Background

In early to mid-2007, the convergence of several factors caused senior members of THDA's finance team to realize that more precise and longer term planning was needed to ensure that the program goals set forth in the organization's first ever strategic plan could be accomplished. Due to a renewed effort at business development and customer service, the single family mortgage program was producing record volume. THDA had created a housing trust fund, and the bulk of funding would come from excess revenues within the bond resolutions. The New Start loan program, a 0% loan made available from THDA funds to non-profits serving homebuyers of very low income, was growing. Finally, THDA had increased the availability of down payment assistance funds to its homebuyers, and those funds also came from excess revenues in the bond resolutions.

In previous years, THDA's finance team had performed simple resource projections to monitor the availability of tax-exempt volume cap, even developing a five-year analysis that would enable senior leadership to make adjustments to the mortgage program depending on the resources available. With other programs now relying on the organization's financial resources, it was determined that a more comprehensive plan was needed. The decision to develop a five-year financial plan was derived from these circumstances.

First Step – Developing Assumptions and Requirements

THDA developed assumptions in a two-category approach. The first category covered production and bond issuance assumptions, and the second category presented cash flow and other detailed assumptions and requirements. All assumptions were influenced by THDA's long-standing philosophy of a conservative, fundamental approach to business.

Considering the recent housing market turmoil, it was assumed that 2010 mortgage production would be lower than normal, with production projected to normalize in years 2011-2014. THDA used historical annual production figures to derive a $360 million "normal" annual production level that could be sustained by projected tax-exempt volume cap over the five-year period. THDA offers multiple loan products that include downpayment assistance grant options for which THDA charges a premium. Therefore, loan mix assumptions were included that fed into liquidity needs for downpayment assistance grants. Because of market conditions and trends, loan mix assumptions were more weighted towards downpayment assistance options for 2010 and 2011, returning to historical levels of fewer downpayment assistance loans for years 2012-2014.

TENNESSEE HOUSING DEVELOPMENT AGENCY
SUMMARY OF NEW PRODUCTION AND PROGRAM WITHDRAWALS
STRATEGIC FINANCIAL PLAN: 2010-2014

Fiscal Year Ending June 30	2010	2011	2012	2013	2014	Total (in thousands)
HOMEOWNERSHIP PRODUCTION:						
Bonds Issued:						
To Date (2009-2):	$ 75,000	$ -	$ -	$ -	$ -	$ 75,000
Future Issues:	220,000	360,000	360,000	360,000	360,000	1,660,000
Total Bonds Issued	295,000	360,000	360,000	360,000	360,000	1,735,000
						-
Funds for Overcollateralization						
Future Funds Required:	10,000	-	-	-	-	10,000
Total Funds for Overcollateralization	10,000	-	-	-	-	10,000
Total Funds Available for Production [1]	$ 305,000	$ 360,000	$ 360,000	$ 360,000	$ 360,000	$ 1,745,000
PROGRAM WITHDRAWALS AND USES OF CASH:						
1974 Resolution:						
1985 Debt Service Reserve	6,000	10,000	10,000	10,000	10,000	46,000
Funds to Overcollateralize New Issues	10,000	-	-	-	-	10,000
Housing Trust Fund [3]	8,182	-	-	-	-	8,182
Underwriter's Fees	2,250	2,740	2,740	2,740	2,740	13,210
THDA Operations - FY09 (Due to)	6,993	-	-	-	-	6,993
	33,425	12,740	12,740	12,740	12,740	84,385
1985 Resolution:						
Downpayment Assistance	8,955	12,240	7,920	7,920	7,920	44,955
Costs of Issuance	640	706	726	746	766	3,584
Capitalized Interest	2,500	1,450	1,100	1,100	1,100	7,250
Less: Bond Premium on New Issues [2]	(2,260)	(2,730)	(2,730)	(2,730)	(2,730)	(13,180)
THDA Operating Expenses	5,150	5,305	5,464	5,628	5,797	27,344
Program Compliance Reserve	1,046	1,046	1,046	1,046	1,046	5,230
Housing Trust Fund [3]	-	6,000	6,000	6,000	6,000	24,000
New Start Loans [4]	11,300	8,000	8,000	8,000	8,000	43,300
Preserve Loan Program	-	-	4,000	4,000	4,000	12,000
	27,331	32,017	31,526	31,710	31,899	154,483
Total Withdrawals	$ 60,756	$ 44,757	$ 44,266	$ 44,450	$ 44,639	$ 238,868

[1] The remaining forecasted production for FY 2010 of $230 million replicates Issue 2009-2, with such issues structured at 20% PSA, and overcollateralized with THDA cash. All remaining production through FY 2014 is structured with level maturity schedules.

[2] Bond premium on new bond issues is assumed to be used to offset THDA's costs of issuance, underwriter's fees, and capitalized interest.

[3] Housing Trust Fund amount for FY10 is $8.182 million, which represents the fund of commitments from prior years. Future Housing Trust Fund expenditures were assumed to be made in the fiscal year after the commitment is made.

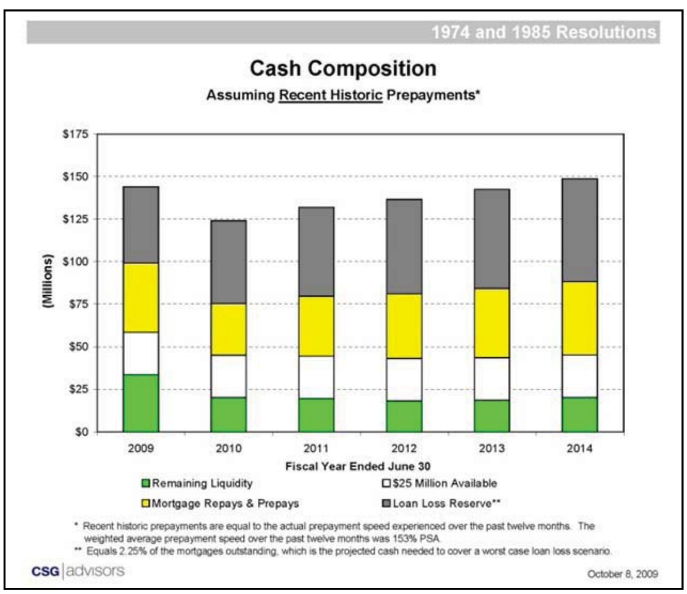
[4] $6 million for FY09 commitments, plus $8 million for FY10, for a total of $14 million. $2.7 million of this was funded by 2009-2, leaving $11.3 million to be funded during FY10.

THDA's finance team worked with the financial advisor to develop a set of bond structure assumptions that would produce competitive mortgage rates, given market conditions. 2010 bond structures modeled Issue 2009-2, the latest bond issue at the time of plan development, which included a premium PAC bond and assumed cash flows at 20% PSA. It should be noted here that THDA's finance team and financial advisor worked previously with the rating agencies for approval to run cash flows at 20% PSA. It was also assumed 2010 bond issues would be overcollateralized with $10 million of THDA funds. 2011-2014 bond structures assumed level maturity schedules and premium PAC bonds.

For cash flow assumptions, the financial advisor first performed historical analyses of prepayment speeds and determined the weighted average PSA for THDA to be 153%. Cash flow scenarios were also run at Slow (75% PSA) and Fast (300% PSA) prepayment speeds to project remaining liquidity under such conditions. Reinvestment rates were .5% and 1.5% for 2010 and 2011 respectively and 3% for 2012-2014. Surplus funds were used to pay future debt service and/or future program withdrawals. It was assumed that bond premium on new issues would offset cost of issuance, underwriter's fees, and capitalized interest. THDA also included other withdrawal assumptions, based on goals outlined in the Strategic Plan. Withdrawal assumptions for initiatives, such as the Housing Trust Fund, New Start Loans, and Preserve Loans, were included at the expected levels approved by the Board. To help alleviate political pressure, THDA assumed $25 million would be available at each June 30, in case the organization is called upon to help during a state budget crisis. Additionally, 2010 and 2011 cash flows were run at rating agency requirements.

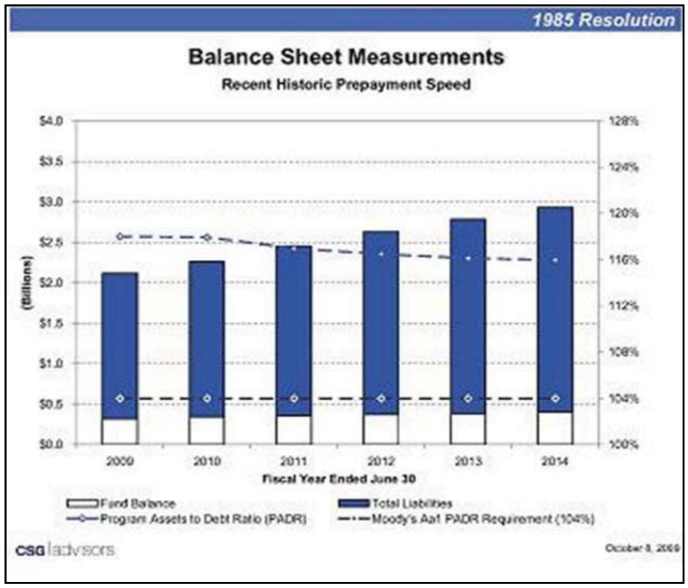
Development of the Plan

In developing the plan, staff looked to THDA's enabling legislation and strategic plan as guiding documents for organizational initiatives and activities. The objective of the financial plan is to show the potential impact THDA's decisions, relative to the use of our resources, may have on our financial position, given a set of assumptions. The plan is designed to be a liquidity analysis tool used by management for decision-making purposes. The primary role of the financial advisor was to bring housing market input to the table, run various scenarios using agreed upon assumptions, and produce a report of schedules and graphs that summarize the analysis.



As a liquidity tool, it was imperative to begin the analysis with the organization's beginning cash position using the current fiscal year's July 1 consolidated cash flows provided to the rating agencies. After confirming the beginning cash position, the financial advisor input all parameters and assumptions into the DBC software and ran the various scenarios at expected prepayment speeds to produce forecasts of remaining liquidity and financial strength. Liquidity, or cash composition, results consisted of liquidity reserves per rating agency requirements, mortgage repayment and prepayments, the $25 million BFC requirement, and remaining liquidity. Financial strength, or balance sheet, results consisted of outstanding loans, debt service and expense, debt service reserves, and bonds outstanding. Debt service and expense represents funds that will be needed for the next scheduled semi-annual debt service payment, mortgage prepayments, and excess or "equity" funds.

The results of the financial plan were presented to the Bond Finance Committee and the full Board. All results were compiled and graphed for presentation purposes. The final results and presentation were reviewed by the entire finance team, which was an important step to ensure all perspectives were given consideration. The board presentation included an executive summary, a schedule of production and program withdrawals, and graphs consisting of cash composition, fund balance, balance sheet measurements. Additional assumptions, such as prepayment speeds and reinvestment rates, were included at the end for reference. The balance sheet graphs were overlaid with forecasted PADR versus rating agency PADR to show continued financial strength for maintaining current credit ratings. The plan is updated on an annual basis.



Why the Plan is Important

While the cost of developing the five-year financial plan is minimal, the benefits have been tremendous. The financial plan has proven to be an invaluable decision-making tool that has allowed THDA to maximize available resources. The plan provided flexibility in developing new mission-oriented initiatives, such as the preserve loan program, to fill resource voids relative to Tennesseans of low and moderate income. THDA was able to identify resources to monetize the first-time homebuyer tax credit. With the rollout of Treasury's NIBP program, THDA decided to establish a new indenture with a rating of Aa2 by Moody's, which requires a PADR of 1.04. Anticipating the issuance of $600 million in bonds (including market bonds), it was determined that $24.1 million was needed for loan loss reserves and additional parity to achieve the desired credit rating. The financial plan was a priceless communications tool to which staff referred Bond Finance Committee and Board members, making it very easy to answer questions about resource identification for the NIBP program.

As with most states, Tennessee has faced significant state budget shortfalls during the past few years. On numerous occasions, THDA has been able to point state and local officials to the specifics in the financial plan that show the organization's commitment to leading Tennessee in creating affordable housing opportunities. Throughout the fiscal year, the plan can be updated with "what if" scenarios to determine current and future impacts of management decisions. This proved to be extremely beneficial when THDA sought and received credit rating increases from AA and Aa2 to AA+ and Aa1 by Standard and Poor's and Moody's respectively. The plan reflected the organization's ability to absorb and maintain the additional financial requirements imposed by the rating agencies, while continuing to fund other initiatives.

Someone said luck is where preparation meets opportunity. The five-year financial plan prepared THDA to engage in new opportunities, such as NIBP, and fund important programs, such as downpayment assistance, yielding $395.5 million in applications during fiscal year 2010. This was the organization's fourth highest year ever, which is remarkable given the challenges HFAs have faced in recent times.

Tennessee Housing Development Agency
Five Year Financial Plan Summary
FY 2010 – FY 2014

Guiding Principles:

Statutory Purpose (TCA 13-23-101)

- To promote the production of more affordable new housing units for very low, low and moderate income individuals and families in the state,
- To promote the preservation and rehabilitation of existing housing units for such persons, and
- To bring greater stability to the residential construction industry and related industries so as to assure a steady flow of production of new housing units.

Five Year Financial Plan Objective:

THDA has made a commitment to maximize the use of our financial resources to fund mortgage programs and other initiatives that fulfill our statutory purpose without compromising our AA+ and Aa1 credit ratings assigned by Standard and Poors and Moody's respectively. The objective of the Five Year Financial Plan is to show the potential impact THDA's decisions, relative to the use of our resources, may have on our financial position, given a set of assumptions. It should be noted that the Five Year Financial Plan is a liquidity analysis tool used by management for decision-making purposes. Thus, this plan should not be used for external financial reporting purposes.

Looking Back:

HERA and ARRA brought, among other things, homebuyer tax credits designed to help jumpstart the economy. HERA also eliminated downpayment assistance from most sources; THDA is still permitted to provide such assistance. For the most part, THDA mortgage rates were higher than outside rates. Additionally, reinvestment rates remained low; the Fed Rate was .25% for much of the year. Despite some of the challenges, THDA performed well financially during FY09. Downpayment assistance along with bond structuring and debt management strategies enabled THDA to do over $200 million in commitments and provide an overall June 30, 2009 Fund Balance of $451 million, which was slightly better than projected. The 1985 General Resolution PADR of 118% was as projected.

Looking Ahead

We have an abundance of tax-exempt resources for single family bonds. Working with our financial advisor, CSG Advisors, we have developed a 5 year financial plan that maintains our financial strength and maximizes resources for programs that benefit Tennessee's very low income and special needs populations (Downpayment Assistance, Housing Trust Fund, New Start, and Homeowner Rehab). With the rollout of Treasury's New Issue Bond Program (NIBP) for HFAs, we estimate production will increase during calendar year 2010 to $500 million. This level of production is not included in the five year plan, as the plan was developed prior to Treasury's rollout of the program; however, we believe liquidity resources already identified in the plan will support such mortgage production.

Summary of New Production and Program Withdrawals

This slide shows liquidity needs for 5 years to fund anticipated homeownership production and other housing program expenses. Liquidity needs for homeownership production is essentially based on the assumption that housing will somewhat normalize in 2011. Other liquidity need assumptions for the housing trust fund, new start mortgages, and THDA operation expenses are the same as in previous years, with the exception of FY2010. Downpayment assistance is still projected to be higher than normal, due to the federal HERA legislation and the monetization of ARRA's homebuyer tax credit.

Financial Results

Cash Composition (1974 Res and 1985 Res)

This slide shows the composition of our cash reserves after planned withdrawals and uses. Liquidity increases from $125 million to $150 million, primarily due to increased loan loss reserves relating to an estimated $2.6 billion outstanding mortgage balance by 2014. Remaining liquidity (resources) for future bond issuance and housing program expenses remains steady at around $20 million over the next five years, after consideration of the 2.25% loan loss reserve required by the rating agencies, $25 million BFC requirement, and mortgage repays and prepays used to call bonds.

Fund Balance (1974 and 1985 Resolutions)

This chart shows that we essentially maintain a healthy fund balance ($459 million in 2014) while using our profits and corpus to continue funding important housing programs, such as downpayment assistance, HTF, and new start.

Balance Sheet Measurements (1974 Res and 1985 Res)

These charts show that at projected production levels and assumed uses of liquidity the Program Asset to Debt Ratios (PADR) for both the 74 Resolution and 85 Resolution remain well above the 104% required by the Rating Agencies, with projected 2014 PADR's of 208% and 116% respectively.

Detailed Assumptions

In addition to the assumptions included on the Summary of New Production and Program Withdrawals, other assumptions for each bond resolution are listed separately, followed by assumptions that are applicable to both resolutions. It should be noted that the 85 Res loan mix for 2010 and 2011 are weighted more towards downpayment assistance programs, as the loan mix reflects current demand for our products. We assumed anticipate a heavier demand for downpayment assistance due to changes enacted by federal legislation (HERA, ARRA), although this assumption may be altered by the recent developments relative to NIBP.

TENNESSEE HOUSING DEVELOPMENT AGENCY
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Fiscal Year Ending June 30						(in thousands)
	2010	**2011**	**2012**	**2013**	**2014**	**Total**
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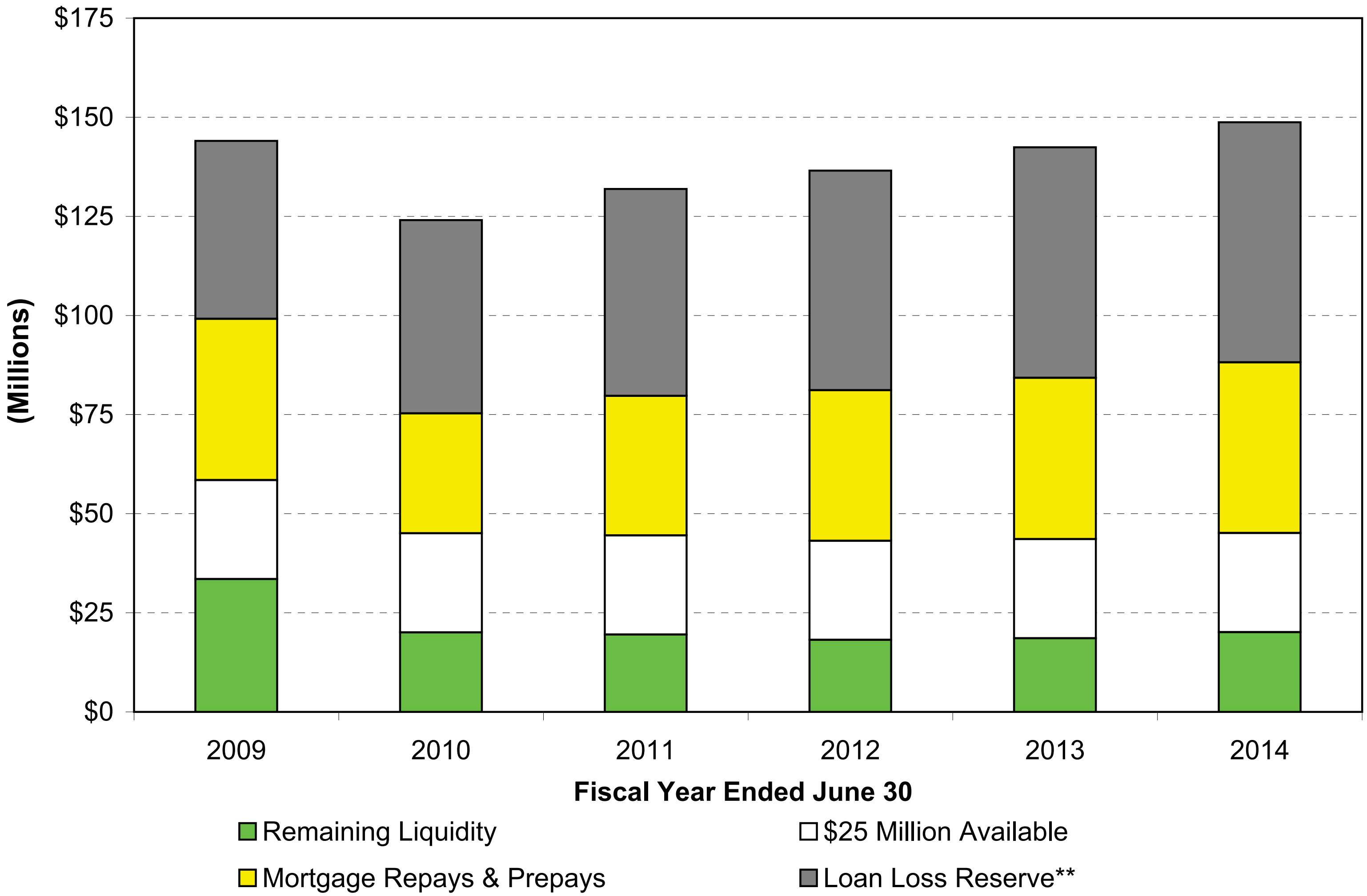
Cash Composition

Assuming Recent Historic Prepayments*

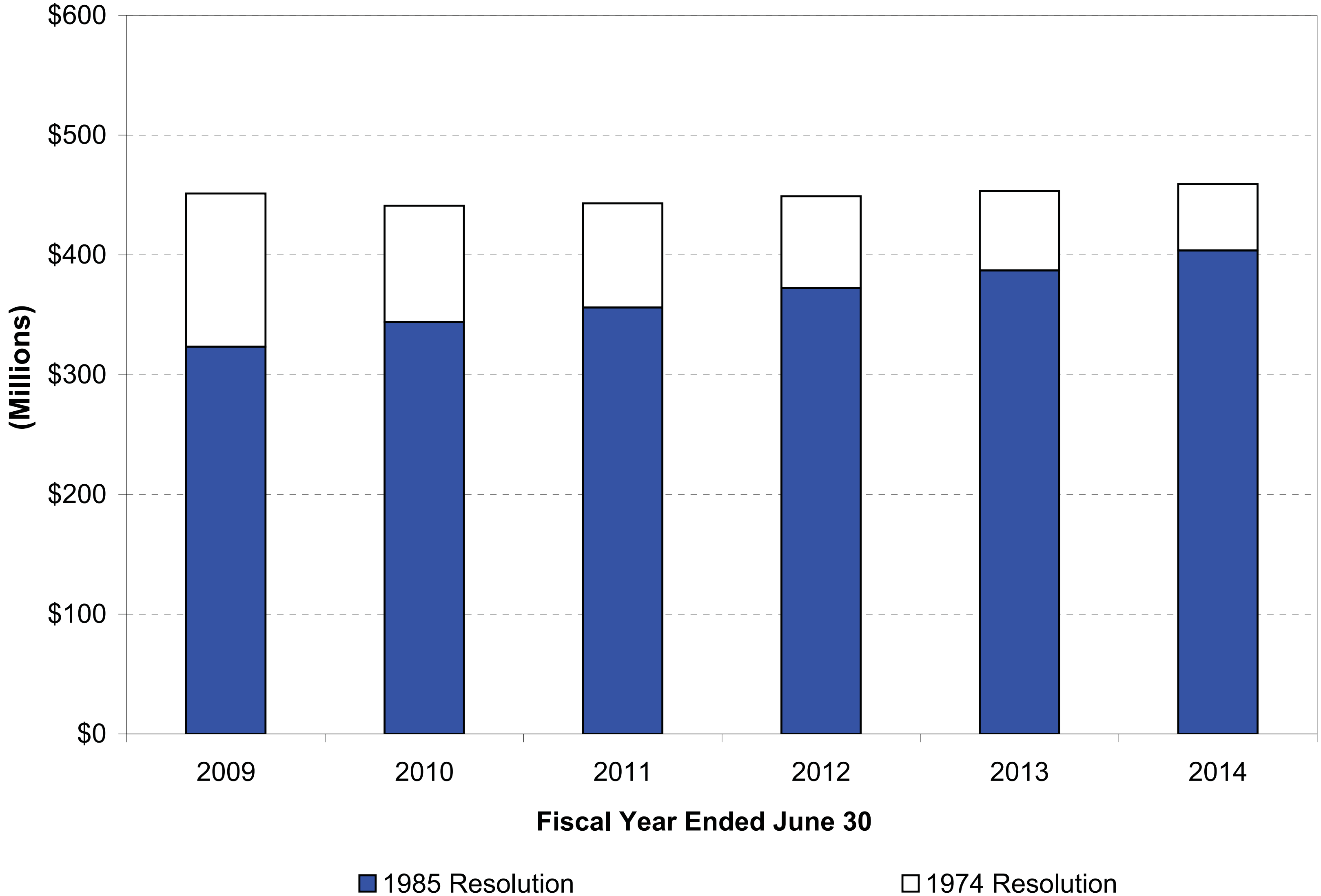


* Recent historic prepayments are equal to the actual prepayment speed experienced over the past twelve months. The weighted average prepayment speed over the past twelve months was 153% PSA.

** Equals 2.25% of the mortgages outstanding, which is the projected cash needed to cover a worst case loan loss scenario.

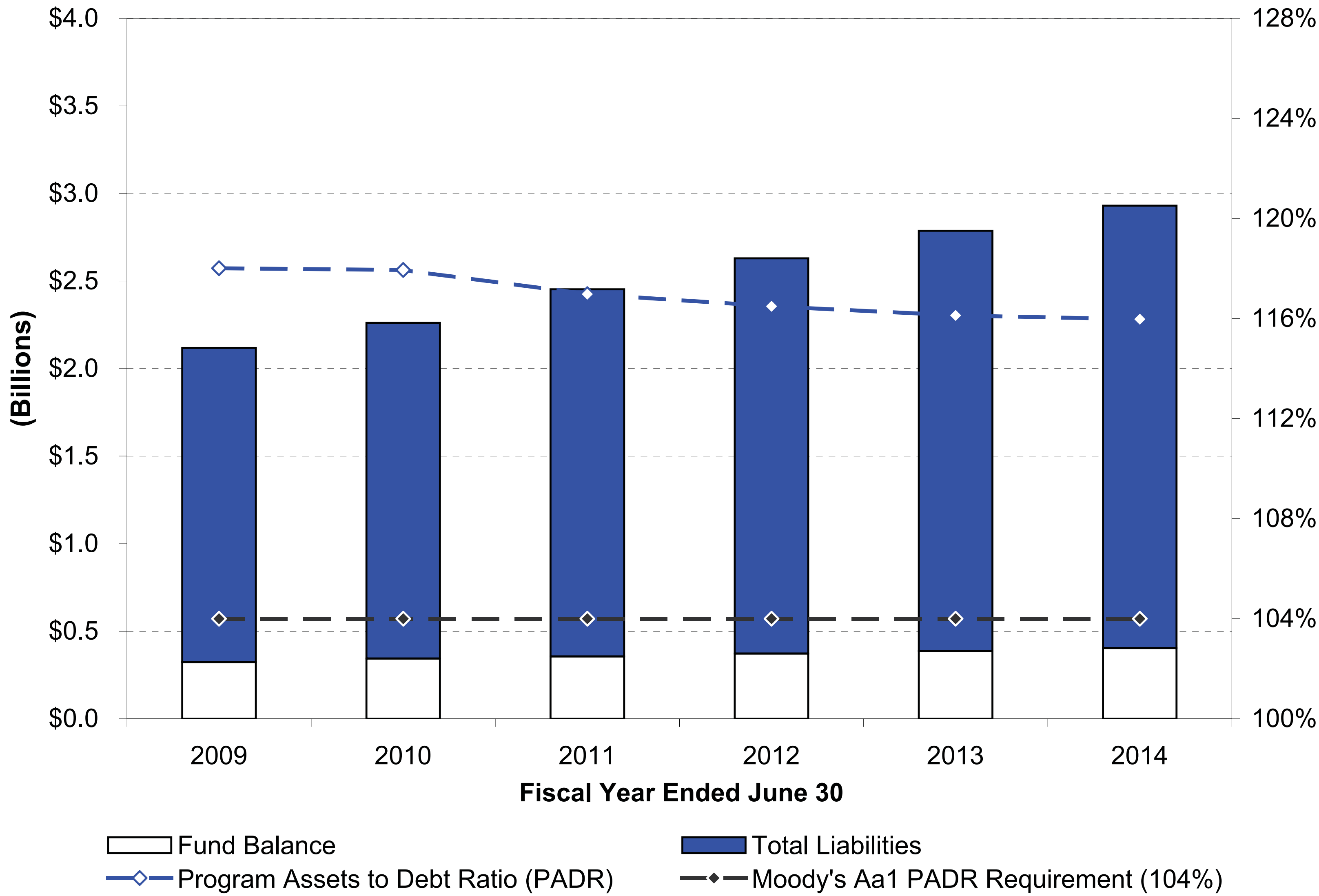
Total Fund Balance

Recent Historic Prepayment Speed



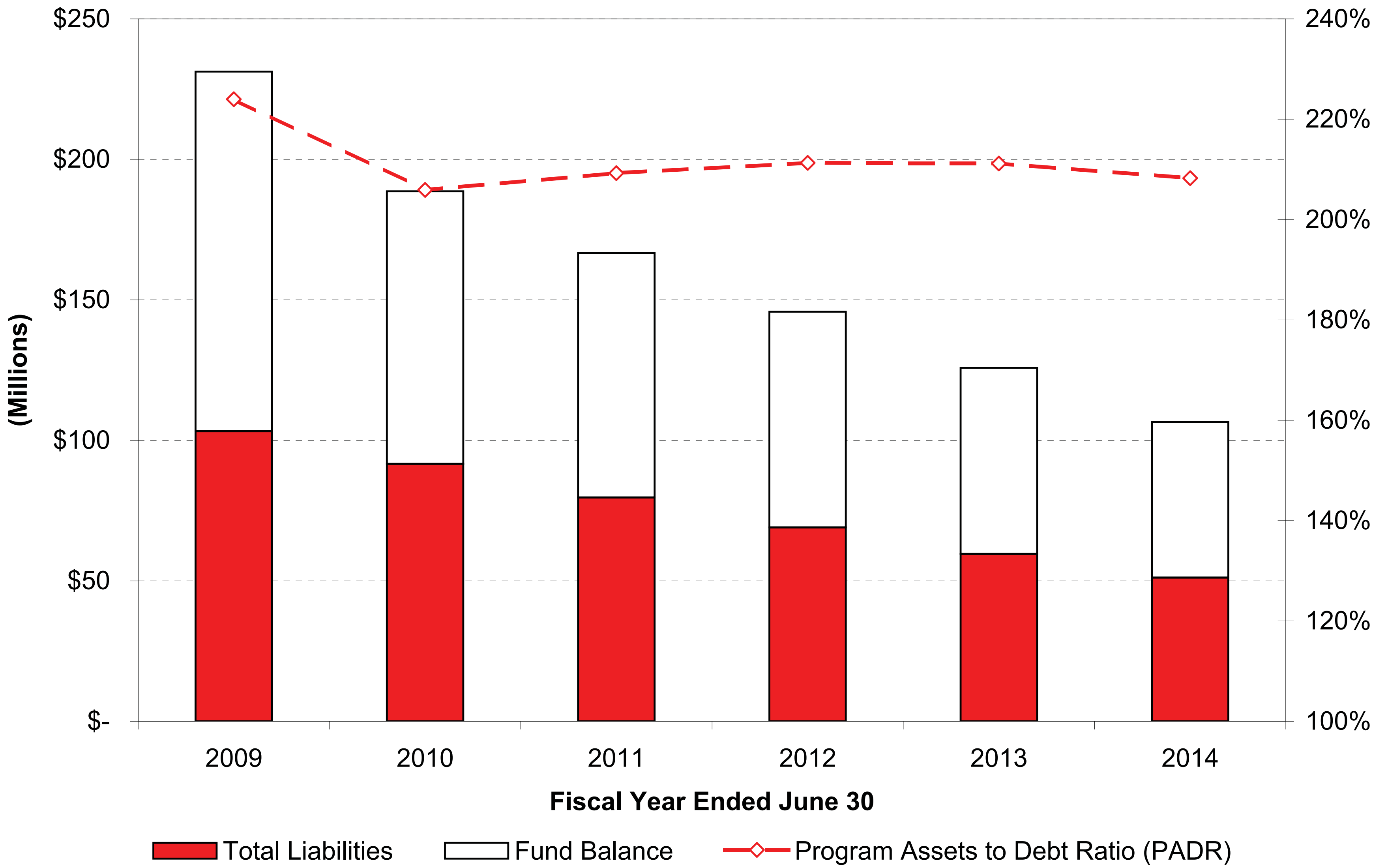
Balance Sheet Measurements

Recent Historic Prepayment Speed



Balance Sheet Measurements

Recent Historic Prepayment Speed



Additional Assumptions

Homeownership Program Bonds (1985 Resolution)

- New Mortgage Loan Mix (% of Total):

	FY10*	FY11	FY-12-14
Great Rate:	28%	10%	40%
Great Advantage:	10%	10%	10%
Great Start:	62%	80%	50%

* consistent with current loan mix.

- Mortgage rates on new bond issues are set at rates necessary to earn 1.00% yield spread.

- Prepayment speeds were assumed as follows:

1985A-L through 2007-4:

Expected Prepayment Scenario:	12 month historical speed within each bond issue (ranges from 100% to 225% Actual PSA, or a weighted average prepayment speed of 153% PSA).
Slow Prepayment Scenario:	one-half the 12 month historical speed.
Fast Prepayment Scenario:	two times the 12 month historical speed.

2008-1 through 2009-2 and all New Production:

Expected Prepayment Scenario:	150% PSA
Slow Prepayment Scenario:	75% PSA
Fast Prepayment Scenario:	300% PSA

Mortgage Finance Program Bonds
(1974 Resolution)

- Prepayment speeds were assumed as follows:

  All Mortgage Loans:

Expected Prepayment Scenario:	150% PSA
Slow Prepayment Scenario:	75% PSA
Fast Prepayment Scenario:	300% PSA

- No new bond issuance in the Resolution.
- Excess Debt Service Reserve is used for funding program withdrawals beginning FY 2011.

Both 1974 and 1985 Resolutions

- All loan, investment, and bond balances are as of July 1, 2009.
- **Reinvestment Rates:**
  Investment rates for both the Debt Service & Expense Fund and the Loan Fund are as follows:

July 1, 2009 through December 31, 2010:	0.50%
January 1, 2011 through December 31, 2011:	1.50%
January 1, 2012 and thereafter:	3.00%

- **Debt Service Reserve:**
  Debt Service Reserve Funds are invested in long-term treasuries and agencies, and thus earn higher yields than funds in the DS&E Fund and Loan Funds. Funds in the Debt Service Reserve are assumed to earn 4.0%.
- **Surplus Funds:**
  Surplus funds accumulate in the respective Debt Service & Expense Funds and thus are available to pay future debt service and/or to fund future program withdrawals.
- **Bond Redemption:**
  Mortgage principal recoveries for Issues 1996-3 through 2001-3 are used to redeem serial bonds first, followed by the redemption of term bonds on a pro-rata basis. Mortgage principal recoveries for Issues 2002-1 through 2009-2 and including new production are used to redeem all term bonds pro-rata, subject to the redemption requirements of all PAC and Supersinker bonds.