and its liquid assets are 6.5% of mortgage loans outstanding.

Chart 4

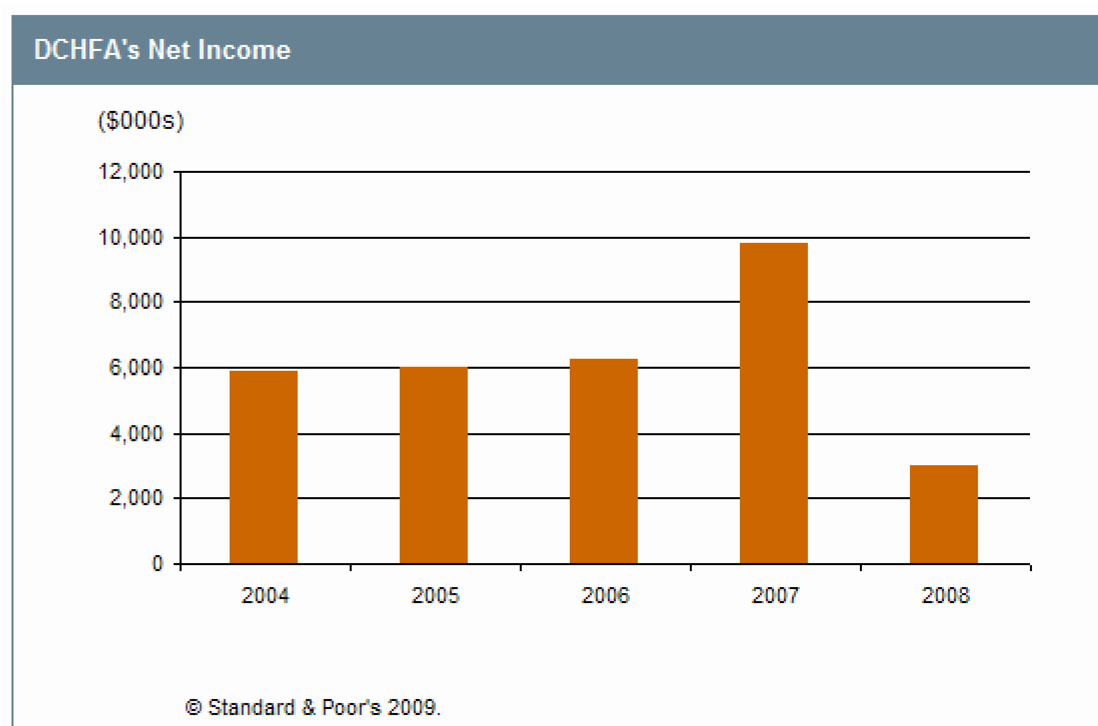

Table 1

Financial Ratio Analysis

	2004	2005	2006	2007	2008	Five-year average
Profitability (%)						
Return on average assets	0.55	0.57	0.52	0.75	0.22	0.52
Return on assets before loan loss provision and extraordinary item	0.70	0.54	0.51	0.90	0.22	0.57
Net interest margin	0.60	0.64	0.42	0.79	0.01	0.49
Asset quality (%)						
NPAs/total loans and real estate owned	0	0	0	0	0	0
Loan loss reserves/total loans and MBS	0	0	0	0	0	0
Loan loss reserves/NPAs	0	0	0	0	0	0
Leverage (%)						
Total equity/total assets	8.54	7.77	6.70	7.08	7.44	7.51
Total equity and reserves/total loans and MBS	15.23	15.20	13.60	12.99	12.53	13.91

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Table 1

Financial Ratio Analysis (cont.)							
Liquidity (%)							
Total loans and MBS/total assets	56.05	51.11	49.23	54.52	59.35		54.05

NPAs-nonperforming assets.

Table 2

Five-Year Average Financial Ratios (2003-2007)

	DCHFA	All 'A+' HFAs	All HFAs
Profitability (%)			
Return on average assets	0.52	0.65	0.83
Return on assets before loan loss provision and extraordinary item	0.57	0.75	0.92
Net interest margin	0.49	0.94	1.34
Asset quality (%)			
NPAs/total loans and real estate owned	0	3.32	2.52
Loan loss reserves/total loans	0	2.06	1.91
Loan loss reserves/NPAs	0	70.41	700.12
Leverage (%)			
Total equity/total assets	7.51	11.62	16.79
Total equity and reserves/total loans	13.91	20.57	26.68
Liquidity (%)			
Total loans/total assets	54.05	64.12	67.62

NPAs-nonperforming assets.

Table 3

Trend Analysis

	2004	2005	2006	2007	2008
Total assets ($000s)	1,005,839	1,125,091	1,282,167	1,332,637	1,346,011
% change	(9.61)	11.86	13.96	3.94	1.00
Total debt ($000s)	875,498	987,053	1,105,422	1,138,323	1,167,051
% change	(5.08)	12.74	11.99	2.98	2.52
Total equity ($000s)	85,852	87,375	85,873	94,392	100,128
% change	7.03	1.77	(1.72)	9.92	6.08
Revenues ($000s)	75,155	78,356	92,403	96,180	80,632
% change	(2.96)	4.26	17.93	4.09	(16.17)
Net income ($000s)	5,856	6,030	6,233	9,771	2,984
% change	(18.33)	2.97	3.36	56.77	(69.46)
Total loans and MBS ($000s)	563,785	574,981	631,241	726,500	798,853
% change	(19.83)	1.99	9.78	15.09	9.96

Debt

The agency's debt component increased during the past few years. As of Sept. 30, 2008, DCHFA's outstanding debt reached an all-time high of $1.17 billion, following a 2.5% increase over the previous fiscal year. Of the total debt,

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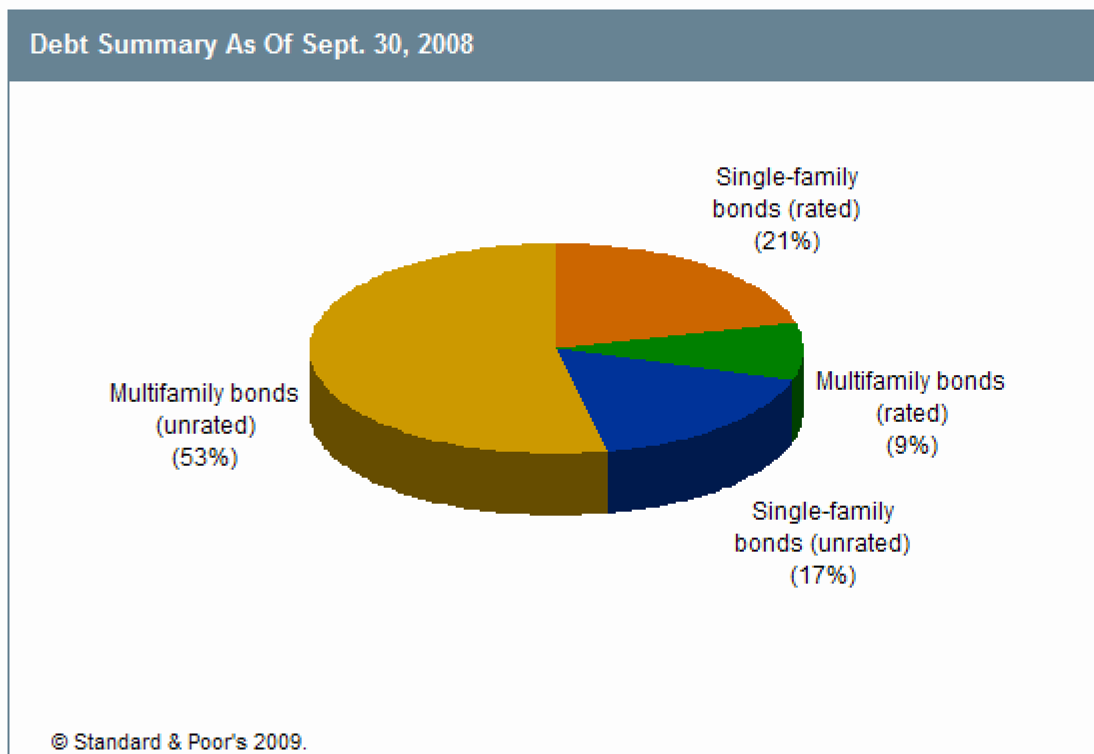
$726 million related to the multifamily conduit bonds which have no recourse to the agency, $439 million consisted of single family bonds and the balance of $1.4 million for the certificates of participation (COPs). Of the total debt, 63% are multifamily bonds and 37% are single-family bonds, most of which are issued at fixed interest rates. Of the total debt outstanding, 21% of the agency's single-family bonds, and 9% of its multifamily bonds, are rated by Standard & Poor's (see chart 5).

The agency issued COPs to finance the purchase of its office building, of which approximately $1.4 million (less than 1% of the total debt) as of Sept. 30, 2008, are payable from any of its available funds. The certificates are insured by Radian Asset Guaranty (BBB-) and have an 'BBB+' SPUR. Standard & Poor's believes the overall impact of the certificates on the agency's bottom line should be minimal. DCHFA's GO debt exposure is negligible because all of its active bonding programs carry stand-alone ratings that are higher than the ICR, due to the strength and stability of the pledged collateral, and the performance of the resolutions. As a result, the programs do not rely on the agency's general funds.

Chart 5



Management: Active And Competent

Standard & Poor's perceives DCHFA's management team and staff as active and transitioning effectively. DCHFA is governed by a five-member board of directors, appointed by the mayor and confirmed by the District Council, to serve two-year terms. The board is assisted by an experienced professional staff, headed by an executive director (secretary to the board). The management sets the goals and objectives primarily through a five-year plan and works diligently to achieve its programmatic and administrative objectives.

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Standard & Poor's continues to view DCHFA's relationship with the District Council positively, and expects this relationship to continue unabated going forward. As further evidence of the district's support for the agency, the district enacted Public Law 104-194 in Sept. 1996, which eliminated the appropriated debt and interest of the agency. This relieved the agency from the financial burden of repaying the initial funds provided to the agency to begin operating. The agency has no other loans outstanding with the district and the district has never appropriated any of the agency's funds despite difficult economic times. DCHFA is an active agency, seeking opportunities outside its local area to meet its mission to provide affordable housing. In addition to its active multifamily and single-family programs, DCHFA manages a number of housing development and rehabilitation programs designed to provide affordable housing and improve existing housing stock.

Standard & Poor's believes the two years of DCHFA's new management team is transitioning into their roles in leadership and actively taking some new initiatives to improve the performance of the agency. DCHFA plans on developing a strategic plan for implementing its five-year goals. DCHFA is considering using financing tools like Payment in Lieu of Taxes bonds (PILOT), TIF's, taxable bonds and other pooled financing options. The agency anticipates issuing its first PILOT bonds to finance townhouses in 2009. In 2009 for its multifamily program the agency is aiming toward some larger projects, and is actively seeking to work with new developers (market rate developers) in addition to typical housing developers. It is also expects to participate in priority projects for the city like the Yards, Southwest Waterfront, Northwest one and Fort Totten. DCHFA is assisting with the city's strategic plan aimed at attracting 100,000 new residents by 2020, increasing the net supply of housing by at least 55,000 units, and striving to increase the city's homeownership rate to 44% from the current 41%.The agency's business plan aims at increasing its reserves, net assets and revenue. The agency aspires to double its asset base over the next two to three years. It also aims at growing its multifamily and single-family programs, expanding agency partnership and presence in the district.

Economy: Stable

The district's economy is unique in that it is largely devoid of a manufacturing sector. Instead, as one would expect from its role as the nation's capital, it is a government town with most jobs (i.e., professional and business services; financial activities; information; trade, transportation, and utilities; and educational and health services) directly or indirectly connected to the federal sector. Government employment dominates the economy, representing nearly 34% of the District's total non-agricultural jobs. The District of Columbia's economy suffered steep job losses in February 2009, reducing its payrolls by 3,600 jobs in one month. The District's economy has been holding up relatively well during this recession, which began at the end of 2007. The information sector has led the job declines, eliminating 1,200 workers from its payrolls. The government sector, education and health sector, and professional and business services also contributed to this decline. Total payrolls in February 2009 remained above their year-earlier level. District payrolls were 1.6% higher than a year earlier (9,600 jobs). Payrolls in the District of Columbia registered significant gains in the first eight months of 2008, with more than 15,000 jobs added. The education sector, state and local government, professional business services, and leisure and hospitality services were relatively strong sectors in 2008. The public sector, directly and indirectly, continues to play a significant role in job creation in the District of Columbia's economy.

According to the Office of Federal Housing Enterprise Oversight (OFHEO), the home prices in DC have decreased by 5% in the first quarter of 2009 from levels seen in the corresponding quarter last year and decreased marginally by 1% from the previous quarter. According to the data provided by the Mortgage Bankers Association, the

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district's subprime and prime mortgage foreclosure rates have strongly diverged from one another during the first quarter of 2009. District-wide, 14.1% of subprime mortgages (compared with 14.3% nationally) entered foreclosure, while 1.5% of prime mortgages entered foreclosure (compared with 2.4% nationally). With these rates D.C. was ranked the 12th highest in subprime foreclosure rate in the U.S., while its ranking for prime foreclosures was 29th highest.

Related Research

USPF Criteria: "Housing Finance Agencies," June 14, 2007

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