Freddie Mac CEO and CFO Discuss Third Quarter 2023 Financial and Business Results

Remarks by Michael J. DeVito, Chief Executive Officer
and Christian Lown, EVP and Chief Financial Officer

November 1, 2023

As Prepared for Delivery

Introduction (Remarks of Mr. DeVito)

Good morning and thank you for joining today's call to review Freddie Mac's business and financial results.

As many of you know, September marked 15 years since Freddie Mac entered government conservatorship. And the company has made significant progress.

While much remains to be done, and this company is committed to the work, today I will cover three topics that illustrate how far Freddie Mac has come since 2008:

- First, how the company has intensified its focus on mission, particularly related to affordable housing.
- Second, how risk has been reduced.
- And finally, how Freddie Mac has made progress in its work to build financial stability.

Then I will turn it over to our CFO, Chris Lown, for an update on the company's third quarter financial performance.

Ongoing Improvement

Mission

Let's start with mission.

Over the past few years, Freddie Mac has strengthened its focus on its mission and embraced an expansive view of support for affordable housing.

Freddie Mac strives to meet or exceed a number of affordable housing-related commitments, such as:

- Affordable Housing Goals in both Single Family and Multifamily,
- The Duty to Serve Plan, which targets high-needs rural regions, manufactured housing, and affordable housing preservation.
- And that includes the company's payments into the Capital Magnet Fund and Affordable Housing Trust Fund, which now top $2.2 billion.
- And finally, Freddie Mac's Equitable Housing Finance Plan, which expands the company's efforts to promote equity in the Single-Family and Multifamily markets.

Regulatory commitments are the baseline expectation. Today, the company approaches mission more broadly, with a range of initiatives to help renters, lenders, diverse developers and other market participants. For example:

- Single-Family improved its technology to help borrowers with thin credit files by allowing lenders to access bank data, tax transcripts and direct deposit data to verify critical information such as income, assets, and on-time rent payments.
- Multifamily is helping renters prepare for homeownership though an on-time rent reporting initiative, which helps them establish or raise credit scores. To date, more than 375,000 renters can participate.
- Freddie Mac has also provided tools to help borrowers receive down payment assistance, including through Special Purpose Credit Programs and the newly launched DPA One tool, both of which I have discussed previously.

This company's commitment to housing affordability is more ingrained in its DNA than ever before.

Reducing Risk

That's equally true for the company's commitment to strong risk management. Today, it is both a requirement and a vital part of Freddie Mac's identity.

Here are just a few of the many examples:

- Since 2008, Freddie Mac has reduced its mortgage-related investments portfolio down to approximately $85 billion. This is less than one-tenth of its $867-billion peak.

- In 2020, the company adopted bank-like capital requirements designed to backstop its risks and has been steadily building total equity to meet those requirements.

- And finally, Freddie Mac pioneered credit risk transfer. CRT brings billions of dollars of private capital into the U.S. housing finance system, dramatically reducing taxpayer exposure and lowering the company's own risk.

    - In fact, the third quarter marked 10-years since the first Single-Family CRT transaction.

    - To date, Freddie Mac's Single-Family CRT program has transferred more than $108 billion of credit risk on approximately $3.3 trillion of mortgages.

    - Multifamily has also protected a half-trillion dollars of loans via its K-Deal program, which started in 2009.

Ensuring Stability

Finally, let me turn to the growing stability of Freddie Mac's financial position after 15 years of change and improvement.

In the third quarter the company earned $2.7 billion and grew its net worth to $44.7 billion.

Furthermore, credit quality today is strong in both the Single-Family and Multifamily mortgage businesses. Chris will say more about that in a moment, but it is clear that the changes the company made since 2008 have set Freddie Mac on a new course.

Keeping What Works

While the company made significant strides to improve its focus and performance over the past 15 years, it still preserved the core elements of Freddie Mac that have worked for decades.

That includes support for the 30-year mortgage—the cornerstone of the American housing finance system and Freddie Mac's business. Thirty-year fixed-rate mortgages accounted for more than 90 percent of the home loans we purchased this year.

Freddie Mac is also helping provide access to housing for low- and moderate-income renters and borrowers.

- Support for first-time homebuyers is near all-time highs at 50 percent of purchase loans.

- And more than 90 percent of the eligible rental units financed were affordable to low-income and working families.

The company also has preserved small lenders' access to the secondary mortgage market via the cash window.

And it enhanced liquidity in the to-be-announced market as one of the leaders in the creation of the uniform mortgage-backed security, one of the most significant changes to the market in a generation.

- Since inception more than $284 trillion of UMBS have been traded.

Finally, Freddie Mac has maintained its counter-cyclical role. The company's market presence in the early days of the pandemic and current support for the housing market are solid examples.

Playing an Important Role

Before I turn it over to Chris Lown, allow me to put the work of thousands of talented people over 15 years into context.

Since 2008, Freddie Mac has:

- Provided more than $8 trillion in liquidity to the mortgage market,
- Helped nearly 11 million homebuyers, including more than 4.1 million first-time homebuyers, and
- Funded more than 8.3 million rental units, 87 percent of which were affordable.

Further the company has returned nearly $120 billion to taxpayers, approximately 67 percent more than it borrowed from the U.S. Treasury.

And most importantly, Freddie Mac is a strong, stable organization that is unwavering in its focus on Making Home Possible for renters and borrowers well into the future.

Now, let me turn it over to Chris.

Financial Results (Remarks of Mr. Lown)

Thank you, Michael, and good morning.

As Michael noted, this morning we reported net income of $2.7 billion for the quarter, an increase of $1.4 billion, or 104 percent, year-over-year. This increase was primarily driven by a credit reserve release in our Single-Family business versus a credit reserve build in the prior year quarter.

Third quarter net revenues were $5.7 billion, an increase of $509 million, or 10 percent, year-over-year. This increase was driven by both higher net interest income and higher non-interest income. Net interest income increased 4 percent year-over-year to $4.7 billion, driven by higher investments net interest income benefiting from higher short-term interest rates. Non-interest income of $941 million was up 50 percent year-over-year driven by higher Multifamily guarantee income and higher investment gains.

An increase in observed and forecasted house price appreciation drove a $263 million benefit for credit losses this past quarter versus an expense of $1.8 billion in the prior year quarter.

In the third quarter of 2022, the provision for credit losses was driven by deterioration in housing market conditions coupled with lower observed and forecasted house price appreciation.

These increases were partially offset by a $751 million, or 41 percent, increase in our non-interest expense, which was primarily driven by an allocation of $313 million for the accrual for the judgement in the Fairholme Funds litigation and a $314 million decrease in Single-Family credit enhancement recoveries due to a decline in expected credit losses on covered loans.

Our total mortgage portfolio at the end of the third quarter was $3.5 trillion, a 2 percent increase year-over-year.

Single-Family Business Segment

Turning to our individual business segments, the Single-Family segment reported net income of $2.3 billion for the quarter, up $1.5 billion, or 176 percent, from the prior year quarter.

Single-Family net interest income of $4.5 billion was up 4 percent year-over-year, primarily driven by higher income on our investment portfolio, which benefited from higher short-term interest rates, partially offset by lower deferred fee income recognition as prepayments slowed due to higher mortgage interest rates. Mortgage interest rates at the end of this quarter were 7.31 percent, up 61 basis points from the prior year quarter. Non-interest income for Single-Family was $393 million this quarter, up $335 million from the prior year quarter. This increase was primarily driven by higher net investment gains which benefited from higher interest rate-related gains.

Our benefit for Single-Family credit losses this quarter was $304 million, primarily driven by increases in observed and forecasted house price appreciation. In the prior year quarter, we had a provision expense of $1.8 billion, which was primarily driven by deterioration in forecasted housing conditions and lower observed and forecasted house price appreciation.

House prices increased by 2.5 percent this quarter and our forecast assumes an increase of 2.9 percent over the next 12 months and 1.7 percent over the subsequent 12 months.

The Single-Family allowance for credit losses coverage ratio at the end of the quarter was 22 basis points, down from 23 basis points a year earlier.

The Single-Family serious delinquency rate declined to 55 basis points at the end of the third quarter, down 12 basis points from the end of the prior year quarter. The Single-Family serious delinquency rate remains historically low and is down 8 basis points from the pre-COVID rate of 63 basis points at the end of 2019.

In the third quarter, we helped approximately 18,000 families remain in their homes through loan workouts. Our loan workouts have continued to decline as the seriously delinquent loan population has declined.

Our Single-Family mortgage portfolio increased 2 percent year-over-year to $3 trillion at the end of the third quarter.

Credit characteristics of our Single-Family portfolio remained strong, with the weighted average current loan-to-value ratio at 53 percent and the weighted average current credit score at 756. At the end of the quarter, 62 percent of our Single-Family portfolio had some form of credit enhancement.

New business activity was $85 billion, up $2 billion from the second quarter. However, year-over-year new business activity declined $36 billion, or 30 percent, as both refinance and purchase activity declined due to higher mortgage interest rates. Home purchase volume of $76 billion made up 89 percent of our total new business activity this quarter. First-time homebuyers represented 50 percent of new Single-Family home purchase loans. The average guarantee fee rate charged on new business was 55 basis points this quarter.

Multifamily Business Segment

Moving on to Multifamily, the segment reported net income of $362 million, down 23 percent, or $108 million, from the prior year quarter. This decrease was primarily driven by higher provision for credit losses and higher non-interest expense in this period.

The provision for credit losses in Multifamily this quarter was $41 million, an increase of $29 million from the prior year quarter primarily driven by deterioration in overall loan performance. The Multifamily allowance for credit losses coverage ratio at the end of this quarter was 54 basis points, up from 14 basis points a year earlier.

Non-interest expense was $266 million, up $94 million, or 55 percent, year-over-year, primarily driven by an allocation for the accrual for the judgment in the Fairholme Funds litigation.

The Multifamily delinquency rate was 24 basis points at the end of the quarter, up from 21 basis points last quarter and 13 basis points at the end of September 2022. This increase was primarily driven by an increase in delinquent loans in our senior housing and small balance loans portfolios. Ninety four percent of these delinquent loans have credit enhancement coverage.

We have seen a continued decline in demand for Multifamily mortgage financing due to higher mortgage interest rates and a slowdown in the Multifamily origination market.

Our Multifamily new business activity was $13 billion for the third quarter, bringing the year-to-date volume to $32 billion versus $44 billion for the same time last year.

Our Multifamily mortgage portfolio increased 4 percent year-over-year to $432 billion, of which 95 percent was covered by credit enhancements.

Capital

On the capital front, our net worth increased to $44.7 billion at the end of the quarter, representing a 27 percent increase year-over-year.

With that I will turn it back over to Michael.

Conclusion (Remarks of Mr. DeVito)

Thanks, Chris.

Before we close, let me say a few words about the recent announcement that I will be departing Freddie Mac in early 2024.

It is a privilege to lead this company. And Freddie Mac is fortunate to have a strong leadership team, ready to meet the challenge of guiding this company into the future, and an outstanding group of employees who are intensely dedicated to its mission and making home possible.

Thank you for joining us today.