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**OFHEO ANNOUNCES SECOND QUARTER 2006
MINIMUM AND RISK-BASED CAPITAL CLASSIFICATION
FOR FANNIE MAE AND FREDDIE MAC**

WASHINGTON, D.C. — James B. Lockhart, Director of the Office of Federal Housing Enterprise Oversight (OFHEO), safety and soundness regulator for Fannie Mae and Freddie Mac (the Enterprises), classified Fannie Mae and Freddie Mac as adequately capitalized as of June 30, 2006.

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.

“Operational, accounting and systems weaknesses at both Enterprises continue. Therefore it remains essential that the Enterprises maintain a strong capital cushion,” said Lockhart.

With this disclosure, OFHEO is continuing to emphasize and disclose the Enterprises’ minimum capital surplus over the OFHEO-directed capital requirement versus the statutory requirement historically disclosed. Fannie Mae’s surplus as a percent of the OFHEO-directed requirement increased to 9.9 percent from the prior quarter’s 8.1 percent. Freddie Mac’s surplus as a percent of the OFHEO-directed requirement decreased from 12.1 percent to 8.0 percent over the quarter due to asset growth. Both Enterprises have agreed to growth restrictions on their retained portfolio. Freddie Mac’s restrictions were effective July 1, 2006 and limit retained portfolio growth to 0.5 percent quarterly until the company becomes timely GAAP-compliant filers of financial statements.

SECOND QUARTER CAPITAL RESULTS:

Fannie Mae's adjusted¹ OFHEO-directed capital requirement on June 30, 2006 was \$38.2 billion and its adjusted statutory minimum capital requirement was \$29.4 billion. Fannie Mae's core capital of \$42.0 billion exceeded the OFHEO-directed capital requirement by \$3.8 billion. Fannie Mae's core capital exceeded the statutory critical capital requirement by \$26.9 billion.

Freddie Mac's OFHEO-directed capital requirement on June 30, 2006 was \$34.4 billion and its statutory minimum capital requirement was \$26.5 billion. Freddie Mac's core capital of \$37.1 billion exceeded the OFHEO-directed minimum capital requirement by \$2.7 billion. Freddie Mac's core capital exceeded the statutory critical capital requirement by \$23.6 billion.

Enterprise Minimum Capital Requirement (Billions of Dollars) ^(a,b)				
	Fannie Mae		Freddie Mac	
	30-Jun-06 ^(c,d)	31-Mar-06 ^(c,d)	30-Jun-06 ^(c)	31-Mar-06 ^(c)
Minimum Capital - Statutory Requirement	29.419	28.708	26.460	25.500
Minimum Capital - OFHEO Directed Requirement	38.245	37.320	34.398	33.150
Core Capital	42.037	40.333	37.139	37.165
Surplus (Deficit) (based on OFHEO Directed Requirement)	3.792	3.013	2.740	4.015

Enterprise Critical Capital Requirement (Billions of Dollars) ^(a,b)				
	Fannie Mae		Freddie Mac	
	30-Jun-06 ^(c,d)	31-Mar-06 ^(c,d)	30-Jun-06 ^(c)	31-Mar-06 ^(c)
Critical Capital Level	15.145	14.779	13.522	13.037
Core Capital	42.037	40.333	37.139	37.165
Surplus (Deficit)	26.892	25.553	23.616	24.128

a. Numbers may not add due to rounding.

b. Subject to revision based upon results of ongoing financial restatement and audit processes.

c. OFHEO has directed both Fannie Mae and Freddie Mac to maintain an additional 30% capital in excess of the statutory minimum capital requirement.

These requirements have been an additional requirement since January 28, 2004, for Freddie Mac and since September 30, 2005, for Fannie Mae.

The minimum capital requirement and minimum capital surplus numbers stated in these charts reflect the inclusion of the additional 30% OFHEO-directed capital requirement.

d. Fannie Mae's minimum capital, critical capital, and core capital are adjusted for accounting errors identified to date.

As of June 30, 2006, Fannie Mae's risk-based capital requirement was \$26.3 billion. Fannie Mae's total capital of \$42.9 billion on that date exceeded the requirement by \$16.6 billion.

¹ The term "adjusted" reflects that Fannie Mae's minimum capital submissions adjust book capital based upon estimated accounting change impacts.

As of June 30, 2006, Freddie Mac's risk-based capital requirement was \$17.0 billion. Freddie Mac's total capital of \$37.5 billion on that date exceeded the requirement by \$20.5 billion.

Enterprise Risk-Based Capital Requirement (Billions of Dollars) ^(a,b)								
Interest Rate Scenario	Fannie Mae				Freddie Mac			
	30-Jun-06		31-Mar-06		30-Jun-06		31-Mar-06	
	Up	Down	Up	Down	Up	Down	Up	Down
Risk Based Capital Requirement	18.843	26.330	17.533	10.529	10.843	17.024	8.801	11.935
Total Capital		42.888	41.174			37.504		37.624
Surplus (Deficit)		16.558	23.641			20.480		25.689

a. Numbers may not add due to rounding.

b. Subject to revision based upon results of ongoing financial restatement and audit processes.

Minimum and Critical Capital

During the second quarter of 2006, Fannie Mae's minimum capital surplus increased by \$0.8 billion to \$3.8 billion, approximately 9.9 percent over the OFHEO-directed capital requirement. The primary driver of the higher surplus was an increase in core capital. Core capital increased by \$1.7 billion to \$42.0 billion due to an increase in retained earnings. The increase in retained earnings reflects contributions from core income and, to a lesser extent, after-tax mark-to-market derivative valuation gains less the \$0.4 billion civil penalty resulting from the settlement agreement with OFHEO and the SEC.

Freddie Mac's core capital was 8.0 percent over the OFHEO-directed capital requirement, and the surplus fell approximately \$1.3 billion to \$2.7 billion from the prior quarter's surplus amount of \$4.0 billion. Freddie Mac's assets grew during the quarter, increasing the OFHEO-directed capital requirement by \$1.2 billion. Core capital was \$37.1 billion, which was virtually unchanged from prior quarter's amount of \$37.2 billion. Retained earnings grew slightly with modest increases in core income and very modest derivative gains being mostly offset by restatement adjustments and stock repurchase activity.

Changes in critical capital mirrored changes in minimum capital for both Enterprises.

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. At the end of the second quarter of 2006, the nine-month average of the 10-year CMT rose to 4.71 percent 29 basis points higher than the nine-month average at the end of the first quarter of 2005. As a result, 10-year CMT levels at the end of the first year in the risk-based capital stress test increased from 7.74 percent to 8.24 percent in the up-rate stress test, and from 2.21 percent to 2.35 percent in the down-rate stress test.

Fannie Mae's risk-based capital surplus decreased from \$23.6 billion to \$16.6 billion. In contrast to last quarter, the down-rate stress test produced a higher risk-based capital

requirement than the up-rate stress test. Fannie Mae's risk-based capital requirement in the down-rate stress test increased \$15.8 billion to \$26.3 billion from \$10.5 billion. Their risk-based capital requirement in the up-rate stress test increased by \$1.3 billion to \$18.8 billion. In the second quarter of 2006, the yield curve shifted upward, but remained flat. As interest rates rose, expected prepayment speeds decreased and fixed-rate mortgage assets lengthened in duration. To better match the duration of their assets, Fannie Mae issued long-term debt and increased its net pay-fixed swap position. This rebalancing caused Fannie Mae to be more exposed to a decline in interest rates this quarter than the prior quarter.

Freddie Mac's risk-based capital surplus decreased from \$25.7 billion to \$20.5 billion due primarily to a higher risk-based capital requirement. The down-rate stress test produced a higher risk-based capital requirement than the up-rate stress test. Similar to the scenario described above, as interest rates rose, expected prepayment speeds decreased and fixed-rate mortgage assets lengthened in duration. Freddie Mac, as a result, also rebalanced their portfolio to better match duration of their assets by issuing long-term debt and executing pay-fixed swaps. Freddie Mac's risk-based capital requirement increased by \$5.1 billion to \$17.0 billion in the down-rate stress test, and by \$2.0 billion to \$10.8 billion in the up-rate stress test.

QUALIFICATIONS AND COMPLIANCE

Fannie Mae

Fannie Mae's capital classification is based upon Fannie Mae's best estimates of its financial condition, as certified and represented as true and correct to the best of Fannie Mae management's belief and knowledge. The classification remains subject to revision during Fannie Mae's re-audit and accounting restatement process.

Fannie Mae remains subject to the requirements imposed by the Consent Order dated May 23, 2006 and the Capital Restoration Plan approved February 17, 2005. The Capital Restoration Plan required Fannie Mae to achieve a 30 percent capital surplus over the minimum capital requirement by September 30, 2005 (OFHEO-directed capital requirement), a requirement Fannie Mae met and has continued to maintain through the second quarter 2006.

Freddie Mac

Freddie Mac's capital classification is based upon Freddie Mac's best estimates of its financial condition, as certified and represented as true and correct by Freddie Mac's management. The capital classification remains subject to revision based upon results from Freddie Mac's ongoing audit, management reviews, and control assessments.

OFHEO imposed a capital surcharge of 30 percent of the minimum capital requirement for Freddie Mac in January 2004 due to increased operational risk. Freddie Mac continued to maintain its minimum capital surplus in excess of the OFHEO-directed capital requirement through the second quarter 2006.

SECOND QUARTER QUALIFYING SUBORDINATED DEBT RESULTS

Additionally, OFHEO is releasing qualifying subordinated debt positions of both Enterprises in accordance with the September 1, 2005 Agreements between OFHEO and the Enterprises. (See 9/2/05 release at <http://www.fhfa.gov/webfiles/2098/9205SubDebtDiscAgreements.pdf>)

Fannie Mae's total capital and qualifying subordinated debt for the second quarter 2006 exceeded the requirements outlined in the Agreement dated September 1, 2005.

Freddie Mac's total capital and qualifying subordinated debt for the second quarter 2006 exceeded the requirements outlined in the Agreement dated September 1, 2005.

Qualifying subordinated debt levels for both Enterprises are disclosed below.

Fannie Mae Qualifying Subordinated Debt Disclosure (Billions of Dollars) ^(a,b)		
	30-Jun-06 ^(c,d)	31-Mar-06 ^(c,d)
Total Capital & Qualifying Subordinated Debt	50.744	49.029
Sub Debt Requirement ^(e)	42.324	41.288
Surplus (Deficit)	8.421	7.741

Freddie Mac Qualifying Subordinated Debt Disclosure (Billions of Dollars) ^(a,b)		
	30-Jun-06 ^(c)	31-Mar-06 ^(c)
Total Capital & Qualifying Subordinated Debt	43.821	42.710
Sub Debt Requirement ^(e)	38.849	37.344
Surplus (Deficit)	4.972	5.366

- a. Numbers may not add due to rounding.
- b. Qualifying Subordinated Debt is defined as subordinated debt that contains the interest deferral feature. The interest deferral requires the deferral of interest payments for up to 5 years if:
 - 1) The corporation's core capital falls below 125% of critical capital, or
 - 2) The corporation's core capital falls below minimum capital AND, pursuant to the corporation's request, the Secretary of the Treasury exercises discretionary authority to purchase the company's obligations under Section 306(c) of the Freddie Mac Charter Act and Section 304(c) of the Fannie Mae Charter Act.
- c. Subject to revision based upon results of ongoing financial restatement and audit processes.
- d. Fannie Mae's minimum capital, critical capital, core capital and qualifying subordinated debt are adjusted for accounting errors identified to date.
- e. The sum of outstanding net MBS times 0.45 percent and on-balance sheet assets times 4 percent.

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, including guaranteed mortgage securities.

The **OFHEO-directed** capital requirement is the amount of capital the Enterprise currently needs to maintain to compensate for increased operational, accounting, and control risks. The level is prescribed by the Director of OFHEO. At this time, both Enterprises are required to hold 30 percent over the statutory minimum capital requirement. This is calculated by multiplying the minimum capital requirement by 1.3 times.

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.

QUALIFYING SUBORDINATED DEBT

Qualifying subordinated debt is defined as subordinated debt that contains the interest deferral feature described below:

The interest deferral requires the deferral of interest payments for up to 5 years if:

- The corporation's core capital falls below 125 percent of critical capital, or
- The corporation's core capital falls below minimum AND, pursuant to the corporation's request, the Secretary of the Treasury exercises discretionary authority to purchase the company's obligations under Section 306(c) of the Freddie Mac Charter Act and Section 304(c) of the Fannie Mae Charter Act.

The September 1, 2005 agreement requires that:

Subordinated debt will be issued in a quantity such that the sum of total capital (core capital plus general allowance for losses) plus the outstanding balance of qualified subordinated debt will equal or exceed the sum of outstanding net MBS times 0.45 percent and total on-balance sheet assets times 4 percent.

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

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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.