S&P Global Ratings

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Century Housing Corp., California; General Obligation

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Credit Highlights

- S&P Global Ratings raised to 'AA' from 'AA-' its issuer credit rating (ICR) on Century Housing Corp. (Century), Calif., and its long-term rating on Century's bonds and sustainable impact notes outstanding.
- At the same time, we affirmed our 'A-1+' short-term rating on Century's commercial paper (CP) outstanding.
- The outlook, where applicable, is stable.
- The rating action reflects our opinion of Century's strengthening capital adequacy and profitability, and financial ratios that well exceed our benchmarks for the 'AA' rating category and that are stronger than those of similarly rated peers.
- The rating action further reflects our view of Century's strategic initiatives in recent years, including implementation of an asset liability model, monthly monitoring of portfolio metrics, improvement of liquidity, and innovation in funding in the market.

Security

The ICR reflects our view of the obligor's general creditworthiness, focusing on its capacity and willingness to meet financial commitments as they come due. It does not apply to any specific financial obligation because it does not consider the obligation's nature and provision, standing in bankruptcy or liquidation, statutory preferences, or legality and enforceability.

Century's general obligation secures the bonds, sustainability notes, and CP outstanding. We view the general obligation at the same level as the ICR given that repayment benefits from revenue that we consider central to Century's purpose and covenants, which, in our view, support creditor security at the senior debt level.

Credit overview

The ICR and long-term rating reflect our view of Century's:

- Extremely strong capital adequacy ratios that have sustained five-year levels higher than those of all other rated community development financial institutions (CDFIs), and availability of capital to absorb loan losses and withstand economic volatility;
- Very high profitability, as is evident in very strong average return on assets, and an average net interest margin ratio stronger than that of rated peers;
- Very strong asset quality, with five-year average nonperforming assets at 2.08% of total loans and real estate owned, which is lower than the median; and
- Strong liquidity, with total investments to assets that is higher than that of peers, although lower-than-average holdings of short-term investments somewhat offset this.

The short-term rating on the CP notes reflects our view of the linkage between long-term and short-term ratings.

Environmental, social, and governance

In our opinion, Century's programs exhibit social capital opportunities, reflecting its mission to finance the creation and preservation of affordable housing throughout the state. We think the need for affordable housing within Century's footprint, especially in California, will continue fueling demand for its programs, and this factors into our capital adequacy analysis.

We view environmental risk for Century's portfolio as somewhat elevated given geographic concentration in the State of California and exposure to wildfire and seismic risk, but the shorter-term nature of the majority of Century's loans and its strong underwriting and insurance requirements partly mitigate this risk. Social and governance risks have neutral implications in our credit analysis, in our view.

Outlook

The stable outlook reflects our view of Century's continued very strong operating performance, equity base, and overall management. We believe that at the 'AA' rating, Century has ample equity to cover projected loan losses and liquidity to cover near-term needs. Furthermore, we believe Century's experienced management team has demonstrated the effectiveness of its strategy to meet its mission while increasing capital and profitability and mitigating loan losses.

Downside scenario

Although we are unlikely to do so during the outlook period given that Century's capital adequacy is well above the rating median, we could lower the ratings should Century's capital adequacy significantly decrease as a result of increased debt, riskier underwriting, or declining loan performance. A significant decline in revenue that negatively affects net income could also lead us to lower the ratings.

Upside scenario

All else equal, if Century's asset quality and liquidity ratios improve compared with those of peers, while the the loan portfolio shifts to loans that we view as less risky (e.g., long-term and permanent loans), resulting in lower assumed loan losses, we could take positive rating action.

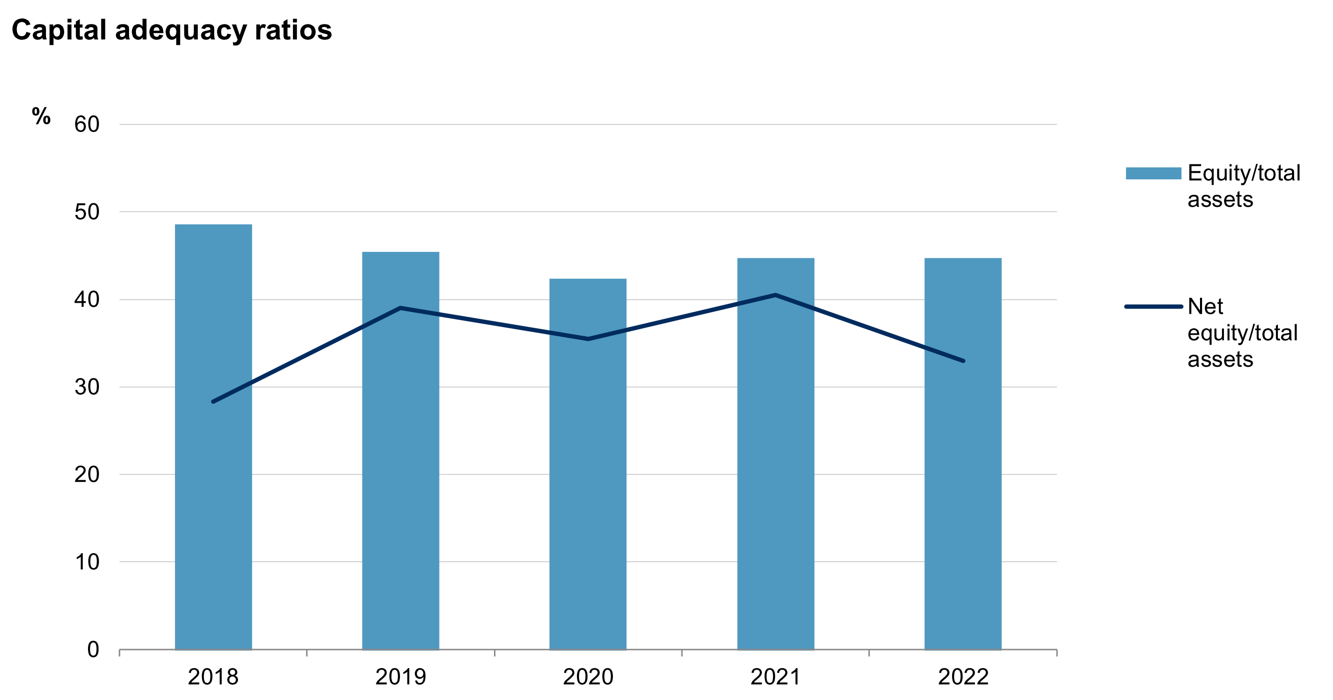
Credit Opinion

Financial Strength

Capital adequacy

Century maintains extremely strong equity ratios as a result of its highly capitalized position, low debt, and profitability. In determining equity and profitability ratios, we applied our standard adjustments (e.g., fair value adjustments for investment securities). Century's total equity increased by 8% a year, on average, in fiscal years 2018 to 2022. Century's five-year average equity to assets and net equity to assets--45.1% and 35.3%, respectively--are extremely strong compared with those of peers. While both ratios have fluctuated year over year primarily as a result of increased leverage, five-year net equity to assets has improved in the past three years as a result of decreased risk in the loan portfolio as well a decline in our loss assumptions given changes in our criteria and our view of loan portfolio characteristics.

Chart 1



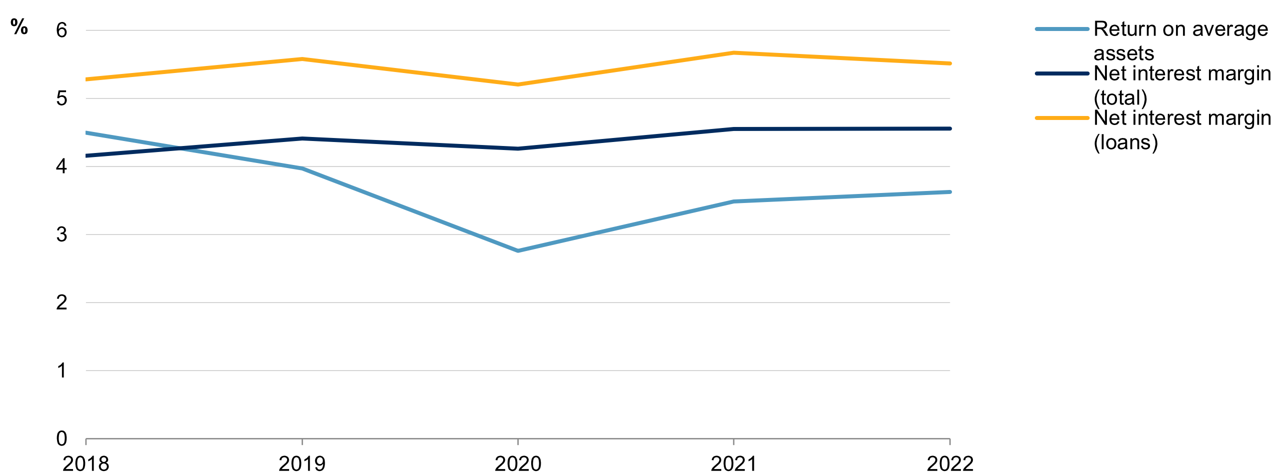
Century's debt profile consists of predominantly fixed-rate debt, but with shorter terms compared with those of a typical municipal housing issuer. The majority of Century's loan portfolio has an average term of approximately 28 months, and the corporation tends to match its lending with the terms of its funding sources. In recent years, Century led several innovative efforts to diversify its funding sources and gain access to capital, such as issuing municipal bonds. In 2022, Century began its own CP program, backed by its self-liquidity and other available sources. As of Dec. 31, 2022, approximately 68% of Century's debt was fixed-rate and the rest variable-rate, and about 80% of total debt included rated bond and note obligations.

Profitability

In our opinion, Century's operating performance remains very strong, reflected in its profitability and self-sufficient business model with minimal reliance on grants income. Century reported net income of approximately $20.5 million in fiscal 2022, up by 9.8% from fiscal 2021 and up by 36.3% from fiscal 2020. Century's five-year average return on assets of 3.7% far exceeds the 2.8% rating median. Furthermore, Century's lending program is very profitable compared with that of peers, demonstrated by its five-year average net interest margin from loans of 5.5%, which is above the 3.3% median.

Chart 2

Profitability ratios



Asset quality

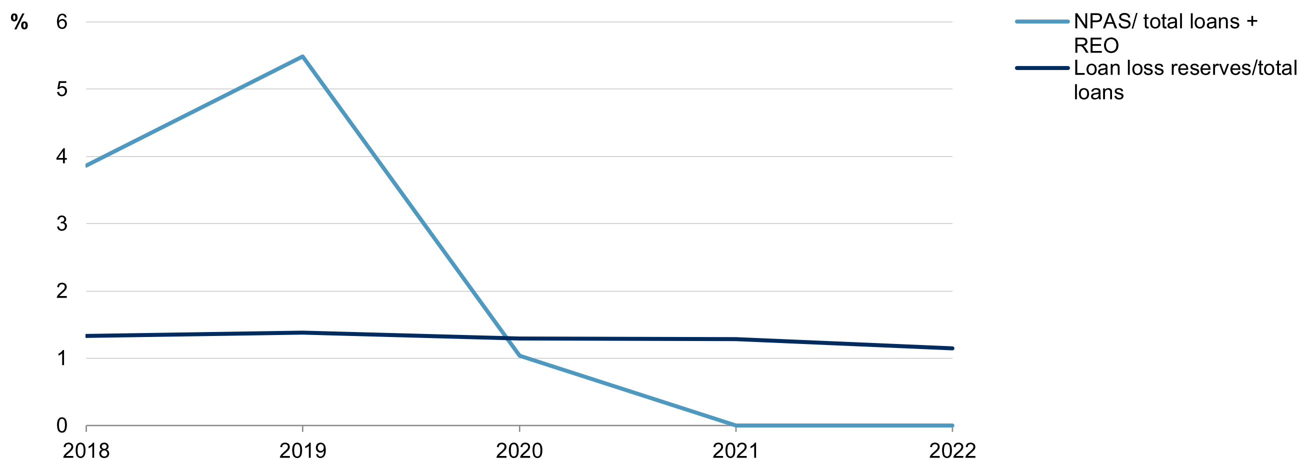
Century's total assets mostly consist of its housing lending portfolio (71.5%). Its niche in the housing market is to provide early financing multifamily loans to repeat clients in California. Century offers acquisition, bridge, construction, predevelopment, and, more recently, permanent financing, and its loan portfolio consists of projects located in California, with more than 70% of borrowers having long relationships with Century.

Century's lending portfolio consists of primarily early financing loans for multifamily housing, including predevelopment, bridge, and acquisition loans. We generally view early financing loans as riskier than permanent loans given greater exposure to repayment and takeout risks, but in certain cases we believe other characteristics such as the presence of low-income housing tax credits (LIHTCs), strong debt service coverage, and low loan-to-value ratios mitigate this risk. The majority of Century's loans (67.1%) are paired with LIHTCs, and 32.6% benefit from Section 8 or other subsidies. As of fiscal 2022, early financing loans represented 70% of total loans outstanding, with the majority (62%) in acquisition loans. In addition, 10.9% of Century's portfolio were construction loans.

Century's loans have historically exhibited very strong performance. Over the past five years, the corporation's average ratio of nonperforming assets to total loans outstanding was 2%, mostly on account of loan forbearances from 2018 to 2022. In fiscal years 2021 and 2022, the ratio stabilized at 0%. While the corporation has maintained very strong loan performance over the years, the nonperforming assets in 2018 and 2019 demonstrated that poor performance of one loan could severely affect asset quality.

Chart 3

Asset quality ratios



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

In our opinion, Century's loan underwriting and monitoring policies are strong. Its underwriting policy consists of identifying key risks (e.g., takeout, construction, and interest rate risk), and applying risk ratings on the borrower and project (e.g., borrower's experience, past relationship with Century, and financial strength and leverage). In its underwriting Century also performs a loan review, which analyzes the proposed project, site characteristics, market analysis, and third-party reports.

Century's asset liability committee monitors loans monthly, and any delinquent loans (over 90 days) biweekly. The frequency of monitoring has improved, in our opinion, from several years ago, when Century reviewed its loan portfolio annually. Century's asset liability committee model assists the corporation in monitoring loan and debt allocations and deploying capital strategically.

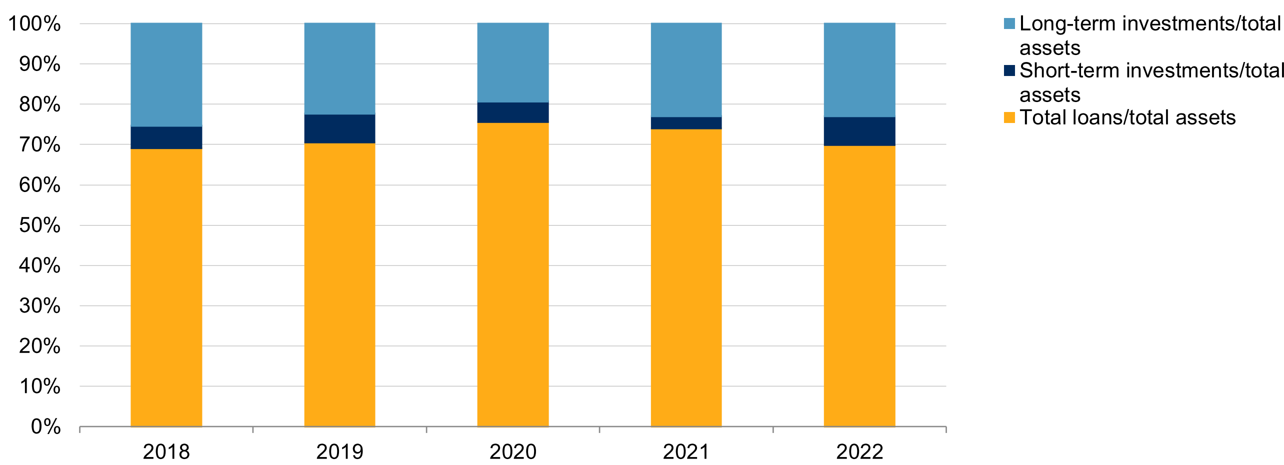
Liquidity

Century maintains strong liquidity, with a five-year average total investment to total assets of approximately 27.7%. Total investments to total assets was 29.7% in fiscal 2022, up from 25.6% in fiscal 2021. Total loans to total assets was

69.1% in fiscal 2022, and the five-year average was 70.8%. These levels are in line with the median of other CDFIs.

Chart 4

Liquidity ratios



Note: Short-term investments include accrued interest receivable on investments and loans. Long-term investments reported net of fair value adjustment.

While Century's ratio of total investments to assets is comparable to that of other rated CDFIs, its short-term investments to total assets is lower than that of peers. However, we think that Century's strategy of asset-to-liability matching mitigates some liquidity risk. Century's policies mandate that it maintain at least 20% of adjusted total net assets in liquid investments or cash. In addition, Century maintains liquidity covenants with its lenders such that liquid assets account for no less than six months of total operating expenses.

We have historically viewed Century's investment strategy as aggressive relative to that of peers and similar entities, but investments are core to Century's capital strategy, used for reserves, liquidity, and operations if need be. At least annually, Century Housing evaluates the allocation within its investment portfolio to various asset classes and takes actions to adjust it in response to changes in leverage and other risks the corporation faces. In recent years, Century has reduced risk in its investment portfolio, winding down its position in equities to less than a third of holdings. In April 2022, Century adopted a further diversification of its portfolio, incorporating a more effective strategy to mitigate inflation. The ratio of equities to fixed income was 29/71 as of Dec. 31, 2022, compared with 60/40 in 2004. Since 2019, Century has reduced equities in its investment portfolio by 4.8%.

Management and federal designation

Century originated as a state agency, formed as a result of the construction of the Century Freeway. In development beginning in 1972, the planned Century Freeway would displace local residents and businesses on its path between Los Angeles International Airport and the City of Norwalk. As a result of Keith v. Volpe, a lawsuit against the construction of the freeway given the freeway's impact on the local community, Century Freeway Housing Program was created to replace the housing lost from the construction of the freeway, and to provide social services to minorities and women. Century was privatized to Century Housing Corp. following the completion of construction in 1993 and meeting its housing development and social service goals. In 2010, Century spun off its social services divisions, focusing primarily on housing development and lending. Also in 2010, Century received CDFI designation from the U.S. Treasury.

Century's core business activities are affordable housing lending and affordable housing development. The corporation's lending operations are through Century Housing, and affordable housing development and preservation through Century Villages at Cabrillo Inc. and Century Affordable Development Inc. Our ICR is only on Century Housing as a stand-alone entity, given that it is Century's lending arm.

In our view, Century's vision is clearly defined and sets forth the corporation's overall strategic plan. We view Century's lending operations as generally self-supporting and contributing to its overall mission. We believe collaboration with public and private entities, external relations, and financial self-sufficiency demonstrate that Century has solid growth potential as it explores expansion opportunities in lending activities. Public and private partnerships are vital to Century's continued success, as they play a key role in expanding its financial position. This includes partnerships with other CDFIs, foundations, and government agencies to source potential expansion opportunities.

Century is committed to developing and preserving affordable housing in California through its lending and development divisions. It uses its own criteria to set general parameters for assessing opportunities designed to further its impact on the communities it serves. These parameters include likelihood of repayment, sector and project risk, collateral analysis, and financial health. We view Century's commitment to community development in relation to the corporation's core values, mission, and overall strategy and management as very strong.

A nine-member board of directors oversees Century. The board members come from a wide array of backgrounds that include housing, nonprofits, public and private enterprises, legal, finance, and government. The board meets every other month, and its responsibilities include executive functions, governance, finance, investments, and audits. Supporting the main board of directors is an established senior management team comprising the CEO, the chief financial officer, the senior vice president of lending, the senior vice president of finance and treasury, and the senior vice president of housing. Senior staff members work closely with one another to meet Century's mission and bring operations and projects into compliance with overall strategic goals. According to the housing corporation, while it has new board leadership in both its chair and vice-chair, they have been members of the board since 2009. In addition, no changes in key personnel or staffing occurred in 2022.

Economy

California's vast and diverse economy remains strong and is growing, albeit at a slower pace than in previous years. Real gross state product increased by 0.4% in 2022, and IHS expects it to increase by 1.1% in 2023 but taper in 2024. According to IHS, employment grew by 0.9% in the third quarter of 2022, despite widespread layoffs in the Silicon Valley region. Employment growth is expected to moderate in the medium term and then fall moderately on a year-over-year basis by the fourth quarter of 2023, as tightening monetary policy and high inflation put the brakes on economic expansion.

IHS reports that although home price growth reached double digits in 2021 and the first half of 2022, the state's housing market came to a near-halt in the second half of 2022 as a result of rising interest rates. According to data from the Federal Housing Finance Agency's purchase-only home price index, home prices in California during the third quarter of 2022 were up 7.6% year over year, a significant deceleration from the 15.9% annual gain seen in the second quarter. This was

the third-lowest price growth in the country in the third quarter, and further weakness is expected over the coming year.

Despite the near-term slowdown, housing affordability will continue to be an issue in the state, with the ongoing challenge of housing moderate- and low-income residents as well as the rising homeless population.

Table 1

Financial ratio analysis

(%)

	2018	2019	2020	2021	2022	Five-year average
Capital adequacy						
Equity/total assets	48.5	45.3	42.2	44.6	44.6	45.1
Net equity/total assets	28.3	39.0	35.5	40.5	33.0	35.3
Net equity/total loans	40.2	54.2	45.9	53.6	46.2	48.0
Equity/total debt	95.7	85.1	76.0	83.5	83.8	84.8
Net equity/total debt	55.9	73.3	63.9	75.8	61.9	66.2
Profitability						
Return on average assets	4.5	4.0	2.8	3.5	3.6	3.7
Net interest margin	4.2	4.4	4.3	4.6	4.6	4.4
Net interest margin (loans)	5.3	5.6	5.2	5.7	5.5	5.4
Asset quality						
NPAs/total loans + REO	3.9	5.5	1.0	-	-	2.1
Net charge-offs/average NPAs	-	-	-	-	-	-
Loan loss reserves/total loans	1.3	1.4	1.3	1.3	1.1	1.3
Loan loss reserves/NPAs	34.5	25.2	124.5	-	-	36.8
Net charge-offs/average loans	-	-	-	-	-	-
Liquidity						
Total loans/total assets	68.0	69.4	74.5	73.2	69.1	70.8
Short-term investments/total assets	5.4	0.1	0.1	0.0	0.1	1.1
Total investments/total assets	30.3	29.0	24.1	25.6	29.7	27.7

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

Table 2

Five-year trend analysis

($000s unless otherwise indicated)

	2018	2019	2020	2021	2022
Total assets	398,604	464,317	530,885	544,371	590,230
% change	16.8	16.5	14.3	2.5	8.4

Table 2

Five-year trend analysis (cont.)

($000s unless otherwise indicated)

	2018	2019	2020	2021	2022
Total gross loans	281,013	334,313	411,048	411,378	421,297
% change	17.3	19.0	23.0	0.1	2.4
Total equity	193,292	210,408	224,139	242,858	263,404
% change	9.4	8.9	6.5	8.4	8.5
Net equity	112,910	181,264	188,552	220,544	194,619
% change	7.1	60.5	4.0	17.0	(11.8)
Net income	16,632	17,116	13,731	18,719	20,547
% change	23.4	2.9	(19.8)	36.3	9.8
Revenue	25,847	29,916	30,213	31,745	36,517
% change	(0.8)	15.7	1.0	5.1	15.0
Expenses	15,985	18,855	17,593	15,177	16,850
% change	27.2	18.0	(6.7)	(13.7)	11.0
Loan loss reserves	1,139	872	903	7	(458)
% change	22.3	(23.5)	3.6	(99.2)	(6,718.1)
Nonperforming assets	10,859	18,343	4,279	-	-
% change	76.0	68.9	(76.7)	(100)	-
Total investments	120,578	134,609	127,976	139,445	175,527
% change	10.0	11.6	(4.9)	9.0	25.9
Total debt	201,948	247,130	295,074	290,997	314,162
% change	24.1	22.4	19.4	(1.4)	8.0

Table 3

Peer comparison

	Century Housing (2018-2022)	Century Housing (2017-2021)	'AA-' CDFIs median*	All CDFIs median*
Capital adequacy (%)				
Total equity/total assets	45.1	46.5	25.5	27.5
Total net equity/total assets	35.3	34.9	11.0	12.9
Profitabliity (%)				
Return on average assets	3.7	3.8	2.6	2.6
Net interest margin (total)	4.4	4.2	2.2	2.6
Net interest margin (loans)	5.4	5.3	2.4	3.0
Asset quality (%)				
NPAs/total loans and real estate owned	2.1	2.6	0.7	0.6
Loan loss reserves/NPAs§	-	-	280.4	236.7
Loan loss reserves/total loans	1.3	1.3	3.9	3.6
Liquidity (%)				
Total loans/total assets	70.8	70.5	51.1	66.3

Table 3

Peer comparison (cont.)	Century Housing (2018-2022)	Century Housing (2017-2021	'AA-' CDFIs median*	All CDFIs median*
Short-term investments/total assets	5.5	5.0	17.6	19.5

*As of the most recent five-year period. Excludes Century for comparison. §NPA average is zero. NPA--Nonperforming asset.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of June 16, 2023)		
Century Hsg Corp taxable cml pap (Sustainability) nts ser 2022-A due 07/28/2023		
Short Term Rating	A-1+	Affirmed