For Immediate Release
August 10, 2007

Statement of OFHEO Director James B. Lockhart

Fannie Mae and Freddie Mac are important players in the mortgage market as they hold or guarantee 40 percent of all mortgages in the U.S. and about two-thirds of the conventional, conforming (non-jumbo) loans. This year their share of the mortgage market has grown rapidly. For this reason their safety and soundness is of paramount importance. The Enterprises have been very active in meeting their mission by providing significant liquidity and stability to the prime markets that they serve. They have entered into an increasingly large volume of securitization business in the conforming loan market -- more than $500 billion dollars in the first half of the year -- and that market is liquid and actively trading. We are encouraging them to increase this securitization activity.

The problems in the mortgage markets are concentrated in product areas outside the authorized normal business of the Enterprises. These markets are adjusting to tightened underwriting standards aimed at reducing losses and protecting borrowers. However, we are exploring with each Enterprise ways for them to enhance their support for affordable housing, both multi-family and single-family.

The portfolio caps were put in place last year because of their serious safety and soundness issues in response to Fannie Mae’s request to increase the portfolio caps, we issued a letter today to Fannie Mae. We also issued a response to Senator Schumer’s recent letter on this topic,
which is attached. The letters indicate that we will keep under active consideration requests for an increase in the portfolio caps, but we are not authorizing any significant changes at this time. We will continue to reassess that position, especially in the affordable housing area.

The marketplace should have confidence that Enterprise securities are trading efficiently. The Enterprises will remain active market participants and OFHEO will continue to closely monitor both the markets and the Enterprises’ safety and soundness. In addition, we will continue to consider changes as needed to ensure that the current liquidity in Enterprise securities remains. We also recognize the important role played by the Federal Reserve in providing liquidity to the market, as evidenced by its actions today.

Response letter follows

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OFHEO’s mission is to promote housing and a strong national housing finance system by ensuring the safety and soundness of Fannie Mae and Freddie Mac.
August 10, 2007

DELCIVERED BY FACSIMILE
AND FIRST CLASS MAIL

The Honorable Charles E. Schumer
United States Senate
313 Hart Senate Office Building
Washington, DC 20510

Dear Senator Schumer:

In your letter of August 7, you raised important questions regarding the liquidity of the U.S. mortgage market and the role Fannie Mae and Freddie Mac are playing, and could be playing, to support that market during this difficult period. OFHEO shares your concern with current market conditions and has been monitoring events on an ongoing basis.

I am pleased to report that, in fact, the Enterprises have provided notable support to the markets consistent with their charter mandates by securitizing and purchasing over $120 billion in mortgages in June alone. In discussions with Enterprise customers and other market participants we have confirmed that the Enterprises have been meeting customer needs. At the same time, I must note that both Fannie Mae and Freddie Mac remain “significant supervisory concerns” after more than three years of remediation efforts.

Present Market Activities

The Enterprises are participating in the mortgage market in two key ways:

First, while there are credit and liquidity issues today in certain segments of the mortgage market, those issues generally are not present in the largest segment of the mortgage market—the prime, conventional, conforming market that Fannie Mae and Freddie Mac traditionally serve. Indeed, the Enterprises have been doing, and are doing an increasingly large volume of securitization business in this market (over half a trillion dollars in the first half of the year), and the market is liquid and actively trading. They are gaining significant market share. We are encouraging them to continue to increase their securitization activities.
There are no caps on the Enterprises' securitization activities. This rapidly growing business makes mortgages more liquid. The Enterprises have more than $3 trillion in outstanding mortgage-backed securities and retained portfolios of about $1.4 trillion. About half of those portfolios are their own mortgage-backed securities that they choose to retain rather than sell. It is also worth noting that, with the same amount of capital, the Enterprises can securitize and guarantee over five times as many mortgages as they can if they retain those mortgages in their portfolios.

Second, the Enterprises recently informed their customers that future Enterprise purchases of non-traditional mortgage products and subprime mortgages must comply with the federal banking agencies’ Guidance on Nontraditional Mortgage Product Risks. The Enterprises will be notifying them shortly on the Statement on Subprime Mortgage Lending. They have also committed to assuring that their future purchases on private label securities are comprised only of loans that satisfy these standards. In that way, and with OFHEO’s encouragement, the Enterprises are doing their part to deter the continued use of loan characteristics and products that have a history of harming borrowers.

**Safety and Soundness**

In Chairman Dodd’s statement on turmoil in the subprime market of August 7, he said that “it may be appropriate, consistent with safe and sound practices as determined by the regulator, to ease the temporary regulatory cap on Fannie and Freddie’s mortgage portfolio.” In May of 2006, OFHEO imposed the portfolio cap on Fannie Mae as part of a consent agreement that included a $400 million fine. The agreement coincided with the release of our Special Examination Report. In July of 2006, Freddie Mac voluntarily agreed to a cap as they too had very significant operational, financial reporting, systems and risk management problems. As we considered a temporary increase in the portfolio caps, a very important consideration remains the safety and soundness of the GSEs.

Four months ago, OFHEO submitted its Annual Report to Congress on the condition of the Enterprises. At that time, we reported that both Enterprises remain “a significant supervisory concern.” Since then, each Enterprise has continued to make progress but much work remains to be done. Neither are timely filers of financial reports to the Securities and Exchange Commission (and Freddie Mac is not yet a SEC registrant). Timely filings would give investors the quality and depth of data made available by all other corporations. The continued lack of timely financial reports is a particularly troubling issue in unsettled markets.

**Market Conditions**

We view the market situation as significant, requiring the Enterprises and OFHEO to carefully assess any response to market conditions in light of safety and soundness concerns and in light of what the Enterprises may contribute to ameliorating any market dislocations. Another point to consider is that, although much smaller in percentage terms than many other market participants, the Enterprises have at this point marked-to-market losses on their portfolios. As I noted at the
outset, the principal market segment served by the Enterprises is liquid and working. Raising portfolio caps would allow the Enterprises to purchase mortgages in this market segment, but would not respond directly to those segments having the most significant difficulties.

OFHEO maintains a daily dialogue with the Enterprises regarding conditions in the primary and secondary mortgage market. We are also in regular contact with the federal banking agencies and other government agencies exchanging information regarding market conditions and market liquidity. Finally, we are in regular contact with market participants and we carefully analyze daily market data. OFHEO will continue to assess the mortgage market and continue to monitor, as you put it in your letter of August 7, whether “spillover from the subprime mortgage market is threatening the liquidity of the mortgage market as a whole.”

Our assessment of market conditions at this moment is that the subprime, Alt-A, and jumbo portions of the mortgage market are having varying degrees of difficulty, and that the conditions driving those difficulties are not the same in each case. Regulators, including OFHEO, and congressional leaders have for months been urging lenders to tighten lending standards in the subprime market and with respect to certain non-traditional mortgage products. While necessary to protect consumers, this tightening has predictably contributed to a shrinking of origination volume. However, the critical point is that the market’s current reaction is keyed to deteriorating credit conditions in these market segments that reflect very poor lending decisions and resulting losses to investors and, in many cases, to borrowers.

The Alt-A market with no or limited documentation also is suffering from past shoddy underwriting practices. The market is in the process of assessing the current credit quality of subprime and Alt-A loans and repricing them accordingly. Such market adjustments take time. We are encouraging the Enterprises to develop strategies to better serve the changing subprime and Alt-A markets in a safe and sound manner.

The jumbo market today appears to be going through a temporary adjustment that reflects liquidity more than credit issues. That market segment is beyond the scope of the GSE charters.

**OFHEO’s Position**

In light of the above facts, we issued a letter today to Fannie Mae indicating that we will keep under active consideration its request for an increase in the portfolio caps, but we are not authorizing any changes at this time. I would note that any needed action would be made for both Enterprises at the same time, consistent with safety and soundness. OFHEO takes very seriously the need to ensure the Enterprises’ public mission of supporting affordable housing and ensuring stability and liquidity of the secondary mortgage market and to do so in a safe and sound manner. Therefore, we are exploring with each Enterprise ways for them to better support affordable housing, both multi-family and single-family, consistent with their mission.
The market should have confidence that Enterprise securities are trading efficiently in the marketplace. The Enterprises will remain active market participants and OFHEO will continue to closely monitor both the markets and the Enterprises’ safety and soundness, and will continue to consider changes as needed to ensure that the current liquidity in Enterprise securities remains. In that way, we also recognize the important role played by the Federal Reserve in providing liquidity to the market, as evidenced by its actions today.

We look forward to working with you, Chairman Dodd, Ranking Member Senator Shelby, and all members of the Senate Banking Committee in the Fall on the much needed GSE reform legislation. Thank you for your communication on this important subject.

Sincerely,

[Signature]

James B. Lockhart
Director