

Iowa Finance Authority; General Obligation

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Credit Profile

Iowa Fin Auth ICR
Long Term Rating

AA/Stable

Affirmed

Rationale

Standard & Poor's Rating Services affirmed its 'AA' issuer credit rating (ICR) on Iowa Finance Authority (IFA). In addition, Standard & Poor's affirmed its 'AA' long-term rating on the authority's general obligation debt. The outlook on all ratings is stable.

The rating is based on our opinion of the following strengths:

- The extremely high quality and very low-risk profile of the authority's asset base;
- Very consistent profitability ratios that are in line with other 'AA' rated housing finance agencies;
- Minimal GO debt exposure; and
- An active management team with strong legislative support.

Offsetting these strengths, in our view, are the following:

- Declining equity over the last six years, which has reduced IFA's capital below comparable 'AA' rated housing finance agencies (HFAs), and
- Reduced profitability over the last two years, in line with the experience of other HFAs.

IFA continues to improve asset quality by originating all single family-loans as securitized MBS with 'AAA' support from Fannie Mae or Ginnie Mae. The authority has decreased loan production, but assets continue to grow as investments increase. An offsetting increase in debt has reduced equity to ratios not experienced at least since 1997. In 2008, IFA completed a five-year plan that emphasized growth, which resulted in lower equity. The authority expected to slow its growth, which we expected to lead to higher equity ratios. However, the authority continued to grow and IFA now finds itself with equity levels more in line with 'AA-' rated HFAs. Part of the recent increase in assets and liabilities results from the authority New Issue Bond Program (NIBP) and a limited obligation note from the Federal Home Loan Bank. These are relatively new initiatives that will expire or that the authority may phase out in the near term.

IFA recognizes its declining equity and has stated its desire to build its ratio to more typical 'AA' levels. Preliminary financial statements for fiscal 2011 show an increase in equity as a percent of assets. Furthermore, IFA's capital adequacy ratios reflect a low risk profile consistent with its current rating. We believe that IFA's equity ratios will strengthen as the new initiatives mentioned above vacate the HFA's balance sheet.

Outlook

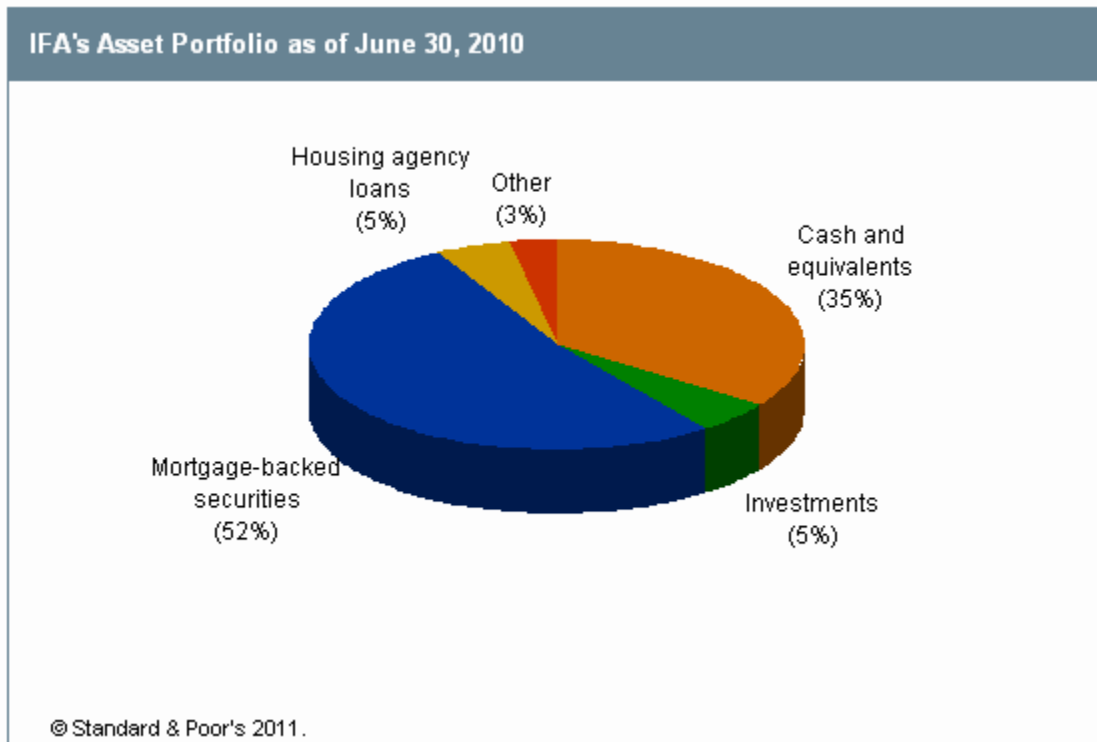
The stable outlook reflects IFA's low-risk equity base and high capital adequacy ratios. IFA's extremely low-risk assets provide stability, and we expect this aspect of the HFA to remain a strength in all real estate markets. Should equity as a percent of assets continue to decline, a negative rating action could result. If equity increases, IFA's ratios

could return to a level more in line with similarly rated HFAs and the rating should remain unchanged.

Asset Quality: High Quality MBS

The authority's balance sheet continues to grow despite a loss in mortgage assets. As of June 30, 2010, the authority's asset base was at an all-time high of \$1.64 billion, a 20% increase from the previous fiscal year. The reason that IFA's assets grew was a large increase in investments of \$380 million in fiscal 2010, the highest dollar increase on record for IFA. The increase was partly the result of unexpended bond proceeds from the New Issue Bond Program, the entirety of which represents \$169 million in assets and liabilities. Another contributor was a Federal Home Loan limited obligation note in the amount of \$122 million. This offset a decline of \$111 million in the MBS and loan pool. Since 2002, the authority's assets have increased by at least 10% every year except 2004 and 2009, with an average growth of 16%. The assets and other financial information Standard & Poor's used for this analysis exclude the state revolving fund that IFA administers as well as any conduit bond issues, which have no recourse to the authority.

Chart 1

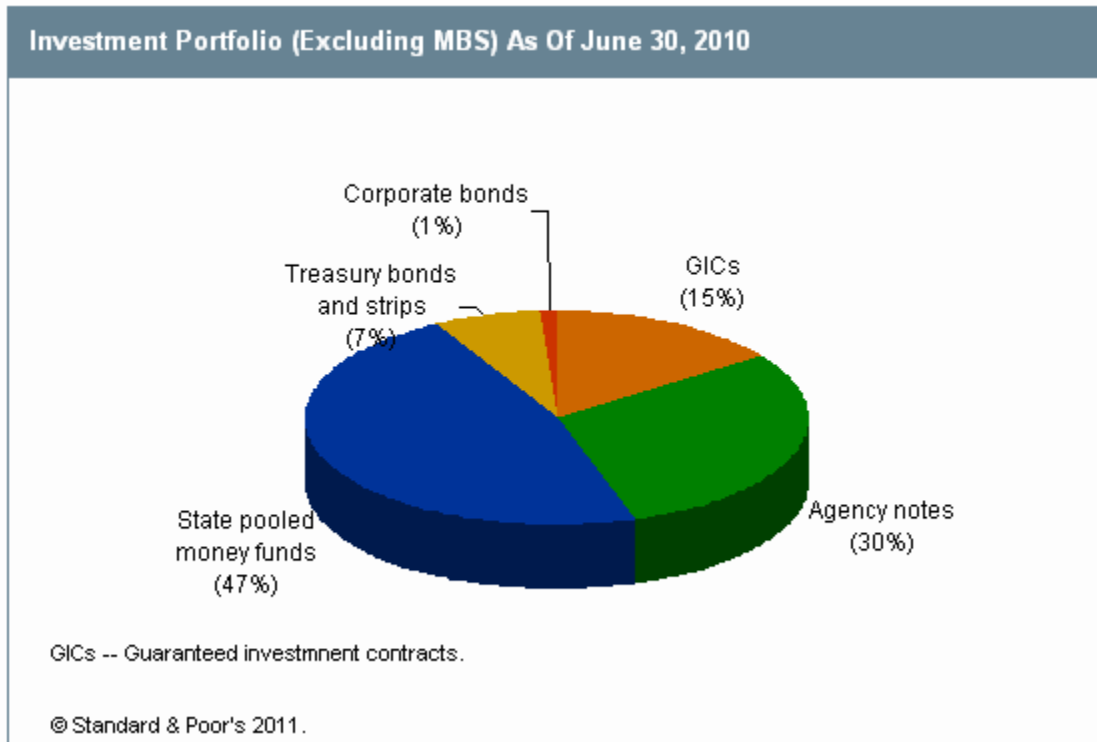


Around 53% of the authority's asset portfolio consists of 'AAA' MBS, the lowest proportion since 2001 and a drop from 68% in 2009. Fiscal 2009 was the second in a row in which combined MBS and loans declined, following eight years of consecutive growth. We anticipate that as NIBP issues transition into a permanent, non-escrow phase, MBS will become larger in number and as a percentage of assets. At the end of fiscal 2010, IFA's loan portfolio consisted of Ginnie Mae and Fannie Mae MBS (91%) and 7% multifamily and single-family mortgage loans. This proportion of MBS is the lowest since 2002 but remains high in comparison to most HFAs. The decline was a result of a dearth of single-family MBS origination and the financing of multifamily non-MBS loans.

We believe that IFA's loan portfolio poses an extremely low risk due to the authority's conservative approach to collateral. As of June 30, 2010, more than 99% of IFA's single-family loans were backed by Ginnie Mae and Fannie Mae MBS. As Standard & Poor's expected, delinquencies and nonperforming assets as of June 30, 2010, were a miniscule 0.1% of total loans and MBS, representing just \$54,000 of loans 60 days or more delinquent or in foreclosure.

Since MBS guarantees payment on the underlying loans, no reserves are required. However, for the remaining loans, IFA has provided reserves to cover potential credit losses on the portfolio. In our opinion, these loans are performing well and have sufficient excess assets that cover any credit shortfall or liquidity issues.

Chart 2



IFA's investments as of June 30, 2010 are, in our view, of high credit quality and provide sufficient liquidity, 88% of which consists of investments in government securities rated 'AAA'.

Management takes what we consider a conservative approach to the oversight and monitoring of the authority's investments. IFA's investments provided just 3.9% of total revenues in 2010, which was very low in our view compared to fiscal 2008, which itself was lower than previous years, at 12.7%. IFA's investment income was just \$6.3 million, the lowest amount on record since 1997, translating to a return on investments of just 0.96%. This decline is due to lower yields on investments, a common occurrence among HFAs.

Earnings Quality And Financial Strength: Stable Revenues

IFA's total revenues have increased steadily and have more than doubled since 2007; much of the increase attributable to grant income. As of June 30, 2010, the authority's total revenues stood at \$160 million, a 25%

increase over 2009, which was 43% higher than 2008. This increase is attributable to a 64% rise in other income, mostly from \$84 million in grant income, which was an increase from \$8 million and \$46 million in fiscal 2009 and 2010, respectively. Expenses had a corresponding increase of 25% over 2009, which was 53% higher than 2008. The cause of this growth was an increase in grant expenses to \$87 million, up from \$14 million and \$50 million in fiscal 2009 and 2010, respectively. Otherwise, income from loans declined \$6.2 million and income from investments declined about \$600,000.

In fiscal 2010, the authority's net income was \$7.7 million, a 15% increase from the previous fiscal year, but a decrease of 22% from 2008. Net income was impacted by the decline in investment income over the last two years.

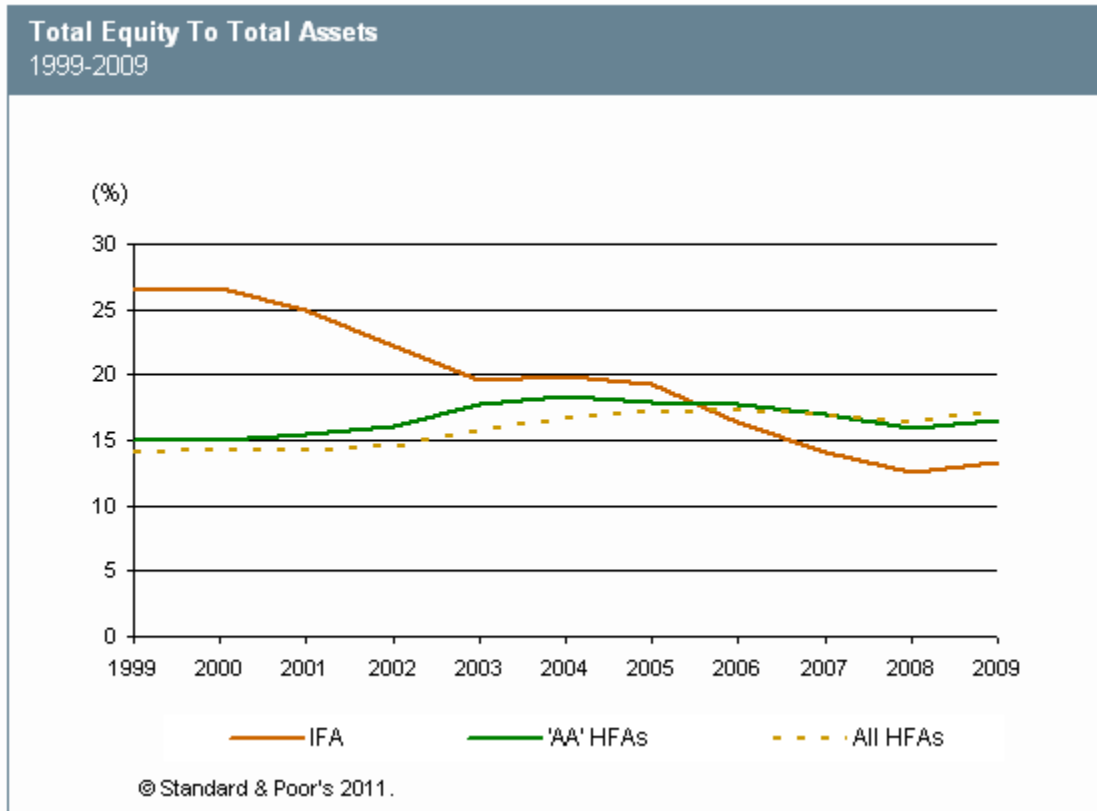
IFA's profitability, as measured by return on assets, increased to 0.51% in 2010 from 0.43% in 2009, while net interest margin (NIM) remained essentially unchanged at 0.69%. These results are well below the norm for IFA, yet the decline is typical for HFAs given current interest rates on loans and investments. But IFA compares favorably to many HFAs in that it has remained profitable over the last two years, and its profitability ratios, while low, have stopped declining. As detailed in table 1, the five-year average of the authority's profitability ratios is similar to those of its 'AA' rated peers, despite a low-risk profile.

Table 1

Five-Year Average Financial Ratios (2005-2009)					
	IFA	All 'AA' HFAs	All 'AA-' HFAs	All 'AA+' HFAs	All HFAs
Profitability (%)					
Return on average assets	0.87	0.71	0.63	0.96	0.72
Return on assets before loan loss provision and extraordinary item	0.89	0.94	0.65	1.05	0.83
Net interest margin	1.08	1.20	1.15	1.85	1.28
Asset Quality (%)					
NPAs/total loans and real estate owned	0.14	4.05	1.00	1.75	2.72
Loan loss reserves/total loans	0.29	2.73	0.62	1.78	1.93
Loan loss reserves/NPAs	264.26	107.51	82.56	4,433.72	813.14
Leverage (%)					
Total equity/total assets	15.10	17.02	14.07	25.92	17.05
Total equity and reserves/total loans	19.73	26.55	20.21	38.46	25.95
Liquidity (%)					
Total loans/total assets	74.99	72.36	72.74	71.94	71.50

IFA's equity grew for the ninth consecutive year. Even though IFA's equity grew during most of the decade, a faster growth in liabilities for the last six years has reduced IFA's equity as a percentage of assets to 11.39%. As a result, IFA's ratio is more in line with a 'AA-' rating. While the HFA's growing balance sheet has diluted equity on a percent basis, much of this growth is associated with the NIBP and FHLB programs described above. As these programs end we expect equity ratios to increase. Furthermore, we believe the authority's equity base is adequate, however, to support its low-risk profile. After adjusting for potential losses, the authority's unrestricted equity as a percentage of debt is 22.54%, above Standard & Poor's threshold of 4.0%, and its liquid assets are 221.5% of loans, in excess of the 2.0% of mortgage loans outstanding. Even though we are comfortable with IFA's equity position as it is projected to change, we are concerned with the long-term decline in equity and will monitor this trend to see if it merits a change in the rating.

Chart 3



Debt: Moderate Risk

As of June 30, 2010, IFA's debt outstanding totaled \$1.32 billion, up 8% from the preceding year and the highest ever.

The issuance of single-family bonds to finance the purchase of MBS under the U.S. Treasury's New Issue Bond Program and First Home Program accounts for the increase in debt. Of the total, 96% are single-family bonds and 4% are multifamily bonds. All bonds issued since 1991 under the single-family First Home Program MBS resolution, which constitutes 83% of the total single-family bonds and around 80% of total debt, are rated 'AAA', which reflects our opinion of the extremely high quality of pledged collateral, which consists of Ginnie Mae and Fannie Mae MBS, the strong credit quality of investments, and cash-flow sufficiency. The remaining single-family bonds are mostly issued under the New Issue Bond Program, also backed by MBS with a government guaranty. The authority's GO debt exposure ratio is 5.73%, or low on Standard & Poor's leverage scale for HFAs. The GO debt was issued under a multifamily resolution opened in 2006.

At the end of June 2010, 39% of the IFA's debt was variable rate, and 37% of single-family debt was variable rate. Sixty percent of IFA's \$361 million in variable-rate, single family bonds have liquidity through the Federal Home Loan Bank of Des Moines (AAA/Stable/A-1+), Wells Fargo Bank, N.A. (AA/A-1+) covers 33% of the variable-rate demand obligations, and State Street Bank and Trust (AA-/Stable/A-1+) provides liquidity support for the remaining 7%. The much smaller multifamily bond program includes \$25 million in variable-rate debt, all with liquidity from

Dexia Credit Local (A/Negative/A-1).

IFA has hedged nearly all of its floating-rate exposure through interest rate swaps and caps entered into with either UBS AG (A+/Stable/A-1) or Goldman Sachs Capital Markets LP, with a guarantee from The Goldman Sachs Group (A/Negative/A-1). Following a review of IFA's 19 interest rate swaps, two basis swaps, and four interest rate caps and corridor transactions, Standard & Poor's assigned the authority a Debt Derivative Profile (DDP) score of '2' on a four-point scale, in which '1' represents the lowest risk and '4' the highest risk.

The overall score of '2' reflects our opinion of:

- Two adequately rated swap counterparties, both of which are required to post collateral before a credit event occurs;
- Low basis risk;
- Low termination risk; and
- Good management oversight.

We believe management is proactive in monitoring risks and benefits associated with swaps, so that the authority's exposure to either of its counterparties does not exceed a defined amount. Standard & Poor's is not factoring in the value at risk as a contingent liability at this time due to what we consider the remoteness of involuntary termination.

Management: Experienced And Active

The authority has its third executive director in three years following the most recent appointment to the post in December 2010. While we consider IFA to have an experienced professional staff, we would like to see greater stability at the most senior executive position. We will monitor this development and make further comment if warranted.

The authority also administers, in partnership with the Iowa Department of Natural Resources, the State Revolving Fund (SRF), which issues tax-exempt bonds to finance wastewater and drinking water facilities. The SRF bonds are rated 'AAA' based on the large size and diversity of the SRF program's loan portfolios, program coverage and reserve levels, structural features, and a management team with a proven track record. Standard & Poor's analysis of the authority's ICR excludes the activities of SRF, as its funds are legally obligated to the program and hence do not contribute to IFA's finances.

IFA's title guaranty division (TGD) was established in 1985 to guarantee title to property in Iowa. The TGD is considered when evaluating IFA's ICR, as surplus funds from TGD, in accordance with state code, are available to support IFA's affordable housing activities. We believe the risk associated with title guaranty to IFA's ICR is minimal, as adequate reserves and reinsurance are in place to cover potential claims.

Standard & Poor's views IFA's relationship with the state as positive and expects this relationship to continue. A tangible sign of IFA's strong relationship with the state is the growth in grant funding and associated responsibilities in 2010. In 2010 the authority received \$137 million in grant income, an increase from \$64 million 2009. The additional funding resulted from state funding for disaster relief, water quality and infrastructure projects, and increased federal funding for the American Recovery and Reinvestment Act (ARRA).

IFA has been engaged by the state during the years to take on nonhousing related activities, including serving as one

of the state's primary bond issuing authorities. In addition to its active single-family program, IFA manages a number of housing development and rehabilitation programs designed to provide affordable housing and improve existing housing stock. IFA also administers federal programs, including the Housing Assistance Fund (HAF), Affordable Assisted Living Program, home- and community-based service Program (HCBS), thus strengthening its legislative mandate.

Economy: Slow Recovery

Iowa did not experience the sharp job losses that plagued other states, but, at the same time, recovery is expected to be comparatively slow. Iowa's economy is based on services, manufacturing, and agriculture. According to IHS Global Insight, the strength of Iowa's agricultural, education/health services, and finance sectors helped partially offset declines in manufacturing, lessening the recession's impact on Iowa's economy. Forecasts show services will continue to be a growth driver as the state emerges from the recession. Unemployment in the state is at a peak of 6.69%, still well below the national rate, and is projected to fall in 2011 and beyond.

We believe that IFA's loan portfolio is well-positioned for any real estate market, given its nearly exclusive securitization from 'AAA' MBS with U.S. government support. Global Insight expects housing demand to increase slightly in 2011 before accelerating the next few years. By 2014 Global Insight expects housing starts to reach more than 11,000, which would surpass the activity in 2007. Home prices never declined significantly and remain above 2008 levels. Iowa is ranked 34th in the percent of loans in foreclosure in the fourth quarter of 2010 and ranks 48th in the percentage of subprime loans in that period. Global Insight projects an average price increase of 3.4% through 2014. We believe higher demand for housing could impact the size of the loan and asset base, but would not affect the agency's real estate, which is mostly guaranteed from the 'AAA' MBS.

Table 2

Financial Ratio Analysis						
	2006	2007	2008	2009	2010	5-Year Average
Profitability (%)						
Return on average assets	1.00	0.89	0.78	0.43	0.51	0.72
Return on assets before loan loss provision and extraordinary item	0.97	0.88	0.71	0.42	0.51	0.70
Net interest margin	1.20	1.21	1.10	0.70	0.69	0.98
Asset Quality (%)						
NPAs/total loans and real estate owned	0.10	0.10	0.18	0.23	0.01	0.12
Loan loss reserves/total loans and MBS	0.33	0.28	0.21	0.19	1.11	0.42
Loan loss reserves/NPAs	314.15	292.40	113.40	81.20	19,811.11	4,122.45
Leverage (%)						
Total equity/total assets	16.41	14.07	12.48	13.28	11.39	13.53
Total equity and reserves/total loans	22.09	17.36	15.61	16.72	18.24	18.00
Liquidity (%)						
Total loans/total assets	73.22	79.76	78.91	78.56	58.88	73.87

Table 3

Trend Analysis					
	2006	2007	2008	2009	2010
Total assets (\$)	949,853	1,166,925	1,388,394	1,368,915	1,636,475
% change	25.86	22.85	18.98	(1.40)	19.55
Total debt (\$)	765,578	953,971	1,159,587	1,224,902	1,324,270
% change	31.10	24.61	21.55	5.63	8.11
Total equity (\$)	155,876	164,191	173,330	181,819	186,397
% change	7.18	5.33	5.57	4.90	2.52
Revenues	60,969	76,383	89,382	127,903	159,896
% change	9.21	25.28	17.02	43.10	25.01
Net income (\$)	8,531	9,450	9,915	5,916	7,736
% change	(12.12)	10.78	4.92	(40.33)	30.76
Total MBS (\$)	672,087	873,810	1,031,423	1,007,655	880,339
% change	31.58	30.01	18.04	(2.30)	(12.63)
NPAs (\$)	720	894	2,008	2,497	54
% change	69.00	24.22	124.57	24.37	(97.84)

Related Criteria And Research

- USPF Criteria: Housing Finance Agencies, June 14, 2007
- USPF Criteria: Single-Family Mortgage-Backed Securities Programs, June 13, 2007
- USPF Criteria: Assumptions: Update to Cash Flow Analysis for Public Finance Housing Bonds, March 3, 2009
- RMBS Criteria: U.S. Interest Rate Assumptions Revised For January 2011, Dec. 14, 2010
- USPF Criteria: Debt Derivative Profile Scores, March 27, 2006

Ratings Detail (As Of April 2, 2011)		
Iowa Fin Auth multifam hsg bnds ser 2006A		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Iowa Fin Auth var rate multifam hsg		
<i>Long Term Rating</i>	AA/A-1/Stable	Affirmed
Iowa Fin Auth var rate multifam hsg bnds ser 2007A&B		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Iowa Fin Auth Multifamily hsg bnds 2008 Ser A (AMT-var rate)		
<i>Long Term Rating</i>	AA/A-1/Stable	Affirmed

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