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NEWS RELEASE

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OFHEO ANNOUNCES THIRD QUARTER 2004 MINIMUM AND RISK-BASED CAPITAL CLASSIFICATION FOR FREDDIE MAC

WASHINGTON, D.C. — Armando Falcon, Jr., Director of the Office of Federal Housing Enterprise Oversight (OFHEO), safety and soundness regulator for Fannie Mae and Freddie Mac (the Enterprises), has classified Freddie Mac as adequately capitalized as of September 30, 2004.

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's capital classification is based on financial information and the application of accounting policies currently involved in the ongoing financial review process. The publication of Freddie Mac financial statements for 2004 will impact both minimum capital surpluses and, to a lesser degree, risk-based capital surpluses as reported and relied upon for classifications by OFHEO. OFHEO will continue to monitor and analyze 2004 capital resubmissions once the financial results for these periods are issued by Freddie Mac.

OFHEO imposed a capital surcharge for Freddie Mac in January 2004 due to increased operational risk. Freddie Mac has maintained its minimum capital surplus in excess of the surcharge during the third quarter 2004.

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THIRD QUARTER RESULTS:

As of September 30, 2004, Freddie Mac's risk-based capital requirement was $5.749 billion. Freddie Mac's total capital of $34.397 billion on that date exceeded the requirement by $28.648 billion.

Freddie Mac's minimum capital requirement was $24.404 billion. Freddie Mac's core capital of $34.227 billion exceeded the minimum capital requirement by $9.823 billion.

Capital data for Freddie Mac as of June 30, 2004 and September 30, 2004:

	Risk-based Capital (1)(2)			
	30-Sept-04		**30-June-04**	
Interest Rate Scenario	Up	Down	Up	Down
Risk-Based Capital Requirement	5.749	2.623	1.322	3.858
Total Capital	34.397			33.081
Surplus (Deficit)	28.648			29.224

Minimum Capital (1)(2)		
	30-Sept-04	**30-June-04**
Minimum Capital Requirement	24.404	24.266
Core Capital	34.227	32.884
Surplus (Deficit)	9.823	8.619

Critical Capital (1)(2)		
	30-Sept-04	**30-June-04**
Critical Capital Level	12.434	12.362
Core Capital	34.227	32.884
Surplus (Deficit)	21.792	20.523

(1) Numbers may not add due to rounding.
(2) Freddie Mac's 9/30/2004 and 6/30/2004 capital numbers are based on financial information and application of accounting policies currently involved in the restatement process. These numbers are subject to change.

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 and Stefanie Mullin at: smullin@ofheo.gov or 202.414.6376.

GENERAL ANALYSIS OF FREDDIE MAC'S REGULATORY CAPITAL RESULTS

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 third quarter of 2004, the nine month average increased by less than 1 basis point to 4.31%. As a result, the stress test interest rate levels were similar to last quarter—7.54% in the up-rate stress test and 2.15% in the down-rate stress test.

While the moving average rate level remained relatively unchanged, spot market interest rates declined significantly during the third quarter. Consequently, the duration of existing mortgage assets shortened as the economic incentives attached to early prepayment increased. Consistent with shorter assets and a falling interest rate environment, the Enterprise moved to shorten liability durations as part of its risk management operations.

Unlike last quarter, the up-rate stress test was binding for Freddie Mac in the third quarter. Freddie Mac's risk-based capital level decreased by $1.2 billion to $2.6 billion in the down-rate stress test and increased by $4.4 billion to $5.7 billion in the up-rate stress test. Freddie Mac's capital surplus declined to $28.6 billion due to a higher binding risk-based capital requirement.

Net interest margin for Freddie Mac increased slightly in the down-rate stress test and fell in the up-rate test compared to last quarter. The results of the down-rate stress test environment were driven by slightly lower funding costs stemming from shorter-term liabilities. The converse occurred in the up-rate environment where shorter-term liabilities led to higher funding costs and, subsequently, lower net interest margin.

Freddie Mac's minimum capital surplus increased by $1.2 billion to $9.8 billion this quarter. The primary driver in the increase in surplus was a $1.3 billion increase in core capital that was partially offset by a $0.1 billion increase in the minimum capital requirement. The increase in the minimum capital requirement was the result of an increase in on-balance sheet assets and off-balance sheet obligations.

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 one new activity - Consumer Price Index (CPI) Coupon Linked Instruments - have been incorporated into the stress test. The actual treatment can be found at http://www.fhfa.gov/Default.aspx?Page=227. This treatment is 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.

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