

# The **GSE** REPORT

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## ***Fannie Mae & Freddie Mac***

- *Fannie Mae and Freddie Mac Automated Underwriting Systems Will Be Directly Available to Consumers:*
- Fannie Mae and Freddie Mac are both working to make their underwriting systems directly available to consumers through the Internet – a new development that has raised some eyebrows in the mortgage industry.

### Fannie Mae

Fannie Mae's program, iQualify ([www.iqualify.com](http://www.iqualify.com)) is a multi-lender web site where consumers can send a loan application that is processed by Fannie Mae's Desktop Underwriter before a consumer even chooses a lender. As we reported in our January 16<sup>th</sup> edition of the *GSE Report*, the web site is a joint program with Fannie Mae and Finet Holdings Corp. (owner of Monument Mortgage). (Please see the January 16<sup>th</sup> edition of the *GSE Report* for more information about the program and the corporate background of Finet Holdings.) Finet Holdings reports that "business through its 'electronic mortgage broker' web site has skyrocketed in recent months because of surging refinance activity." Roger Conley, Fannie's Mae's VP for Technology Marketing, believes the program represents a "profound change in the mortgage industry....one that redefines the consumer's relationship to the lender in ways that are more empowering than any changes that have come before." Monument Mortgage is using the iQualify web site to solicit its current servicing customers and, through a pilot program with Stewart Title, can close a refinance loan the same day a borrower initiates the transaction. If the appraisal requirements can be handled by statistical evaluations or waived because of a same-lender refinance, the title company (Stewart) prepares the closing documents electronically and the borrower can meet at the closing agent's office with just a pay stub in order to close the loan. Monument is also working with a delivery service to possibly deliver the closing documents to the borrower's work or home to execute the deal.

### Participants in the Fannie Mae/Finet Program – Loans Steered to Lenders Chosen by Finet

Approximately 40 lenders are participating in the program, according to James Noack, chief information officer at Finet Holdings but Mr. Noack declined to report what the terms of participating in the program are. Mr. Noack stated that some of the applications are referred to Monument Mortgage (owned by Finet) but the system refers the Fannie Mae Direct Underwriter-approved customer to participating lenders based on geography and capacity. Finet will monitor the lender turnaround to make sure consumers are referred to a lender that can handle the business.

### Cost of Fannie Mae/Finet Program

The lender who closes the loan absorbs the cost of running an application through Fannie Mae's Desktop Underwriting system. Finet absorbs the cost if the loan is not closed. The system pulls a merged credit report, and the borrower pays a \$39 fee online for up to three tries at the underwriting system.

### Freddie Mac

Freddie Mac in its initial phase of their Online Mortgage Explorer (OME) project will allow potential borrowers to submit a profile of their credit needs anonymously to a web site. Software at the web site will then compare the borrower's input to the program criteria listed by participating lenders, and refer the borrower to a list of participating Freddie Mac lenders. In the second phase of the project, the loan applications will be run through Freddie Mac's Loan Prospector, said Robert Habert, vice president of strategic alliances at MPACT Immedia, the Toronto firm that is building the Internet connection. The lenders will be available from Freddie Mac's Goldworks subscribers. Freddie Mac has also begun discussing a program in which Loan Prospector would be available directly to consumers through the Internet and fees for Loan Prospector could be waived to encourage lenders to participate in the program. OME is similar to Fannie Mae's HomePath Network in that, like HomePath, Fannie Mae connects borrowers directly with 65 lenders. Under OME, the computer actually hooks up borrowers with, eventually 900 lenders over the Internet. But Freddie Mac's Griff Straw, said Freddie Mac is still not interested in dealing directly to consumers, but "our only role is in providing the network for the lender to get to OME," he said. "All we're providing is the network." But while Freddie's program is far from a fully-digital transaction, it is the first time the secondary mortgage market has turned directly to the Web to provide origination assistance.

### Concerns in the Mortgage Industry

While some working in the mortgage industry are afraid of these developments, Mr. Noack's response was they are the future and "lenders have to get used to it." One mortgage banking official suggested that delivering Fannie Mae's Desktop Underwriter directly to consumers was trampling against the spirit of Fannie's charter by positioning the lender, not the consumer, as Fannie Mae's customer.

### Agency Responses to Concerns

Roger Conley, Fannie Mae's senior vice president for technology marketing, said Fannie Mae "is providing tools to its lender customers that the lenders are carrying into the primary market in lots of different ways. DU is being integrated into the processing system to take advantage of streamlining. It's no different than a lender taking an application at a retail branch and feeding it into Desktop Underwriter." (*Inside Mortgage Finance*, 1/30/98; *National Mortgage News*, 2/2/98; *Inman News Feature* 2/4/98; *Mortgage Marketplace*, 2/2/98; *Washington Times Home Guide*, 2/6/98; *Real Estate Finance Today*, 2/2/98)

- *Agencies' Implicit U.S. Guarantee Lures Foreign Investors:*
- Fannie and Freddie are attracting foreign investors. With turmoil in overseas markets, the implied government guarantee of Fannie and Freddie securities may offer foreign investors some calm. A senior analyst with Salomon, Smith Barney, Thomas O'Donnell, said the GSEs are a "good proxy for Treasury debt...with even more benefits. Non Americans are not as aware of the agency market as they should be and as they will be over time. It's a way for them to get implied government backing on the debt. And it's higher-yielding than Treasury debt."

Fannie Mae:

Fannie Mae Announces First 10-Year Benchmark Note; Moves to Build Yield Curve:

Fannie Mae announced the offering of \$4 billion in 10-year noncallable Benchmark Notes, the second in a series of large-size securities that Fannie Mae has committed to issue regularly. The \$4 billion 10-year Benchmark Note will be priced with a maturity date of Feb. 15, 2008. Coupon payment dates will be each Feb. 15 and Aug. 15 beginning Aug. 15, 1998. Settlement will be on Feb. 5, 1998. As announced in December 1997, Fannie Mae expects each Benchmark Note to be between \$2 billion and \$5 billion in size. Subject to market conditions, Fannie Mae's intent is to issue a 5-year and a 10-year Benchmark Note each quarter. The company plans to use Benchmark Notes for up to one-half of its expected \$80 billion in long-term debt issuance in 1998. "Because of the flight to quality and shortage of Treasuries, it is an excellent time for Fannie to bring these to market," Mr. O'Donnell said.

The prospect of conversion to the euro scheduled for release in 1999 has also helped to boost Fannie Mae's second benchmark note issue. William Lloyd, director and head of market strategy and credit research for Barclays Capital, said "buying U.S. governments or quasi-U.S. governments is a relatively safe way for Europeans to play the market." The Benchmark notes are viewed by investors as a proxy for government debt, said Mr. Lloyd and European investors are attracted to the agency debt securities because the high credit quality creates a government surrogate and because of the liquidity, Mr. Lloyd said.

Large and Increasing Foreign Commitment

Preliminary figures show that U.S. investors committed themselves to buy 60% of Fannie's note issued- European investors, 32% and Asians, 8%, according to Linda Knight, senior vice president and treasurer at Fannie Mae. The share of foreign investment increased since the first \$4 billion note issue, a five-year security issued in January, when 23% were European and 13% were Asian.

#### Supply Exceeds Demand for Fannie Mae Benchmarks

Wall Street has registered demand far outweighing the supply of Fannie's Benchmark notes. "We were bowled over by the customers," said Robert Lunder, senior managing director in the government bond department at Bear, Stearns & Co. "There's been nothing to date that has been as much in demand as this. It's the first time that we've had people overrunning our position looking for bonds."

#### Freddie Mac:

##### Freddie Mac Plans to Launch Five-Year Bond Similar to Fannie's "Benchmark Notes":

Freddie Mac has also been trying to attract additional foreign investors. Raymond Redlingshafer Jr., director of Freddie Mac's international investors, said international markets will be "100% of my focus going forward." "Ironically, many of them are coming to us because they see this non-credit-sensitive asset that gets you a higher yield than Treasuries and they want to know more," Mr. Redlingshafer said. According to Mr. Redlingshafer in an *American Banker* article on 2/4/98, Freddie Mac has not come out with a product to rival Fannie's program but Freddie has some plans for the arrival of a common currency next year in Europe. However, in a *Reuters* London wire story on 2/1/98 it was reported that Freddie Mac is expected to issue a \$1.0 billion five-year bond soon. Freddie Mac said no official mandate had been awarded yet, but it was likely to be issued soon. Pricing was expected to be in line with where Fannie Mae five-year paper was trading. "Fannie Mae's \$4.0 billion five-years are trading around 16/17 basis points over U.S. Treasury notes, and Freddie Mac pricing is expected to be in line with these," a syndicate manager at a U.S. Banker in London said. Fannie Mae launched its \$4.0 billion five-year bonds, the first of its new benchmark notes, on January 9th to yield 19 basis points over Treasuries. The deal's strong performance reflects investor preference for liquidity and quality, bankers said.

##### Freddie Mac Plans to Push MBS Bonds Overseas – Investors Attracted to "Government-Backing":

Freddie Mac also plans to increase overseas sales of its mortgage-backed bonds this year in the "billions" of dollars, according to Ray Redlingshafer, director of international investors at Freddie Mac. The higher the demand for Freddie Mac securities, the more profitable it is for the company to buy mortgages from banks. Mr. Redlingshafer stated "many people overseas are viable investors in mortgages and have never looked at them." He reported that Freddie Mac plans to make its biggest sales pitch in Europe, but it is also targeting Asian investors. Only about 12% of all mortgage bonds are held outside the U.S. Most investors assume the government would never let Freddie Mac or its bonds fail, since the company was set up by Congress to help finance home ownership for low- and middle-income Americans. That makes the securities attractive not only to U.S. investors, but also to central banks and institutional investors looking for higher yields

than Treasury bonds. (*Milwaukee Journal Sentinel*, 2/1/98; *Reuters*, 2/1/98; *Business Wire*, 2/2/98; *American Banker*, 2/4/98, 2/10/98)

- *Municipal Bond Insurance Trade Association Believes Fannie and Freddie May be Doing Mortgage Insurance:*
  - The Association of Financial Guaranty Insurers (AFGI), which represents insurers and reinsurers of municipal bonds and asset-backed securities, released a new study that reports that the agencies may have designs on the private mortgage industry and pose a threat to both MIs and other guarantors. Fannie and Freddie have developed products “that incorporate” mortgage insurance in the loans they are willing to purchase. AFGI says the products in question are “spread account” and 80-10-10 mortgages. Susan Tyskland Sweet, an outside consultant who worked on the AFGI report, noted that under a spread account mortgage the consumer does not use an MI policy and instead builds up a cash reserve account with the lender/servicer. If the loan goes into default, the cash reserve (spread account) is tapped to cure the default. She said that the concern to the MI is that Fannie and Freddie are creating loans that remove the need for mortgage insurance. Darryl Thompson, president of Triad Guaranty Insurance Corp., thinks MI firms should worry at least somewhat, citing 80-10-10 loans as one of the biggest concerns. In an 80-10-10 structure, a borrower puts down 10%, takes out a first mortgage that covers 80% of the loan amount and then a second lien for the remaining 10%. Both Fannie Mae and Freddie Mac believe AFGI’s conclusions are inaccurate and overblown because the loans in question generate such small volumes that no MI should feel threatened. But one MI said, “it’s not now we’re worried about. It’s later on.” MI executives are concerned about the Fannie and Freddie duopoly in the conventional secondary mortgage market. “Fannie and Freddie have the mustard to do anything they like,” said Mr. Thompson. “They are always looking for new markets and a way to grow their earnings.” (*National Mortgage News*, 2/2/98)
- *ABS Players Worry about Expansion of Fannie and Freddie:*
  - Some players in the home equity and manufactured housing areas of the asset-backed securities (ABS) market worry that Fannie and Freddie may move into areas outside the conforming mortgage loan sector. During the ABS West conference, panelists discussed their concerns about the potential unfair competition from the GSEs. Fannie Mae was represented at the panel discussion, Freddie Mac was not. The discussion centered on the interest expressed by Fannie and Freddie to go after subprime borrowers. Henry McCall III, senior vice president of United Companies Financial Corp. said that Freddie Mac was more committed to the idea than Fannie Mae and cited comments from Freddie Mac’s chairman at the MBA conference in New York, that Freddie “would participate in subprime to the extent we are comfortable with the risk.” Freddie Mac’s participation could give UCFC and others in this sector of the ABS market a powerful competitor with significantly more leverage. “I’m a competitive person,” McCall said, “but I want to play on a level playing field.” Gregory Witherspoon, executive vice president of Aames Financial Corp. said that the GSEs would have a significant edge in terms of cost of capital, or rate of return a business can earn using an alternative investment with equivalent risk. Witherspoon also believes that the GSEs do not understand this market

and that Freddie Mac's credit statistics on below grade A borrowers "are not good." He said that data collected and analyzed in the prime borrower market is simpler than that gleaned at lower levels. "Sticking it into a computer and spitting out an answer is no way to write subprime loans," he said. The ABS participants believed they currently have good working relationships with the GSEs. Steven Campo, managing director at MBIA Insurance Corp., noted that his company has worked with Fannie Mae in the guarantee of some deals. "The questions are more Freddie Mac related," Campo said - adding that the GSEs entry into this industry "could upset the balance of an already efficient industry." He also questioned why the GSEs were considering what seemed to be a change in course from their mandate of providing affordable housing. Sharon Stieber, a vice president at Fannie Mae, said that Fannie "hasn't prioritized this to the same extent" that Freddie apparently has. "It's not consistent with our charter," she said, and added that at this point of time, "we don't fully understand it. We have neither the capability nor the will." Any movement by Fannie Mae into this area would be done "slowly and cautiously" and would not present a threat to players in the market. (*Reuters*, 2/6/98)

- *Analysts See Privatization of Fannie and Freddie Unlikely in the Near Future:*
  - In response to the recent Cato study calling for privatization of Fannie and Freddie (see January 16<sup>th</sup> *GSE Report* for more details on Cato study), a Wall Street equity analyst who tracks Fannie Mae said changing the current system would be "very undesirable," adding that the GSEs serve the market "very well." "The agencies have done the job of providing liquidity to the housing market and have not exposed the market to undue risk," the analyst said, adding that calls to change the system were "political." The Fannie Mae analyst as well as an analyst who tracks Freddie Mac said privatization would be very unlikely because of political support for the agencies in Congress. David Jeffers, vice president of corporate relations for Fannie Mae, said similar challenges have been made to the GSEs before, but the agencies' strong bipartisan support on Capitol Hill has kept them afloat. A Freddie Mac spokesperson said reports similar to the Cato report come out "every so often," but a move to change their status rarely goes beyond the Congressional hearing stage. (*Mortgage Marketplace*, 2/2/98)
- *Fannie Mae and Freddie Mac Approve of Streamlined Refinancings:*
  - Fannie Mae and Freddie Mac have approved of mortgage bankers using an in-file credit report and waived the need for property appraisals as long as the to-be-refinanced-loan exists within their portfolios or the original lender resells the loan and as long as the value of the property backing the loan has not declined. (*Real Estate Finance Today*, 2/2/98)
- *Fannie Mae and Freddie Mac Support Federal Disaster Bill:*
  - The House Banking Subcommittee on Housing approved legislation seeking more federal assistance for disaster insurers. The bill called for a federal reinsurance program for state catastrophe pools to provide insurance in disaster-prone areas, according to the Chairman of the Housing Subcommittee Congressman Rick Lazio (R-NY) who also introduced the bill. The bill allows the U.S. Treasury to offer voluntary, single-year Federal insurance contracts to eligible state insurance programs to cover residential losses in the event of

natural disaster. The American Bankers Association, America's Community Bankers, Freddie Mac, Fannie Mae, National Association of Realtors, and the National Association of Homebuilders signed a letter to Chairman Lazio and the other Members of the Subcommittee in support of the disaster insurance legislation. (*BNA Daily Report for Executives*, 2/3/98; *Reuters*, 2/4/98)

- *Administration's New Revenue Raising Proposal May Eliminate the GSEs from Municipal Market:*
  - Seventeen state and local government groups sent a joint letter to Capitol Hill raising their concerns about a revenue raising proposal included in President Clinton's 1999 budget proposal that would raise \$100 million over five years by extending the pro rata disallowance of tax-exempt interest expense to all "financial intermediaries." The group warned that the proposal would eliminate government-sponsored corporations like Fannie Mae from the municipal market. The proposal would limit the market-making ability of securities firms and squeeze demand for housing bonds because it takes aim at Fannie Mae and Freddie Mac, which buy up to 25% of all housing debt issued. Several industry and government sources have said that the provision is aimed particularly at Fannie Mae and to a lesser extent, Freddie Mac. "Fannie Mae really loaded up on tax exempts," said a Treasury source, who noted that both agencies have been buying large amounts of tax-exempt debt. Michael Decker, the Bond Market Association's director of policy analysis, said that if Fannie Mae, Freddie Mac, and Sallie Mae leave the market for housing and student loan bonds, there is "no doubt that the cost of financing for housing and student loan issuers will increase." (*Reuters*, 2/12/98; *Bond Buyer*, 2/3/98, 2/4/98, 2/9/98)
- *More Community Banks Using Fannie and Freddie to Protect Themselves Against Refinancing Boom:*
  - More community banks are using the secondary market to try to insulate themselves against the current refinancing boom. Brian Smith of the America's Community Bankers (ACB) expects the trend to continue because there is a current preference for fixed-rate mortgages by new borrowers and refinancers. According to ACB Senior Economist Paul Taylor, the good economy is the reason why thrifts and community banks, which are typically portfolio lenders, are holding fewer loans. "That's what the secondary market's for, to lay off risk," he said. "And savings institutions are doing it to a greater extent and with more conduits." "A refinance boom, and the conversion of adjustable-rate mortgages into fixed-rate mortgages, and a very flat yield curve are coming together in 1998. And that clearly could convince some of our members to utilize the secondary market more fully," Mr. Taylor said. The ACB's annual market survey reported that sales to wholesale servicers and private conduits had increased dramatically in last year. Of the 280 institutions that were polled, 16.1% were selling to these purchasers (a 29% increase from 12.5%). Nevertheless, the majority of sales were still to Fannie Mae and Freddie Mac. Of the 280 institutions polled, 31.4% participate in the secondary market through Freddie Mac and 19.6% through Fannie Mae. Last year, those figures were 30.6% and 20.7% respectively. (*National Mortgage News*, 2/2/98; *American Banker*, 2/3/98)

- *First American CREDCO Decides Against Removing Credit Scores from Reports After Legal Review and Discussions with Groups such as Fannie and Freddie:*
  - First American CREDCO, the nation's largest provider of specialty credit reports, announced that it would not allow the removal of any repository's credit score from its InstantMerge™, MergePlus™ or RMCR credit reports once delivered. First American has been asked on occasion to remove one or more credit scores from its InstantMerge™ report once a client has requested the more comprehensive MergePlus™ or RMCR reports. Since scores from the credit reporting agencies, TRW, Equifax, and Trans Union, can differ in collected credit information, recipients may request the removal of scores that are deemed too low or below normal lending thresholds. After a legal review and discussions with the Associated Credit Bureaus (ACB), Fannie Mae and Freddie Mac, First American CREDCO found no legal reason for disallowing this practice, since there is no direct mention of the issue in the Fair Credit Reporting Act (FCRA). But the parties agreed that the purposeful removal of credit scores could easily be misinterpreted as removing derogatory credit information. "Since our industry has worked so hard and for so long to eliminate the stigma of impropriety that the practice of inappropriately removing derogatory data causes, and since our secondary market trading partners oppose it, First American CREDCO will not allow the removal of credit scores once delivered on a report," said Don Robert, President of First American CREDCO. (*PR Newswire*, 2/11/98)
- *Agency MBS Growth Goes from Lows to Highs:*
  - The annualized growth rate for Fannie Mae MBS bounded from 2.9% in the 1997 second quarter to 9.5% in the 1997 fourth quarter. Freddie Mac MBS also had dramatic increases – net MBS additions went from only \$218 million for the month of July to \$5 billion in December of 1997. (Net additions reflects new MBS, after old MBS are liquidated.) At mid-year, officials at the agencies were concerned about the low levels of securitization as lenders seemed to be putting more loans in portfolio. Low rates coupled with a flat yield curve would explain the MBS increase. (*Mortgage Marketplace*, 2/2/98)

## ***Fannie Mae***

- *Fannie Mae Tops 100% LTV (150% LTV) Program in Minneapolis & St. Paul:*
  - Fannie Mae introduced its HomeStyle purchase-and-rehabilitation loan program in Minneapolis and St. Paul with new special features available only to the Twin Cities area. One feature allows up to 50% of a standard mortgage to be used for rehabilitation and that limit can be waived up to 75% within the cities of Minneapolis and St. Paul to address issues of vacant houses that might need to be gutted for total replacement of interiors. In addition, the kind of work that can be done is unrestricted as long as it's part of the real estate. Some previous programs allowed only work needed to bring the property up to code. Another feature allows combined loans of 150% of the home's

value if the amount over 100 percent comes from a nonprofit or government agency. Other sources of purchase-rehab lending have existed, among them community-development loans, loans through the FHA and lenders who usually held such loans in their own portfolios. But Fannie Mae's entry into this type of lending means a potentially vast reservoir of funds and a great expansion of use. (*Star-Tribune Newspaper of the Twin Cities Minneapolis-St. Paul*, 2/7/98)

- *Fannie Mae Commits to Record Monthly Mortgage Buys:*
  - Fannie Mae's commitment to buy mortgages for its portfolio grew by a monthly record of \$12.1 billion in January, about double December's gain and \$1 billion above the prior record set in 1993. The net mortgage portfolio expanded \$3.5 billion in January to \$319.8 billion, for an annualized growth pace of 13.2% - above December's rate of 8.0% growth rate. Mortgage purchases rose to \$7.6 billion in January from \$6.7 billion in December. Portfolio liquidations were \$4.2 billion, down slightly from \$4.6 billion in December. Total MBS outstanding rose \$5.2 billion in December to \$714.7 billion (an 8.7% annualized growth rate-up from 8% in December). MBS outstanding net of securities held in portfolio grew at 5.5% annualized growth rate, increasing \$2.7 billion in January to \$581.8 billion. (*Reuters*, 2/11/98)
- *Fannie Mae Participates in Low-to-Moderate Income Pilot that Allows Borrowers to Make Only a 1% Downpayment:*
  - Fannie Mae is making available at least \$24 million in mortgage financing to help low and moderate income families in Allegheny County, PA. The program, which is part of a six-city experiment, will allow borrowers to buy a home with only 1% down. The mortgages are available to borrowers whose annual income doesn't exceed the median household income in the region (\$49,000). Income limits are waived, however, if a home is purchased in either a low or moderate income area (approximately 30 neighborhoods in Pittsburgh qualify). The average loan amount is expected to be \$50,000. According to Julie Gould, a vice president at Fannie Mae, the credit criteria for getting a loan will be "very flexible." That means that borrowers who've been turned down for a mortgage in the past still may qualify for a loan under this program, she said. Besides Pittsburgh, other participating cities in the pilot are Chicago, Des Moines, Cincinnati, Syracuse, and the Bronx. (*Pittsburgh Post-Gazette*, 1/31/98)
- *Fannie Mae Purchases Tax-Exempt Mortgage Revenue Bonds in Texas:*
  - Fannie Mae and the Montgomery County Housing Finance Corporation have entered into a \$10 million home mortgage bond finance agreement that will allow Montgomery County home buyers to have access to below-market mortgage rates. Fannie Mae will purchase the single-family, tax-exempt mortgage revenue bond issuance from the Montgomery County HFC. Fixed-rate, 30-year mortgages are available at 6.8%. The Montgomery County HFC will pay 3% of the borrowers' downpayment or closing costs. Fannie Mae's Community Home Buyer's Program and Fannie 97 can also be used by applicants in conjunction with the Montgomery County HFC's downpayment and closing

cost assistance. (Fannie's Flexible 97 requires a down payment of just 3% which can come from a family member, a loan from non-profit organization or a credit card. (*Houston Chronicle*, 10/15/97)) Purchasers may obtain new homes priced at no more than \$103,298 and existing houses for up to \$94,039. (*National Mortgage News*, 2/2/98)

- *Fannie Mae Brings Flexible 97 Program to Orange County:*
  - The Fannie Mae program, Flexible 97, will now be offered in Orange County, CA. The program allows eligible Orange County home shoppers with good credit to buy a home with as little as 3% down. The downpayment can come a family member, loan from a non-profit, or a credit card. Fannie Mae has set aside \$30 million for the program in Orange County. (*Orange County Register*, 2/8/98)
- *Fannie Mae Unveils New Multifamily Technology:*
  - Fannie Mae announced plans to introduce its Multifamily Committing and Delivery System, which will provide online loan commitments with less data and cut the time needed to confirm loan commitments from 24 hours to an hour. The system will be required of Fannie Mae's Delegated Underwriting and Servicing lenders for all loan commitments and deliveries by March 1. (*Inman News Feature*, 2/3/98)
- *Fannie Mae Foundation Awards Nebraska Grants:*
  - The Fannie Mae Foundation presented \$114,000 in housing and community grants to nine nonprofit Nebraska community groups. Grant recipients were the Family Housing Advisory Service, Elkhorn Valley Community Development Corp, Holy Name Housing Corp., Nebraska Commission on Indian Affairs, Nebraska Community Foundation, Nebraska Community Foundation (2 grants), Omaha 100 Incorporated, Housing and Neighborhood Developers. (*Omaha World-Herald*, 1/30/98)

## ***Freddie Mac***

- *Freddie Mac Decides Not to Do Conduit Plan:*
  - Freddie Mac decided (at least for the time being) not to do its plan to act as a conduit to Wall Street for small apartment owners and developers. Freddie Mac worked to set up the parameters for the conduit program last year, but Freddie Mac decided to wait awhile since some competitors are now subsidizing their apartment loans. Senior vice president Tom Watt said that as far as he can determine, in many cases, the sector's successful conduits use loans on multifamily projects just to fill out their pools. But with spreads falling on other types of commercial loans, he expects spreads on apartment loans to improve. And when that happens, he said, Freddie Mac would launch its conduit program. (*National Mortgage News* web site, 2/9/98)
- *Borrower Reaps Cash from High Risk Loans Used to Purchase Freddie Mac Properties:*

- Kevin Sisti, went on a real estate shopping spree in December of 1995, shortly after his conviction for helping his father hide money when the firm his father co-founded, Colonial Realty Co., was failing. Mr. Sisti received extravagant loans from a lender for blighted properties in New Britain, Hartford, and Meriden but ended up using most of the loan money to fund his legal defense in a new criminal case. The blighted properties are still in the same condition two years after he obtained the loans. Sisti bought eight multifamily properties for a total of just under \$100,000. Six of the houses were vacant and boarded. Using the houses as collateral, he received loans totaling approximately \$300,000 from the mortgage company, Express Funding, Inc. For example, he paid \$1 for a pair of abandoned shells on Willow Street in Meriden and received a \$42,000 loan from Express Funding. He paid \$8,3000 for a long-vacant house on High Street in New Britain and received a \$44,800 loan. Mr. Sisti was able to receive the loans within 72 hours of each purchase, which took place over four weeks (November 30 to December 20, 1996). Six months after receiving the loans, Mr. Sisti was indicted on new charges in the failure of Colonial Realty. Mr. Sisti said he stopped paying back the loans when he was indicted and used much of the loan money to pay his criminal-defense lawyers and support his extended family. Bankers Trust of Irvine, CA foreclosed on the properties last summer. Express Funding, which provided him the loans, is now defunct. Mr. Sisti bought five of the eight properties from Freddie Mac, which sells houses that were once financed by savings banks that later failed. He bought the other three properties from private owners. The Freddie Mac properties all remain vacant. Suzanne Cary, the former Freddie Mac real-estate specialist who sold Mr. Sisti the five properties, was surprised at the size of the loan. “Oh my God, that’s amazing. No way they were worth that,” Cary said. “I find it hard to believe that those loans could be justified.” She said Freddie Mac’s sales prices are always based on fair market value, as determined by a broker and an appraiser working for the agency. Cary said she couldn’t begin to guess what Express Funding’s values were based on. “We held the Willow Street properties for over a year and marketed them without success for \$5,000,” Cary said. “We gave them to Kevin Sisti because he wrote in his business plan that he intended to rehab the properties...Obviously, that didn’t happen.” (*Hartford Courant*, 2/1/98)
- *Surge in Refinancings Causes Freddie’s Purchase to Increase in December:*

  - Freddie Mac’s loan purchases increased in December (by far its best month of the year). Freddie purchased \$17 billion worth of loans. The reason for the strong showing in December was the surge in refinancings. Freddie Mac purchased \$121.4 billion in loans in 1997, a 5% decline from 1996 when it purchased \$128.5 billion. Of the \$17.04 billion that Freddie Mac purchased, \$689 million was in multifamily loans. Freddie’s multifamily acquisitions increased 464% in December. At the end of 1997, Freddie held \$164.4 billion in its retained portfolio (a 19% gain from 1996). With rates falling so much, economists now anticipate that 1998 could yield as much as \$950 billion in residential originations, 40% of which could be refinancings. Because the secondary market reflects the primary market, both Fannie and Freddie stand to gain volumes. (*National Mortgage News* web site, 2/2/98)
- *Computer-Based Training Program Developed for Freddie Mac P&I Custodial Accounts:*

- Mortgage Professionals, Inc. (MPI) have developed a computer-based training module, MPI Mentor ® for Freddie Mac P&I Custodial Account Reconciliations. The program is designed for investor accounting departments of mortgage servicers involved in the preparation and management of Freddie Mac P&I custodial account transactions. (*Business Wire*, 2/11/98)

## ***Federal Home Loan Banks***

- *Possible Consolidation of Federal Home Loan Bank System?:*
- Speakers at an elite conference discussed the possibility of a FHLBank System consolidation. The conference, “Midwinter”, is an invitation-only conference of 100 top thrift and mortgage executives sponsored by the former chairman of the FHLBank Board, Richard Pratt. The speakers did not agree about how the System would be redesigned. Michael Jessee, president and CEO of the FHLBank of Boston believed market forces would drive consolidation. Key factors he mentioned affecting the System’s future were: (1) growth of commercial banks as shareholders and customers; (2) technology-driven changes in the delivery, processing, and production channels for financial services; (3) product innovation; and (4) possible statutory changes. Because institutions currently operate in more than one region it makes it impossible for them to be members of one home loan bank system. James Montgomery, former chairman of Great Western Financial Corp., and a member of Freddie Mac’s board agreed and thought capital requirements should be uniform for all the FHLBanks to facilitate mergers. Mr. Montgomery stated that institutions operating in multiple regions could shop around for a home loan bank that is willing to make advances on its weakest loans (“adverse selection”).

### Investments Not Related to Housing

Bruce Morrison, the current chairman of the Finance Board, said he does not think that broad consolidation is possible in the near future, but he acknowledged there was pressure in Congress to revamp the System. A key question he thought the System must answer is, “Why is the funding advantage of a government- sponsored enterprise being used to arbitrage products unrelated to its mission?” Mr. Morrison was referring to investments by the System that aren’t related to housing. Mr. Jessee reported in his presentation that these investments are becoming more important because spreads the banks receive on advances to members have shrunk, putting pressure on profits. The spreads averaged 16 basis points in 1997 (down from 64 basis points in 1993). A mandate by the Financial Institutions Reform, Recovery, and Enforcement Act is one reason for the shrinkage. The Act required that banks make 20% of their advances on a nonprofit basis. The investments unrelated to their mission have allowed the banks to maintain a stable dividend yield. (*American Banker*, 2/13/98)

- *Controversial Chicago FHLBank Pilot Reports Strong Demand:*

- The controversial Chicago FHLBank pilot that allows the FHLBanks to indirectly fund conventional loans in a manner similar to Fannie and Freddie, has racked up \$170 million in master commitments since its inception last June. The “Mortgage Partnership Finance” (MPF) pilot has funded, through its members, \$43 million in MPF loans (\$10 million of that coming in the first 20 days of January). The MPF program allows participating residential lenders to originate loans in their own names and then upstream the product to the FHLBank which holds it in portfolio. Through this upstreaming arrangement the lender escapes “sales treatment” and avoids holding extra capital against the loan. “This is a loophole we are exploiting,” said David Feldhaus, external affairs representative for the FHLBank. Some conventional portfolio lenders have complained that the pilot creates another GSE to compete against. The Federal Housing Finance Board has also been sued (case still pending) for approving the MPF pilot. The Chicago FHLBank is the only FHLBank to launch a pilot that allows for the indirect funding for conventional loans. The pilot also pits the FHLBank against Fannie and Freddie to some degree. The average MPF loan size is \$97,916 and 45% of the loans are made to consumers who are considered low-to-moderate income. The Chicago FHLBank says its members strongly support the MPF program and so far, six members have used the program and as many as 14 more are expected to participate sometime in the future. (*National Mortgage News*, 2/2/98)

### ***Farmer Mac***

- *South Dakota Bank Acts as a Middleman for Small Banks and Farmer Mac:*
- First Dakota National Bank is assisting small community banks in selling farm loans to the secondary market, by preparing large long-term agriculture real estate loans at fixed-rates for resale through its Dakota Mac arm. The bank is currently processing these loans for 33 banks in 10 states. Dakota Mac charges a 20-basis-point fee to prepare the loans for resale through Farmer Mac and by acting as a middleman, Dakota Mac streamlines a procedure that can be tedious for banks with limited staff that process only one or two of the loans per year, according to Dennis Everson, executive vice president at First Dakota. Mr. Everson also added that Dakota Mac’s loan volume has increased significantly since Congress revamped Farmer Mac in 1996. (*American Banker*, 2/9/98)

### ***Ginnie Mae***

- *Ginnie Mae Plans to Add More New Products*
- Ginnie Mae plans to add more multifamily innovations and possibly introduce strip securities. President Kevin Chavers said they are considering the possibility of offering a strip product but they are not committed to doing it. Mr. Chavers said the agency will be taking a “fairly deliberative approach” to the issue, taking into account the agency’s risk exposure to the operational issues and suitability concerns. One recent product improvement Ginnie Mae cited is their new resecuritized real estate mortgage investment conduit products, which are designed to allow more flexibility in bundling different

agencies' securities. Mr. Chavers said Ginnie Mae is "the only opportunity in the market" for re-REMIC structures backed by both Fannie and Freddie REMIC securities, as long as those REMICs are backed by Ginnie Mae collateral. Ginnie Mae's first deal of this type, 98-1, was \$486 million in size and a second re-REMIC deal was \$247 in size and contained Freddie Mac collateral. Mr. Chavers said these products have been "very well received" by Wall Street dealers and investors. Other new Ginnie Mae products included the "MX" product where a swap option is built into the security. The option allows for the creation of an exchangeable class that can be swapped for other classes within the securitization. Ginnie Mae has also been issuing a new resecuritized "Platinum into Platinum" securities that combine smaller, illiquid pieces of REMIC securities into one larger security that is easier to trade. Three of these issues have been done since last fall (a \$33 million deal, a \$25 million deal, and a \$45 million deal). (*National Mortgage News*, 2/2/98)

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