

The *GSE* REPORT

Fannie Mae & Freddie Mac

- *Former CEO of Fed. Home Loan Mortg. Corp Responds to Forbes article, "Fall of the house of Fannie:"*
- Kenneth Thygerson (CEO of Federal Home Loan Mortgage Corp., 1981-1985) congratulated *Forbes* magazine for "its excellent analysis of Fannie Mae." "It and its sister, Freddie Mac, hire most of their potential critics and make sure others aren't heard by sponsoring journals and putting their staff on editorial boards. But some day banks will recognize the profits they could be making if Fannie and Freddie didn't have a subsidized lock on portfolio lending and private market securitization. If the Fannie charter is as good as they say it is, let anyone have one. Banks could put one in their holding companies." (*Forbes*, 11/17/97)
- *Resolution for MBA Task Force to Address GSE Encroachment; Encourages Privatization of Fannie and Freddie:*
 - The Mortgage Bankers Association intends to form a task force to analyze the impact of privatizing Fannie Mae and Freddie Mac. Tom LaMalfa, director of Wholesale Access, Columbia, MD, introduced the resolution calling for the creation of the task force. He asked the MBA to allocate \$500,000 for a study to consider the proper role of the GSEs and to calculate their costs to the mortgage banking industry. His resolution was accepted by the MBA's Secondary Market Committee and Residential Loan Production Committee, and is subject to revision. The task force, according to Mr. LaMalfa's resolution, would "examine the government-sponsored enterprises' effects on the market's existing structure, capital position, competitive environment and other factors." Claiming to be speaking for a silent majority of mortgage bankers, Mr. LaMalfa said that the current role of the GSEs diminishes the profitability of companies in the private sector since they dominate the conventional market. "They [the GSEs] determine for lenders what documents they must submit, what kind of waivers they can get and what products they can sell," he said, adding, "they are in a position where they call all of the shots, and that's why they make all of the money. What you have to remember is that

there are two conforming, conventional conduits, Fannie Mae and Freddie Mac – they have no competitors.”

- Describing what would occur if the GSEs were privatized, Mr. LaMalfa said, “Suddenly, they are stripped of their privileges; guess what, Countrywide, Norwest, Fleet and a dozen other companies set up mini-Fannies and Freddie’s. Suddenly, neither the brokers or the mortgage bankers would not have only two companies to sell to, but would have the opportunity to sell to 6 or 12 or 18 companies.” Mr. LaMalfa sees the recent announcement by Freddie Mac that it will move into the subprime market as evidence of a continuing pattern of encroachment by the agencies into the private sector. Arguments opposed to and in favor of the agencies are divided most violently on the question of whether the GSEs enjoy an implicit guarantee of the government. Freddie Mac contends that an implied guarantee does not exist. Mr. LaMalfa believes, however, that the behavior of investors indicates that it is widely accepted that this guarantee, though implicit, exists. This can be seen, he said, in the ability of agencies to borrow at preferred rates, as well as the agencies’ exemption from state and local taxes, and their exemption from SEC registration requirements. These save the agencies more than \$300 million annually, according to Mr. LaMalfa. “I am not trying to do away with these agencies, I’m trying to strip them of privileges that create a clash between two different market structures,” he said. (*National Mortgage News*, 10/27/97).

- *GSE Automated Underwriting Systems Increasingly Dictate Lenders’ Choices:*
 - As more lenders use automated underwriting systems provided by Fannie Mae and Freddie Mac, those AU systems are changing the way the lenders order credit report information. Don Robert, president of First American Credco, says that Desktop Underwriter and Loan Prospector, the Fannie Mae’s and Freddie Mac’s AU systems, increasingly dictate how lenders obtain credit report needs. “Fannie Mae and Freddie Mac have only a limited number of credit reporting agencies that are authorized to interface with their systems,” Mr. Robert explained. He believes that gives an edge to firms with sophisticated technology and electronic data interchange capabilities. The rise of the AU systems will put smaller credit reporting companies at a disadvantage, he said. “Smaller, less technologically savvy credit companies are going to find themselves on the outside looking in,” he said. Mr. Robert expects to see more lenders relying on mortgage scores, which are credit scores specifically tailored for the mortgage industry, as opposed to standard credit scores. (*National Mortgage News*, 11/10/97).

- *APPAM Panel Addressed GSEs:*
 - On November 7, the 19th Annual Research Conference of the Association for Public Policy Analysis and Management (APPAM) featured a panel on “The Benefits and Costs of Government-Sponsored Enterprises (GSEs).” The conference, held in Washington, DC at the ANA Hotel, focused on papers presented by Mario Ugoletti of the U.S. Department of the Treasury, Charles Capone of OHFEO, and Robin Seiler, Jr. of the Congressional Budget Office. The paper topics include conceptual issues involved in measuring the benefits of GSE status (Mario Ugoletti); the net value generated from Fannie and Freddie’s housing goals (who is involved and what other delivery

mechanisms could be used) (Charles Capone); and the similarities between GSEs and investor-owned public utilities (Robin Seiler, Jr.).

- *GSEs Seek Overseas Investments:*
 - Freddie Mac is continuing its efforts to increase sales to overseas investors by increasing sales to central banks and foreign institutional investors, which have appetites for higher yielding, non-credit sensitive assets. Foreign buyers hold about 10% of mortgage investments; industry consultants said that percentage is growing. Fannie Mae and Ginnie Mae said they are seeing interest from foreign investors. Certain Ginnie Mae securities are popular with Asian investors, said George Rose, a securities marketer at Ginnie Mae. Fannie Mae, which scans international markets to find investors for its mortgage-backed securities, is also making a big push overseas to sell the company's debt, said Gene Spencer, VP for mortgage securities investor marketing at Fannie Mae. (*American Banker*, 11/4/97)
- *GE Capital Mortgage Insurance Expands into Australia:*
 - GE Capital Services has agreed to buy Housing Loans Insurance Corp. Ltd., Australia's largest mortgage insurer, from the Australian government. GE Capital Mortgage Insurance already owns mortgage insurers in Canada and the United Kingdom. "Strategically, we are looking to diversify our risk around the world," said Mark Steinman, vice president of business development for GE Capital Mortgage Insurance. GE will manage old business for the Australian government but will assume risk only on new policies. "The old insurance risks stay with government. We are essentially buying a new company with a fresh balance sheet," Mr. Steinman said. As opposed to the US, mortgage insurance in Australia benefits lenders only. There are no Australian agencies similar to Fannie Mae and Freddie Mac, who will not buy low-down-payment loans unless they are insured. Mr. Steinman claims there is a growing secondary market for securitized mortgages in Australia. Mortgage insurance has been highly profitable in recent years, and lenders are pressuring insurers to share profits. An international acquisition might be a good way for insurers to spend excess capital. "I suspect you'll see more international expansion going on. The industry is just flooded with money," said Edwin Ciskowski, an analyst with Equitable Securities, Nashville, TN (*American Banker*, 11/6/97).
- *GSE Pool Insurance May Now Be Probed by HUD:*
 - The last issue of *The GSE Report* reported that a California Assemblyman claimed that lenders are reaping the benefits of GSE pool insurance and failing to pass along the savings to consumers. He believes this may be a violation of RESPA and has asked CA insurance regulators to look into the issue for possible violations. Sarah Rosen, a senior official at HUD, stated that HUD is looking at the issue of pool insurance noting that, "We may have something more to say soon." (*National Mortgage News*, 11/10/97)
- *Senate Passes PMI Bill That May Give Fannie and Freddie Regulatory Authority:*

- The Senate passed the PMI bill before adjourning. The bill grants Fannie Mae and Freddie Mac “regulator” authority by allowing the agencies to develop the guidelines that define “high risk” mortgages. Senators Chris Dodd (D-CT) and John Kerry (D-MA) were the original authors of the amendment that would require Fannie and Freddie to define “high-risk loans.” The amendment continues to be criticized. Mike Farrell, legislative counsel at the MBA stated that “since there is no regulator in the Senate version, Fannie Mae and Freddie Mac would decide at which point PMI could be canceled for some of these loans and that’s giving them too much power.” (*National Mortgage News*, 11/10/97)
- *GSEs Exploring High LTV Niche:*
 - Fannie and Freddie are seriously analyzing the high LTV market to see what role they can play in this booming market. Investment bankers and executives involved in this market indicate that both firms are far along on their research, but are taking slightly different routes. “Freddie is considering portfolioing this stuff,” said one investment banker. “Fannie, at least initially, wants to act as a guarantor.” FirstPlus Financial (one of nation’s top high LTV lenders/securitizers) has been contacted by Fannie Mae to discuss the issue. Those involved in the high LTV market agree that if the GSEs enter this \$20 billion niche, profit margins will be compressed. “They’re already moving into B&C lending - and now this,” said one mortgage banker. “Who’s going to stop these guys?” One high LTV executive stated that if the GSEs entered the market, they could “give us a good execution on our securities. But I know that over time we will make less money.” One lender commented that the “bankers are not going to be overjoyed by this. High LTV lending means debt consolidation-and that means the credit card and personal loan business will get hurt.” One advisor said that MBIA, a bond insurer will get hurt. “If Fannie and Freddie enter this market and act as a guarantor, that means less business for MBIA on asset-backed deals.” A Freddie Mac spokesperson said that have been approached by lenders “who are looking to sell this stuff to us.” One source noted that Freddie served a guarantor of a mortgage-backed deal with Black Rock Financial. “The paper was HUD loans with LTVs of 80% to 90% but when you factor in the arrears on the loans, these were high LTV mortgages.” A Fannie Mae spokeswoman said the company, “is not seriously looking at high LTVs.” However, at a recent high LTV/Alternative ‘A’ conference in Washington, three Fannie and five Freddie officials were registered as attendees. (*National Mortgage News*, 11/3/97)
- *GSE Limits Look to Rise*
 - The conforming loan limit, based on changes in the Federal Housing Finance Board index from October to October, will be announced on November 26. It is estimated that both the Fannie Mae/Freddie Mac and the FHA loan limits will rise about 6 percent next year. Under this scenario, the Fannie Mae/Freddie Mac single-family loan limit would rise from the current level of \$214,600 to \$227,500, and the single-family FHA loan ceiling for so-called “high-cost” areas would rise from \$160,950 to \$170,600. Any hike in the Fannie Mae/Freddie Mac loan limits is expected to but into the business of private

conduits and lenders that operate in the jumbo mortgage market. Likewise, any increase in the FHA loan limit is seen as cutting into future private mortgage insurance activity. (*Inside Mortgage Finance*, 11/14/97)

- *GSEs to Expand Score Availability to Service Bureaus:*
 - The loss mitigation and collection scoring technologies developed by Fannie Mae (Risk Profiler) and Freddie Mac (EarlyIndicator) will be available through several service bureaus by early next year. Both systems aim to identify the probability of a past due mortgage remaining delinquent and continuing through to foreclosure. This information is designed to enable servicers to target higher risk loans for workout or intensified collection efforts. “We are working with Alltel, Excelsis, Fiserv and others to have EarlyIndicator integrated in some form for service bureau functionality in a way that makes it easier, faster and simpler for people to access the EarlyIndicator scores,” said Steve Blose, a spokesman for the Freddie Mac/MGIC alliance. According to Blose, the significance for users of the technology will be a “simplified process for selecting the loans to be scored by EarlyIndicator, or submitting the loan data to the scoring models and for viewing and using the scores in a productive way, which would be putting them in predictive dialers or other queuing technology, or into spread sheets or database software for analysis.” Currently, EarlyIndicator can be used by servicers without the software being integrated into third-party servicing software. Explaining her company’s arrangement with Fannie Mae, Alltel spokeswoman Darlene LeGrand said, “We are working with Fannie Mae to develop a standard extract that will give them [Alltel clients] all the data they need to run Risk Profiler. So, clients don’t have to go outside the system and develop these standard extracts based on what Fannie Mae is requiring. It will automatically generate that for them.” (*National Mortgage News*, 11/10/97)
- *One Account with Mortgage Loan as Core:*
 - Virgin Enterprise, best known for its entertainment and transportation businesses, is getting into the financial services industry through their company, Virgin Direct (partnership with Australian Mutual Provident Society). Since it lacks a banking license, Virgin Direct is joining forces with The Royal Bank of Scotland to launch *One* - an account that can include mortgage, credit card, personal loan, and transactions all in one account. The company said they are actively considering entering the U.S. market, but “would only do so in conjunction with a U.S.-based partner.” To be eligible for the account, one must be a Virgin Direct customer and a property owner. Paychecks must be deposited directly into the account, and the depositor’s home must serve as collateral for the loan. The property value must be at least \$83,000. All borrowings are at a mortgage rate. (*Royal Bank of Scotland Press Release* 10/17/97, *American Banker*, 11/7/97)
 - Citicorp announced its “Citibank Account,” an account that will let customers avoid monthly service charges by consolidating their assets and debt into one account. A \$6,000 monthly minimum balance is required. “This looks like the next evolution for basic banking relationships,” said Les Dinkin, of NBW Consulting Group. (*American Banker*, 11/7/97)

- *Federal Reserve & Others Raises Caution of Low-Income Defaults:*
 - Federal Reserve Chairman Alan Greenspan recently expressed concern about rising defaults among low-income homeowners. Default rates on subsidized mortgages have risen from 3% to 4% for overall mortgage portfolios. “Some problems are occurring that should alert us all to potential dangers,” Greenspan told bankers in San Francisco in mid-October. Even some that promote homeownership to low-income families worry that the push can be overly aggressive. For a family with little savings and modest income, loss of a job or a major repair can force a default. Suzanne Snyder of the Home Ownership Center, which works with community groups that prepare low-income families to apply for mortgages, stated that lenders find low-income business profitable and good business, but she raised some concern by stating that “Unfortunately, we’ve got a lot of (real estate agents) out there who say there’s lots of programs. Once you get in, you can fix that roof. But most programs have long waiting lists. There is a concern that there’s an effort to get everyone into a home before they’re ready.” (*Pioneer Press*, 11/2/97)

- *Fannie, Freddie Rebound After Stock Market Tumbles:*
 - Mortgage company share prices rode the stock market roller coaster two weeks ago, fluctuating wildly as the Dow Jones industrials average fell and then rose at record rates before falling slightly again. The stocks proceeded to plummet on Monday, Nov. 3 when the Dow fell a record 557 points, then recovered on Tuesday when the Dow was up a record 337. The market then gained eight points on Wednesday and gave 125 back on Thursday. Despite the falloff on Thursday, some mortgage company shares were actually at just about the same level as they were at the start of the stock market’s fluctuations. Freddie Mac was the most conspicuous winner for the week, up \$1.65 a share to close at \$37.87 ½. Fannie Mae was essentially unchanged with a loss of 7.5 cents to \$48.62 ½. When investors started buying, Fannie Mae and Freddie Mac were two stocks that came back quickly. Like the other companies listed on the Dow, Fannie and Freddie have vast amounts of stock outstanding and are actively traded by professional investors who regard the two companies as symbolic leaders of the U.S. financial system. Investors bailed out of the two big mortgage companies Monday, Nov. 3, then came back Tuesday and Wednesday when they realized the market decline was not going to be severe enough to do any real damage to the U.S. financial industry. Since Fannie and Freddie are so big and successful, they are also popular refuges for conservative investors who want to own stocks without taking on much risk. Others were not as fortunate. Dallas-based Firstplus Financial Group, a subprime lender specializing in high loan-to-value ratio mortgages and home improvement loans, experienced the most turbulent ride of all mortgage companies. The company’s stocks had been soaring for months. Last Monday, Nov. 3, the day of the Dow’s largest single-point drop in history, Firstplus’ stock dropped a remarkable 9.25 points from 52.88 to 43.75. Mike Diana, an analyst with Bear Stearns & Co., used one word to describe the tough week for B&C lenders, “volatile.”
 - Among conventional lenders, the savings and loan stocks were most violently affected by the stock market’s fluctuations, though as a group the traditional lenders were more stable than the broader stock market. Tom O’Donnell, an analyst with Smith Barney, said,

“(The mortgage companies) did better than the overall market. They didn’t go down as much, which is what you would expect because they are domestic companies that are insulated from international pressures, plus it’s a healthy business with good credit quality. Fears that hit other companies (and drove down their share price) didn’t hit mortgage companies. In the end, the GSEs will come out ahead of the game. The savings and loans dropped but bounced back as a group, though they didn’t hold up as well (as certain other conventional lenders).” (*National Mortgage News*, 11/3/97; *The Washington Post*, 11/3/97).

- *Fannie Mae and Freddie Mac Ranked as one of the World’s Most Admired Companies:*
 - *Fortune Magazine* and the consulting firm, the Hay Group, created a first-ever list of global companies ranked by their peers. *Fortune* described the companies listed as having not only terrific products or services, shrewd financial management, and far-sighted marketing but also “guts.” “Their managers are willing to take some risks so bold they may cause shareholders, stock analysts, and employees to seriously question their sanity - at least until they turn out to be right.” *Fortune* asked peers to rate the companies on the eight criteria they use to rank America’s most admired: innovativeness, overall quality of management, value as a long-term investment, responsibility to the community and the environment, ability to attract and keep talented people, quality of products or services, financial soundness, and wise use of corporate assets, and a new ninth category - the company’s effectiveness in doing business globally. The company’s overall ranking is the average of all nine attributes. In the Securities and Diversified Financial Category Fannie Mae was ranked number three and Freddie Mac was ranked 6th. (*Fortune Magazine*, 10/27/97)

Fannie Mae

- *Fannie Mae Tops 100% LTV in Washington Affordable Housing Pilot Program:*
 - Fannie Mae and PMI Mortgage Insurance have launched a pilot program for low- and moderate-income borrowers who will obtain mortgages that have a combined LTV of 102% Under the pilot program, First Mutual Bank will originate 30-year, 97% LTV mortgages that will be insured by PMI and purchased by Fannie Mae. Fannie Mae will also purchase second mortgages originated by First Mutual that will go up to 5% above the purchase price of the home. However, PMI will not insure these loans. The second liens will have 15-year terms and can be used to finance the downpayment or closing costs. The City of Bellevue is providing \$400,000 to help finance the second mortgages. A Fannie Mae spokesperson stated that “this is one of the few instances that Fannie Mae has decided to purchase second mortgages with that high of an LTV.” Borrowers can also reduce their downpayment and closing cost expenses using gift money donated by family members and grants from nonprofits, employers and government agencies. To qualify, borrowers can earn no more than 80% of the Seattle-Bellevue-Everett median income (about \$30,900 a year for a single person, \$44,080 for a family of four, up to

\$51,100 for family of six). Borrowers must also have two months reserves from their own funds. The maximum borrower debt-to-income ratios are 33/41 percent. Homes must be in Bellevue and cost \$120,000 or less. Fannie Mae and PMI expect the pilot program to generate \$15 million in mortgages. Officials expect the program to prove a success, however they concede its long-term chances depend on continuation of the region's strong economy and the relatively low interest rates. If those change, the program could run into trouble. Faith Lumsden, Bellevue's assistant director of planning and community development, stated that "if the market crashed, then we'd all have a lot of problems." (*National Mortgage News*, 11/10/97; *The Seattle Times*, 11/7/97; *PR Newswire*, 11/6/97)

- *GMAC-RFC and Fannie Mae to Make AssetWise Available to Select Desktop Underwriter Subscribers:*
 - GMAC-RFC announced that together with Fannie Mae, it will make its automated credit underwriting and pricing system, AssetWise, broadly available to select Desktop Underwriter subscribers who are GMAC-RFC clients. During the first phase of a pilot program that began last fall, GMAC-RFC and Fannie Mae linked the MORNET-Plus Desktop Originator and Desktop Underwriter system components with AssetWise to provide lenders with point-of-origination loan decisions on mortgages in which GMAC-RFC will invest. These include jumbo loans, sub-prime loans, home-equity loans and other loans that are outside Fannie Mae purchase parameters. In addition, GMAC-RFC and PMI announced that they are in the process of integrating GMAC-RFC's AssetWise with the pmi-AURA/DecisionWise automated underwriting system. (*Mortgage Banking*, 11/97).
- *Fannie Mae Guarantees Oregon Health Housing Education & Cultural Facilities Authority's Multi-Family Housing Revenue Bonds:*
 - S&P assigned a triple-A rating to Oregon's Health Housing Educational & Cultural Facilities Authority's multi-family housing revenue bonds once it was guaranteed by Fannie Mae. (*CNN Custom News*, 11/6/97).
- *Fannie Mae Guarantees Nevada Housing Division's Multi-Unit Housing Revenue Bonds:*
 - S&P assigned a triple-A rating to Nevada Housing Division's multi-unit housing revenue bonds once they were guaranteed by Fannie Mae. The FNMA pledge for each of the transactions maintains the implied backing of the United States, and qualifies as triple-A eligible collateral. (*Business Wire*, 11/11/97).
- *WMF Closes Its Largest Transaction with Fannie Mae for Credit Facility for REITs:*
 - Washington Mortgage in Vienna, Virginia has completed a \$375 million commitment for a master revolving credit facility for The Town and Country Trust, an equity REIT. The financing uses a credit facility, developed by Fannie Mae and Washington Mortgage

specifically for publicly traded REITs, that offers flexible financing at lower costs than traditional bank lines of credit. (*Mortgage Banking*, 11/97).

- *Fannie Mae Chairman and CEO Sets Goal of 75% Homeownership:*
 - In his remarks at the MBA annual convention, Fannie Mae Chairman and CEO James Johnson urged all members of the mortgage industry to strive for the homeownership equivalent of “full employment”. What this will mean is that every American who has the desire, and the economic capacity to pay a mortgage is able to own a home.” He has estimated the full homeownership level to be 75 percent, and has embraced it as a goal to drive the business of Fannie Mae and hopes his customers will follow suit. He projects that each percentage point increase in the homeownership rate will add 1.5 percent of the growth of the primary mortgage market. He outlined his five-point plan to cut costs for homebuyers and lenders, and excerpts of his plan are as follows:
 - *Technology.* “We just made a major new announcement of our Desktop Underwriter (DU 4.0), through which we have shortened the loan approval process from 4 weeks to 4 minutes, and reduced the number of documents required from lenders from 40 pages to 40 data points. Usage of Desktop Underwriter is growing by more than 10 percent a month – a growth rate equal to that of the Internet.”
 - *Servicing.* “Technology is critical to the second key area in which we can cut costs. We are fundamentally changing the way we go about servicing loans. Our Risk Profiler enables lenders to identify those delinquent loans most likely to become foreclosures. Servicers using Risk Profiler may concentrate collection and workout efforts on higher risk loans.”
 - *Foreclosures.* “Lenders who work with us to intervene early to develop repayment plans prevent about three-quarters of the defaulted loans from going into foreclosure. But sometimes a workout just doesn’t work out. When that happens, we work with lenders and borrowers to complete a preforeclosure sale. We are placing seasoned servicing professionals in our customers’ shops on a more regular basis to make decisions, improve efficiency, and save money for our customers.”
 - *Preparing More People for Homeownership:* “Homebuyer education plays a particularly important role today, given the focus on B&C lending. A subprime loan can cost a home-buying family one to three additional points, one to three times more in fees, and \$50 to \$150 more per month than a traditional A quality loan. I believe that we at Fannie Mae, and all of us in this industry, can make our most significant contribution by committing ourselves to making more A’s. With the help of homebuyer counseling, many potential homebuyers with past credit problems can qualify for a loan in the A market. Clearly, there is a need and a place in housing finance for subprime lending. It serves a market need and for some people it is the only alternative. But our industry is pledged, and expected to provide a service at the lowest possible cost. Therefore, today I call upon every man and woman in this industry to make a new commitment – consistent with our bedrock values and mission. It’s a commitment to try our hardest to make “A’s.” Making A’s can save homebuyers thousands of dollars over the life of their loan, and will make an enormous contribution to the ability of American families to share in the benefits of the American dream.”

- *Developing New Products.* “We still have areas of substantial inefficiency in the mortgage finance system that result in people paying far more than they need to pay. This is true in rehab lending – an area we have addressed aggressively in the last two years with products like our HomeStyle mortgage. We also are exploring better ways to finance manufactured housing. We are working to expand the availability of low downpayment options and are working closely with local communities through our Partnership Offices. And as the National Association of Home Builders has pointed out so persuasively, by supporting efforts to reduce regulatory barriers to affordable housing, we can cut the cost of a typical new home by at least \$12,000.” (*National Mortgage News*, 11/3/97)
- *Fannie Mae to Buy Fifth Third Bank Mortgages:*
 - Fannie Mae has agreed to buy \$200 million in mortgages made by Fifth Third Bank to low- to moderate-income homeowners. About \$91 million of the loans are held by borrowers in Cincinnati. The deal marks the first time Fannie Mae has acquired loans in a partnership that involves an Ohio bank and community groups that help low-income residents buy homes. Richard Bondie, Fifth Third’s head of mortgage lending, said the deal allows the bank to enhance its mortgage program for low-income residents. For example, the bank will waive private mortgage insurance and \$795 in closing costs for qualified borrowers effective immediately. The loans Fifth Third sold to Fannie Mae were held by roughly 3,500 homebuyers in the suburbs, and about 1,700 of the loans were made within Cincinnati. Fifth Third is not the city’s first bank to sell these types of loans to Fannie Mae. Provident, Cincinnati’s third-largest bank, began selling home loans targeted for low-income residents to Fannie Mae two years ago. (*The Cincinnati Enquirer*, 11/13/97)
- *Fannie Mae Pilot Program to Use Electronic Imaging to Transmit Mortgage Lien Documents:*
 - Electronic images are replacing paper documents as part of the process of buying or refinancing homes in Orange County, California. Fannie Mae is participating with HomeSide Lending, GMAC Mortgage Corp., and the Office of the Orange County Clerk-Recorder, to transmit mortgage-lien release documents electronically using a computerized imaging system. More than 60 lien release documents have been successfully transmitted since the pilot began in late September. Currently, California is the only state that allows recording via imaging technology. About 40% of the documents sent to Orange County from title companies for recordation come in electronically. To date, the Orange County Recorder’s office has successfully recorded more than 60,000 documents electronically.
 - “We’re always looking for new ways to apply technology to make the mortgage process more efficient and less costly,” said Anita Champ, Fannie Mae’s director of acquisitions and custody. She claims Fannie Mae’s interest in the pilot is to promote electronic commerce, and also said Fannie Mae began investing in imaging technology four years ago, quickly re-engineering front-end processes as a result. But a look at back-end loan servicing functions revealed opportunities to extend the technology on that side of the

business. "By bringing knowledge of the national mortgage process to the county level in this fashion, Fannie Mae hopes to accelerate the adoption of imaging use," said Champ. Linda Hunstad, director of liquidations at GMAC Mortgage, which has had experience serving loans in each of the 50 states stated that "we wish more counties would adopt this." "Extending imaging technology to other parts of the mortgage process eventually can lead to electronic recordation of assignments, satisfaction, and other mortgage-related documents," Champ said. "The reason Fannie Mae is doing this is because we think it is the way the industry is going, and we want to facilitate that." Ms. Champ said the pilot is another step in moving the mortgage industry toward paperless processing.

- The pilot was authorized for two years by the CA legislature, which may consider legislation next year to open the pilot to the entire state of CA. Fannie Mae is talking with other jurisdictions that may be interested in electronic lien release pilots, including Duvall County, FL, Fairfax County, MD and the state of MD. Fannie Mae believes that its size and stature as a GSE helped to persuade CA authorities that Fannie should be a participant in the pilot. (*Los Angeles Times*, 11/12/97, and *Mortgage Servicing News*, 11/97)

- *Low-Down and No-Down-Payment Lending Programs (Such as Those by Fannie) Are Gaining Momentum and Some Criticism:*
 - "These loans are generally for the up-and-coming professional whose income is going up," said Julie Webb, a senior loan officer with Old Kent/National Pacific Mortgage Corp., who has helped clients buy homes with no money down. "It's not the best loan but it lets you get in a home and build your equity and get into a position to refinance with a better loan. I don't think this is for people who are barely making it." 100% financing can open doors to homeownership, enables borrowers to capitalize on rising real estate values, the high interest is tax deductible, and frees up a sizable amount of money to be used for other expenses. But monthly payments are often substantially higher than with traditional financing, it takes longer to build equity in the home, and the owner is much more likely to suffer a big loss if property values were to decline. Some sellers also frown on the idea of a buyer offering nothing down.
 - In spite of these detriments, numerous lending programs are available to creditworthy home shoppers who do have not saved enough for a down payment, including:
 - *Fannie Mae Flexible 97 Loan* - This program has been test marketed in selected cities nationwide, and will become more widely available in 1998. It provides homebuyers with a mortgage covering 97 percent of the purchase price. The buyer can get the remaining 3 percent from anyone other than a source involved in the transaction. The maximum loan is \$214,600, with the interest rate dependent on the market rate at the time of origination. (*Orange County Register*, 11/3/97)

- *Top Fannie Mae Officials On the Road to Riches :*
 - Jamie Gorelick, current vice-chariman of Fannie Mae, earned \$639,000 with Miller, Cassidy, Larroca & Lewin, a well-respected litigation boutique before joining the Clinton administration. Last spring when she left the government, she was wooed by suitors from

industry and firms offering seven-figure packages. She opted for the vice-chairman's job at Fannie Mae, where she's flirting with seven figures in base salary, according to industry sources. Judging by her predecessor at Fannie Mae, current OMB director Franklin Raines, the full package may be even fatter. Raines received \$5.8 million in salary and "other compensation" from Fannie Mae last year, plus \$5.9 million from exercising stock options, according to his annual government disclosure form. (*The Washington Post*, 11/3/97).

- *Smith, Barney Affirms Fannie as a "Buy":*
 - Smith Barney affirmed its "Buy" rating on Fannie Mae and raised its target price on its stock from \$51 to \$58. Smith Barney also raised its 1997 and 1998 EPS estimates on Fannie Mae's stock. Smith Barney now projects 1997 EPS to total \$2.82, up from its previous prediction of \$2.80, and 1998 EPS to total \$3.20, up from its original estimate of \$3.15 per share. Smith Barney believes that "ironically, an uncertain rate environment could spur mortgage portfolio growth, going forward, as many lesser players-ignoring rate risk-have been investing in mortgages and mortgage -backed securities, thereby lessening the volume available for Fannie Mae. Rate uncertainty could cause them to disgorge product, which Fannie Mae could then acquire." Smith Barney commented that "Fannie Mae is the only major financial services company to have reported ten years of consecutive double-digit earnings growth. The third quarter underscores the fact that this record shows no sign of ending. It is our expectation that steady, predictable earnings growth will lead to ongoing multiple expansion." (*National Mortgage News*, 10/27/97)
- *Rep. Jim Leach (R-IA) Joins Fannie Mae Chairman Johnson at Iowa Press Conference Focusing on Fannie's Contributions to Affordable Housing in Iowa:*
 - House Banking Committee Chairman Jim Leach attended a conference in Iowa last week where Fannie Mae's contributions to affordable housing in Iowa were spelled out. Officials updated progress of the HouseIowa initiative, within sight of a house being constructed in Cedar Rapids with the help of a Fannie Mae program. Fannie announced that in the first year of a program to help first-time or rural homebuyers, it has provided \$662 million in mortgage financing for thousands of Iowa families. HouseIowa is Fannie's \$3 billion investment plan to provide mortgage financing for 40,000 Iowa families over five years. So far, 8,470 families have received mortgages through HouseIowa. Metro Area Housing Program (MAHP) president Mary Schoen-Clark said partnerships such as those with Fannie Mae have helped Metro Area Housing commit \$30 million to projects in the past five years. MAHP received \$200,00 at 1-percent interest to help continue its affordable housing efforts. Among new initiatives announced by Johnson is a program allowing qualified buyers to buy a home with down payments as low as 3%. Another program allows the purchase of a home with no down payment in qualifying rural areas. (*The Cedar Rapids Gazette*, 11/4/97, and *Omaha World-Herald*, 11/4/97).
- *Fannie Mae Plan Lets Rent Subsidies Help Pay Mortgages :*

- A pilot plan announced recently will allow 50 Minneapolis families with at least one adult working full-time to use their rent subsidy to help make monthly mortgage payments. They would pay 30% of the family's income toward mortgage and escrow payments. The Section 8 subsidy would pay the remainder for up to five years. To qualify, adults must have been employed at least a year and family income must fall between \$16,000 and \$28,500. Only 50 of the 2,800 Minneapolis households with Section 8 certificates will be allowed to participate. The Minneapolis plan includes home-ownership counseling and a partnership with lending institutions. TCF Mortgage and Norwest Mortgage have agreed to provide mortgages and accept federal Section 8 payments as part of the mortgage payment. Fannie Mae has set aside \$4 million to purchase the mortgages for the secondary market. (*Pioneer Press*, 10/31/97)
- *New Mortgage Program To Assist Borrowers With Disabilities:*
 - Washington State has been chosen as one of the first to participate in a pilot program offering mortgages to low- and moderate-income people who have disabilities or who have family members with disabilities living with them. Fannie Mae is offering the program, called HomeChoice, in which customers will work with Fannie Mae-approved lenders and may choose between 15- or 30-year fixed-rate loans. The loan may be used to purchase a house or condominium, so long as it's used as a principal residence. According to Fannie Mae, HomeChoice differs from other mortgage loans in several ways. It requires lower down payments – from \$250 up to 2 percent of the home's sales price or appraised value, whichever is less. Nontraditional credit histories are accepted and borrowers with incomes at or below 50 percent of the area median income can qualify based on their personal budgets – not just the debt-to-income ratios most loan programs use. To be eligible, the person's disability must be among those defined by the Americans with Disabilities Act of 1990 or the Fair Housing Amendments Act of 1988. (*The Seattle Times*, 11/8/97)
- *Fannie Mae Program Aimed at Immigrants:*
 - In March 1998, the Latin American Association will host a daylong bilingual home-buying seminar sponsored by Fannie Mae. Fannie Mae has been funding programs in target cities nationwide that provide step-by-step guides to home buying in seven languages. Fannie Mae's guides are in English, Spanish, Chinese, Vietnamese, Korean, Russian and Haitian-Creole. Fannie Mae hopes to add more languages and Atlanta will likely be among the U.S. markets where the guides will debut. In September, Fannie Mae met with leaders in the Asian community to plan homebuying seminars similar to the one being offered for Latin Americans. A Fannie Mae official said future outreach efforts would likely involve the large Vietnamese community in the Atlanta area. (*Atlanta Business Chronicle*, 11/3/97)
- *Fleet Hosts National Event with Fannie Mae to Celebrate 20th Anniversary of CRA:*
 - Fleet Financial Group hosted a national two-day symposium for the 20th anniversary of CRA on November 5th and 6th at the Capitol Hilton in Washington. The co-sponsors

were Neighborhood Reinvestment Corp., Local Initiatives Support Corp., National Urban League and Fannie Mae. (*Business Wire*, 11/5/97)

- *Fannie Mae Commissions Study on Year 2000:*
 - Fannie Mae commissioned a survey on the Year 2000's effect on U.S. financial-related businesses. Among other findings, the study found that 94% of U.S. financial-related companies are aware of the problem, and 71% of these say that they have taken steps to address it. The survey sampled over 400 experts drawn from a universe of 9000 financial-related businesses, including national and state commercial banks, insurance brokerages and carriers, savings institutions and credit unions. (*Business Wire*, 11/6/97)
- *National Association of Realtors and Fannie Mae Announce Partnership for Osteoporosis Health and Education Campaign:*
 - NAR and Fannie Mae announced a two-year Osteoporosis Awareness and Health Education Campaign. Beginning in 1998, this national campaign will provide the Realtor community with information on the disease, its detection, prevention and treatment. In addition, a free bone density screening, valued at \$300, will be available to Realtor members and their spouses at various state Realtor association conventions and at the NAR mid-year meeting in Washington, DC. This initiative grows out of Fannie Mae's commitment to women's health, an initiative begun at Fannie Mae in 1994. (*PR Newswire*, 11/13/97)
- *National Association of Realtors and Fannie Mae Foundation Announce "Partners in Housing" Awards:*
 - NAR and Fannie Mae Foundation announced this year's winners of local initiatives to address low- and moderate-income housing needs. The award recipients were selected by members of NAR's Housing Needs Committee and representatives of the Fannie Mae Foundation. The Fannie Mae Foundation awarded grants totaling \$50,000 to the winners. (*PR Newswire*, 11/13/97)
- *Fannie Mae Foundation Day with Washington Wizards NBA Basketball Players:*
 - Washington Wizards players Calbert Cheaney, Chris Whitney, Ben Wallace and Terry Davis joined volunteers on November 6 at the Fannie Mae Foundation Work Day to help demolish and repair a house in Washington, DC. Fannie Mae eventually will make the refurbished house available to first-time home buyers at a low interest rate. Over the past four years the team and Fannie Mae have made nine homes available in Washington's Shaw neighborhood. (*Washington Post*, 11/4/97)
- *Fannie Mae Official to Chair Child Care Governing Committee:*
 - Two low-income areas of Philadelphia will be the focus of a \$10.7 million effort to improve child-care services. The initiative, called Child Care Matters, is funded by the

William Penn Foundation and the United Way of Southeastern Pennsylvania. “The evidence supporting the importance of early childhood development and the devastating societal impact of inadequate child care are all too plain to see,” said Ken Bacon, senior vice president of Fannie Mae for the northeastern United States, who will chair the governing committee for the new Philadelphia effort. Among the regional goals are to support efforts for accreditation of child-care facilities, to boost teacher education, and to link up with the business community to focus on child-care issues. “When parents have problems with child care, their employers feel the impact,” Bacon said. “That’s why we’re determined to include business leaders in Child Care Matters, to help all of us find solutions.” (*The Philadelphia Inquirer*, 11/6/97)

- *Fannie Mae Factoid: Americans and Football Games, Chores:*
 - Fannie Mae conducted a monthly poll and asked 1,000 homeowners where they like to watch football games. More than half of the respondents reported they prefer the comforts of home, while others enjoyed the homes of friends or relatives (4%); and 3% watch at a bar, restaurant or stadium. Nearly one-fourth don’t watch at all. Fannie also asked about fall chores: 27.7% said putting away their summer wardrobe and replacing it with winter clothes was the household chore they dreaded most, closely followed by raking leaves (24%); installing storm windows (6.5%) and having the furnace serviced (6.1%). The Fannie Mae Factoid is a monthly poll by Fannie Mae, designed to provide consumer insight on a variety of topics related to the home and family. Information is gathered from calls to Fannie’s Consumer Resource Center. This month, 1,000 callers were surveyed. In an article on the study, *The Milwaukee Journal Sentinel*, stated “Why Fannie Mae would care, we don’t know.” (*The Milwaukee Journal Sentinel*, 11/2/97; *Business Wire*, 10/30/97).

Freddie Mac

- *Freddie Mac Executive Attends NRSC Fundraiser with Big Money Donor Executives:*
 - The National Republican Senatorial Committee (NRSC) held a fundraiser on November 5th in Washington, DC. R. Mitchell Delk of Freddie Mac was listed as a Vice Chairman of the dinner. Donors who either gave or raised \$100,000 or more were designated Vice Chairman. (*Washington Post*, 11/5/97)
- *First Union Bundles CRA Asset-Backeds:*

- We reported in the last *GSE Report* that First Union Corp. and Freddie Mac have accomplished a financing first by packaging CRA loans into mortgage-backed securities. In a recent article regarding the deal, it was stated that because Freddie Mac guaranteed the issue, it gave the bonds nearly the same credit quality as U.S. government debt. The article further stated that while Freddie Mac isn't a government agency, investors assume the mortgage giant's role in U.S. homeownership is so integral that the government would not let it fail. (*Dayton Daily News*, 11/10/97)
- *Freddie Mac Unveils New Features for Loan Defaults Service:*
 - Freddie Mac announced a new set of features for its EarlyIndicator loan default management service at its recent annual Servicer Conference. EarlyIndicator is a modeling system that allows lenders to assess the probability of late-paying borrowers becoming delinquent on their loans. The new features of EarlyIndicator include: (1) extending the amount of time available for collecting late mortgage payments while decreasing the number of calls required for collection; (2) lowering the number of loans that need loss mitigation property and increasing the number of days to conduct inspections on "low risk" loans; (3) reducing the number of loans requiring proactive loss mitigation solicitation; and (4) decreasing the number of loans that require foreclosure referral packages. (*Reuters*, 11/4/97)
- *Use of Freddie Mac Early Indicator Is Increasing Among Freddie Mac Seller/Servicers:*
 - About 40 to 50% of Freddie Mac lenders are testing or using Freddie Mac's automated risk modeling tool. Paul Peterson, senior vice president of Freddie Mac, said Freddie hopes to adapt Early Indicator so lenders can use it on loans not purchased by Freddie Mac. For instance, Freddie Mac is currently testing the system as a tool servicers can use to evaluate FHA loans. This follows a pattern similar to the one that guided Loan Prospector, Freddie Mac's Automated Underwriting system, which has also been adapted for use with non-conforming loans. (*Mortgage Servicing News*, 11/97)
- *Freddie Mac Developing Portfolio Management Tool:*
 - Freddie Mac announced that it is developing a new mortgage portfolio management tool, available only through its GoldWorks electronic network, that is devised to help servicers lessen investor reporting errors. The new product, Investor Accounting Manager, is a web application that also aims to synchronize various loan data files with those of Freddie Mac. If loan discrepancies occur, the servicer is automatically provided key loan information that can simplify research and correct errors. A "special request reports" function will enable servicers to reduce the time it takes to get portfolio reports from Freddie Mac from several days to less than 24 hours. Freddie Mac said it would pilot the new product with a few servicers during the first quarter of 1998. The full rollout is targeted for mid-1998. Freddie Mac's office stated that "It is this commitment to innovation that has made Freddie Mac a technology leader." (*Reuters*, 11/12/97; *Bloomberg* 11/12/97)

- *Freddie Mac Adds New Technology to Web Site:*
 - Freddie Mac is tying its recently-hoisted web site, HomeSteps, with an announcement this weekend that the site will incorporate “push” technology, which uses both the capabilities of a PC and the Internet to deliver enhanced content. The HomeSteps site features searches of foreclosed homes and provides updates for members who are interested in finding a certain home in a certain area. (*LA Times – Inman News Feature*, 11/13/97)
- *Freddie Mac Co-Sponsors High-Tech Real Estate Summit:*
 - Inman News Features announced it would help form a voluntary commission that will issue guidelines to protect consumers buying and selling real estate on the Internet at its March 1998 summit. Inman News also announced Real Estate Connect 98 co-sponsors, including Freddie Mac, Bank of America, Microsoft, Prudential Real Estate, DataQuick, and GTE, among others. (*BusinessWire*, 11/12/97).
- *Freddie Mac Prepares for Year 2000:*
 - Freddie Mac expects their systems will be Year 2000 compliant by the end of 1998, and they plan to have full integration testing of all systems beginning in late 1998 and lasting through 1999. (*Freddie Mac Securities Bulletin*, 10/97)
- *Freddie Mac Plans Loan Origination Year Data Coming in December :*
 - Freddie Mac plans to make Loan Origination Year (LOY) data available for all newly issued pools. LOY data is loan count, percent of loans and percent of unpaid principal balance (UPB) broken down by the year in which the loan was originated. Beginning with December 5th, the Daily New Issue file will have original (as of pool formation) LOY data for all pools. On January 7th, current LOY data will be available on all pools. (*Freddie Mac Securities Bulletin*, 10/97)
- *Freddie Mac Foundation is Partner in Virginia Program For Children:*
 - The Freddie Mac Foundation is a co-sponsor of a program in Arlington, VA designed to provide a continuum of essential services to vulnerable families with young children. The program will build a system of coordinated health care for children age six and under in Arlington. In addition, the program will start a system of intensive home visiting support for enrolled families to improve their parenting skills and family functioning. The program is free, voluntary, and open to those who are pregnant or have children six and under. (*PR Newswire*, 11/7/97)

Federal Home Loan Banks

- *FHLBank Bill Would Expand Powers:*
 - Senator Chuck Hagel (R-NE) introduced his FHLBank reform bill. Senator Hagel's bill is modeled after the FHLBank bill crafted by Cong. Richard Baker (R-LA). The four main components of the bill are: (1) easing membership requirements for small banks; (2) making thrift membership voluntary; (3) replacing the fixed REFCorp. obligation paid by the system as a whole with one based upon income of individual banks; and (4) transferring day-to-day management of FHLBanks from the Finance Board to individual institutions. Senator's Hagel's bill also expands the mission of the FHLBank system to benefit community banks with less than \$500 million in assets. Community banks would be able to use FHLBank advances to make secured small-business loans and agricultural loans, as well as finance rural and low-income development projects. Currently, advances may only be used to fund housing finance and limited community development loans. Aides in Senator Hagel's office have indicated that Senator Hagel would push for hearings on the measure early next year. The bill is co-sponsored by Senators Robert Bennett (R-UT), John Kerry (D-MA) and Rod Grams (R-MN). (*BNA*, 11/14/97, *National Mortgage News Bulletin*, 11/10/97; *American Banker*, 11/13/97)

- *FHFB Approves FHLB of Seattle Pilot to Purchase Mortgages for Rent-to-Own Housing Program:*
 - The Federal Housing Finance Board approved a pilot program allowing the FHLB of Seattle to purchase up to \$25 million in federally insured mortgages to help finance rent-to-own housing programs for low- and moderate-income households. FHFB also approved new policies and procedures for considering future pilot programs through which the 12 FHLBanks could propose to support housing finance and targeted community development projects in new ways. Under the pilot program, the FHLBank of Seattle may purchase and hold up to \$25 million in FHA-insured residential mortgages originated by the Bank's member institutions and non-member mortgages to affordable housing developers and local government agencies. Proceeds from the purchases of the FHA-insured mortgages then will be used to help finance rent-to-own housing programs in low- to moderate-income neighborhoods. FHFB Chairman Bruce Morrison stated that this pilot program is a "new and innovative way for the FHLB of Seattle to carry out its housing finance mission at minimal risk." Generally, members and non-member borrowers of the FHLBank of Seattle that are FHA-approved lenders accumulate pools of FHA-insured mortgages for packaging into securities issued by Ginnie Mae. Under the Seattle pilot program, members and non-members sell those loans directly to the FHLB of Seattle, rather than holding them in portfolio until the institutions build up sufficient quantity for Ginnie Mae pooling. The Finance Board has determined that the pilot program adequately addresses risk exposure, and poses no threat to the FHLBank System's triple-A credit rating. Before the pilot can officially begin, the Finance Board's office of supervision must complete a preimplementation exam to ensure that the FHLBank of Seattle has established the necessary policies, procedures and controls to manage the risks associated with the program. Charlotte Bahin, regulatory counsel for America's Community Bankers, stated this "particular pilot does serve a useful need, but that does not diminish our concerns about pilots in general." The ACB still has concerns

about the scope of the FHLBank of Chicago pilot program approved earlier this year. ACB has sharply criticized the Finance Board for approving pilot programs without providing the public an opportunity to comment on them. The Finance Board also formalized internal procedures for processing amendments to existing pilot programs and for reviewing future pilot programs. One of the provisions states that the Finance Board will not render a decision on a proposal until after all public comments have been reviewed and analyzed by agency staff. (*BNA*, 11/13/97)

- *FHLBank Provisions in Financial Services Modernization Bill:*

- The last issue of *The GSE Report* reported that Subtitle H of H.R.10, the section of the omnibus financial services reform package expanding the powers of the Federal Home Loan Banks, was deleted from the House Commerce Committee's version of the bill reported out of Committee. Although, the financial services modernization bill will not be considered this year, the Banking and Commerce Committees will continue negotiations over the recess and hope to take up the bill next year. The Committees have agreed to restructure the finances of the FHLBanks and allow system members to use advances for small-business, economic development, and agricultural loans. (*American Banker*, 11/7/97)

- *Regulatory Relief Bill Contains FHLBank Provisions:*

- A regulatory burden relief bill introduced recently by Senators Richard Shelby (R-AL) and Connie Mack (R-FL) contains several FHLBank provisions. One amendment would require the Board of Directors of the FHLBs to establish net debit caps for daylight overdrafts incurred by FHLBs and would allow the board to exempt the banks from fees and penalties for daylight overdrafts. Another section of the bill removes a number of provisions turning authority for certain management decisions over to the individual FHLBs instead of with the Board of Directors as currently provided by law. The bill would also allow banks to accept second mortgages that are insured by the federal government as primary collateral for advances, and would remove the current restriction limiting the acceptance of other real estate collateral to no more than 30% of the bank's capital. The bill is co-sponsored by all 10 Republican members of the Senate Banking Committee and three Democrats – Senators Richard Bryan (D-NV), John Kerry (D-MA), and Carol Moseley-Braun (D-IL). (*BNA*, 11/10/97)

- *WSJ Op-Ed on FHLBanks – “Get Ready, Here Comes Flubbie Mae:”*

- Holman Jenkins, Jr. in an op-ed for the *WSJ* describes the FHLBanks as “flubs” whose goal is to become another Fannie Mae or Freddie Mac. In his opinion, the FHLBanks are envious of all the money and political power that Fannie and Freddie currently enjoy. He noted that *Fortune* recently reported that Fannie had the higher profits per employee than any other big company - \$826,000 per head and Fannie's CEO James Johnson made \$6 million last year. Fannie and Freddie have “achieved the ultimate insurance any federal program can have against its own obsolescence. They now wield so much financial and

political clout that Congress is afraid to enact any serious attempt to slow them down.” Fannie and Freddie have “Uncle Sam’s credit card.”

- The heads of the FHLBanks, however, are not making that much money, and Congress has been threatening them with obsolescence. The FHLBanks have the “Uncle Sam credit card” too, “all they need to do is figure out how to become so big that no politician will ever dare to take it away again.” The FHLBanks answer to this problem is to offer themselves as “competition” to Fannie and Freddie – this is the new mission of the FHLBanks. “Tell the politicians that you’re the last, best hope of reining those arrogant buzzards in.”
- This competitive outlook acted as a catalyst for the Chicago FHLBank. The Chicago pilot program is very clever because it has zeroed in on a “political vulnerability” of Fannie and Freddie – homeowner’s subsidization of another higher region’s default rates. California has the highest default rate (.7%) from 1992-1996. Arkansas, on the other hand, has 0.05% - 14 times lower than CA. The FHLBank of Chicago pilot program is attempt to capitalize on these differences. The FHLBank of Chicago will buy the mortgage itself and pay the originator a servicing fee tied to the historical default rate. “That allows the flub to outbid Fannie and Freddie, while allowing the originator to earn a nicer spread in return for its good judgement in choosing whom to lend money to.” He acknowledges that the pilot is small, but the other 11 FHLBanks have expressed an interest in duplicating it.
- Tom Stanton, a Washington lawyer and authority on the subject, told Congress that “the real lesson of Fannie and Freddie is that such programs ought to be sunsetted before they can become political powers unto themselves.” Mr. Jenkins believes Mr. Stanton is right. “As clever and elegant as the Chicago program is, the solution to Fannie and Freddie is not to foster yet another one.” (*Wall Street Journal*, 11/12/97)
- *Charter One Chairman Opposes Chicago FHLBank Pilot Program:*
 - In discussing his company’s opposition to the pilot program by the FHLBank of Chicago to invest in \$750 million of fixed-rate mortgages made by its members, Charles John Koch, Chairman of Charter One Financial, said that if the FHLBanks became large mortgage investors-on the order of Fannie and Freddie-they would “force more people out of mortgage lending” by making fixed-rate loans cheaper. Charter One is among a group of thrifts suing the Chicago bank to stop the pilot program. (*American Banker*, 11/6/97)
- *FHLBank’s Finance Committee Chairman Testifies About FASB Proposal:*
 - Alex Pollock, Chairman of the FHLBanks’ Finance Committee, recently addressed the House Banking Securities Subcommittee, on FASB’s derivatives accounting proposal. Mr. Pollock stated that the FHLBanks are active users of hedges to reduce and control the risks of their Bank. He summarized his views to the following:
 - He believes there should be concern over the negative, unintended consequences of the proposal on the home mortgage market. “The \$4 trillion home mortgage market requires active hedging, as the savings and loan collapse taught us, and it certainly

seems worthwhile to ensure that our mandatory accounting rules represent such reduction of risk as accurately as possible.”

- The FASB proposal is a complicated and many financial professionals are highly critical of the proposal. Re-exposure and additional discussion of the proposal is called for.
 - The FASB proposal does not achieve its own primary criterion that “financial reports should portray similar transactions and circumstances similarly.”
 - The potential implications for the home mortgage market are serious. He urged that discussion not be cut off. (*National Mortgage News*, 10/27/97)
- *FHLBanks Provide Matching Funds:*
 - The FHLB of NY has program called “First Home Club” with a number of participating local banks that provides matching funds to would-be buyers who participate in a savings plan to build up funds for a down-payment. The FHLBank provides up to \$2 in grants for every \$1 a participant places into a dedicated savings account. The grant limit is \$5,000. Roosevelt Savings Bank of Garden City has 33 families enrolled in its program. Half the \$1 million that the FHLB of NY has allocated to its member banks for the First Home Club program will go to families making 50% or less of an area’s median income; the other half goes to families making up to 80% of median. To participate in such programs, both lenders and Fannie Mae require homebuyers to receive mortgage and home maintenance counseling, which is given free or at a minimal cost either by lenders themselves or by nonprofit groups. (*New York Times*, 11/2/97)
 - FHLBank of Seattle will provide a \$70,000 grant to the Women’s Opportunity Resource Development (WORD) and Western Federal Savings Bank for a matching savings program. The FHLBank of Seattle will kick in \$3 for every dollar a family deposits at Western Federal Savings Bank. The program is restricted to first-time homebuyers with annual incomes between 60 to 80% of the median income. (*MSNBC Montana Regional News*, 11/5/97)
 - *FHLBank of Topeka Provides Grant To Affordable Housing Program:*
 - The FHLBank of Topeka provided a \$168,000 Affordable Housing Program Grant for a five-acre senior apartment community, developed by Mennonite Housing. The community includes an on-site manager, library, craft area and community rooms in addition to the apartments. There are 16 two-bedroom units and 40 one-bedroom units, each with emergency call systems in the bathroom and bedrooms. In addition, the Kansas Department of Commerce and Housing issued tax credits to Fannie Mae in a partnership with Enterprise Social Investment Corp. (*Wichita Business Journal*, 11/10/97)
 - *FHLBank of Pittsburgh Helps Fund Historic Warehouses to Become Apartments:*

- The FHLBank of Pittsburgh, Fulton Bank, and the Lancaster County Redevelopment Authority will be funding a project to transform historic warehouses into apartments designed to provide housing for low-income residents 55 years and older. The project would rehabilitate the building's outward facade to its original appearance. In addition to 24 one-bedroom apartments, the plans include a community room, elevators, handicapped access ramps, and parking. The first phase of the project should begin by the end of the year. (*Intelligencer Journal* (Lancaster Newspaper), 11/6/97).
- *FHLBank of Boston Sponsors Expo:*
- The FHLBank of Boston will present the New England Partnership Expo on November 19th at the Centrum Centre in Worcester. The daylong event will feature workshops, exhibits and awards. Scheduled speakers include FHLB of Boston Chairman Elizabeth Mitchell and FHLB President and CEO Michael Jessee. (*Boston Herald* 11/7/97)

Farmer Mac

- *Farm Credit System Competition - Topic for ABA Conference:*
- The issue of Farm Credit System Competition was a topic at the 45th annual National Agricultural Bankers Conference sponsored by the ABA. Bert Ely, president of Ely & Co., updated his 1990 report "The Farm Credit System: Reckless Lender to Rural America." At the conference, Mr. Ely called for the privatization of the Farm Credit System. With plenty of private funding sources from commercial banks, insurance companies, and private agricultural finance firms, he said the Farm Credit System only "gums up the works." He further stated "commercial banks and other private sector lenders can fully meet rural America's financial needs. I don't think in a free market you need a government-sponsored lender." Mr. Ely said he particularly worries that the system which was bailed out in 1987, will use its growing pool of retained earnings to undercut commercial competitors. "The Farm Credit System could "really start stealing business," he said, though "it's not happening yet." He believes that the agricultural economy is in good shape now, but bankers should be wary if Farm Credit System lending practices become too liberal or credit quality deteriorates. Many attending the conference supported his vies. "There's no way we can fund the loans internally to match them," said David Spencer, VP of Mercantile Trust and Savings Bank, Quincy, IL. "They're a very aggressive lender." Some bankers also said they fear the system will gain expanded powers and make further inroads into their business. The ABA and the IBAA are embroiled in a lawsuit over a rule that allows Farm Credit lenders to offer loans to farm-related businesses, like equipment manufacturers and seed sellers. The associations believe that the agency should only be lending to farmers. Member banks are prohibited from taking deposits, but the system does use its backing as a GSE to cheaply raise funds. "My biggest concern is their funding source," said one banker at the

conference. "It really doesn't create a level playing field." (*American Banker*, 11/10/97; *American Banker* 11/14/97)

- *Farm Credit System Increases Competition by Offering Loan Applications Over Internet:*

- Last week, Farm Credit Services began accepting loan applications through its Web site. Potential borrowers provide basic information, such as name, address, loan amount requested, and farm income. Decisions are made in as little as a day. Though Farm Credit Services operates in 11 states, it will act as a clearinghouse for electronic loans nationwide. Outside its market, other farm credit banks will make the loans. Doane Agricultural Services completed a survey that found almost 35% of farmers have computers with modems. Among farmers who said they plan to expand their operations, half said they have a modem. Dennis White, president and CEO of First Bancshares of Valley City, ND, said competing with an on-line system will be tough. (*American Banker*, 11/10/97)

- *Farmer Mac Gets a Boost With Farm Credit System Reform Act:*

- Congress reorganized Farmer Mac and while no one thinks it will match Fannie and Freddie's volumes in the non-farm residential markets, it has been retooled using the exact same model that has allowed Fannie and Freddie to dominate their markets. Farmer Mac lost money every year until last year. The Farm Credit System Reform Act of 1996 has recently given Farmer Mac the authority to work directly with lenders, just as Fannie and Freddie do. Farmer Mac is now allowed to set its own pricing and terms, and to develop new loan products. Most importantly, it can now come to market with securities regularly. It has averaged an issue about every 60 days since last July, based on product it buys through a cash window from an active pool of 60 or 70 different lenders. And while the old Farmer Mac had to structure a 10% subordinated interest in the mortgage-backed securities that was not easy to sell, the revamped GSE now can sell securities for all of the loans it buys. The cash window and the 100% pass-through of loans for securities are both similar to procedures used at Fannie and Freddie. With loan product coming in regularly and with Farmer Mac taking a 50 basis point cut, the agency last year earned \$777,000, its first yearly profit and a considerable turnaround from 1994, when it lost more than \$1.3 million. In addition, the agency went to the capital markets for a stock offering last December and made enough to take it above fully phased-in capital requirements. Thomas Clark, vice president of Farmer Mac, does not believe that Farmer Mac leads the market. But over time, he can see Farmer Mac having some of the same kind of power in making a market for a loan that Fannie and Freddie have. (*U.S. Banker*, 11/19/97)

- *Farmer Mac Announces Public Offering of 300,000 Shares of Class C Non-Voting Common Stock:*

- Farmer Mac announced an underwritten public offering of 300,000 shares of its Class C Non-Voting Common Stock. The offering is exempt from registration under the Securities Act of 1933. In December 1996, Farmer Mac had an offering of 1,437,500

shares of Farmer Mac's Class C Non-Voting Common Stock. The net proceeds of their offering will be added to Farmer Mac's working capital and will be used for general corporate purposes. (*PR Newswire*, 11/12/97)

- *Farm Credit System Reports 1997 Third Quarter and Nine-Month Net Income:*
 - Farm Credit System announced a combined net income of \$328 million and \$935 million for the three and nine months ending September 30, 1997, respectively. This compares to a combined net income of \$289 million and \$950 million for the same periods last year. James Brickley, president and CEO of the Federal Farm Credit Banks Funding Corp. stated that the "System is investing in its infrastructure, expanding products and services, and developing alternative delivery channels while continuing to enhance its strong capital position." (*Business Wire*, 11/12/97)

Ginnie Mae

- *Mortgage Firm is 1st in Nation to Implement Electronic Data Interchange with GNMA:*
 - James B. Nutter & Company, Mortgage Bankers, has become the first mortgage firm in the nation to test and implement electronic data interchange with Ginnie Mae. (*PR Newswire*, 11/7/97)

Connie Lee

- *Connie Lee's Rating Improves As It Nears Deal with AMBAC:*
 - S&P reinstated its AAA rating on the insured bonds of Connie Lee after it agreed to be acquired by AMBAC Assurance Corp. S&P placed a temporary negative credit watch on Connie Lee last month due to stagnating business. Since Connie Lee relinquished its status as a GSE this past February, business has practically come to a halt. Part of that is attributable to the pending sale and part is attributable to the July departure of the departure of their longtime CEO. (*Washington Business Journal*, 11/3/97)

Postal Service

- *New Bill Would Greatly Expand Powers of Postal Service:*
 - A bill recently introduced by Senator Thad Cochran (R-MS), would give the Postal Service sole discretion over its financial activities. It would permit the Postal Service to be a customer of private institutions and make investments in private companies. The current role of the U.S. Treasury as regulator of the Postal Service's financial decisions

would be eliminated. The bill puts the Postal Service into a position similar to that of Fannie and Freddie in relation to Treasury.

- Opposition to the bill and to Senator's Cochran's controversial decision to put the bill on a fast-track, caused the Senator to pull his bill from full Senate consideration recently. The bill was criticized by many, including the Advertising Mail Marketing Association (AMMA), for allowing the Postal Service to invest in companies that are "closely related to postal operations." AMMA called this "the broadest expansion of the Postal Service's authority in the 200-plus history of the American postal system."
- Postmaster General Marvin Runyon during a recent Senate Subcommittee hearing to review the postmaster general's annual report stated that the "Postal Service has no plans to acquire any of its competitors if it gets authority to invest in private securities." Both Postmaster Runyon and Senator Cochran commiserated over the inability to win fast-track Senate approval of the bill.
- On November 5th, the Postal Rate Committee Chairman Edward Gleiman told an Arkansas audience that he has "been troubled by the notion that the Postal Service must enter new, unrelated markets and strive to capture market share from private enterprises. Maybe I am old fashioned, but I think the Postal Service is here to provide a government sponsored (as opposed to government subsidized) service, and that service is delivering hard copy messages and parcels. Generally speaking, new postal products are okay, but I think the nation would be better served if Headquarters' management would spend more time improving existing services and increasing operating efficiency and less time looking for ways to compete with businesses, large and small. The preoccupation with growth by a government agency - not only must volume increase, but so too must market share - has in my opinion, taken on a particularly troubling character." (*AMMA Web Site*, 10/31/97, 11/6/97; *Washington Post Digest*, 1/4/97)

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