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Ratings

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Housing Trust Silicon Valley, California; General Obligation

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Housing Trust Silicon Valley ICR		
Long Term Rating	AA-/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'AA-' issuer credit rating (ICR) on Housing Trust Silicon Valley, Calif. The outlook is stable.

The rating reflects our view of Housing Trust's:

- Very strong financial and capital adequacy ratios that are among the highest of publicly rated community development financial institutions (CDFIs);
- Extremely strong history of loan performance, demonstrated by a very low nonperforming assets ratio;
- Increased self-sufficiency to more than 100% in fiscal 2019, as evidenced by growth in revenue, profitability, and ability to pay operating expenses without grant funds;
- Market position in an economy with extremely strong demand for affordable housing, supported by the political and business climates; and
- Experienced and prudent management, with an updated strategy that capitalizes on the influx of capital to Housing Trust's footprint.

Partly offsetting the above strengths, in our opinion, are Housing Trust's:

- Growth in loan portfolio, affecting capital adequacy ratios in fiscal 2019, with net equity to total assets declining to 15.9% from 22.7%; and
- Exposure to early financing and predevelopment loans, which represent approximately 80% of the balance of loans outstanding. We view this as carrying inherently more risk than loans secured by cash-flowing properties.

In our opinion, Housing Trust's financial strength, management strategy, and economic profile are in line with our 'AA-' rating. We believe Housing Trust has a strong capital base and that its management and strategy drive a strong market position in the area economy, including partnerships with public and private entities that help further its mission. Housing Trust's financial position has strengthened, with its asset base and equity (i.e., net assets) growing to $75 million in fiscal 2019 from $40 million in 2015. Housing Trust's asset base continues to experience year-over-year growth, rising an average of approximately 30% a year to more than $166 million in fiscal 2019 from $52 million in 2015. While Housing Trust's asset base is smaller than that of other rated CDFIs, Housing Trust is among the highest capitalized, as measured by the ratio of its five-year average equity to total assets (61.8%). Housing Trust's most recent year net-equity-to-assets ratio was 15.9%, after taking estimated losses into account. Although Housing Trust's net income and profitability ratios have fluctuated in the past five years because of grant volatility, we believe that the high growth in assets and revenue from its loan activity and investments offsets this volatility, with total loan revenue growing 500% in fiscal years 2015 to 2019. As of June 30, 2019, Housing Trust had $109.4 million in loans outstanding, net of allowance for loan losses, its highest balance to date. In the past five fiscal years, Housing Trust has increased its loan balance by an annual average of 30%. Housing Trust maintains an average of 2.9% loan loss reserves over total loans, which is lower than that of 'AA-' rated HFAs and CDFIs (3.2% and 3.5%, respectively), but we believe that this level is commensurate with its extremely low delinquencies of 0.05% when compared with HFA and CDFI peers (3.2% and 0.7%, respectively). Last, we believe Housing Trust practices prudent risk management and has conservative lending policies compared with other CDFIs. While the majority of its assets are in the form of loans, at 62% in fiscal 2019, we believe that Housing Trust has sufficient liquidity and proactively manages its assets and liabilities, maintaining 10.5% in short-term investments to total assets, only nominally lower than the five-year average of 10.8% for CDFIs. Overall, we believe Housing Trust is well positioned to handle its planned growth and to take advantage of the influx of capital planned for housing in California in the next several years.

Outlook

The stable outlook reflects our view of Housing Trust's strategy and management, increasing asset base and capital, extremely low delinquencies, and sufficient net assets to cover potential losses. The outlook also reflects our view of Housing Trust's recent achievement of 100% self-sufficiency, eliminating its reliance on grant funding to sustain its programs.

Downside scenario

If the S&P Global Ratings-calculated adjusted-equity-over-assets ratio increases as a result of estimated losses, resulting in a reduction in capital adequacy or an increased debt burden without a commensurate increase in assets, we may take negative rating action.

Upside scenario

Conversely, if Housing Trust's loan portfolio shifts to loans that pose less risk (e.g., long-term and permanent loans), resulting in lower estimated loan losses, or if Housing Trust's adjusted net-assets-to-total-assets ratio improves beyond that of other rated CDFIs, we would consider taking a positive rating action.

Financial Strength

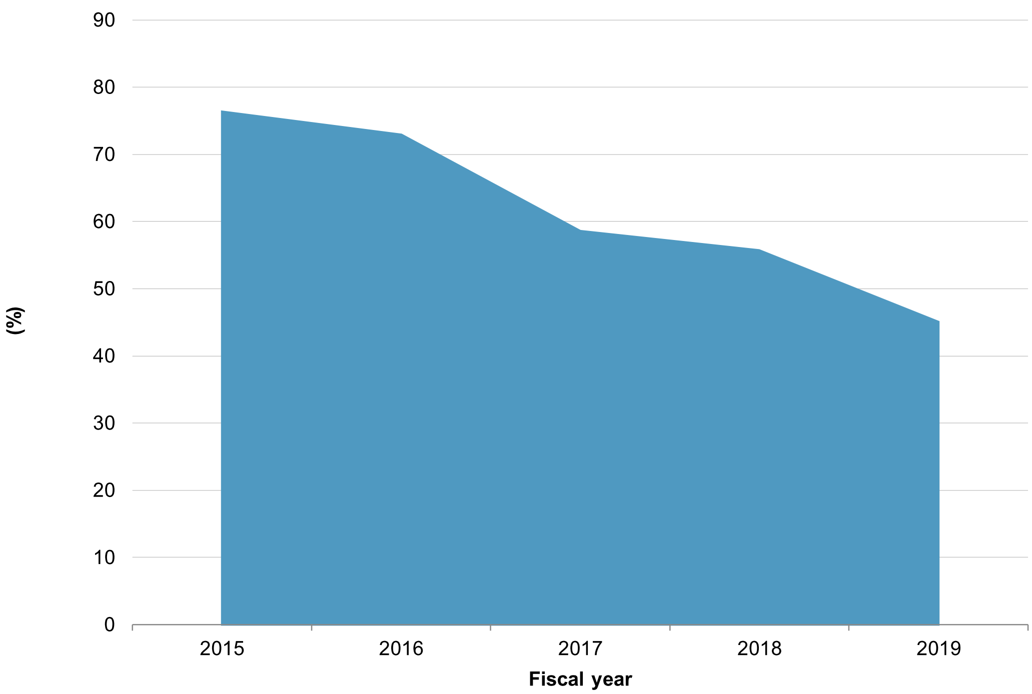
In our opinion, Housing Trust has shown improving financial strength over the past five years, despite declines in some key ratios. Capital adequacy ratios have mixed trends: While equity increased steadily from 2015 to 2019, net equity to total assets and net equity to total debt have declined as a result of loan portfolio growth and additional leverage. Additionally, while Housing Trust's profitability has fluctuated as a result of grants in the past five years, return on average assets remains well above our benchmark for its rating category.

Capital adequacy

We consider Housing Trust well capitalized with very strong capital adequacy and leverage ratios. Housing Trust's equity-to-total-assets ratio averaged 61.8% a year in fiscal years 2015 to 2018. While we consider this level extremely strong, it declined steadily year over year to 45.1% in fiscal 2019 from 76.4% in fiscal 2015. This is due to Housing Trust's strategy of leveraging and taking on more debt obligations to increase its assets.

Chart 1

Housing Trust Silicon Valley: Equity To Assets
2015-2019

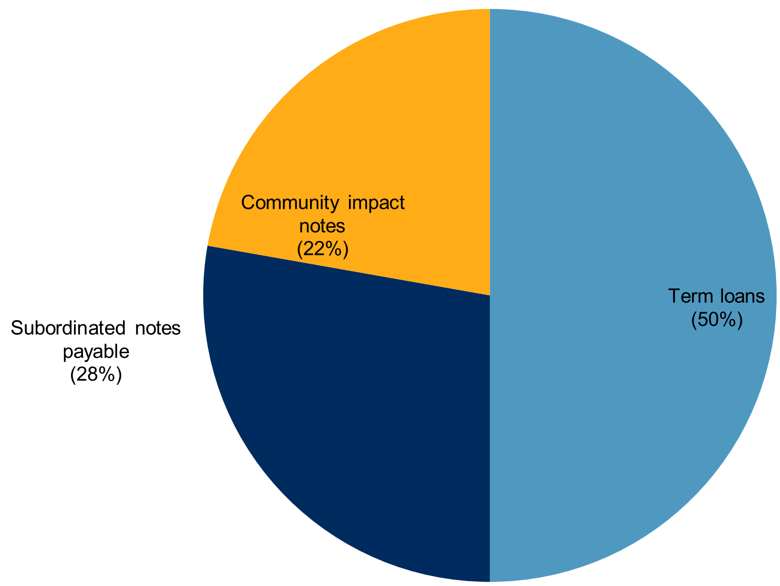


Source: S&P Global Ratings.

In the past several fiscal years, Housing Trust has increased its capacity and access to financing, but its balance sheet does not carry significant debt compared with its equity. Housing Trust's total debt outstanding grew to $75.9 million in fiscal 2019 from $44 million in fiscal 2018. This compares to $5.6 million in fiscal 2014. As a percentage of debt, total equity as a five-year average was 344.2% in fiscal 2019 compared with 451.3% in fiscal 2018. In fiscal 2017, Housing Trust secured $25 million of financing from the CDFI Bond Guarantee Fund, but did not draw down on the facility until after the close of fiscal 2019. Housing Trust's liabilities under its credit agreements include unsecured borrowings bearing a simple interest rate, of 0% to 3%, as of each borrowing date. Interest on the borrowings is payable quarterly or semiannually.

Chart 2

Housing Trust Silicon Valley: Debt Profile
Fiscal 2019



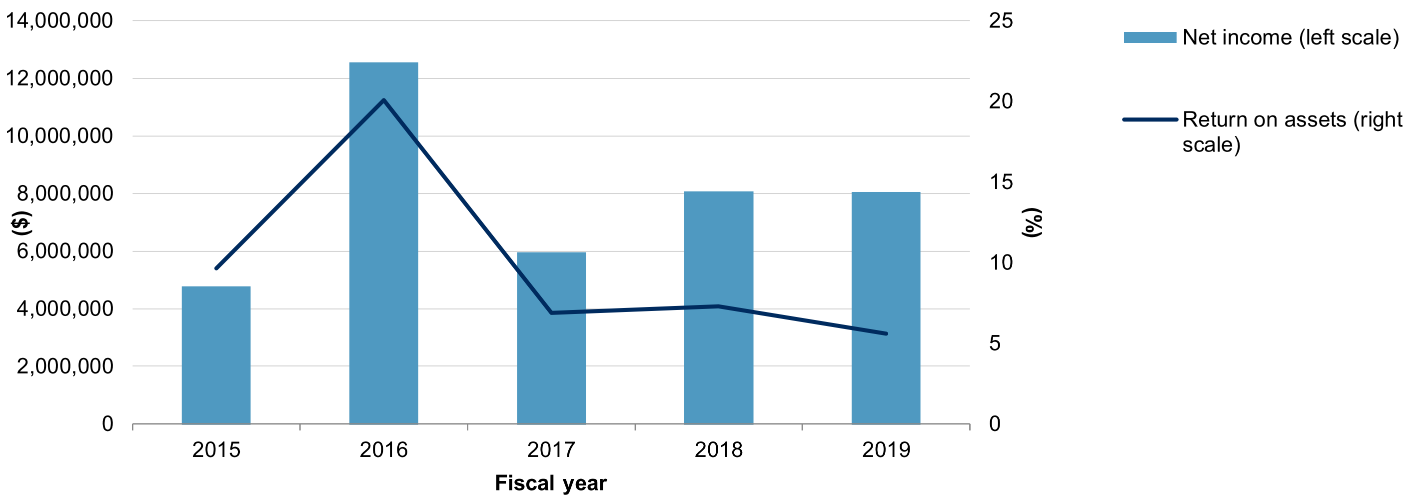
Source: S&P Global Ratings.

Profitability

Despite year-over-year volatility, return on average assets averaged 9.9% in fiscal years 2015 to 2019. We view Housing Trust's revenue stream as primarily dependent on contributions and grants, but the organization regularly applies for available grants to further its mission to stimulate community development and affordable housing activity. In 2015 to 2019, an average of 26% of Housing Trust's revenue came from nongrant sources such as interest income from loans, investment income, origination fees, and contract services. This figure rose to 45% in 2019 from approximately 15% in 2015, when we initially rated Housing Trust. In our view, Housing Trust's revenue stream has begun to diversify, as the organization continues to use contributions and grants to increase its investment returns and interest income. However, we believe the manner in which Housing Trust fulfills its mission--as with most CDFIs, using its status to apply for and use grants to create sustainable communities--could lead to year-over-year revenue stream volatility.

Chart 3

Housing Trust Silicon Valley: Net Income And Return On Assets
2015-2019

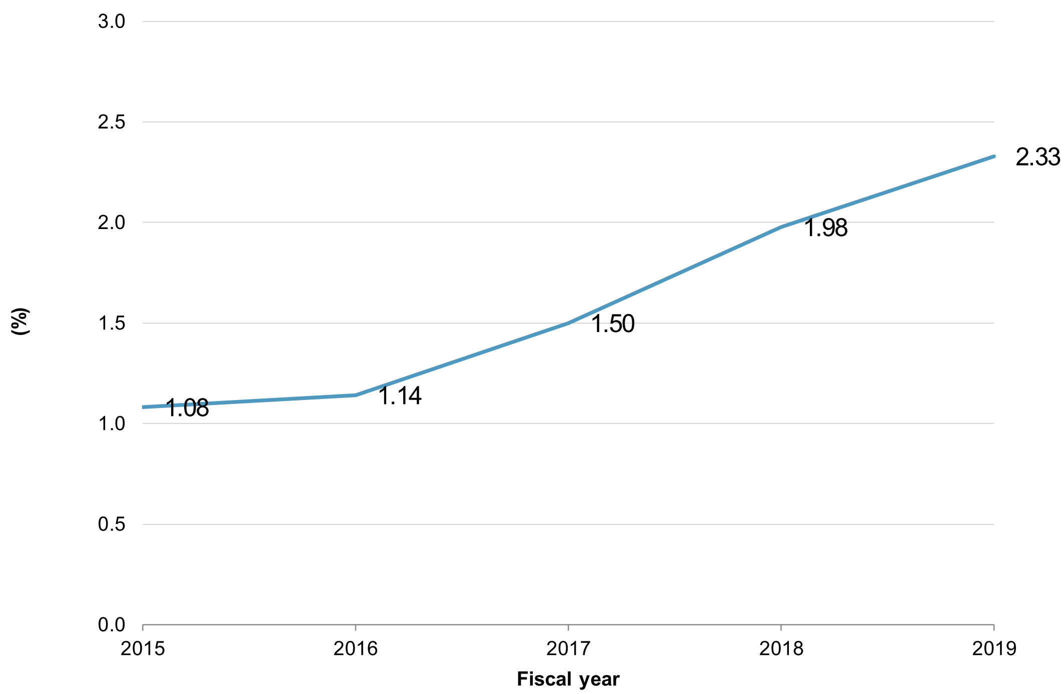


Source: S&P Global Ratings.

Housing Trust's net interest margin surpassed 2% in fiscal 2019, and the five-year average as of fiscal 2019 was 1.6% (see chart 3). While this is lower than the average for similarly rated CDFIs (3.3%), we view this as sufficient and believe that the steady growth of net interest margin demonstrates the strength of the lending portfolio.

Chart 4

Housing Trust Silicon Valley: Net Interest Margin
2015-2019

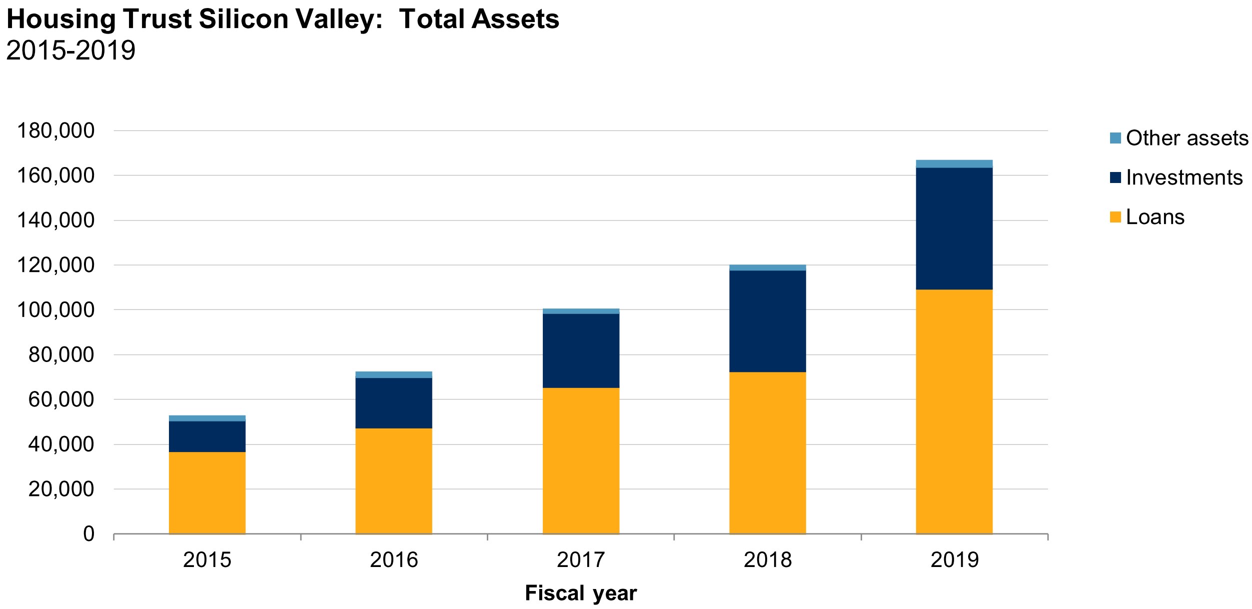


Source: S&P Global Ratings.

Asset quality

Housing Trust had $109 million in loans outstanding as of fiscal 2019, growing 50.5% compared with fiscal 2018 and more than doubling its portfolio in four years. Housing Trust has averaged a 30% average annual increase in loans for the past five years, signaling rapid growth as we have seen throughout the CDFI sector. Total assets increased to $166 million in fiscal 2019, more than tripling compared with five years prior.

Chart 5



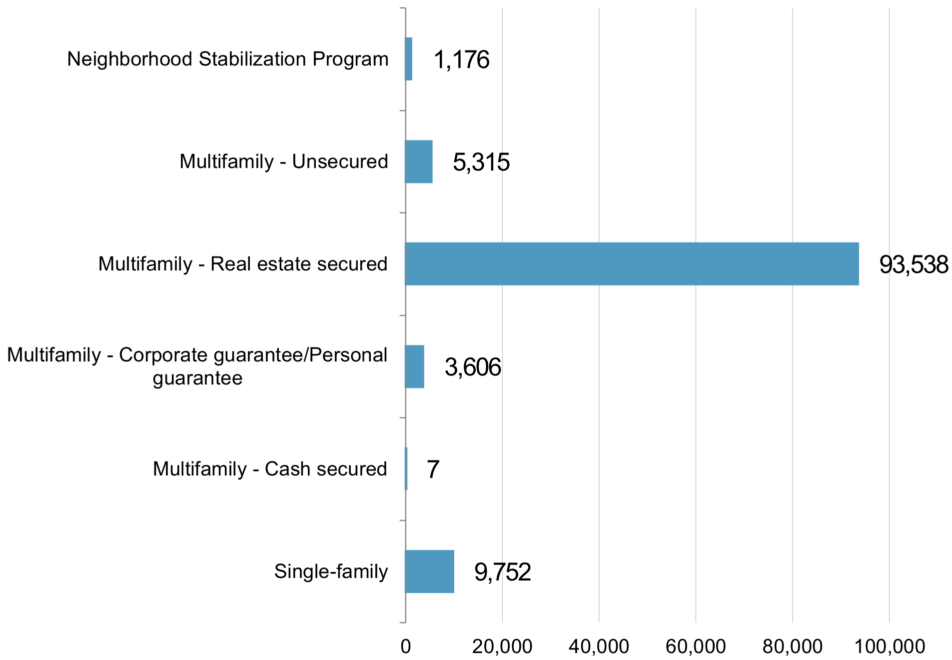
Source: S&P Global Ratings.

Housing Trust had a 3.3% loan-loss-reserve-against-all-loans ratio in 2019, with a five-year average of 2.8%, despite a history of generally low loan loss reserves. This level has increased gradually in the past five years along with Housing Trust's loan portfolio growth. In our view, Housing Trust's allowance for its loan loss practice shows the institution has prudent risk management, in line with that of similarly rated CDFIs. In evaluating Housing Trust's loan portfolio, we applied our HFA single-family and multifamily loss-coverage assumptions. These loss estimates for fiscal 2019 were approximately 46% of the total loan portfolio, which is high given the nature and percentage of non-real-estate-secured, early financing loans, or lack of data regarding loans with higher liens. While the loss estimate has declined compared with fiscal 2018, it is high compared with Housing Trust's loan delinquency history. Nonetheless, Housing Trust's capital position after consideration of these losses continues to be one of the healthiest we have seen in the sector.

As noted in chart 5, the majority of Housing Trust's loans are for multifamily projects and are real estate secured. Over 50% of the loan portfolio is secured by real estate and a first lien. Housing Trust's risk rating and lending policies are conservative, in our view, compared with those of similarly rated CDFIs.

Chart 6

Housing Trust Silicon Valley: Loan Portfolio
Fiscal 2019



Source: S&P Global Ratings.

Liquidity

We believe Housing Trust has adequate liquidity, with its short-term investments to total assets hovering at 10% to 12% in the past five years. Short-term investments over total assets was 10.3% in fiscal 2019, up from 9.9% in fiscal 2018. Total loans to total assets is 65.7% and averages 65.6% from fiscal 2015-2019. While these levels are slightly worse than those of CDFIs in that rating category, Housing Trust also has access to approximately $10 million in unused external liquidity, which we view as a credit positive.

Management, Legislative Mandate, Or Federal Designation

Housing Trust, formally known as Housing Trust of Santa Clara County Inc., is a 501(c)(3) corporation incorporated on May 22, 2000 and headquartered in San Jose, Calif. Housing Trust is the sole member of LTOA LLC, a California-based limited-liability company formed on July 2, 2012. Housing Trust is leading the effort to create a strong affordable housing market in 13 counties of Silicon Valley and the greater Bay Area. From the homeless to renters to first-time homebuyers, Housing Trust assists a wide range of residents with programs across the entire spectrum of housing issues. Housing Trust Housing Trust is a direct lender for affordable housing, community development, and other nontraditional credit needs, using its financial expertise and extensive private and public sector partnerships so that local residents can secure stable and affordable housing. Housing Trust was designated by the U.S. Department of the Treasury as a CDFI in September 2013.

Housing Trust is overseen by an active 16-member board of directors, all of whom are voting officers serving three-year terms. Housing Trust plans to bring on new board members and increase the total number of members to 21 in the coming years. Board members come from a wide array of backgrounds with several affordable housing finance experts, real estate developers, and lenders at respected financial institutions. An established senior management team--consisting of the CEO, chief financial officer, chief lending officer, chief compliance and risk officer, and chief development officer--supports the board, which has six committees. In 2019, Housing Trust hired a chief lending officer with years of CDFI experience, deepening its leadership capacity. Housing Trust also has a formal succession plan with planned transitions in place for normal and emergent circumstances. Senior staff members work closely with one another to meet Housing Trust's mission and to bring operations and projects into compliance with overall strategic goals. Housing Trust has institutionalized internal policies and procedures built into the fabric of all operations.

Since its inception, Housing Trust has made funds available for the purchase of more than 2,500 homes under its first-time homebuyer program and 9,760 affordable multifamily homes under its rental housing program, and has helped more than 7,200 individuals under its homelessness prevention and assistance program. Housing Trust has also provided security/utility deposit assistance grants for individuals considered either homeless or at risk of homelessness.

While CDFIs are somewhat susceptible to year-over-year government grants and private contributions, which could be nonrecurring, Housing Trust has reduced its dependency on grants overall. Housing Trust steadily improved its self-sufficiency as a percentage of operating revenue over operating expenses, calculated by S&P Global Ratings, to 109%, in 2019 from 96.8% in 2018. This compares to slightly less than 60% in 2015.

In our view, Housing Trust's vision is clearly defined and sets forth the organization's overall strategic plan. This plan covers a variety of topics, including Housing Trust's effect on the community it serves, organizational growth, and scope and financial stability. The plan was updated in 2019 to clarify Housing Trust's mission and vision, include the following strategic objectives: build on success of its core lending programs, adjust the business model to balance sustainability with innovation, launch lending programs that provide housing for people who otherwise would not be helped, and expand the long-term organizational capacity necessary for lending innovation and investor engagement. We view these objectives as value added and focused on Housing Trust's mission.

In addition, we believe collaboration with public and private partners, external relations, and financial self-sufficiency show the organization has solid growth potential. Public support is vital to Housing Trust's continued success because public and private partners play a key role in augmenting its finances. This includes partnerships with local businesses that contribute annually, nonprofits with which Housing Trust works to facilitate community programs, and banking partners that Housing Trust can leverage for access to affordable capital. Housing Trust's primary value is providing equal access to credit to create affordable housing in neighborhoods of all income levels and ethnicities. We view their commitment to community development as relates to the organization's core values, mission, and overall strategy and management as very strong. Housing Trust also has a wide array of donors to help fulfill its mission with the U.S

Department of Housing and Urban Development and Santa Clara County as its top donors over the past five years. Housing Trust also recently announced large investments by Google Inc. and Apple Inc. in its programs to support affordable housing in the greater San Francisco Bay Area. As indicated in our report "Home Is Where The Funding Is: West Coast Housing Issuers And The Recent Capital Flow," published Oct. 10, 2019 on RatingsDirect, the planned capital infusion on the West Coast--especially in California--could strengthen financial profiles for organizations such as Housing Trust.

Economy

According to IHS Global Insight, Employment growth in California edged upward for the second consecutive quarter. In the third quarter of 2019, nonfarm payrolls advanced 1.8% year over year, slightly faster than the 1.7% pace set in the second quarter and ahead of the 1.4% pace in the first. Resurgence in both the construction and information sectors relative to early 2019 provided much of the boost. Job growth helped push the unemployment rate down in September to 4%, its lowest level in the postrecession era.

Every major sector of the California labor market added jobs over the past year. Manufacturing payrolls ticked up 0.9% on strength in the durables segment, particularly the computer and electronics products category, which added 4.6% year over year. The construction sector added 3.9%, its largest increase since the end of 2018. The information sector gained 2.7%. Payrolls in the professional and business services sector increased 3%. Education/health services and leisure/hospitality services payrolls climbed 2.9% and 2.3%, respectively. The public sector added 1.5%. The finance and trade/transportation/utilities sectors both turned in underwhelming performances, but managed to remain in positive territory.

In 2018, California's real gross state product grew 3.5% compared with 2.9% growth for GDP. Per capita GSP, at $75,034, edged up to 120% of GDP in 2018 from 116% in 2016. State population growth, which had been above the U.S. level until 2016, grew 0.4% in 2018 to 39.6 million, but less than the 2018 national growth rate of 0.6%. The state is younger than average; its age dependency ratio of 58.3% is below the nation's 61.8% and has risen more slowly than the nation's in recent years.

On the housing front, low supply of existing homes for sale combined with strong demand keep home values in California rising rapidly, leaving homeownership out of reach for many households whose incomes are not able to keep up. According to the Federal Housing Finance Agency, home prices rose by 8.5% year over year in the fourth quarter of 2017. Prices now stand at 94.3% of their peak during the bubble in the second quarter of 2006. At the end of the second quarter of 2019, total loans in foreclosure in the state averaged 0.3% against a national average of 0.9%, ranking the state 48th. Conventional loans in foreclosure averaged 0.3% (compared with the national average of 0.8%). Given the increasing affordability gap, the market for Housing Trust's loans remains strong and the increasing need for affordable housing bodes well for Housing Trust's mission and programs.

Housing Trust Silicon Valley: Financial Ratios 2015-2019

	2015	2016	2017	2018	2019	Average
Leverage (%)						
Total equity (net assets)/total assets	76.38	72.94	58.63	55.78	45.06	61.76
Net equity/total assets	N/A	N/A	N/A	22.70	15.93	19.31
Total equity + reserves/total loans	105.59	107.55	86.05	88.39	64.95	90.51
Total equity/total debt	603.62	608.27	259.03	150.91	98.92	344.15
Net equity/total debt	N/A	N/A	N/A	61.41	34.97	48.19
Profitability (%)						
Return on average assets	9.63	20.07	6.87	7.29	5.59	9.89
Return on assets before loan loss prov & extraordinary items	8.47	17.96	6.34	7.44	5.63	9.17
Return on average equity	12.54	26.99	10.62	12.78	11.29	14.84
Net interest margin	1.08	1.14	1.50	1.98	2.33	1.61
Net interest margin (loans)	1.38	1.45	1.41	2.22	2.39	1.77
Asset quality (%)						
NPAs/total loans + REO	0.00	0.06	0.15	0.02	0.01	0.05
Net charge-offs/average NPAs	0.00	167.32	10.31	0.00	130.00	61.53
REO/total loans	0.00	0.00	0.00	0.00	0.00	0.00
Loan loss reserves/total loans	2.70	2.53	2.56	3.28	3.33	2.88
Loan loss reserves/NPAs	0.00	4,029.18	1,745.91	15,866.67	24,310.00	9,190.35
Net charge-offs/average loans	0.19	0.06	0.01	0.00	0.02	0.06
Liquidity (%)						
Total loans/total assets	70.54	65.93	65.58	60.53	65.65	65.64
Short-term investments/total assets	10.22	12.38	9.41	9.93	10.32	10.45
Long-term investments/total assets	15.86	18.74	23.58	27.83	22.48	21.70
Total investments/total assets	26.08	31.12	33.00	37.75	32.80	32.15
Other assets/total assets	3.38	2.95	1.42	1.71	1.55	2.20

NPA--Nonperforming asset. REO--Real estate owned.