

FANNIE MAE
Opening Remarks from Inaugural Connecticut Avenue Securities Transaction Media Call
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10:00 a.m. ET

Andrew BonSalle: Good morning and thank you for joining today. We're going to take a few minutes to provide an update on our inaugural credit risk sharing transaction under our Connecticut Avenue Securities deal. I'll give a short background and I'll ask Laurel to give more details on the transaction.

In the way of background, obviously, private capital participation is a key component to building a future housing finance system and this deal helps lay the groundwork. This transaction is just one way we are transferring risk away from the company and taxpayers and helping build a stronger and more sustainable future system.

As you know, Fannie Mae is the largest credit investor in the United States with roughly \$2.8 trillion in the single family guaranty book of business and has roughly 45 percent market share of new single family mortgage and security issuances as of the end of Q2.

As active credit risk managers, we manage the credit risks on our books through our comprehensive end-to-end risk management approach that focuses on lender, loan and servicing quality.

You know, at the beginning of September, we held a call with potential credit investors in anticipation of our first transaction and we walked them through how we can control risk through the entire loan lifecycle. That presentation is available for download on our website if you're interested in reading it.

Over the past year and a half, we've been working to build a systemic program to take a portion of the credit risk we acquire and transfer it out to the private market. This program was created so that it's sustainable and scalable over time to promote liquidity and also flexible enough to react to feedback from the marketplace.

From a strategic perspective, these offerings provide an additional avenue for Fannie Mae to manage the credit risk on its book. We believe this is a critical piece to moving us forward to this future state of mortgage finance.

I know many of you have been following this deal and likely know we priced the deal yesterday afternoon.

The deal has been very well received by investors. So much so that we moved the transaction up from our original timeline and accelerated the pricing date to yesterday.

You know, the loans in this deal represent Fannie Mae's strongest performing book of business. These are newly originated, qualifying mortgages underwritten using our strict credit standards implemented after the housing crisis.

I'll ask Laurel now to provide more specifics on the transaction.

Laurel Davis: Great. Thanks, Andrew.

As Andrew said, we're very pleased to say that we priced the inaugural C-deal transaction late yesterday. I'd like to just take a few minutes, walk you through the structure and then we can open up for questions.

If you have been following what's going on in risk transfer and specifically saw Freddie Mac's STACR deal back in July, you'll see that our C-deal structure is very similar. That is definitely by design.

We have been working with Freddie Mac under the direction of our regulator FHFA. As we approached risk sharing, with the goal of creating similar transactions, it was important to have basic structures that are very similar. We feel that that's important from a liquidity perspective in the market. And so you'll see that as I walk through this, the basic structure and a lot of the transaction details are very similar.

There are some differences and there are enough differences to allow us to test different features in the market and take a look at investor preference for different features.

So let me just walk through the structure itself. It is a direct debt issuance of Fannie Mae. What makes it different from Fannie Mae's other senior unsecured debt is that the repayment of the notes that we issue will be subject to the credit and the prepayment performance of a reference pool of loans.

The reference pool for our first transaction was a pool of loans approximately \$27 billion in UPB. It was a portion of production that we acquired during the third quarter of 2012. During that quarter, we acquired \$231 billion of total production.

The \$27 billion is a subset of the total production and is based on particular eligibility criteria that we applied, including 30-year fixed rates, loans that were not originated under our Refi Plus program, 60 to 80 LTV slice and other criteria and then the \$27 billion represented a random sample of that production. All the loans in the reference pool currently are held in Fannie Mae guaranteed MBS pools.

We issued two classes of notes, \$675 million total, across an M-1 and an M-2 class evenly split. And basically this transferred a portion of the mezzanine risk. So essentially, Fannie Mae kept a first-loss position of 30 basis points. We sold the next 270 basis points worth of risk and then we reattached at the senior level credit position at 3 percent, so essentially Fannie Mae is retaining the top 97 percent of the transaction.

Both of the notes priced at par.

The M-1 notes carry an investment grade rating BBB- from Fitch. The M-1 notes were priced yesterday at a coupon of LIBOR plus 200 basis points, that's one month LIBOR plus 200 basis points.

The M-2 notes carry a coupon of LIBOR plus 525 basis points. These are monthly floaters. They are uncapped.

We had close to 80 investors that participated in the transaction-and it was a broad investor base. We had a mix of asset managers, mutual funds, hedge funds, insurance companies and even a couple of REITs and credit unions.

We feel like the investment grade rating on the M-1 class opened up our investor participation. We did see a wider variety of accounts than Freddie Mac and we feel that that was a result of feedback that we received from investors after the Freddie Mac transaction that investors felt that a rating would promote secondary trading and liquidity in the transaction.

Let me continue with the structure. As I mentioned, the M-1 and M-2 notes are uncapped LIBOR floaters. There is a 10-year legal final term on maturity. Like the STACR transaction, we do have a fixed severity schedule and that's designed such that as loans in the underlying reference pool hit credit events largely defined as hitting 180 days delinquent, then that acts as a loss to the transaction. The losses start reversed sequentially, so they hit the class B first, which is the most subordinate class, then the M-2, the M-1, which are the mezzanine classes, and finally the class A, which is the most senior class.

As I mentioned, we retained both the first loss piece (the B class) as well as the senior credit support (the A class) as well as a vertical slice of the transaction that was approximately 6 percent.

I would just add a couple of final points, in terms of participation in the transaction, Bank of America Merrill Lynch was our lead structuring manager and joint bookrunner. Bank of America Merrill Lynch also acted as our advisor throughout the past year as we've been building the program.

Credit Suisse was the co-lead manager and joint bookrunner and then we had co-managers, Barclays, Morgan Stanley and RBS. CastleOak Securities participated in the transaction as a selling group member.

I would also point out that we launched new web pages today on fanniemae.com that provide an overview of the program and the goals and benefits of credit risk sharing and details on the transaction.