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Monterey County Housing Authority, California; Affordable Housing

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Long Term Rating	A+ (sf)/Stable	Affirmed
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Long Term Rating	A (sf)/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'A+ (sf)' and 'A (sf)' ratings on the Monterey County Housing Authority, Calif.'s (Casanova Plaza and Parkside Manor apartments) series 1999A and 1999C multifamily mortgage revenue bonds, respectively. The outlook is stable.

The ratings reflect our view of:

- The very strong financial performance of the project, reflected in three years' average debt service coverage (DSC) of 1.53x and 1.41x maximum annual debt service (MADS) coverage on the 1999A and C bonds, respectively;
- Extremely strong loss coverage for the project, indicated by low loan-to-value (LTV) ratios and sufficient reserves; and
- Experienced management and oversight of the apartments, which are owned by an affiliated nonprofit organization.

Partially offsetting the above credit strengths is our view of weaker operating performance, evidenced by lower occupancy levels compared with those of rated peers.

The bonds were issued to finance the acquisition and rehabilitation of Casanova Plaza and Parkside Manor apartments, located in Monterey County, Calif. (approximately 71 miles south of San Jose). Current bonds outstanding is approximately $3.88 million for the senior series 1999A bonds, and $290,000 for the subordinate series 1999C bonds. Three-year average DSC is 1.53x and 1.41x for the series 1999A and 1999C bonds, respectively, and includes annual subsidies to very low-, lower-, and low-income residents.

Outlook

The stable outlook reflects our view of the properties' strong financial performance and management expertise. We also expect the properties will maintain stable operations due to the project's market and economic fundamentals.

Upside scenario

If the properties can demonstrate consistently strong operating performance, we could consider raising the rating.

Downside scenario

Conversely, should expenses increase significantly, a negative rating action could be warranted.

Enterprise Risk Profile

Industry risk

We view risk as low for the affordable housing industry. Residential rental markets typically pose less risk than other property classes, and the increased need for affordable housing during times of economic stress lends further stability. Competitive risk is fairly low owing to effective entry barriers in many jurisdictions, relatively low substitution risk, and overall stability in growth and margins. In addition, ongoing governmental subsidies, other support, and oversight generally limit volatility, with the overall importance of the service delivered, thereby limiting the potential for negative governmental intervention.

Economic fundamentals and market dependencies

We view the project's economic fundamentals and market dependencies as strong, reflected in the high demand for housing in its market. We expect these conditions to remain stable, based on high occupancy rates and above-average rental growth projected for the Monterey County-Salinas area. IHS Global Insight forecasts the population will grow by 0.16% annually over the next four years, while REIS Inc. forecasts market rents to grow by 3.60% annually over the same period. The property's average rent was 55.40% of market rent, based on a REIS fourth-quarter report for fiscal 2018. These trends, along with a projected rapid increase in the elderly population nationwide, point to the growing demand for housing in Monterey County.

Government support

While the properties receive minimal ongoing governmental support with respect to housing, they do benefit indirectly from property tax exemptions (based on the sponsor's nonprofit status) and access to tax-exempt bond financing.

Strategy and management

The owner, MCHI Affordable Acquisitions Inc., used the bond proceeds to purchase the properties from the authority and to fund reserves. MCHI is a California-based 501(c)(3) organization established by the authority for the sole purpose of owning the properties. The authority also serves as property manager. We rank MCHI as "good" under our owner evaluation guidelines. The executive team is, in our view, competent and well trained in areas of expertise.

Additionally, we view the sponsor's track record and operational effectiveness as strong, owing to no prior instances of technical default involving its properties, its demonstrated ability to respond to emerging and unexpected operational risks that occasionally affect cash flows, and DSC of at least 1.0x for the vast majority of its properties. We rank management's strategic planning processes as strong, reflecting the use of a specific strategic plan and a formal organizational structure. The sponsor's governance structure has a neutral impact on our view of strategy and management.

Financial Risk Profile

Loss coverage

We view the project's loss coverage as extremely strong. Projected losses are derived in accordance with our commercial mortgage-backed securities property evaluation criteria. We use an LTV ratio of 38.80%, net cash flow, and DSC primarily to determine the transaction's credit enhancement. The transaction maintains a debt service reserve fund at 12 months' MADS and a replacement reserve. Management invests funds in accordance with permitted investment provisions detailed in the trust indenture.

Financial strength

The project's financial performance remained strong in fiscal 2018. Three years' average DSC for the project based on audited financials ended 2018 reported 1.53x and 1.41x of MADS for the series A and C bonds, respectively, which includes annual subsidies to very low-, lower-, and low-income residents.

Asset quality

The properties have what we view as adequate asset quality. Parkside Manor, built in 1973, is an 88-unit senior housing complex in Salinas. It consists primarily of one-bedroom units that average 530 square feet. The project's 88 units are clustered into two 40-unit buildings occupied by seniors, along with eight family-occupied townhouse units. Casanova Plaza, in Monterey, is an 86-unit, senior-occupied apartment facility built in 1972; it consists primarily of one-bedroom units that average 560 square feet.

Operating performance

The properties' benefits from low vacancy rate. The project's three-year weighted average vacancy is 5.01%, while very strong, is slightly higher compared to rated peers. According to the owner, Parkside's and Casanova Plaza's occupancy rates were 96% as of December 2018.

Financial policies and practices

We view management's financial policies and practices as adequate; this incorporates our view of its loan origination and portfolio monitoring policies.