

State of California

# MEMORANDUM

**To:** Board of Directors

**Date:** July 21, 2022



**From:** Erwin Tam, Director of Financing  
**CALIFORNIA HOUSING FINANCE AGENCY**

**Subject:** RESOLUTION AMENDING RESOLUTION 22-08 TO AUTHORIZE HEDGING INSTRUMENTS FOR MBS BONDS

## **Background**

Since 2013, CalHFA has exclusively funded its single family production through the To-Be-Announced (“TBA”) market. The TBA market offers CalHFA a pre-determined price of a mortgage backed security (“MBS”) that the Agency will deliver in 60 days securitizing individual mortgages. This certainty around pricing is an advantage of the TBA market.

On March 15, 2020, the Federal Open Market Committee (“FOMC”) announced purchases of at least \$200 billion in MBS to “support the smooth function of markets for agency MBS.” Actual agency purchases were significantly higher than announced \$200 billion. In addition, from June 2020 to November 2021, the FOMC purchased \$40 billion of MBS monthly, above reinvestments. The FOMC’s MBS purchase activities in excess above reinvestments stopped in March 2022.

The reduction in FOMC purchases of MBS has resulted in a significant deterioration of the TBA market. As a result, CalHFA staff have been exploring other alternatives.

## **Fixed-Rate Pass-Through MBS Bonds**

One potential alternative is a pass-through bond. This would involve the purchase of the MBS through the issuance of taxable municipal bonds. Tax-exempt bonds using this structure would require volume cap. CalHFA would capture the economic difference between the interest rate on the taxable municipal bonds and the coupon on

the MBS. In certain markets, this would provide superior execution to the TBA market.

### **Purpose of the Resolution**

The Resolution removes the prohibition on Hedges with relation to MBS pass-through bonds. Unlike the TBA Market, which locks in the economics of the TBA market 60 days prior to financial closing, the pass-through market is subject to market forces. If rates decline in this period, CalHFA would stand to benefit financially through a lower cost of capital versus a higher than market rate MBS coupon. However, the opposite is true as well. If rates increase, CalHFA would suffer losses due to a higher cost of capital financing a lower than market rate MBS coupon. CalHFA is seeking to enter into cash-settled hedges or similar hedges to mitigate the potential changes in interest rates.

### **Substitution of Resolution / Section 22**

The current single family bond resolution specifically prohibits the use of hedges with respect the MBS bonds. This resolution is to both remove the prohibition and authorize the use of hedges. CalHFA's external counsel, currently assigned to single family programs, advised that the additional language allowing for the hedges was insufficient in its prior version of the Resolution as distributed and therefore a substitute was submitted to address the issue and allow CalHFA to hedge as intended, should the resolution be approved by the Board of Directors.

1 BOARD OF DIRECTORS  
2 OF THE CALIFORNIA HOUSING FINANCE AGENCY

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4 RESOLUTION NO. 22-20  
5 RESOLUTION AMENDING RESOLUTION 22-08 TO AUTHORIZE HEDGING  
6 INSTRUMENTS FOR MBS BONDS  
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8 WHEREAS, the California Housing Finance Agency (the “Agency”) has  
9 determined that there exists a need in California for providing financial assistance, directly or  
10 indirectly, to persons and families of low or moderate income to enable them to purchase or  
11 refinance moderately-priced single family residences (“Residences”);  
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13 WHEREAS, the Agency has determined that it is in the public interest for the  
14 Agency to assist in providing such financing by means of various programs, including whole  
15 loan and mortgage-backed securities programs (collectively, the “Program”) to make loans to  
16 such persons and families, or to developers, for the acquisition, development, construction and/or  
17 permanent financing of Residences (the “Loans”);  
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19 WHEREAS, pursuant to Parts 1 through 4 of Division 31 of the Health and Safety  
20 Code of the State of California (the “Act”), the Agency has the authority to issue bonds to  
21 provide sufficient funds to finance the Program, including the purchase of mortgage-backed  
22 securities (“MBSs”) secured by Loans, the payment of capitalized interest on the bonds, the  
23 establishment of reserves to secure the bonds, and the payment of other costs of the Agency  
24 incident to, and necessary or convenient to, the issuance of the bonds;  
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26 WHEREAS, the Agency, pursuant to the Act, has from time to time issued  
27 various series of its Home Mortgage Revenue Bonds (the “HMP Bonds”), its Housing Program  
28 Bonds (the “HP Bonds”), and its Residential Mortgage Revenue Bonds (the “RMR Bonds”), and  
29 is authorized pursuant to the Act to issue additional HMP Bonds, HP Bonds, and RMR Bonds  
30 (collectively with bonds authorized under this resolution to be issued under new indentures, the  
31 “Bonds”) to provide funds to finance the Program;  
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33 WHEREAS, the Bonds may be issued for the primary purpose of purchasing  
34 MBSs (“MBS Bonds”) or for debt management purposes of the Agency (“Debt-Management  
35 Bonds”); and  
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37 WHEREAS, the Agency has determined that hedging instruments could be used  
38 to address interest rate risk in the current market should the Agency issue MBS Bonds.  
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40 NOW, THEREFORE, BE IT RESOLVED by the Board of Directors (the “Board”) of the  
41 California Housing Finance Agency as follows:  
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43 Resolution 22-08, “Resolution authorizing the Agency’s single family bond indentures, the  
44 issuance of single family bonds, credit facilities for home ownership purposes, and related  
45 financial agreements and contracts for services” is amended as follows:  
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1 Article II, Section 10 is restated:

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Section 10. **Fixed-Rate Bonds Only.** MBS Bonds shall be issued only as fixed-rate bonds.

Article II, Section 22 is added as an addendum:

Section 22. **Authorization of Other Financial Agreements Related to Bonds.** The Executive Director is hereby authorized to enter into, for and in the name and on behalf of the Agency, any and all agreements and documents designed to (i) reduce or hedge the amount or duration of any payment, interest rate, spread or similar risk, (ii) result in a lower cost of borrowing when used in combination with the issuance or carrying of bonds or investments, or (iii) enhance the relationship between risk and return with respect to the Program or any portion thereof. To the extent authorized by law, including Government Code Section 5922, such agreements or other documents may include, but are not limited to, (a) interest rate swap agreements; (b) forward payment conversion agreements; (c) futures or other contracts providing for payments based on levels of, or changes in, interest rates or other indices; (d) contracts to exchange cash flows for a series of payments; (e) contracts, including, without limitation, interest rate floors or caps, options, puts or calls to hedge payment, interest rate, spread or similar exposure; or (f) contracts to obtain guarantees, including guarantees of mortgage-backed securities or their underlying loans; and in each such case may be entered into in anticipation of the issuance of bonds at such times as may be determined by such officers. Such agreements and other documents are authorized to be entered into with parties selected by the Executive Director, after giving due consideration for the creditworthiness of the counterparties, where applicable, or any other criteria in furtherance of the objectives of the Program.

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3 SECRETARY'S CERTIFICATE

4 I, Claire Tauriainen, the undersigned, do hereby certify that I am the duly authorized  
5 Secretary of the Board of Directors of the California Housing Finance Agency, and hereby  
6 further certify that the foregoing is a full, true, and correct copy of Resolution No. 22-20 duly  
7 adopted at a regular meeting of the Board of Directors of the California Housing Finance Agency  
8 duly called and held on the 21st day of July, 2022, at which meeting all said directors had due  
9 notice, a quorum was present and that at said meeting said resolution was adopted by the  
10 following vote:

11 AYES:

12 NOES:

13 ABSTENTIONS:

14 ABSENT:

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19 IN WITNESS WHEREOF, I have executed this certificate hereto this 21st day of  
20 July, 2022.

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23 ATTEST:

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25 CLAIRE TAURIAINEN  
26 Secretary of the Board of Directors of the  
27 California Housing Finance Agency  
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