



OFFICE OF FEDERAL HOUSING ENTERPRISE OVERSIGHT
1700 G STREET NW WASHINGTON DC 20552 (202) 414-3800

NEWS RELEASE

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CONTACTS:
Corinne Russell 202.414.6921
Stefanie Mullin 202.414.6376

OFHEO ANNOUNCES SECOND QUARTER 2005 MINIMUM AND RISK-BASED CAPITAL CLASSIFICATION FOR FREDDIE MAC AND FANNIE MAE

WASHINGTON, D.C. — Stephen Blumenthal, Acting Director of the Office of Federal Housing Enterprise Oversight (OFHEO), safety and soundness regulator for Fannie Mae and Freddie Mac (the Enterprises), classified Freddie Mac and Fannie Mae as adequately capitalized as of June 30, 2005.

The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 requires the OFHEO Director to determine the capital level and classification of the Enterprises not less than quarterly, and to report the results to Congress. OFHEO classifies the Enterprises as adequately capitalized, undercapitalized, significantly undercapitalized or critically undercapitalized. The Enterprises are required by Federal statute to meet both minimum and risk-based capital standards to be classified as adequately capitalized.

Freddie Mac

Freddie Mac's management has certified that the June 30, 2005 minimum capital report filed with OFHEO is in compliance with GAAP. Freddie Mac has also published June 30, 2005 financial data on August 30, 2005.

In addition, OFHEO has determined that Freddie Mac remained adequately capitalized for the first quarter of 2005, the March 31, 2005 reporting period. OFHEO has also determined, based upon analysis of information submitted by Freddie Mac, that the Enterprise is not required to resubmit a risk-based capital report for the first or second quarters of 2005.

OFHEO imposed a capital surcharge of 30 percent of the minimum capital surplus for Freddie Mac in January 2004 due to increased operational risk. Freddie Mac continued to maintain its minimum capital surplus in excess of the surcharge through the second quarter 2005.

Fannie Mae

Fannie Mae's capital classification is based on estimated financial information provided by the Enterprise and the application of accounting policies currently under review by OFHEO. The capital classification also utilizes current best estimates, as certified and represented by Fannie Mae management of its financial condition, including adjustments for additional accounting errors. This capital classification is subject to change as additional information becomes available, such as Fannie Mae's certification of its financial statements; and, OFHEO's completion of its special examination of accounting policies and practices at the company.

As of June 30, 2005, based upon information provided by Fannie Mae and adjustments for the impact on capital of estimated accounting errors, Fannie Mae has achieved an estimated \$5.9 billion surplus through earnings retention and asset sales. This projected surplus over the minimum capital requirement is sufficient to absorb uncertainties in the estimated impact to capital of the accounting errors, based on current information. Accordingly, OFHEO has determined that Fannie Mae remains adequately capitalized as of June 30, 2005.

Fannie Mae remains subject to the requirements imposed by the Agreement dated September 27, 2004, supplement dated March 7, 2005, and the Capital Restoration Plan dated February 10, 2005, which requires Fannie Mae to achieve a 30 percent capital surplus over the minimum capital requirement by September 30, 2005. OFHEO continues to actively monitor Fannie Mae's compliance with the Capital Restoration Plan on a weekly basis. At this time, based upon current assessments of accounting deficiencies and estimates of other potential impacts to capital, OFHEO anticipates Fannie Mae will meet the capital target for September 30, 2005. OFHEO will report on compliance with this requirement once third quarter financial information is officially reported and certified by Fannie Mae and verified by OFHEO.

SECOND QUARTER RESULTS:

As of June 30, 2005, Freddie Mac's risk-based capital requirement was \$11.144 billion. Freddie Mac's total capital of \$36.099 billion on that date exceeded the requirement by \$24.955 billion.

Freddie Mac's minimum capital requirement was \$24.073 billion. Freddie Mac's core capital of \$36.140 billion exceeded the minimum capital requirement by \$12.067 billion.

As of June 30, 2005, Fannie Mae's risk-based capital requirement was \$23.061 billion. Fannie Mae's total capital of \$36.144 billion on that date exceeded the requirement by \$13.083 billion.

Fannie Mae's minimum capital requirement was \$29.727 billion. Fannie Mae's core capital of \$35.641 billion exceeded the minimum capital requirement by \$5.914 billion.

Capital data for Freddie Mac and Fannie Mae as of March 31, 2005 and June 30, 2005:

Enterprise Risk-Based Capital Requirement (Billions of Dollars) (1)								
Risk Based Capital	Fannie Mae				Freddie Mac			
	30-Jun-05 (2)		31-Mar-05 (2)		30-Jun-05 (4)		31-Mar-05 (4)	
	Up	Down	Up	Down	Up	Down	Up	Down
Interest Rate Scenario								
Risk Based Capital Requirement	23.061	0	6.355	1.214	11.144	2.873	7.678	5.787
Total Capital	36.144		35.495		36.099		35.885	
Surplus (Deficit)	13.083		29.140		24.955		28.207	

Enterprise Minimum Capital Requirement (Billions of Dollars) (1)				
	Fannie Mae		Freddie Mac	
	30-Jun-05 (2, 3)	31-Mar-05 (2, 3)	30-Jun-05	31-Mar-05 (5)
	Minimum Capital Requirement	29.727	30.959	24.073
Core Capital	35.641	34.998	36.140	35.618
Estimated Surplus (Deficit)	5.914	4.039	12.067	11.869

Enterprise Critical Capital Requirement (Billions of Dollars) (1)				
	Fannie Mae		Freddie Mac	
	30-Jun-05 (2, 3)	31-Mar-05 (2, 3)	30-Jun-05	31-Mar-05 (5)
	Critical Capital Level	15.255	15.861	12.297
Core Capital	35.641	34.998	36.140	35.618
Estimated Surplus (Deficit)	20.385	19.137	23.843	23.495

1. Numbers may not add due to rounding.
2. Fannie Mae's capital calculation is based upon financial information and the application of accounting policies currently under review by OFHEO. The outcome of the review may result in a restatement of prior period results and a revision of the respective capital calculations.
3. Fannie Mae's minimum capital, critical capital and core capital are adjusted for accounting errors identified to date.
4. OFHEO determined that the risk-based capital resubmissions are not required for 1Q05 and 2Q05 as minimum capital remains the binding capital requirement and the impact on the surplus from restated financials is minimal.
5. Resubmitted by Freddie Mac

GENERAL ANALYSIS OF THE REGULATORY CAPITAL RESULTS

Freddie Mac

Minimum Capital

Freddie Mac increased its minimum capital surplus amount by \$0.2 billion to \$12.1 billion, approximately 50.1% over the minimum capital requirement. The primary driver for an increase in the surplus amount was an increase in retained earnings. Freddie Mac's total assets grew for the quarter, increasing the minimum capital requirement by \$0.3 billion. In addition, an increase in retained earnings resulted in a \$0.5 billion increase in core capital.

Risk-based Capital

By statute, stress test interest rate levels are a function of the average 10-year Constant Maturity Treasury (CMT) over the most recent nine months. During the second quarter of 2005, the nine-month average declined by 5 basis points to 4.21%. As a result, stress test 10-year CMT levels dropped from 7.45% to 7.37% in the up-rate stress test, and from 2.13% to 2.10% in the down-rate stress test.

Similar to the tightening trend in the nine-month average rate level, spot market interest rates moved lower during the quarter with 10-year CMT 50 basis points below first quarter levels. With the decline in rate levels, prepayment speeds increased which in turn led to shorter durations on fixed-rate mortgage assets of the Enterprises. To manage this interest rate exposure, Freddie Mac responded to shorter duration assets by rebalancing its debt and derivative portfolios.

Similar to last quarter, Freddie Mac's risk-based capital requirement was higher in the up-rate stress test. Freddie Mac's risk-based capital requirement increased to \$11.1 billion in the up-rate stress test, and decreased to \$2.9 billion in the down-rate stress test. Freddie Mac's risk-based capital surplus decreased from \$28.2 billion to \$25.0 billion due primarily to the higher binding risk-based capital requirement.

Fannie Mae

Due to the ongoing accounting review and the absence of publicly available data, OFHEO is not disclosing analysis of Fannie Mae's capital results.

TREATMENTS FOR NEW ACTIVITIES

Each quarter OFHEO must incorporate into the stress test all new activities and instruments before determining whether an Enterprise is adequately capitalized (new activities are defined in section 3.11.1 of the risk-based capital regulation). When OFHEO requires more time for analysis to determine the appropriate capital treatment for a new activity, the activity will receive an interim treatment in the stress test. Final treatment for these instruments is determined after additional analysis, based upon consideration of the risks associated with the item. As part of this quarter's capital classification, final treatments for two new activities - Split-Rate ARM Loans and Pre-refunded Tax-Exempt Municipal Bonds - have been incorporated into the stress test. The actual treatments can be found at <http://www.ofheo.gov/media/pdf/newactivities92805.html>. New activities treatments are applicable to both Enterprises.

DEFINITION OF CAPITAL STANDARDS

Minimum capital represents an essential amount of capital needed to protect an Enterprise against broad categories of business risk. For purposes of minimum capital, an Enterprise is considered adequately capitalized if core capital — common stock; perpetual noncumulative preferred stock; paid in capital; and retained earnings — equals or exceeds minimum capital. The minimum capital standard is 2.5 percent of assets plus 0.45 percent of adjusted off-balance-sheet obligations.

OFHEO's **risk-based** capital requirement is the amount of total capital — core capital plus a general allowance for loan losses less specific reserves — that an Enterprise must hold to absorb projected losses flowing from future adverse interest-rate and credit-risk conditions specified by statute, plus 30 percent mandated by statute to cover management and operations risk. The risk-based capital standard is based on stress test results calculated for the two statutorily prescribed interest rate scenarios, one in which 10-year Treasury yields rise 75 percent (up-rate scenario) and another in which they fall 50 percent (down-rate scenario). Changes in both scenarios are generally capped at 600 basis points. The risk-based capital level for an Enterprise is the amount of total capital that would enable it to survive the stress test in whichever scenario is more adverse for that Enterprise, plus 30 percent of that amount to cover management and operations risk.

The **critical** capital level is the amount of core capital below which an Enterprise must be classified as critically undercapitalized and generally must be placed in conservatorship. Critical capital levels are computed consistent with the Federal Housing Enterprises Safety and Soundness Act of 1992 as follows: One-half of the portion of minimum capital requirement associated with on-balance-sheet assets plus five-ninths of the portion of the minimum capital requirement associated with off-balance-sheet obligations.

Technical questions regarding these results should be directed to: rbcquestions@ofheo.gov.

Media questions regarding these results should be directed to Corinne Russell at: crussell@ofheo.gov or 202.414.6921 or Stefanie Mullin at: stefanie.mullin@ofheo.gov or 202.414.6376.

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