FannieMae

Expected Loss Overview for FHFA

Leslie Deich
Shelley Klein

April 2012

FHFA.Overview.2012.04.13.v2.ppt

Key Takeaways

- The allowance reached its highest level in Q4 2011 and is expected to reduce to $69B by year-end 2012
  - New models being implemented are likely to result in a further decline of the allowance as they will include recent history that reflects improved performance
- We believe the allowance as of year-end 2011 was appropriate
- Credit losses are expected to remain elevated through 2013 as delayed foreclosures from prior periods come through the pipeline; losses decrease in 2014 and 2015 as delinquencies are cleared through default or workout
  - The biggest risks to the current forecast are policy changes driving further decline in home prices

Agenda

Credit Loss Forecast

- Overview
- Loss Forecast Model
- Credit Forecast Drivers
- Analysis
- Sensitivities

Comparative Analysis

- Home Price Forecast Benchmark
- FAS 114 Methodology
- Guaranty Book of Business
- Credit Metrics

Key Takeaways

Credit Loss: Basic Calculation

Defaults X Severity = Credit Losses

Defaults

Count of Defaults for 5-year period (2011-2015):

1.46 million

Severity

Average Severity of Loss (Avg. UPB * Avg. Severity):

\$168K * 40% = \$67K

Credit Losses

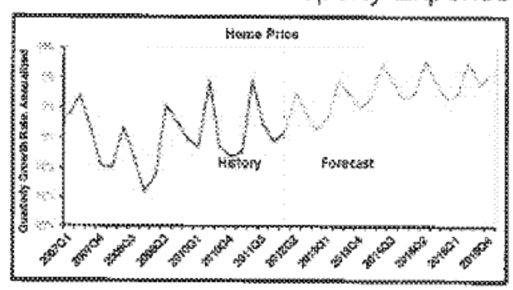
Total 5-year Credit Losses:

\$98 billion (approximately)

Defaults predicted using transition rates:

Monthly Transition Rates		Roll To					
		Current	30 DLQ	60 DLQ	90+ SDQ	Default	Prepay
Roll From	Current	0.97	0.01	0.00	0.00	0.00	0.01
	30	0.30	0.46	0.23	0.00	0.00	0.01
	60	0.10	0.15	0.35	0.40	0.00	0.00
	90+	0.02	0.01	0.01	0.93	0.03	0.00

Severity predicted using recent trends for REO and non-REO charge-offs, indexed to home price forecast, as well as recent trends for Foreclosed Property Expenses



February 2012 Base Forecast (December Book)

What is the Loss Forecast Model?

- The Loss Forecast Model (LFM) is a system of equations designed to predict the credit performance of Fannie Mae's Single Family book of business from a given point in time, including new loan acquisitions and modifications
- The LFM is built to mimic the actual life cycle of a loan, modeling the monthly transitions with discrete outcomes of either prepayment, default, or delinquency status
- The primary business application of the LFM is the SF Corporate Expense Forecast, a 5 year projection of Credit Loss and Credit Expense
- LFM has also been used to:
  - Evaluate solvency of MI companies
  - Quantify impacts of high touch servicers as part of their compensation
- LFM is needed when timing of loss and/or delinquency is required
- LFM is also used in many other internal reports and applications across the corporation

house prices generally rule everything, but now so much underwater - the [illegible] of the borrower [illegible] default.

Top Drivers of the Credit Expense Forecast

Economic Drivers

Home price forecast
- The most important driver of the forecast, as it affects both the default volume and severity
- Peak-to-trough metric indicates overall decline, but long term recovery is key as well

Interest rate forecast (prepayments)
- Prepayments have little effect on credit results, as loans that are likely to default tend not to prepay

Book Profile

Delinquency status
- A key driver of default probability

MTMLTV
- Also a key driver of default probability, but also the key driver of severity

Actual Results

REO values, sale prices, expense rates, and inventory levels
- Recent actuals are a secondary driver of severity

rely on the model on the longer term - [illegible]

Modeling Assumptions

Default speed (the rate at which SDQs are liquidated)
- Primarily affect the timing of credit losses
- Slower default speed pushes credit losses further into the future and increases the allowance in the near term

Business Outlook

Workout volumes
- A key driver of overall results, as workouts reduce defaults and therefore credit loss, but have an associated credit expense

REO sale volume
- Slower REO sales increase Foreclosed Property Expense (FPE)

SF Credit Loss and Credit Expense Forecast

L.P.on any C.O.

cost of dms.?

total provision in financial statement

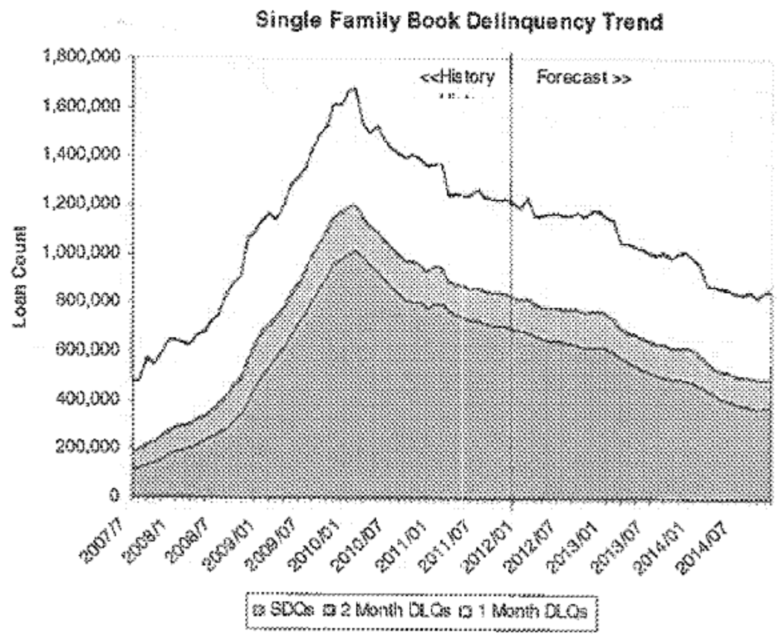
(Dollars in millions unless otherwise noted)	February 2012 Base Forecast (Dec Book)								
	2009	2010	2011	2012	2013	2014	2015	2010-2014	2011-2015
Charge-offs	12,064	20,407	17,038	18,679	21,818	16,603	11,156	94,545	85,294
Foreclosed Property Expense	1,182	2,658	1,890	2,276	3,274	3,061	2,212	13,159	12,713
Total Credit Loss	**13,246**	**23,066**	**18,929**	**20,955**	**25,091**	**19,664**	**13,368**	**107,705**	**98,007**
SOP 03-3 Charges, gross	20,241	177	116	52	51	54	65	451	339
Prior Year SOP 03-3 Contra	(722)	(2,033)	(2,042)	(2,142)	(2,258)	(1,573)	(1,062)	(10,048)	(9,078)
~~Impact of new HSA Loans~~	347	58	(569)	(11)	-	-	-	(521)	(579)
Incremental Provision	38,199	1,622	10,795	(6,708)	(11,698)	(14,217)	(11,511)	(20,207)	(33,339)
Total Credit Expense (Corporate)	**71,310**	**22,890**	**27,229**	**12,146**	**11,186**	**3,929**	**860**	**77,380**	**55,349**
Total Defaults (#)	184,638	344,141	290,937	296,721	344,744	290,901	232,750	1,567,444	1,456,053

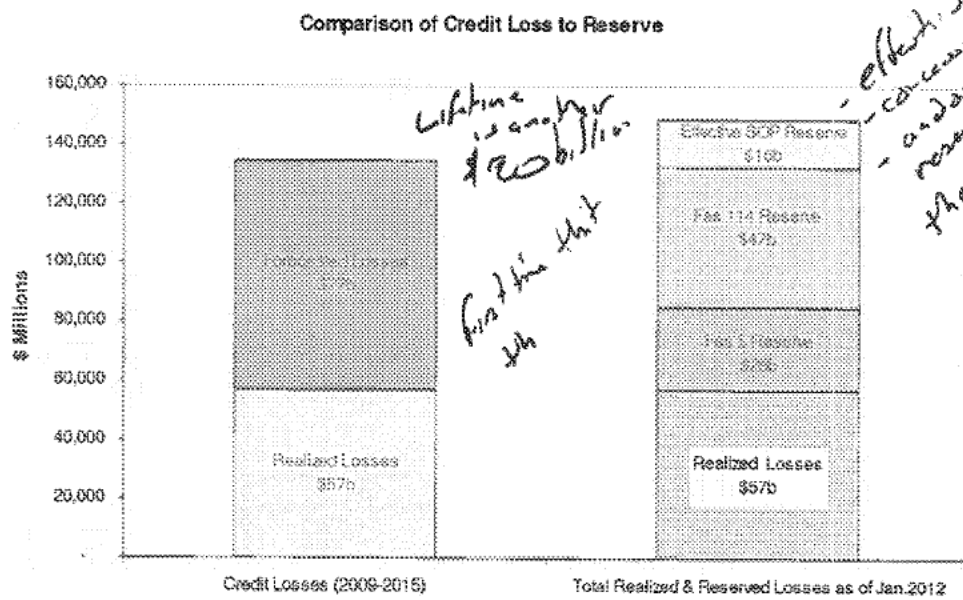
LPM-dollars

close to economic losses

Credit losses remain elevated through 2013 as delayed foreclosures from prior periods come through the pipeline; losses decrease in 2014 and 2015 as delinquencies are cleared through default or workout.

Credit Losses Expected to Decline as Book Continues to Improve





Lifetime is another $20 billion

find the third th

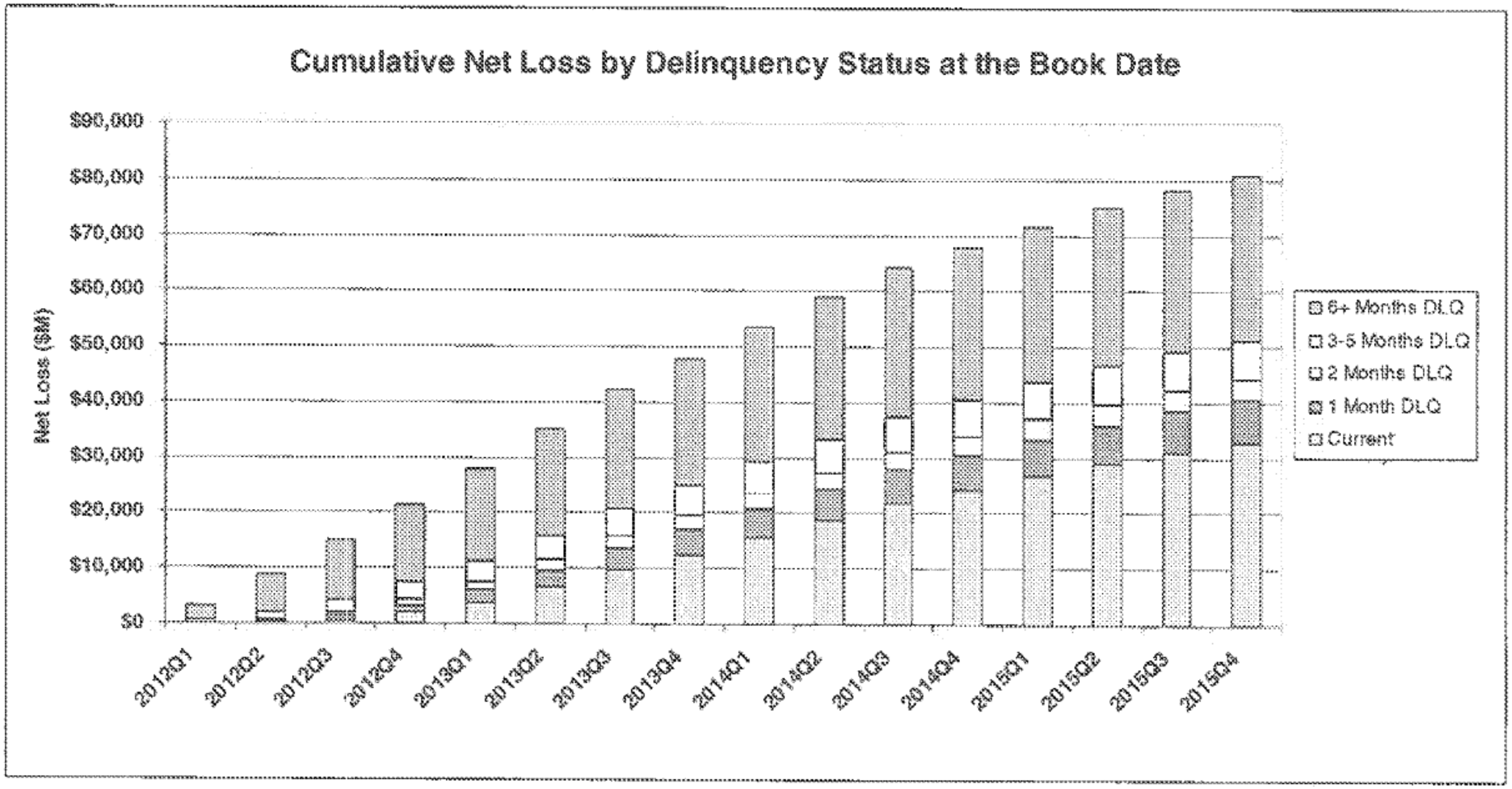
- effective
- concession
- and ... reserve of the term

While SF Book delinquency status has consistently improved since January 2010, the allowance only recently peaked. Given forecasted credit losses, we believe Fannie Mae is adequately reserved.

FannieMae

SF Losses by Current Delinquency Status

LFM captures about 4/5 or 80% of

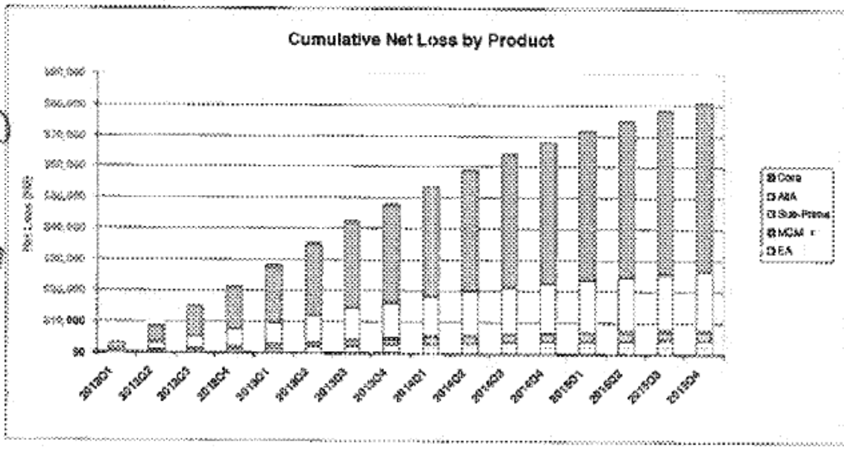


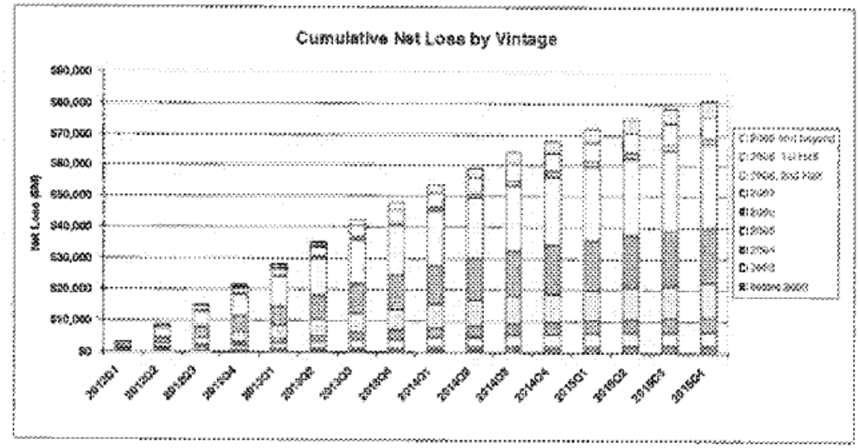
Approximately 41% of forecasted credit losses through 2015 come from loans that are not yet delinquent.

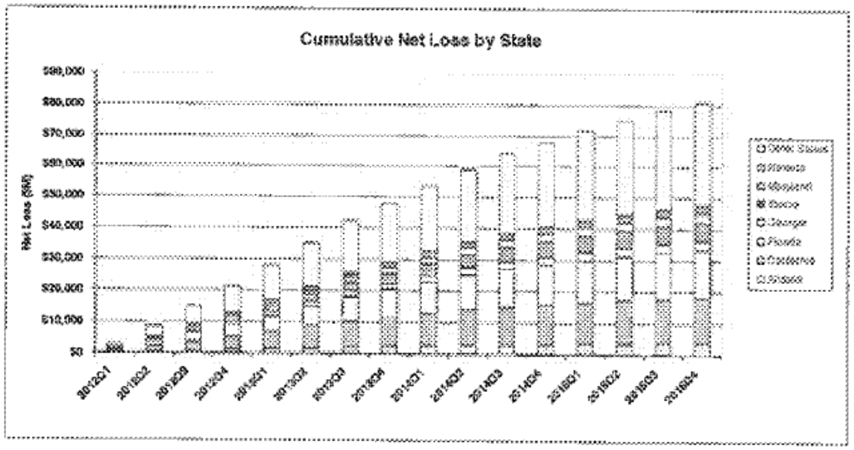
FHFA00070615

SF Losses by Vintage, Product, and State

Losses looking Forward







- No expectations of shift in losses by vintage from prior forecast
- Top 7 losses by state over 5 years: FL, CA, AZ, NV, MI, NY, IL

FHFA00070616

42% ... ms Stakeholder per Default

Sensitivities of Single Family Credit Forecast

	Single Family Credit Sensitivities ($ in Billions)	Current Projections[2]		Impact on Credit Losses (+ Increases Losses)	
		2012	2012-2015	2012	2012-2015
	Current forecast of Single Family credit-related expenses				
Influenced by Management Actions	[illegible]				
	Modification Effectiveness[1]: Increase effectiveness rate for existing and forecasted modifications to 49%[2] (2012-2015 cumulative effective rate projection is currently 44%)	42%	44%	($1.2)	($3.6)
	Modification Volumes: Increase modification volume by 10%	122K	331K	($0.0)	($1.1)
	REO:				
	REO Execution: Increase of 2% in REO sales execution ratio (sales proceeds to carrying value)	98%	98%	($0.4)	($1.8)
	Preferred Loss Mitigation Strategy (PLMS):				
	PLMS Execution: 500 basis point increase in sales execution for pre-foreclosure and third party sales	62%	66%	($0.5)	($2.1)
	Other:				
	NUC Recovery Rates: Increase recovery rate to 85% *(2011-2015 cumulative recovery rate projection is currently 75%)* Claims brands	N/A	75%	N/A	($2.2)
Exogenous Factors	Foreclosure Volumes: Accelerate REO Acquisitions (increase 2012 by 10% with corresponding 2013-2014 decrease)	208K	881K	$1.6	$0.3
	Default Expense: Increase REO default expense by 10% for foreclosure delays	$11K	$13K	$0.2	$1.0
	Home Price Index Sensitivity: National peak-to-trough decline to -31% and lower recovery from trough to the end of 2015 *(current national peak-to-trough decline projection is -24% in Q1 2013)*			$1.4	$22.0

[1] *Mod Effectiveness is defined as % of defaults avoided by successfully completing a loan modification as opposed to taking no action.*

[2] *Sensitivity assumes existing and forecasted modifications from 2009 to 2015.*

Note: Sensitivities are mutually exclusive.

Do not Add together

(defers Periods)

FHFA00070617

Agenda

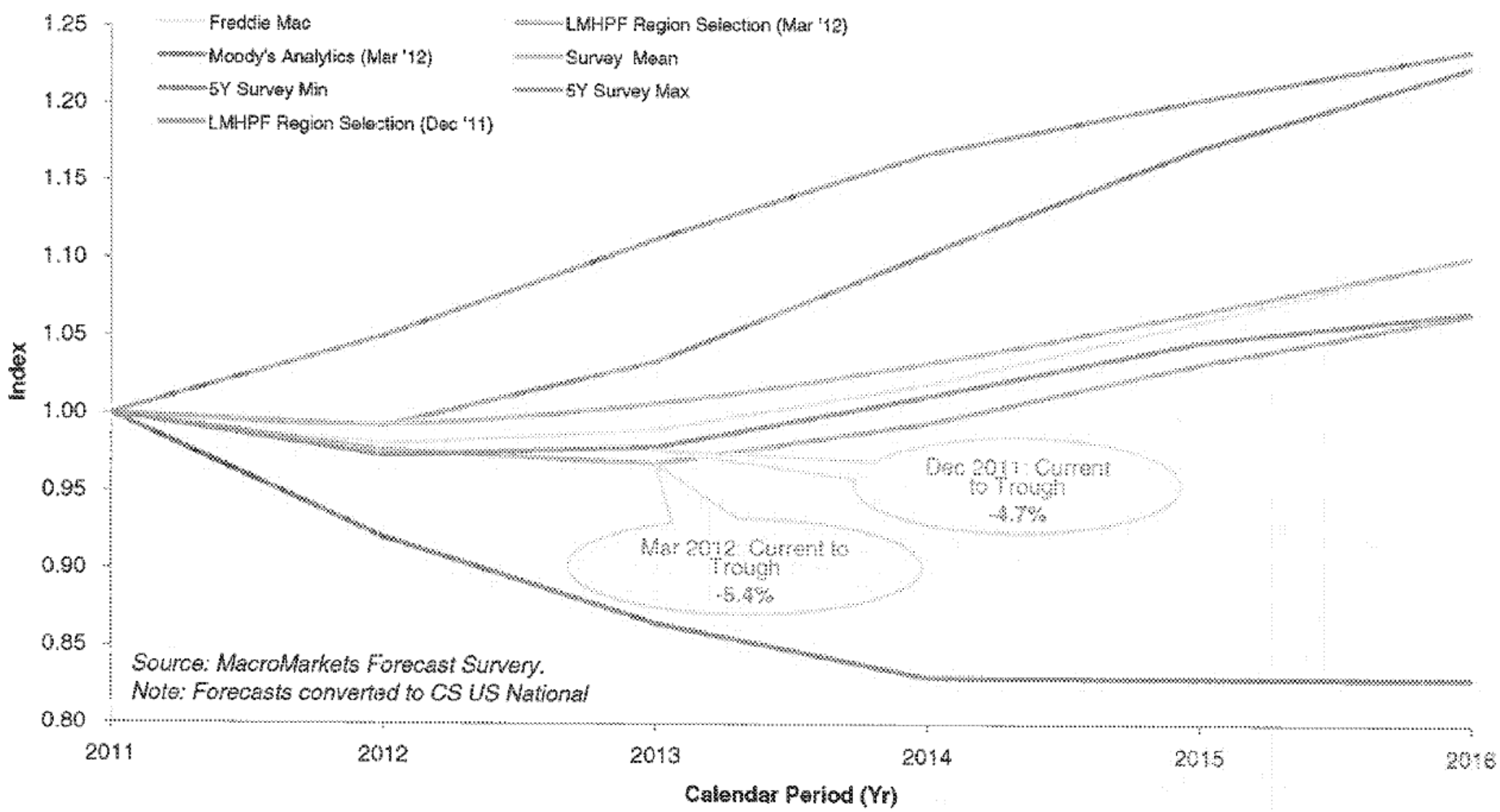
Credit Loss Forecast
- Overview
- Loss Forecast Model
- Credit Forecast Drivers
- Analysis
- Sensitivities

Comparative Analysis
- Home Price Forecast Benchmark
- FAS 114 Methodology
- Guaranty Book of Business
- Credit Metrics

Key Takeaways

Home Price Forecast Benchmarking

March 2012 Forecast Survey Q4 to Q4



Forecast similar to Consensus in short run and pessimistic in the longer run.

External Benchmarks for FAS 114 Methodology

	Foreclosure Not Probable			Foreclosure Probable
	Measurement Approach	Horizon of Estimate	Type of Cash Flow Projection	Measurement Approach
FNMA	Expected Loss	Life of Loan	Stochastic	Current collateral value less cost to sell
FRE	Incurred	Existing events and conditions	Single Path	NPV of incurred cash flows
Bank A	Expected Loss	Partial life	Single Path	Unknown
Bank B	Incurred	Existing events and conditions	Hybrid	Unknown

Key:
- *High contribution to increase in incremental allowance between FAS 5 and FAS 114 treatment.*
- *Moderate contribution to increase in incremental allowance.*
- *Low contribution to increase in incremental allowance.*

Note: Incurred measurement approach refers to the methodology where reserve is held for loans that have already suffered the loss-generating event and no projection of future economic condition is used.

Our FAS 114 methodology is very conservative when compared to external benchmarks.

SF Guaranty Book as of December 31, 2011

Freddie Mac

	[illegible]	Alt-A	IO	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Balance (UPB $Bn)	$1,746	$84	$72	$8	$56	$118	$11	$167
% of Portfolio	100%	5%	4%	0%	3%	7%	1%	10%
Wtd Avg OLTV	72%	73%	74%	71%	77%	77%	98%	98%
OLTV > 90 %	10%	4%	3%	2%	20%	18%	100%	100%
Wtd Avg MTMLTV	80%	107%	120%	119%	93%	93%	108%	106%
MTMLTV > 100%	20%	52%	69%	63%	37%	38%	50%	54%
Wtd Avg FICO	735	718	720	711	587	642	586	713
FICO < 620	3%	4%	5%	4%	100%	0%	100%	7%
% Fixed Rate	92%	64%	25%	0%	93%	92%	97%	97%
% Primary Residence	91%	82%	84%	75%	96%	94%	98%	96%
Origination Year								
2011	14%	0%	0%	0%	4%	5%	8%	17%
2010	19%	0%	1%	0%	6%	6%	8%	20%
2009	18%	0%	1%	0%	4%	6%	5%	12%
2008	7%	8%	11%	0%	8%	8%	8%	7%
2007	10%	30%	39%	2%	25%	20%	30%	16%
2006	7%	27%	28%	11%	14%	14%	10%	8%
2005	8%	19%	17%	59%	12%	14%	7%	5%
2004 and Prior	17%	15%	3%	28%	27%	27%	27%	18%
% Credit Enhancement	14%	13%	11%	18%	28%	28%	80%	56%
SDQ Rate[1]	3.58%	11.87%	17.61%	20.49%	12.53%	8.43%	15.38%	6.72%

Source: FRE 2011 10K Credit Supplement page 25 - Single Family credit guarantee portfolio characteristics
[1] Includes structured transactions where loan characteristics exist.

Fannie Mae

	[illegible]	Alt-A	IO	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Balance (UPB $Bn)	$2,762	$182	$130	$9	$88	$185	$19	$276
% of Portfolio	100%	7%	5%	0%	3%	7%	1%	10%
Wtd Avg OLTV	71%	73%	75%	71%	77%	77%	98%	98%
OLTV > 90 %	10%	7%	8%	0%	22%	20%	100%	100%
Wtd Avg MTMLTV	78%	101%	118%	101%	91%	82%	115%	111%
MTMLTV > 100%	18%	43%	61%	48%	33%	33%	61%	56%
Wtd Avg FICO	738	717	725	707	587	641	591	713
FICO < 620	3%	1%	1%	7%	100%		100%	7%
% Fixed Rate	89%	67%	31%	1%	80%	93%	78%	89%
% Primary Residence	89%	78%	85%	69%	87%	84%	89%	85%
Origination Year								
2011	16%	3%	2%		9%	5%	9%	16%
2010	19%	2%	4%		3%	5%	3%	15%
2009	17%	1%	3%		2%	4%	1%	8%
2008	7%	2%	8%		8%	8%	3%	9%
2007	10%	24%	33%	2%	26%	22%	36%	21%
2006	7%	26%	25%	25%	15%	14%	18%	9%
2005	7%	19%	16%	29%	11%	12%	9%	6%
2004 and Prior	18%	25%	8%	45%	32%	30%	27%	16%
% Credit Enhancement	14%	16%	17%	55%	28%	27%	86%	72%
SDQ Rate	3.91%	12.43%	15.27%	7.57%	13.47%	10.16%	18.87%	8.08%

Source: NSO Servicing Optimization.

Credit Related Results Comparison

Overall Summary Information (i.e. Single Family/Multi-Family)

	Freddie Mac					Fannie Mae				
	Q4 2011	Q3 2011	Q2 2011	Q1 2011	Q4 2010	Q4 2011	Q3 2011	Q2 2011	Q1 2011	Q4 2010
Allowance for Credit Losses ($ Millions)	39,461	39,744	39,095	39,305	39,926	76,938	75,641	74,756	72,101	66,251
Guaranty Book of Business ($ Millions)	1,899,718	1,932,034	1,942,344	1,950,250	1,916,299	3,037,549	3,037,381	3,066,961	3,088,136	3,054,488
Allowance / Book (bps)	208	206	201	202	208	253	249	244	233	217
Nonperforming Loans ($ Millions) [1]	120,514	119,081	114,819	115,083	115,478	201,417	202,522	200,793	206,098	212,858
Charge-offs, Net ($ Millions) [2]	3,156	3,230	3,100	2,981	2,897	4,180	3,266	3,881	4,704	2,527
Credit Losses ($ Millions) [2]	3,236	3,451	3,127	3,238	3,114	4,217	3,999	3,403	5,192	3,209
Credit Losses / Book (bps) [4]	17.0	17.9	16.1	16.6	16.3	13.9	13.2	11.1	16.8	10.5
Allowance/Nonperforming loans	32.74%	33.38%	34.05%	34.15%	34.57%	38.20%	37.35%	37.23%	34.98%	31.12%
REO Acquisitions (Nbr. of Properties) [3]	24,763	24,385	24,799	24,709	23,777	47,323	45,260	53,771	53,599	46,083
Disposition of REO (Nbr. of Properties) [3]	23,824	25,387	29,355	31,628	26,584	51,425	58,348	71,252	62,851	50,343
Ending Inventory (Nbr. of Properties) [3]	60,555	59,616	60,618	65,174	72,093	118,788	122,890	135,978	153,459	162,711
SF SDQ ($ Millions)	64,435	66,416	74,692	79,553	85,722	123,557	128,134	126,261	138,972	149,471
SF SDQ Rate [5]	3.58%	3.51%	3.50%	3.63%	3.84%	3.91%	4.00%	4.08%	4.27%	4.48%
Complete Modifications	19,048	23,919	31,049	35,158	37,203	51,936	60,025	59,019	68,759	89,691
Completed Modifications / SDQ (Count)	5%	6%	8%	8%	8%	8%	8%	8%	9%	11%
SF Allowance/SF SDQ	60%	59%	51%	48%	46%	61%	58%	57%	51%	43%

Notes

[1] Includes TDR, HomeSaver Advance loans and loans more than 2 months delinquent (single family only).

accrual policy change. FNM allowance without interest is 74,442. FNM Allowance / Book (bps), when excluding interest, is 245 compared to Freddie's 206

[2] FNM Net Charge-offs exclude the impact of acquired credit-impaired loans (SOP03-3) and losses on accrued interest.

[3] REO counts include both single family and multifamily loans.

[4] Calculated values.

[5] Includes structured transactions.

- FNM's ALL/Book ratio has been higher than that of FRE mainly driven by (1) FNM has a worse book profile as indicated by higher SDQ rate; (2) FNM has a higher proportion of book under FAS 114 treatment and has a higher FAS 114 impairment rate than FRE; (3) different model sensitivities to book profile changes and economic conditions.
- Additionally, FNM completed modification volume is 2.5 x FRE's volume, resulting in higher FAS 114 reserves for FNM. FNM has been focusing on FNM specific modifications, while in general, Freddie is less active in modification activity due to a better book profile and different loss mitigation strategies. Additionally, FNM's modification activity has contributed to the decrease in its SDQ rate while FRE's SDQ rate has been increasing over the past few quarters.

Loan Loss Reserves by Collective and Individually Impaired

	Freddie Mac						Fannie Mae					
	QoQ Delta	Q4 2011	Q3 2011	Q2 2011	Q1 2011	Q4 2010	QoQ Delta	Q4 2011	Q3 2011	Q2 2011	Q1 2011	Q4 2010
Collective Reserve - FAS5 ($ Millions) [1]	-3.44%	24,115	24,974	27,537	28,911	31,094	-0.32%	28,922	29,015	28,849	28,957	26,640
Individual Impairment - FAS114 ($ Millions) [1,2]	3.90%	15,346	14,770	11,558	10,394	8,832	2.98%	48,016	46,626	45,907	43,144	39,611
Total Allowance	-0.71%	**39,461**	**39,744**	**39,095**	**39,305**	**39,926**	1.71%	**76,938**	**75,641**	**74,756**	**72,101**	**66,251**
FAS114 / Total Allowance	4.64%	38.89%	37.16%	29.56%	26.44%	22.12%	1.25%	62.41%	61.64%	61.41%	59.84%	59.79%
Recorded Investment for FAS 114 ($ Millions)	4.60%	62,707	59,952	48,652	44,443	39,142	2.08%	169,840	166,384	156,503	152,472	148,042
FAS114 Impairment / Recorded Investment for FAS 114		24.47%	24.64%	23.76%	23.39%	22.56%		28.27%	28.02%	29.33%	28.30%	26.76%

[1] Includes reserves for accrued interest receivable and taxes and insurance.

[2] FRE excludes HAMP trials when reserving for individually impaired loans. FNM includes both HAMP trials and closed HAMP modifications in FAS 114 allowance calculations.

- FRE's total reserve decreased by approximately $200M in Q3'11 driven by an $800M decrease in their collective reserve which more than offsets a $600M increase in the individually impaired reserve.
- Both FNM's and FRE's impairment rates stayed relatively flat over the last quarter.
- FNM's FAS 114/ALL ratio is significantly higher than FRE's not only as a result of higher modification volumes, but also because of FNM's booking of makewhole benefits for FAS 114 loans under FAS 5.

Key Takeaways

- The allowance reached its highest level in Q4 2011 and is expected to reduce to $69B by year-end 2012
  - New models being implemented are likely to result in a further decline of the allowance as they will include recent history that reflects improved performance
- We believe the allowance as of year-end 2011 was appropriate
- Credit losses are expected to remain elevated through 2013 as delayed foreclosures from prior periods come through the pipeline; losses decrease in 2014 and 2015 as delinquencies are cleared through default or workout
  - The biggest risks to the current forecast are policy changes driving further decline in home prices