

# **We Open Doors for America's Families**

Freddie Mac's  
Annual Housing Activities Report  
for 2002

March 17, 2003

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## About this Report

Freddie Mac provides this report to the Committee on Banking, Housing, and Urban Affairs of the Senate, the Committee on Financial Services of the House of Representatives and the Secretary of Housing and Urban Development (HUD), in fulfillment of the Federal Home Loan Mortgage Corporation Act ("the Freddie Mac Act")<sup>1</sup> and regulations issued by HUD ("the Final Rule").<sup>2</sup>

This report describes Freddie Mac's central role in the housing finance system and housing finance activities in 2002, including information Freddie Mac is required to report under the Freddie Mac Act and the Final Rule.<sup>3</sup> This report provides a comprehensive picture of Freddie Mac's secondary mortgage market activities and the benefits we provide to the housing finance system and to America's homeowners and renters.

2002 was an outstanding year for Freddie Mac and the families we serve. Our mortgage purchases enabled millions of families to obtain low-cost mortgages, strengthened the housing market and helped bolster the national economy. We met all of the housing goals and reinforced our strong commitment to increasing minority homeownership with new initiatives in support of the President's goal. Freddie Mac is proud of the role we play in making the world's best housing finance system even better for America's families.

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<sup>1</sup> 12 U.S.C. § 1456(f) (1997).

<sup>2</sup> HUD, Office of the Secretary, 24 C.F.R., Part 81, The Secretary of HUD's Regulation of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac); 24 C.F.R. § 81.63.

<sup>3</sup> Appendix 1 to this Report lists these information items and the portions of the report that address them.

## Executive Summary

The United States has a housing finance system that is the envy of the world. What America's homebuyers take for granted – the ability to obtain a 30-year fixed-rate mortgage with a low down payment, the option to prepay this mortgage at any time, and the continuous availability of mortgage credit under a wide range of economic conditions – does not exist in most countries.

Freddie Mac's secondary market activities play a central role in the success of America's housing finance system. By purchasing mortgages from lenders around the country every day and maintaining a broad and deep investor base for the mortgage-backed and debt securities we use to finance our mortgage purchases, Freddie Mac ensures that lenders have a continuous source of funds for lending. The continuous availability of low-cost mortgage credit is a key reason why the 2002 housing market remained strong in spite of a recession and a relatively weak economic recovery.

In 2002, Freddie Mac provided unprecedented service to the nation's mortgage market. We once again demonstrated our vital role in the world's best housing finance system and the many benefits we bring to homeowners, renters and the mortgage market. For more than 30 years, Freddie Mac has consistently supported homeownership and rental housing. Continuing that track record during 2002, Freddie Mac:

- Purchased a record \$592 billion in mortgages eligible for goal reporting, including a record \$13 billion in multifamily mortgages, to finance homes for nearly 4.6 million families (about 18,000 homes every business day)
- Provided a stable supply of low-cost mortgage credit that saved families billions of dollars in lower mortgage costs and helped bolster the national economy
- Attracted capital worldwide to finance America's housing
- Accepted President Bush's call to increase minority homeownership by launching 25 high-impact initiatives called *Catch the Dream*
- Financed homes for nearly 2.5 million low- and moderate-income families or families living in underserved areas, representing more than half of our purchases, and once again met all the housing goals despite an economic environment that made this particularly challenging

These and many other achievements during 2002 show that Freddie Mac remains steadfast in our mission of improving the quality of life by making decent, accessible housing a reality.

## **Freddie Mac's Record Purchases Supported Record Mortgage Activity in 2002**

During 2002, America's families borrowed record amounts of mortgage credit. Spurred by the lowest mortgage rates in a generation, an all-time high of \$2.5 trillion of single-family mortgages were originated in 2002, representing nearly 38 percent of total single-family mortgage debt outstanding. This incredible level of mortgage activity could not have occurred without a vibrant and liquid secondary mortgage market.

In 2002, Freddie Mac supported the market by purchasing from banks and other lenders a record \$592 billion<sup>4</sup> of single-family and multifamily mortgages<sup>5</sup> eligible for reporting under the housing goals.<sup>6</sup> As a result of Freddie Mac and the secondary market, millions of borrowers from all across the country save billions of dollars in lower mortgage payments each year. In total, homeowners with conforming mortgages eligible for purchase by Freddie Mac save up to \$23.5 billion per year in interest costs.<sup>7</sup>

Our 2002 purchases financed homes for 4.6 million families. Nearly 2.5 million of these families, representing 54 percent of our total mortgage purchases, were very-low-, low- or moderate-income families or families living in underserved areas. We financed homes for 217,000 first-time homebuyers. By financing nearly one out of six first-time homebuyer mortgages originated last year, Freddie Mac played a significant role in boosting the national homeownership rate to an all-time high of 67.9 percent in 2002. We also financed homes for 619,000 families who rent apartments in multifamily buildings or single-family houses.

Our single-family mortgage purchases financed homes for 576,000 minority families, including mortgages for nearly 100,000 African-American and 190,000 Hispanic families. Freddie Mac's purchases of mortgages made to minority families comprised 17.3 percent of our total mortgage purchases in 2002.

As in previous years, most of Freddie Mac's single-family mortgage purchases in 2002, including those fulfilling the housing goals, came from our standard purchase activities. At the same time, Freddie Mac continued a broad range of targeted efforts to expand markets and extend the availability of affordable mortgage credit to very-low-, low- and

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<sup>4</sup> Freddie Mac purchases totaled \$642 billion in 2002 inclusive of non-Freddie Mac guaranteed securities (primarily Ginnie Mae mortgage-backed securities, mortgage revenue bonds and other mortgage-related securities) that are ineligible for reporting pursuant to the Final Rule.

<sup>5</sup> "Single-family" refers to properties with one to four dwelling units, while "multifamily" refers to properties with five or more units.

<sup>6</sup> The Final Rule, 24 C.F.R. § 81.63.

<sup>7</sup> J. Pearce and J. Miller, *Freddie Mac and Fannie Mae: Their Funding Advantage and Benefits to Consumers*, January 2001.

moderate-income families, families in underserved areas and minority families. Freddie Mac also maintained our leadership in promoting responsible lending practices and financial literacy.

To promote access to mortgage credit, in 1995 Freddie Mac pioneered the use of automated underwriting for mortgages. Loan Prospector<sup>®</sup>, our state-of-the-art automated underwriting service, has now been widely adopted by lenders across the country. Loan Prospector enables lenders to evaluate mortgages faster, at lower cost and with greater accuracy and consistency. Automated underwriting has revolutionized the mortgage industry, and Freddie Mac is proud of our leadership in using technology to expand the market.

Freddie Mac's multifamily mortgage financings in 2002 totaled \$13.3 billion, nearly 12 percent higher than our 2001 purchase volume of \$11.9 billion. Our multifamily purchases financed housing for 333,000 families. The vast majority of the multifamily units we financed – 93 percent – was affordable to very-low-, low- and moderate-income families. In 2002, we again combined our financing activities with public resources and offered the mortgage products needed to make rental housing more affordable for very-low-, low- and moderate-income families. In addition, we increased our penetration of underserved market segments such as mortgages on small multifamily properties.

Since 1993, Freddie Mac's multifamily activities eligible for goal reporting have totaled nearly \$54 billion, financing rental housing for more than 1.6 million families. Whether the mortgages we purchase finance a high-rise in a city, a small building in a rural town or a garden apartment complex in a suburb, our multifamily activities increase the availability of affordable rental housing and bring liquidity and standardization to the multifamily market.

### **Freddie Mac's Activities Support the Economy**

Freddie Mac an essential part in supporting and stabilizing the national economy in 2002, as the housing market remained strong despite weakness elsewhere in the economy. Home construction and remodeling fueled the economy. Home sales set an all-time record as about one in every 12 homes changed hands. Record refinancing reduced families' monthly payments and enabled them to tap home equity to improve their homes and increase spending and investment. Recent estimates attribute as much as one-third of the nation's economic growth since 2000 to the housing and mortgage markets.<sup>8</sup> Because of Freddie Mac and the secondary market, mortgage credit was available to meet unprecedented demand and support the housing and mortgage markets.

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<sup>8</sup> "The Economic Contribution of the Mortgage Refinancing Boom," Economy.com, December 2002, p 2. Available at [http://www.homeownershipalliance.org/media/press/zandi\\_december2002\\_updated.pdf](http://www.homeownershipalliance.org/media/press/zandi_december2002_updated.pdf).

### **Freddie Mac Is Committed to Expanding Minority Homeownership**

The nation's homeownership rate reached a record high of 67.9 percent, with more families of all racial and ethnic backgrounds owning homes than ever before. However, fewer than half of America's minority households have achieved the dream of homeownership. In his State of the Union address on January 29, 2002, President George W. Bush called for "broader homeownership, especially among minorities." On June 17, 2002, the President called on the housing industry to make homeownership a reality for 5.5 million additional minority families by the end of this decade.

Freddie Mac was pleased to respond to the President's challenge by launching *Catch the Dream*. Building on our strong record of expanding access to the mortgage market during the past 30 years, *Catch the Dream* consists of 25 high-impact initiatives to accelerate the growth in minority homeownership. Our initiatives range from best-in-class homebuyer outreach and education to new technologies and mortgage products designed to put families into homes they can afford and keep. Freddie Mac is implementing these initiatives in collaboration with mortgage lenders, nonprofit housing and community organizations, and other industry leaders. Freddie Mac is committed to purchase \$400 billion in mortgages made to minority families by the end of this decade.

### **Freddie Mac Achieved All of the Housing Goals For the Seventh Consecutive Year**

Our continued efforts to extend the benefits of the mortgage market to very-low-, low- and moderate-income families and people living in underserved areas enabled Freddie Mac to meet all three of the housing goals established by HUD for the seventh consecutive year:

- 51.3 percent of the homes Freddie Mac financed were affordable to low- and moderate-income families. These purchases totaled \$189 billion and financed housing for 2.0 million families. The low- and moderate-income housing goal for 2002 was 50 percent of the total number of homes financed by our mortgage purchases.<sup>9</sup>
- 31.8 percent of the homes Freddie Mac financed were located in underserved areas. These purchases totaled \$128 billion and financed housing for more than 1.2 million families. The underserved areas goal for 2002 was 31 percent of the total number of homes financed.<sup>10</sup>

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<sup>9</sup> Low- and moderate-income families have incomes at or below 100 percent of the area median income.

<sup>10</sup> The Final Rule defines underserved areas to mean: (1) for OMB-defined metropolitan areas, census tracts having a median income at or below 120 percent of the median income of the metropolitan areas and a minority population of 30 percent or greater; or a median income at or below 90 percent of median income of the metropolitan area; and (2) for nonmetropolitan areas, counties having a median income at or below 120 percent of the state nonmetropolitan median income and minority population of 30 percent or

- 20.6 percent of the homes Freddie Mac financed were affordable to low-income families in low-income areas or to very-low-income families.<sup>11</sup> These purchases totaled \$57 billion and financed housing for 778,000 families. The special affordable housing goal for 2002 was 20 percent of the total number of homes financed. In addition, \$5 billion of Freddie Mac's purchases eligible for the special affordable goal were multifamily mortgages. The multifamily housing target within the special affordable goal was \$2.11 billion.

Exhibit 1 shows that Freddie Mac's purchases exceeded each of the goals established by HUD.

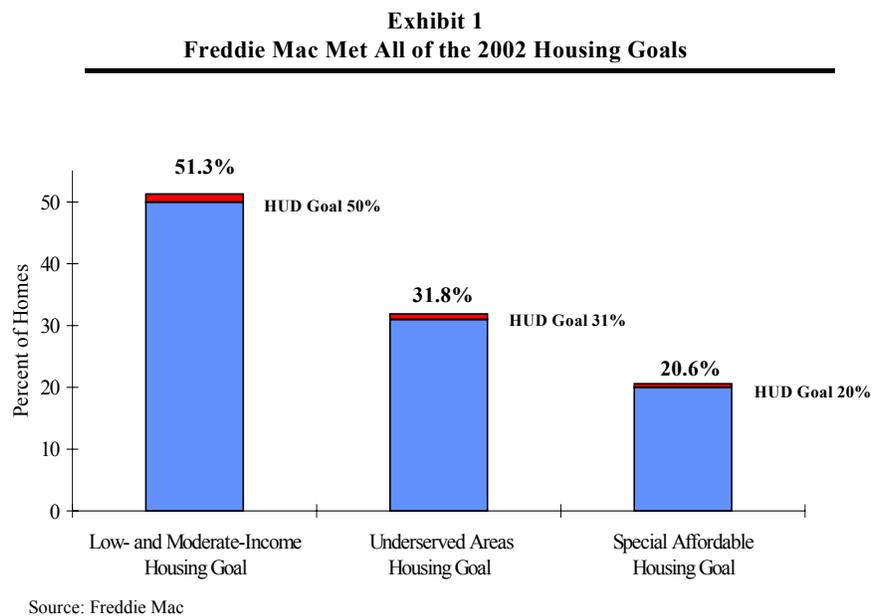


Exhibit 2 shows the dollar volume and number of homes that we financed for owner-occupied and rental properties related to each of the goals.<sup>12</sup>

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greater; or a median income at or below 95 percent of the greater of the state nonmetropolitan median income or the nationwide nonmetropolitan median income. 24 C.F.R. §81.2.

<sup>11</sup> Low-income areas refer to census tracts in which the median income is at or below 80 percent of the area median income. Low-income families have incomes at or below 80 percent of area median income, while very-low-income families have incomes at or below 60 percent of the area median income.

<sup>12</sup> 24 C.F.R. 81.12-81.14.

**Exhibit 2**  
**Freddie Mac's 2002 Mortgage Purchases**  
**That Met the Affordable Housing Goals**

	<u>Low- and Moderate- Income Housing Goal</u>		<u>Underserved Areas Housing Goal</u>		<u>Special Affordable Housing Goal</u>	
	<u>Volume (\$ billions)</u>	<u>Homes Financed</u>	<u>Volume (\$ billions)</u>	<u>Homes Financed</u>	<u>Volume (\$ billions)</u>	<u>Homes Financed</u>
<b>Single-family</b>						
<b>Owner-occupied</b>	\$159.6	1,435,038	\$112.2	926,413	\$43.6	482,830
<b>Rental</b>	17.6	247,473	9.9	144,510	8.6	142,027
<b>Multifamily</b>	<u>11.5</u>	<u>297,979</u>	<u>5.9</u>	<u>153,914</u>	<u>5.0</u>	<u>152,791</u>
<b>Total</b>	\$188.7	1,980,490	\$128.0	1,224,837	\$57.2	777,648

Note: Single-family rental consists of rental units in investor-owned 1-4 unit properties and owner-occupied 2-4 unit properties. Dollar volumes and homes financed may not sum to the total due to rounding.

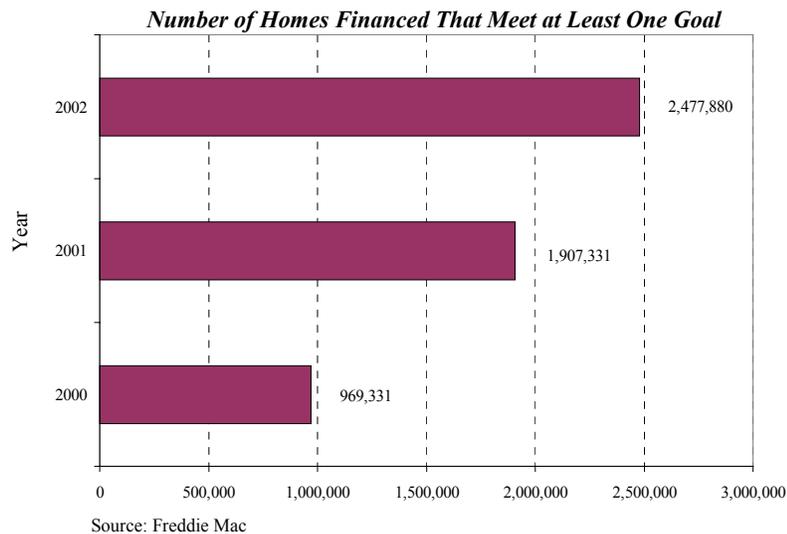
Source: Freddie Mac

Exhibit 3 shows the total number of homes funded by Freddie Mac that fulfilled one or more of the housing goals since 2000. From 2000 to 2002, the number of homes Freddie Mac financed for very-low-, low- and moderate-income families and families in underserved areas more than doubled.

Freddie Mac's success in achieving all of the housing goals in 2002 is particularly noteworthy, as the record low interest rates reduced the relative availability of mortgages meeting the goals. Lower rates attracted large numbers of middle- and higher-income borrowers to refinance their mortgages. As a consequence, low- and moderate-income borrowers comprised a smaller share of the market than in previous years. In addition, growth in the single-family market outpaced growth in the multifamily market. While Freddie Mac purchased a record volume of multifamily mortgages in 2002, multifamily purchases – almost all of which meet one or more of the goals – comprised a smaller share of our overall purchases because of the high demand for single-family mortgages.

**Exhibit 3**  
**Freddie Mac Has Substantially Increased Purchases of**  
**Mortgages Meeting the Housing Goals Since 2000**

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**Conclusion**

2002 was an outstanding year for Freddie Mac and the families we serve. Our mortgage purchases enabled millions of families to obtain low-cost mortgages, strengthened the housing market and helped bolster the national economy. We met all of the housing goals and reinforced our strong commitment to increasing minority homeownership with new initiatives in support of the President's goal. Freddie Mac is proud of the central role we play in making the world's best housing finance system even better for America's families.

## **Chapter 1: Opening Doors for America's Families**

Freddie Mac and the secondary mortgage market play a key part in the ongoing vitality of U.S. housing and mortgage markets. Even during recent periods of economic weakness and uncertainty, America's families had ready access to low-cost mortgage credit and the housing and mortgage markets remained robust – indeed they buoyed a weakened economy.

Congress created Freddie Mac in 1970 to establish and maintain a national secondary market for conventional residential mortgages. In our charter, Congress articulates four purposes for Freddie Mac:

- Provide stability in the secondary market for residential mortgages
- Respond appropriately to the private capital market
- Provide ongoing assistance to the secondary market for residential mortgages (including mortgages on housing for low- and moderate-income families) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing
- Promote access to mortgage credit throughout the nation (including central cities, rural areas, and other underserved areas) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing<sup>13</sup>

We fulfill these purposes every day by purchasing mortgages from our nationwide network of lenders, overseeing the servicing of 10 million loans, providing tools to keep mortgage lenders at the forefront of a changing market, issuing debt and mortgage-backed securities to meet investor needs, managing our retained mortgage portfolio and maintaining sufficient capital to meet existing and future market needs. Through superb execution of these functions, we bring stability and liquidity to the housing finance system. This ensures that mortgages are continually available at the lowest possible cost to a widening cross-section of America's families.

### **Freddie Mac's Central Role in the U.S. Housing Finance System**

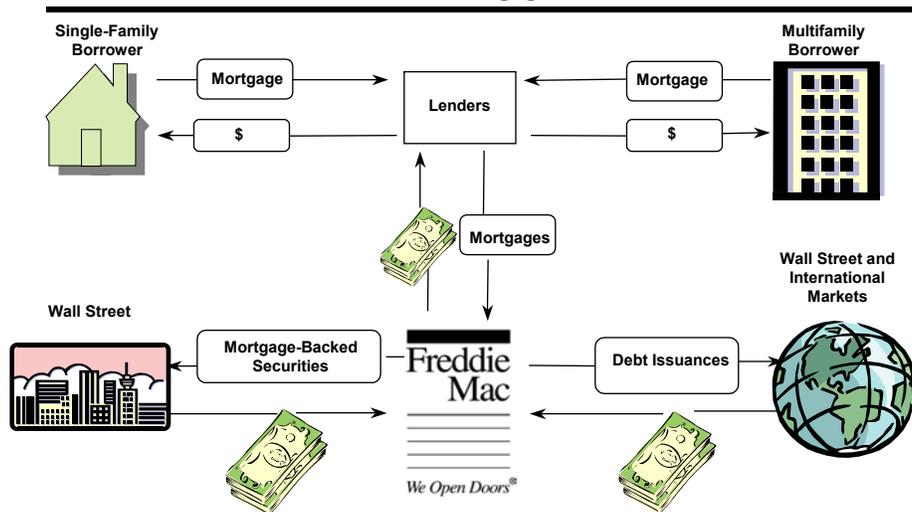
Exhibit 4 shows the basic elements of the housing finance process and Freddie Mac's central role in it. In the primary market, families borrow mortgage funds from primary lenders such as banks, thrifts, mortgage companies or credit unions. Increasingly, instead of seeking a lender directly, borrowers use a mortgage broker as an intermediary. Lenders obtain mortgage funds in a variety of ways, often through selling either newly originated or seasoned portfolios of mortgages in the secondary mortgage market. The secondary market encompasses institutions such as Freddie Mac that are engaged in buying and selling mortgages and mortgage-related securities. Freddie Mac's purchases

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<sup>13</sup> Freddie Mac Act, Section 301(b).

of mortgages and mortgage securities and our issuances of mortgage and debt securities to finance those purchases channel funds back to the primary market and to new borrowers. Our business activities are vital to ensuring the continuous supply of funding to support America's housing finance system.

**Exhibit 4  
Freddie Mac Facilitates the Steady Flow of  
Low-Cost Mortgage Funds**



This system of financing America's housing works extremely well. The activities of Freddie Mac and the secondary market ensure borrowers have access to a steady supply of mortgage credit in a wide variety of economic environments. During 2002, the lowest interest rates in nearly 40 years resulted in the origination of a record \$2.5 trillion in single-family mortgages – 38 percent of the \$6.5 trillion in single-family mortgage debt outstanding at the end of the year. Average daily originations equaled \$10 billion – meaning that nearly 70,000 homes were purchased or refinanced *every* business day.<sup>14</sup> Freddie Mac's funding of \$575 billion of single-family mortgages – 23 percent of total single-family originations – played a central role supporting these record mortgage volumes.

### Linking Mortgage and Capital Markets

Key to the role Freddie Mac plays is our ability to tap global capital markets and deliver funds to the nation's lenders (and ultimately borrowers). As shown in Exhibit 4, Freddie

<sup>14</sup> The average daily origination amount is based upon \$2.5 trillion in single-family originations during 250 business days in 2002 with an average loan amount of \$150,000.

Mac uses two complementary funding vehicles to accomplish this: mortgage-backed securities and debt.

Freddie Mac has led the development of innovative mortgage-backed securities. In 1971, Freddie Mac pioneered the development of the conventional mortgage-backed securities market by creating Mortgage Participation Certificates (PCs), passthrough mortgage-backed securities backed by conventional loans. Building on the success of this single-class security, in 1983 we issued the first multiclass mortgage security, the forerunner of today's Real Estate Mortgage Investment Conduit (REMIC). Multiclass securities customize mortgage cash flows to meet the investment objectives of particular investors. During the 1990s, we continued to introduce innovative security products. For example, we pioneered one of the first securities backed by mortgages originated by depository institutions to meet their Community Reinvestment Act (CRA) objectives. The high quality and liquidity of our securities makes them attractive to investors, ultimately reducing mortgage rates for homebuyers. During 2002, Freddie Mac issued \$547 billion in PCs.

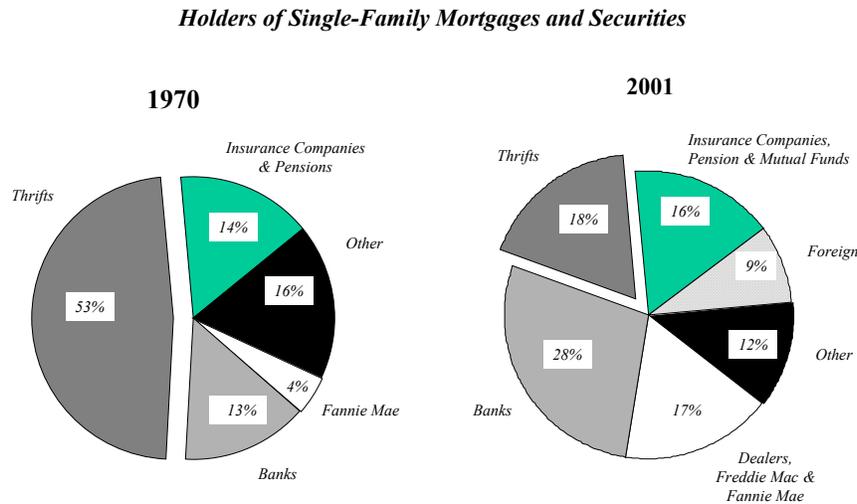
As of the end of 2002, about 43 percent of the mortgages owned (or guaranteed) by Freddie Mac were held in our retained portfolio. Freddie Mac finances this portfolio by issuing debt securities. During the past decade, the use of debt funding has become an increasingly important method of financing Freddie Mac's mortgage purchases and has enabled us to create a worldwide investor base for America's housing finance system. Some investors, particularly those outside of the United States, prefer debt to mortgage-backed securities. International investors often are unfamiliar with 30-year, fixed-rate mortgages, which are not readily available in most countries. These investors may not wish to assume the prepayment risk of mortgage-backed securities and prefer the fixed payment schedule that debt provides. By issuing debt securities we are able to tap the global capital market more effectively than if we offered only mortgage-backed securities. As a major investor in mortgage-backed securities, we provide a significant amount of liquidity to the market, which, in turn, lowers mortgage rates for homeowners. As explained below, Freddie Mac's access to the global debt market proved crucial during two recent periods of financial market turmoil, the Asian debt crisis in the fall of 1998 and the aftermath of the September 11, 2001 terrorist attacks.

### **Broadening the Investor Base**

Before the development of the secondary mortgage market, the uncertain nature of mortgage prepayments and defaults largely limited mortgage investment to thrifts, restricting the supply of mortgage funds. Today, with the success of the mortgage-backed security market, other investors have expanded their mortgage investments. In 1970, single-family residential mortgage debt outstanding totaled about \$0.4 trillion, more than half of which was held by thrifts. Today, an estimated \$6.5 trillion in single-family residential mortgages and mortgage-backed securities are held by a wide range of institutions, including thrifts, commercial banks, life insurance companies and pension

funds, as shown in Exhibit 5.<sup>15</sup> Furthermore, foreign investors held approximately 9 percent of mortgage debt, primarily in the form of Freddie Mac and Fannie Mae securities, at year-end 2001 (the most recently available data).

**Exhibit 5**  
**Sources of Mortgage Credit Have Broadened Since 1970**



Source: Federal Reserve System, *Inside MBS & ABS*, May 2002

The broad set of investors in mortgages and mortgage-backed securities is a testament to the liquidity the secondary market helps to create. Liquidity – the ability to sell an asset very quickly with little or no price concession – is a critical attribute for a security to have to assure an active market with many investors looking to hold the asset. Based on mortgage-backed security trading volumes, it is clear that the secondary market enhances the liquidity of mortgage investments. The trading volume of the total of Freddie Mac, Fannie Mae and Ginnie Mae mortgage pass-through securities passed \$40 trillion in 2002, or a record \$160 billion per business day.

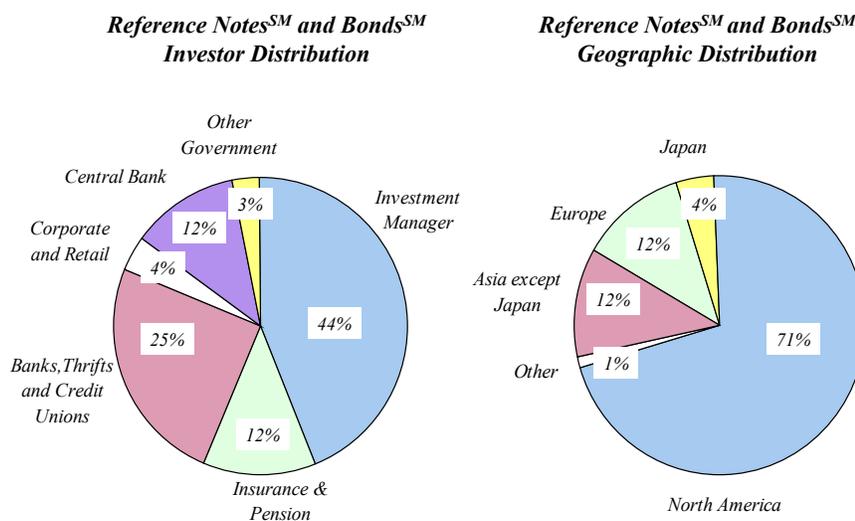
Likewise, as illustrated in Exhibit 6, the broad investor base for our debt reflects Freddie Mac's success in attracting capital from around the world to finance America's housing. A highly diversified investor base benefits America's families by making the housing finance system more resilient. When market or regulatory changes reduce the role of one investor group (such as thrift institutions) or dramatically increase the amount of credit needed by homebuyers (such as during the record refinancing boom of 2001-2002), the

<sup>15</sup> The distributions are calculated from estimates of mortgage debt outstanding prepared by the Board of Governors of the Federal Reserve System (exclusive of mortgage-backed securities) and estimates of mortgage-backed securities holdings published in *Inside MBS & ABS* (May 2002).

diverse investor base provided by Freddie Mac helps ensure that a steady flow of funds remains available to support loan demand.

The high quality and liquidity of Freddie Mac's mortgage-backed and debt securities are key factors in enabling us to raise funds in the global markets to supply funds to primary market lenders. By increasing the global appeal of our securities, Freddie Mac helps stabilize the secondary market for residential mortgages and reduces the cost of mortgage credit.

**Exhibit 6**  
**The Investor Base for Freddie Mac's Debt Securities Is Diverse**



Source: Freddie Mac

### Reducing Funding Costs Through Technology

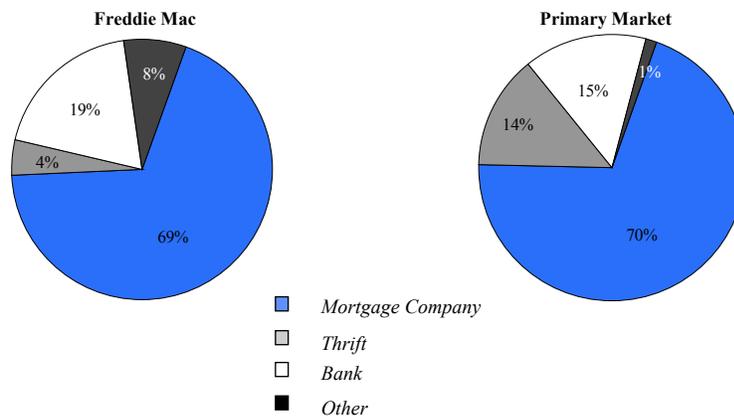
An important part of integrating global capital markets with the mortgage markets is the ability to provide investors convenient mechanisms for buying and selling the debt securities that finance housing. To help meet investors' needs, Freddie Mac has pioneered the use of technology to issue and trade debt securities. In recent years, Freddie Mac introduced internet-based debt auctions, debt repurchase operations, and debt exchanges. These mechanisms benefit investors by providing more uniform pricing, greater transparency and faster price discovery – all of which makes Freddie Mac debt more attractive to investors and reduces the cost of funding mortgages.

### Purchasing Mortgages from Vast Lender Network

Freddie Mac purchases mortgages from a nationwide network of lenders, benefiting borrowers throughout the nation. Spanning the U.S. and its territories, this network includes approximately 3,000 institutions. As Exhibit 7 shows, Freddie Mac purchases loans from all major lender types. Some of these firms sell loans to us regularly, while others sell to us only occasionally. Of the total seller network, about 1,350 lenders sold loans to us in 2002. Minority- or women-owned lenders comprised 2.7 percent of the lenders in Freddie Mac's network at the end of 2002. The \$5.5 billion in loans that Freddie Mac bought from these lenders financed housing for 45,000 families.

**Exhibit 7**  
**Freddie Mac Purchases Loans from All Major Lender Types**

*2002 Freddie Mac Purchases and 2001 Primary Market Originations Sold by Institution Type*

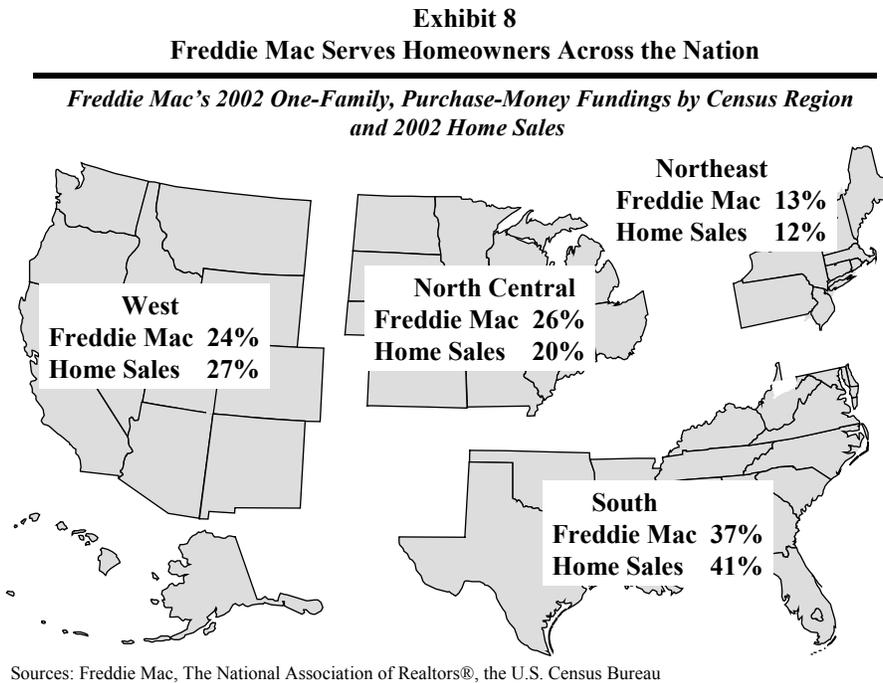


Sources: Freddie Mac and 2001 Data Reported Under HMDA

To ensure that lenders can fully benefit from the secondary market, we provide training and related materials to help our customers conduct secondary market sales and benefit from the innovations that Freddie Mac has introduced. We create mutually beneficial relationships that enhance our lender partners' abilities to meet the specific demands of their markets.

## Serving Families Nationwide

Freddie Mac's nationwide network of lenders enables us to serve families from all over the country. As shown in Exhibit 8, the mortgages Freddie Mac bought in 2002 financed home purchases nationwide in about the same proportion as home sales.<sup>16</sup>



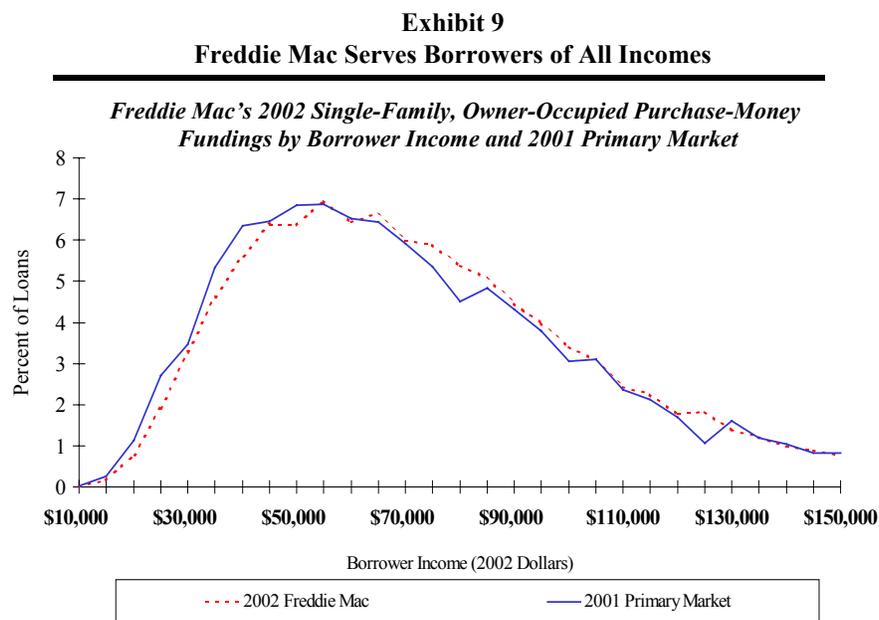
Freddie Mac's relatively lower share of purchases from the West census region resulted from high home prices in California, where a much higher than average portion of mortgages exceed the maximum dollar limit Freddie Mac is permitted to purchase. Freddie Mac's relatively lower share in the South census region primarily reflects the higher market shares of mortgages insured by the Federal Housing Administration (FHA), which usually are securitized as Ginnie Mae securities instead of being sold to Freddie Mac.

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<sup>16</sup> Total one-family home purchase sales are the sum of sales of previously occupied houses and condominiums, published by the National Association of Realtors® and sales of newly built homes, reported by the U.S. Census Bureau.

### Serving Families Across the Income Distribution

Freddie Mac's mortgage fundings serve families from across the income spectrum. As shown in Exhibit 9, the income distribution of families whose home purchases Freddie Mac financed closely matched the income distribution of all primary market home purchase loans, as reported to the Federal Reserve under the Home Mortgage Disclosure Act (HMDA).<sup>17</sup> Household incomes for families whose homes were financed through Freddie Mac's purchases in 2002 generally ranged between \$10,000 and \$150,000. One-half of the families whose homes we financed earned less than \$63,000.



Sources: Freddie Mac and Freddie Mac estimates based on 2001 Data Reported Under HMDA

In 2002, Freddie Mac purchased mortgages from a wide range of neighborhoods. Nearly 500,000 of Freddie Mac's mortgage purchases financed homes for borrowers living in low- or very-low-income neighborhoods. Another 2.3 million of our purchases financed homes in middle-income neighborhoods.<sup>18</sup> The geographic distribution of Freddie Mac's purchases largely matches originations of prime mortgages.

<sup>17</sup> For Exhibit 9, primary market data are taken from the HMDA public-use data for 2001, the most recent data available. The data reflect conventional originations with loan principal at or below the one-family conforming loan limit and exclude loans made by lenders operating primarily in the subprime and manufactured housing markets. The market data are adjusted to 2002 dollars based upon the Consumer Price Index.

<sup>18</sup> Very low- and low-income neighborhoods are census tracts with median incomes less than 80 percent of the local area median income. Middle-income neighborhoods are census tracts with median incomes ranging from 80 percent to 120 percent of the local area median income.

## **Expanding Homeownership Opportunities**

Along with purchasing mortgages, Freddie Mac supports a nationwide secondary market and promotes access to mortgage credit throughout the nation by lowering the cost, improving the accuracy and increasing the speed of credit underwriting. These efforts are key elements of our success in expanding homeownership opportunities for more of America's families.

## **Pioneering Advances in Credit Underwriting**

Freddie Mac pioneered the use and widespread adoption of automated underwriting technology to expand the mortgage market. We introduced Loan Prospector<sup>®</sup>, our state-of-the-art automated underwriting service, in 1995, and have continually refined it ever since. Loan Prospector is built on an analysis of which loan, borrower and property characteristics, separately and in combination, affect mortgage performance. As described in Chapter 4, Loan Prospector has transformed the way mortgages are originated. With Loan Prospector, approving mortgages is faster, costs are lower and the application of objective underwriting criteria is more consistent. Additionally, by more accurately measuring risk, Loan Prospector extends the benefits of the mortgage finance system to more borrowers, including those with slightly blemished credit profiles or limited savings.

Our efforts have helped bring about broad changes in industry underwriting practices that benefit borrowers. A study commissioned by HUD concluded that underwriting innovations from Freddie Mac and Fannie Mae have "fundamentally changed the lending industry's view on what borrowers and properties are bankable and what financial terms are prudent."<sup>19</sup> Freddie Mac's continuing efforts to re-examine our business practices to eliminate constraints to mortgage lending help us find new ways to deliver low-cost financing to America's families.

Approximately two-thirds of all newly originated mortgages that Freddie Mac purchases are processed through Loan Prospector. In a typical transaction, a lender or broker enters credit, loan and property information into a computer or website linked to Loan Prospector. The automated underwriting service evaluates the data, and within seconds returns a Freddie Mac purchase decision to the lender or broker. The lender could then approve the loan.

Use of Freddie Mac's automated underwriting service surged in 2002. In 2002 alone, lenders and brokers used Loan Prospector to evaluate more than 8 million loan applications, 12 percent more than in 2001. Since its introduction, Loan Prospector has evaluated more than 25 million mortgage applications.

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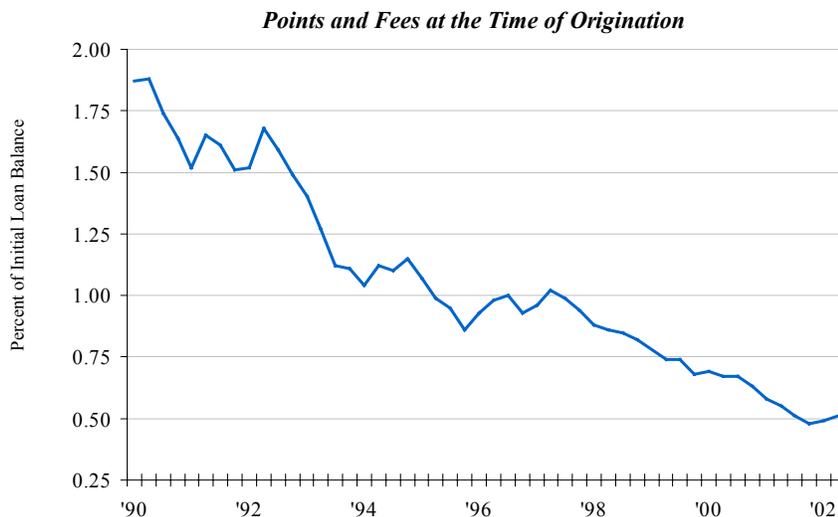
<sup>19</sup> *Successful Mortgage Lending Strategies for the Underserved*, David Listokin and Elvin K. Wyly, U.S. Department of Housing and Urban Development, 1998, Volume 1, p. 106.

During 2002, Freddie Mac implemented enhancements that enabled lenders to approve more loans while adhering to sound risk management principles. Loan Prospector's accuracy allowed us to make lower cost prime mortgages available to some borrowers who may have previously qualified only for subprime loans.

In addition, we enhanced Loan Prospector to allow automatic data transfer and make available an online fulfillment management service that allows mortgage lenders and brokers to order appraisals, flood zone determinations and title products from third-party vendors.

Innovations in the originations process, including automated underwriting, appear to have reduced origination costs substantially. As illustrated in Exhibit 10, between 1990 and 2002, mortgage transaction costs have fallen by more than 70 percent from 1.87 points to just 0.50 points – a decline of \$1,370 per \$100,000 borrowed. These savings can enable more families to achieve the dream of homeownership.

**Exhibit 10**  
**Mortgage Transaction Costs Have Declined Since 1990**



Source: Federal Housing Finance Board

### **Lower Mortgage Rates**

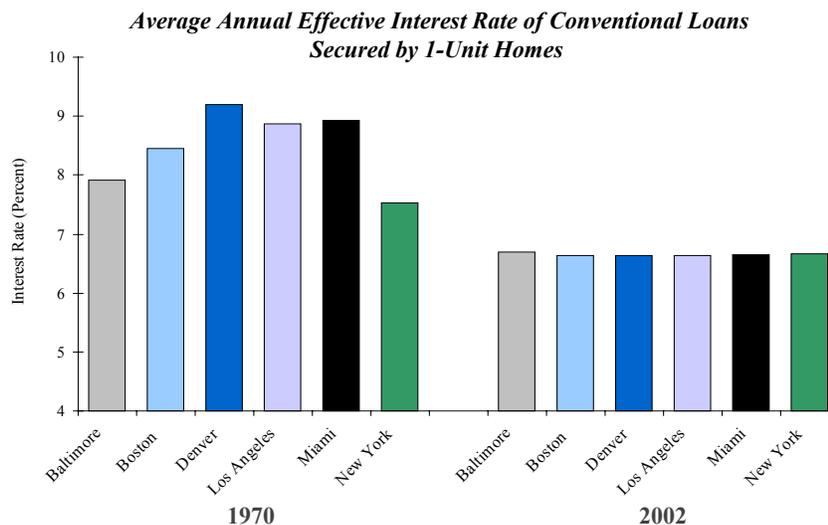
Borrowers obtaining mortgages in the conforming segment of the residential market that Freddie Mac serves pay less for mortgage credit. Research confirms that over the past decade, mortgage rates on prime conforming, fixed-rate, single-family loans ranged from one-quarter to one-half of a percentage point less than rates on jumbo loans. Lower mortgage rates produced by the activities of the Freddie Mac and the secondary market

have been estimated to save America's homeowners between \$8.4 billion and \$23.5 billion annually in interest costs.<sup>20</sup>

### Geographically Stable Rates

As a result of the efforts of Freddie Mac and the secondary market, mortgage credit is readily available across the country at about the same interest rate, regardless of whether a local housing market is in a peak or trough. This was not the case prior to the development of a secondary market for conventional mortgages. As shown in Exhibit 11, conventional mortgage rates varied by 1.7 percentage points across the country in 1970, and varied by only 0.07 percentage points in 2002. For a \$100,000 30-year loan originated in 1970, a family in Denver would have paid \$42,000 more in interest over the term of the loan than a family in New York; in 2002 these costs were virtually identical in both locations.<sup>21</sup>

**Exhibit 11**  
**Regional Differences in Mortgage Rates Have**  
**Virtually Been Eliminated**



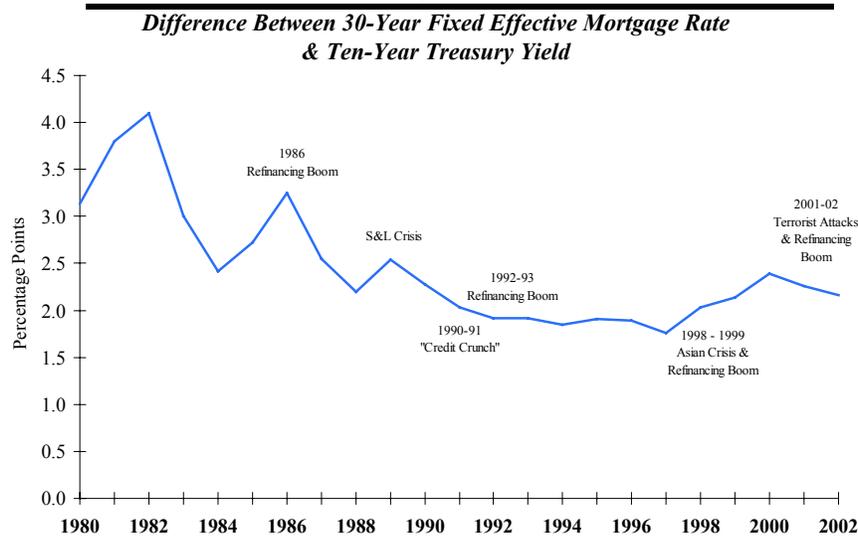
Sources: "Determinants of Regional Mortgage Rates Under Varying Economic Conditions," *Quarterly Review of Economics and Business*, Spring 1982 and HSH Associates

<sup>20</sup> J. Pearce and J. Miller, *Freddie Mac and Fannie Mae: Their Funding Advantage and Benefits to Consumers*, January 2001.

<sup>21</sup> Mortgage rates in 1970 are from Stephen T. Zabrenski, James R. Barth and Michael L. Marlow, "Determinants of Regional Mortgage Rates under Varying Economic Conditions," *Quarterly Review of Economics and Business*, Spring 1982, p. 82. Conforming mortgage interest rates in 2002 are from HSH Associates, Butler, NJ.

In addition to smoothing regional fluctuations in mortgage rates, Freddie Mac and the secondary market help to keep mortgage rates relatively stable across different economic environments. This is illustrated by comparing the government's and the homebuyer's cost of funds over time. Exhibit 12 shows that in the 1980s, mortgage rates typically ranged between 2.5 and 3.5 percentage points above the ten-year Treasury rate, though the difference was much higher during the 1981-82 recession and the refinance boom in 1986.<sup>22</sup> Since 1988, however, the difference between conforming mortgage rates and Treasury yields has remained low and relatively stable, even in the face of significant disruptions in other parts of the financial system. Through the S&L crisis in the late 1980s, the unprecedented refinance waves of 1993, 1998 and 2001-2002, and the financial market turmoil of 1998 and the fall of 2001, spreads generally remained under 2.5 percentage points.<sup>23</sup> Any of these periods of stress would have made mortgage funds more expensive and difficult to obtain in the absence of Freddie Mac and the secondary market.

**Exhibit 12**  
**Home Mortgage Rates Have Remained Relatively**  
**Low Under a Variety of Market Conditions**



Sources: Freddie Mac Primary Mortgage Market Survey (PMMS), Federal Reserve Board

<sup>22</sup> The yield spreads are the differences between the average effective 30-year fixed-rate mortgage rate from Freddie Mac's Primary Mortgage Market Survey and the average 10-year constant-maturity Treasury yield from the Board of Governors of the Federal Reserve System for each year.

<sup>23</sup> The uptick in mortgage rate spreads to Treasuries starting in 1998 is partly a consequence of reduced government borrowing, manifested most dramatically in the elimination of the 30-year Treasury. Indeed, the slight rise in spreads to Treasury securities in recent years has occurred across a wide range of debt, for example, AAA industrial bonds.

### U.S. Market Offers Borrowers More Attractive Loan Terms

As a result of Freddie Mac and the secondary market, America's homebuyers can choose among a wide range of mortgage products, including long-term, fixed-rate, prepayable mortgages – the mortgage of choice for many families. Such loans are less readily available in the jumbo market in the United States<sup>24</sup> and, as shown in Exhibit 13, are largely absent in many other countries. For example, British homebuyers can obtain mortgages with low down payments and prepayment options, but long-term, fixed-rate mortgages are uncommon. In France, 15 years is the typical term for fixed-rate mortgages, and prepayment typically requires the borrower to pay a fee of 1 to 3 percent of the remaining loan balance. The larger choice of mortgage products and terms in the U.S. gives America's families much greater flexibility in financing their homes.

**Exhibit 13**  
**U.S. Market Offers Families More Attractive Loan Terms**

Mortgage Product	United States	United Kingdom	Germany	Canada	France	Japan
Fixed-rate mortgage common	Yes	No	Yes	No	Yes	Yes
Typical loan term	30 years	2-5 years*	5-10 years*	5 years*	15 years	3-10 years*
Prepayable without penalty	Yes	Yes	No	No	No	No**
Typical down payment	20%***	30%	20-40%	25%	20%	30-45%
* Typical period until first rate adjustment						
** Nominal prepayment fee charged						
*** Lower down payment loans widely available						

Sources: Freddie Mac, European Mortgage Federation, Federal Housing Finance Board, Homeownership Alliance

### Freddie Mac Supports the Housing Market and the Economy

Freddie Mac's diverse investor base, nationwide network of lenders and commitment to expanding homeownership opportunities helps to keep low-cost mortgage funds flowing to America's homeowners during both economic booms and recessions and under a variety of market conditions. The ongoing vitality of housing and mortgage markets has been a key contributor to growth of the broader national economy during the past several years. Indeed, according to recent estimates, nearly one-third of the nation's economic

<sup>24</sup> According to the Federal Housing Finance Board's Mortgage Interest Rate Survey, in 2002, adjustable-rate mortgages comprised about 52 percent of jumbo loans but only 14 percent of conforming loans.

growth since 2000 is directly attributable to the housing and mortgage sector.<sup>25</sup> The recession of 2001-2002 would have been substantially more severe and the recovery much weaker if not for the support provided by these markets. Freddie Mac played an integral role supporting these sectors.

Freddie Mac's vital role was illustrated most recently by our ability to provide a steady supply of low-cost home mortgage credit during the extended single-family refinance boom of the last two years. Thanks in part to Freddie Mac, the housing sector remained strong throughout 2001 and 2002. Indeed, as the year ended and economic growth slowed, the buoyant housing market helped to keep the economy from slipping back into recession. Federal Reserve Board Chairman Alan Greenspan noted our important role, stating:

“Especially important in the United States have been the flexibility and the size of the secondary mortgage market. Since early 2000, this market has facilitated the large debt-financed extraction of home equity that, in turn, has been so critical in supporting consumer outlays in the United States throughout the recent period of stress.”<sup>26</sup>

During the 2002 refinancing wave, families with conforming mortgages converted \$160 billion in home equity into cash. A study by the Federal Reserve Board found that about one-half of the money from cash-out refinancing went toward consumer spending and home improvements, adding directly to economic growth. The use of the remaining funds was approximately split between the repayment of other debts and various financial or business investments.<sup>27</sup> Based on this study, we estimate that the expenditure of funds from cash-out refinancing accounted for roughly one-fifth of the \$360 billion increase in nominal gross domestic product during 2002.

Even more important to the economy, noted Chairman Greenspan in a March 4, 2003 speech, was an additional \$350 billion in home equity that homeowners received upon the sale of their homes. Together with cashout refinancings and second lien home equity borrowing, the Federal Reserve estimates that households extracted \$700 billion in home equity during 2002. The equity extracted by home sellers in particular “[p]rovided an even greater support to the economy than cashouts.... It is highly likely ... that home sellers, after setting aside a down payment for the family's next home, expended a

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<sup>25</sup> “The Economic Contribution of the Mortgage Refinancing Boom,” Economy.com, December 2002, p 2. Available at [http://www.homeownershipalliance.org/media/press/zandi\\_december2002\\_updated.pdf](http://www.homeownershipalliance.org/media/press/zandi_december2002_updated.pdf).

<sup>26</sup> Speech before the Council on Foreign Relations, Washington, D.C. November 19, 2002.

<sup>27</sup> “Mortgage Refinancing in 2001 and Early 2002,” Glenn Canner, Karen Dynan and Wayne Passmore, *Federal Reserve Bulletin*, December (2002).

considerable part of their home equity extraction on goods and services.”<sup>28</sup> Had it been more difficult or costly for homeowners to extract their home equity, the economy would have been much weaker.

### **Freddie Mac Cushions Economic Volatility**

Freddie Mac supports housing and the economy in a wide variety of economic conditions, and during periods of economic stress and volatility we play a key role in providing liquidity. This role was dramatically illustrated in the wake of the September 11 terrorist attacks. Despite the severe disruption of financial markets, Freddie Mac continuously purchased mortgage loans and securities, maintaining a stable supply of low-cost mortgage funds. As *The Wall Street Journal Europe* reported, “Mortgage activity did grind to a near-standstill for several days last week, in part because lenders were unclear how to price loans due to the temporary closure of the bond market. But the market was bolstered significantly, lenders said, by the presence of Fannie Mae and Freddie Mac, which buy mortgages from lenders in order to allow banks to make more loans.” By maintaining our mortgage purchase and financing activities in the aftermath of September 11, Freddie Mac inspired strength and confidence in the mortgage and capital markets and provided an important foundation for economic recovery.

During the fall of 1998, global financial markets were thrown into turmoil by economic problems in Asian and Latin American economies and the August 1998 default of the Russian government on its bonds. Although conditions in the U.S. economy were sound, the problems abroad led to a liquidity crunch in several domestic market sectors, including commercial and subprime residential mortgages, as investors fled most investments and poured funds into a few favored areas, such as U.S. Treasury securities. Because demand for Freddie Mac's debt securities remained high, Freddie Mac was able to keep funds flowing into the residential mortgage market by purchasing mortgages and mortgage securities for our retained portfolio. In so doing, we fulfilled our charter purposes by maintaining high levels of liquidity and stability in the residential market. Our activities ensured continued borrower access to low-cost mortgage credit and made possible a then-record volume of home sales and refinancings. As one study concluded, “for consumers in the home loan market during the financial crisis of 1998, mortgage credit remained available *and* affordable” because of the presence of Freddie Mac.<sup>29</sup>

Freddie Mac's willingness to fund mortgages in times of crisis not only supported the housing and mortgage markets – it supported the nation's economy. Investors knew that

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<sup>28</sup> Remarks by Federal Reserve Board Chairman Alan Greenspan at the annual convention of the Independent Community Bankers of America, March 4, 2003.

<sup>29</sup> “An Economic Analysis of Freddie Mac's and Fannie Mae's Contribution to Liquidity in the Residential Mortgage-Backed Securities Market During the Credit Crunch of 1998,” Capital Economics, May 2000 (emphasis in original).

Freddie Mac offered high quality securities, which in turn allowed Freddie Mac to continue to purchase mortgages. This gave financial markets a benchmark for pricing, which is a cornerstone of well-functioning financial markets.

## **Conclusion**

In summary, Freddie Mac and the secondary market are the keys to a robust housing finance system. By developing products and innovations that attract investors to housing, by using the most efficient mechanisms to ensure a steady supply of low-cost mortgage credit and by developing a diverse lender network, Freddie Mac continues to provide extraordinary service to America's families.

## **Chapter 2: Opening Doors to Affordable Homeownership**

The economic environment in 2002 enabled Freddie Mac to serve record numbers of homebuyers of all incomes and racial and ethnic backgrounds. At the same time, it made achieving the housing goals more challenging. Once again Freddie Mac demonstrated our unwavering commitment to expand the reach of the secondary market to more borrowers and neighborhoods.

### **The Record-Breaking Single-Family Market in 2002 and Its Impact on Freddie Mac's Purchases**

The single-family market during 2002 set an all-time record in mortgage origination volume. Interest rates for 30-year, conforming, fixed rate home mortgages averaged 6.54 percent (with 0.6 points) for the year as a whole, down 43 basis points (and 0.3 points) from the previous year. Rates hit a low of 5.93 percent (with 0.6 points) for prime, conforming loans for the week of December 26. Refinancing activity rose to 75 percent of total lending during the fall months and averaged 59 percent for the year, the highest annual refinance share on record.

Low mortgage rates and strong underlying demand for housing resulted in record home sales during 2002. According to the U.S. Census Bureau, sales of newly built homes during 2002 totaled 976,000 units, 68,000 more than in 2001. Existing home sales, including condominiums and cooperatives, reached 6.4 million units during 2002, as reported by the National Association of Realtors®. Together, home sales for 2002 totaled 7.4 million, an increase of 6 percent from 2001.

As illustrated in Exhibit 14, single-family mortgage originations reached an estimated \$2.5 trillion in 2002, up from \$2.1 trillion in 2001. This increase was attributable to higher refinance activity and home purchase originations in 2002 over 2001, as well as strong house price appreciation. The increase in total home sales, house prices and refinancing activity during 2002 led to a substantial increase of single-family mortgage debt growth. Single-family mortgage debt outstanding is estimated to have totaled \$6.5 trillion at the end of 2002, up 11.3 percent from 2001.

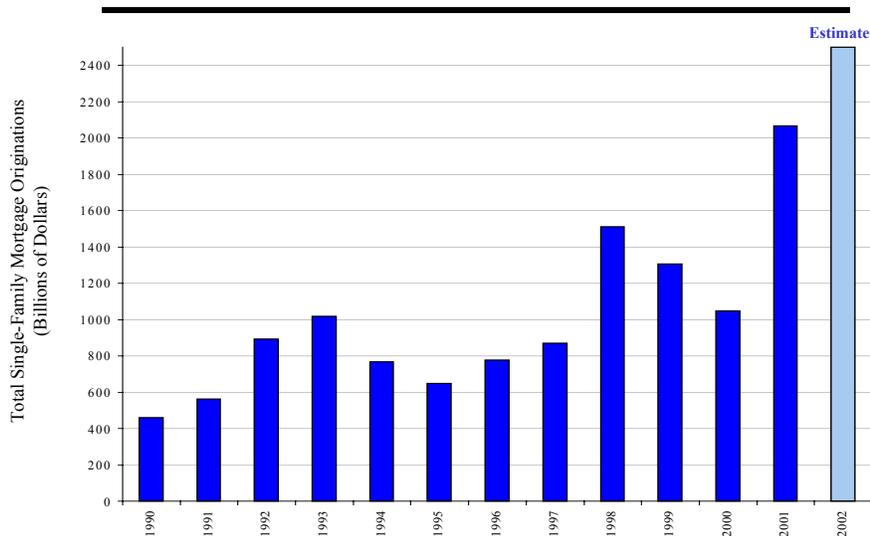
While the economy remained weak throughout 2002, and unemployment rose to an eight-year high, home mortgage defaults rose only slightly. Nationally, the percentage of prime conventional loans that were non-performing (90 days or more past due or in foreclosure) rose from 0.73 percent in the third quarter of 2001 to 0.79 percent at the end of the third quarter of 2002.<sup>30</sup> Over this same period, Freddie Mac's non-performing loan rate remained unchanged at 0.38. This strong credit performance reflects rising home prices, which increased borrower equity, as well as widespread use of automated

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<sup>30</sup> Delinquency rates obtained from the *National Delinquency Survey*, conducted by the Mortgage Bankers Association of America, for the third quarter of 2002.

underwriting tools that more accurately assess credit risk and automated servicing tools that help mitigate losses.

**Exhibit 14**  
**Mortgage Originations Have Been Quite Strong**



Sources: Freddie Mac, HUD

Low mortgage rates and a strong housing market created very high demand for mortgage credit. Freddie Mac met this demand by purchasing a record \$578 billion of single-family mortgages eligible for reporting. These purchases financed single-family homes for 4.2 million families, including 576,000 minority families and 286,000 families who rent. Our purchases of home purchase and refinance mortgages each set all-time records. \$164 billion of our 2002 purchases were for families buying homes. Mortgages to 217,000 first-time homebuyers accounted for 26 percent of the home purchase loans we bought last year. By financing about one out of six first-time homebuyer mortgages originated last year, Freddie Mac helped boost the national homeownership rate to an all-time high of 67.9 percent. Freddie Mac also purchased \$414 billion in refinance mortgages, enabling families to reduce housing costs, consolidate higher cost debt and increase other spending.

Market conditions in 2002 made Freddie Mac's achievement of meeting all of the housing goals in 2002 particularly noteworthy. Record low interest rates attracted large numbers of middle- and higher-income borrowers to refinance their mortgages. As a consequence, low- and moderate-income borrowers comprised a much smaller share of the market than in previous years. While Freddie Mac's purchases of mortgages meeting the goals increased substantially in 2002, meeting the goals proved challenging because overall purchases also increased dramatically. Freddie Mac's achievement of the goals during such a year underscores our commitment to extending the benefits of the

secondary market to very-low-, low- and moderate-income families and families in underserved areas.

## **Expanding Minority Homeownership**

The nation's homeownership rate has reached a record high of 67.9 percent, with more families of all racial and ethnic backgrounds owning homes than ever before. However, fewer than half of America's minority households have achieved the dream of homeownership. As a result, President Bush called for "broader homeownership, especially among minorities" in his State of the Union address on January 29, 2002. On June 17, 2002, the President called on the housing industry to make homeownership a reality for 5.5 million additional minority families by the end of this decade.

### ***Catch the Dream***

Freddie Mac responded to the President's challenge by launching *Catch the Dream*. Building on our strong record of expanding access to the mortgage market during the past 30 years, *Catch the Dream* consists of 25 high-impact initiatives to accelerate the growth in minority homeownership. Our initiatives range from best-in-class homebuyer outreach and education to new technologies and mortgage products designed to put families into homes they can afford and keep. Freddie Mac will implement these initiatives as part of a team effort with mortgage lenders, nonprofit housing and community organizations, and other industry leaders. As part of *Catch the Dream*, Freddie Mac is committed to providing \$400 billion in mortgage financing for minority families by the end of this decade.

*Catch the Dream's* 25 initiatives address all phases of the Homeownership Lifecycle, resulting in a systematic approach to dismantling barriers. It begins with creating greater awareness of the possibilities for homeownership and leads to homeowners' successful accumulation of home equity. The cycle is self-reinforcing: A portion of the wealth built up through one generation of homeowners can be passed to the next, so that the cycle can begin again. The five phases of the Homeownership Lifecycle, and the corresponding initiatives of *Catch the Dream*, are as follows:

**Catching the Dream** seeks to overcome the many intangible barriers to homeownership, including misinformation about the home-buying process, mistrust, fear of rejection or disclosure of financial information. *The goal of this phase is to foster the belief that homeownership is desirable and within reach.*

1	Dispel the Myths	Homeownership information ad campaign in select areas involving leaders within the minority community
2	Toolkits and Kiosks	New, multilingual marketing campaign using unconventional outreach techniques, such as homeownership kiosks
3	Trusted Intermediaries	Engage national nonprofit minority organizations and community-based nonprofits in the provision of homebuyer information
4	Faith-Based Solutions	Harness new and existing faith-based strategies to put more families on the path to homeownership
5	CreditSmart <sup>SM</sup> Español	Spanish-language version of Freddie Mac's highly acclaimed CreditSmart financial literacy campaign

**Finding Affordable Homes** recognizes that many families become discouraged because they cannot find homes they can afford in areas in which they want to live. *The goal of this phase is to ensure that consumers have greater choice of affordable, attractive homes and that incentives are in place to encourage investment in homeownership.*

6	Breaking New Ground	Promote quality construction of new, affordable single-family housing, particularly starter homes for first-time buyers
7	Community Hope	"Best practices" campaign to rejuvenate urban communities, including promotion of place-based employer-assisted housing and reclamation of deteriorated and abandoned property
8	New Urban Initiatives	Encourage investment in urban neighborhoods, including exploring the viability of equity assurance products to protect home values in economically weak areas
9	Military Housing	Collaborative effort with the Department of Defense to address the housing and financial literacy needs of military personnel
10	Section 8 to Homeownership	New broad-based approaches for using Section 8 rental assistance for homeownership developed in conjunction with HUD and national nonprofit intermediaries

**Equipping the Industry** recognizes that mortgage and real estate professionals often lack the technology and other tools to help consumers overcome credit, down payment and other barriers to homeownership. This phase also focuses on strengthening the nation's network of housing counseling organizations. *The goal of this phase is to assist the industry in meeting the financing needs of the next generation of homebuyers.*

11	Banking the Unbanked	Explore new approaches to attract unbanked consumers into the financial mainstream, in conjunction with lenders, the Treasury Department and nonprofit service providers
12	Tools and Technology	Provide state-of-the-art technology to emerging "first contact" agents, e.g., community-based nonprofits and faith-based institutions, as well as mortgage and real estate professionals
13	Cross-Border Credit	Create international initiative to enhance the acceptability of foreign national credit information for US mortgage underwriting
14	Housing and Mortgage Market Diversity	Industrywide internships and other efforts to attract minority men and women entering the workforce to careers in mortgage banking, real estate, homebuilding, etc.
15	Multilingual Documents	State-focused effort to translate key mortgage documents and educational materials into other languages

**Getting the Loan** focuses on efforts to continually improve mortgage underwriting and expand access to financing. *The goal of this phase is to ensure that consumers obtain the lowest-cost mortgage financing available.*

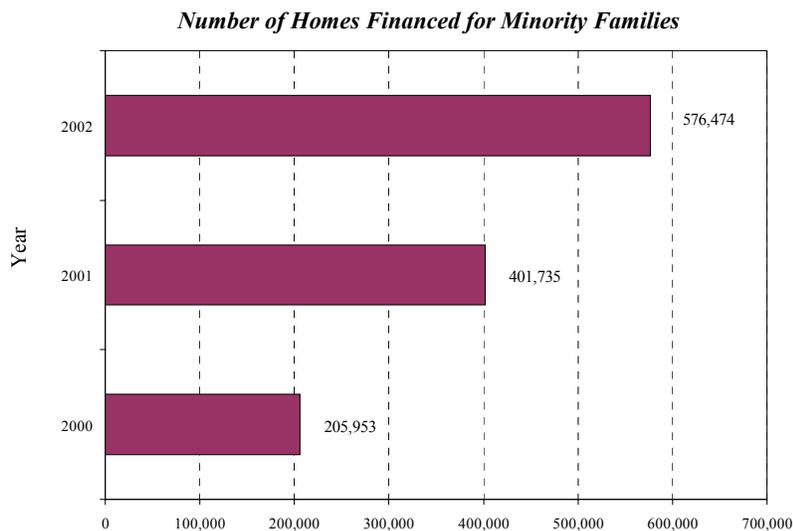
16	Automating the Use of Nontraditional Credit	Develop viable means for automated underwriting systems to evaluate sources of nontraditional credit
17	Solutions for Blemished Credit	Increase access to affordable mortgage products for borrowers with weak or blemished credit
18	Financing for Islamic Families	Create standard home-finance product to address religious objections to payment of interest
19	Down Payment Assistance	Solutions for borrowers unable to accumulate funds for down payment
20	Expanded Approval Rates	Higher mortgage approval rates means greater homeownership opportunities
21	Innovative Risk Sharing	Involve lenders and nontraditional intermediaries in the creation of innovative risk-sharing lending arrangements

**Building Wealth for the Future** recognizes that it is not enough simply to put people in homes - they need to succeed as homeowners in order to build wealth for retirement or other needs. *The goal of this phase is to support families in making timely mortgage repayment and to help them avoid predatory lending scams.*

22	Don't Borrow Trouble	Expanded effort to take award-winning Don't Borrow Trouble consumer awareness program to more communities nationwide
23	Moving Subprime Borrowers Into Prime	Pilot program to provide automated underwriting tools to select group of subprime lenders to identify applicants who qualify for conventional conforming mortgages
24	Ban on 5-Year Prepayment Penalty in Subprime	Freddie Mac's ban on purchasing subprime mortgages with prepayment penalties that exceed three years
25	High-Touch Servicing	Proactive, focused servicing initiatives designed to identify, contact and assist borrowers in Freddie Mac's affordable mortgage products

*Catch the Dream* builds upon Freddie Mac's ongoing efforts to reduce costs and make mortgage money available for minority families. Exhibit 15 shows a steady increase in Freddie Mac's funding of mortgages for minority families since 2002.

**Exhibit 15**  
**Freddie Mac Has Substantially Increased Purchases of Mortgages**  
**Financing Homes for Minority Families Since 2000**



Source: Freddie Mac

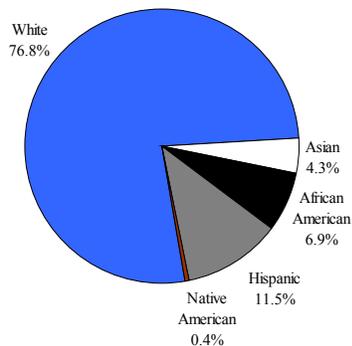
In 2002, our single-family owner-occupied mortgage purchases financed homes for 576,000 minority families, including mortgages for nearly 100,000 African-American and 190,000 Hispanic families.<sup>31</sup> Freddie Mac's purchases of mortgages to minority families comprised 17.3 percent of our single-family, owner-occupied mortgage purchases in 2002. Our 2002 purchases of mortgages for minority families were more than double our purchases of such loans during the previous large refinance boom in 1998.

Freddie Mac's mortgage purchases for minority families were representative of the origination of mortgages for minority families in the primary mortgage market. One way to illustrate this is to compare our purchases to the share of home-purchase loans with private mortgage insurance.<sup>32</sup> As shown in Exhibit 16, Freddie Mac's fundings of low down payment mortgages for minority families closely matched the share of insured loans in 2001 (the most recent year for which market data are available). The respective shares for African American and Hispanic borrowers were 18.4 percent for Freddie Mac and 17.8 percent for all insured loans. Including Asian and Native American borrowers, the minority shares were 23.2 percent for Freddie Mac and 22.0 percent for the insured market.

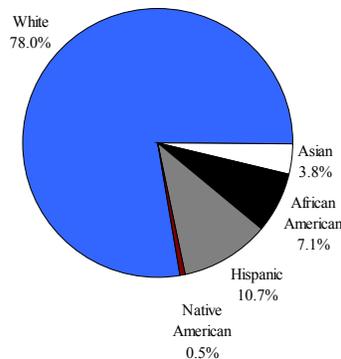
**Exhibit 16**  
**Freddie Mac Purchases Closely Match the Primary Market**

*Conventional, conforming purchase-money mortgages in metropolitan areas*  
*Borrower race and ethnicity*

**2001 Freddie Mac Purchases  
of Loans with LTV Above 80%**



**2001 MICA Insured**



Sources: Freddie Mac, Federal Financial Institutions Examination Council

<sup>31</sup> These figures include families in which one borrower is minority and the other borrower is either white or did not disclose race/ethnicity.

<sup>32</sup> Based on metropolitan area data provided to the Federal Financial Institutions Examination Council by the Mortgage Insurance Companies of America.

The diversity of family composition in America is also reflected in Freddie Mac's loan purchases. In 2002, 63 percent of the loans we purchased were made to couples, 21 percent were made to single males and 16 percent were made to single females. HMDA data for 2001 (the most recent year available) indicate a similar percentage distribution in the primary market.

We are proud of our achievements in serving the diversity of America's families. We know more remains to be done. Freddie Mac is committed to increasing minority homeownership rates across the country by reducing mortgage costs, using technology that accurately assesses loan performance, and developing national and local alliances and initiatives. We use a multi-faceted approach that includes working with minority-owned lenders, creating targeted loan products, reaching out to minority-based organizations and designing homebuyer education that enables families to achieve and maintain good credit. Specific initiatives Freddie Mac used in 2002 are discussed in Appendix 2.

### **Promoting Responsible Lending Practices**

During 2002, Freddie Mac continued to take a leading role in promoting responsible lending practices by implementing a vigorous set of measures to combat abusive practices. These measures included corporate policies, targeted mortgage products and an educational campaign in communities across the country.

### **Freddie Mac's Anti-Predatory Lending Policies**

*Prepayment Penalties* – Since 2000, Freddie Mac has not purchased mortgages that impose a prepayment premium for a term of more than five years. In March 2002, Freddie Mac announced that we will no longer purchase mortgages with a prepayment premium of more than three years. Our new policy took effect on October 1, 2002. Freddie Mac is the only secondary market financial institution to adopt such a stringent policy on prepayment penalty mortgages.

*High-cost HOEPA Loans* – Freddie Mac does not purchase high-rate or high-fee loans that are covered by the Home Ownership and Equity Protection Act of 1994 (HOEPA). HOEPA sets limits on the mortgage rate and number of points, above which additional disclosure must be provided to the borrower. While such loans are legal to originate, in 2000 Freddie Mac determined that, as part of our anti-predatory lending initiative, we would not purchase them.<sup>33</sup> Freddie Mac was the first secondary market institution to adopt this policy.

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<sup>33</sup> Freddie Mac also has implemented the provisions of the Final Rule that, for purposes of determining compliance with the housing goals, prohibits the counting of certain high-cost mortgages and mortgages

*Single Premium Credit Insurance* – Freddie Mac does not purchase mortgages containing a prepaid single-premium credit life, credit disability, credit unemployment or credit property insurance policy obtained in connection with the origination of the mortgage, regardless of whether the premium is financed in the mortgage amount or paid from the borrower's funds. This prohibition does not apply to credit insurance products in which premiums are calculated, earned and paid on a monthly or other regular, periodic basis. This prohibition also does not apply to prepaid hazard, flood or mortgage insurance policies.

*Credit Reporting* – Freddie Mac requires all lenders servicing Freddie Mac loans to report monthly borrower mortgage payments to all four major credit repositories. As a result, the repositories will have on file not only information about borrowers who fail to make mortgage payments, but also information about borrowers who are making timely payments on their mortgages. This will permit borrowers to obtain lower-cost loans as their credit history improves.

*Good Business Practices* – Freddie Mac conducts onsite reviews of our customers and holds them accountable if their business practices do not meet Freddie Mac's standards. We have refused to conduct business with some of the largest participants in the subprime market segment because of concerns we have with their lending practices.

*EarlyIndicator*<sup>SM</sup> 4.0 – This tool helps servicers resolve borrower payment problems quickly and efficiently by helping delinquent borrowers avoid the accumulation of interest charges and penalties that could reduce the equity in their homes. EarlyIndicator is the first commercially available tool containing predictive collection and loss mitigation models specifically designed for subprime mortgages. More than 80 percent of mortgage servicers are currently licensed to use EarlyIndicator to improve collections and reduce losses.

### **Freddie Mac's Mortgage Products and Initiatives to Help Curb Predatory Lending**

Freddie Mac is also bringing benefits to borrowers who otherwise might fall victim to predatory lending practices by providing a wider range of mortgage products that make credit less costly and more sustainable. We are continually introducing innovative loan products aimed at giving borrowers with impaired credit greater mortgage choices and initiatives that help borrowers avoid the pitfalls of predatory lending.

These products and initiatives include:

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defined by HUD as being contrary to good lending practices or having unacceptable terms or conditions. 42 C.F.R. part 81, §81.16(b)(12).

*CreditWorks<sup>SM</sup>* – Freddie Mac's CreditWorks mortgage loan product is part of a \$100 million national initiative by Freddie Mac, the National Foundation for Credit Counseling (NFCC) and participating NFCC member agencies (many of whom operate under the name Consumer Credit Counseling Service) to expand homeownership opportunities for minority and lower-income families. This initiative helps people burdened with excessive debt and impaired credit to become eligible for a prime market rate mortgage faster than would otherwise be possible.

*Affordable Merit Rate<sup>SM</sup> Mortgage* – Freddie Mac's Affordable Merit Rate product for A-minus borrowers promotes good lending practices in the subprime market and delivers more homeownership opportunities to borrowers with slightly impaired credit. By taking advantage of efficiencies with Loan Prospector automated underwriting technology, Affordable Merit Rate permits borrowers to qualify at an initial interest rate that in many cases is lower than the usual subprime rate. Borrowers receive an additional 1 percent interest-rate reduction after they have made their mortgage payments on time for 24 consecutive months.

*Home Equity Loss Protection (HELP)* – The HELP initiative combines a flexible refinance mortgage product with special long-term education and counseling requirements. It is designed to help homeowners with impaired credit and excessive debt to obtain refinancing on affordable terms and to help homeowners avoid predatory lending practices.

*LeasePurchase Plus Initiative* – This initiative is a cooperative effort with state and local housing authorities that allows borrowers to overcome down payment costs and credit issues. This program provides down payment and closing cost assistance as well as comprehensive counseling for borrowers who have had credit issues in the past or who have not yet established a credit history. Potential borrowers can learn about homeownership, budgeting and credit while making lease payments and preparing for the future when they assume the mortgage and become a homeowner. During 2002, we entered into several new markets under this initiative and have purchased more than \$16 million in loans.

### **Don't Borrow Trouble<sup>SM</sup>**

Don't Borrow Trouble combines an extensive public education campaign with comprehensive counseling services to help homeowners avoid scams and resolve any financial difficulties they may be experiencing in an informed and prudent manner. It is the first comprehensive consumer awareness/foreclosure prevention campaign of its kind.

Don't Borrow Trouble was pioneered in Boston by Boston Mayor Thomas M. Menino and the Massachusetts Community & Banking Council. Freddie Mac has expanded the campaign nationwide. As of the end of 2002, the campaign has been launched in 30 metropolitan areas.

Messages in the advertising campaign combine a warning about scams along with an instruction to call a toll-free telephone number. Campaign materials include brochures, direct mailings, posters, transit ads and television commercials to inform the public that a reliable source of information is available to answer questions if they are considering taking out a loan or to provide assistance if they are already in a predatory lending situation.

A person who calls the toll-free number is connected to a counselor who has been trained to identify and assist in preventing or resolving predatory lending issues. Depending on the particular problem a caller faces, he or she is referred to one or more forms of assistance: a credit counseling agency for those overburdened with debt, housing counseling for those looking to purchase or refinance a home, home improvement assistance for those with urgent home repair needs, foreclosure prevention services for those facing imminent foreclosure, or legal assistance for those requiring the advice or assistance of an attorney.

*U.S. Conference Of Mayors* – Freddie Mac, in cooperation with the U.S. Conference of Mayors and the City of Boston, made Don't Borrow Trouble available to approximately 1,100 cities whose mayors are members of the U.S. Conference of Mayors. At the request of its mayor, each city receives a comprehensive toolkit containing materials to use in creating its local campaign, as well as the services of a marketing consultant who provides guidance on how to use the materials.

Under the U.S. Conference of Mayors portion of the expansion, more than 200 Don't Borrow Trouble toolkits have been mailed to members of the U.S. Conference of Mayors. About a dozen recipients have called the marketing consultant for guidance as they review the materials and consider implementing campaigns. Five cities – Columbus, Sacramento, Dallas/Ft. Worth, Macon, GA and Bloomington, IN – are implementing Don't Borrow Trouble campaigns. La Crosse, WI conducted a six-month campaign in 2002.

*Web Site* – To provide information on the campaign and additional assistance to consumers, Freddie Mac launched [www.dontborrowtrouble.com](http://www.dontborrowtrouble.com), which contains information on local campaigns, consumer tips on avoiding predatory lending, information on how to start a local campaign and additional resources.

*Forums* – Freddie Mac launched a series of Don't Borrow Trouble forums throughout the country to equip housing professionals with the tools they need to protect their communities from predatory lending practices. Forum participants learned how to detect, avoid and remedy abusive practices. Don't Borrow Trouble forums were presented in New York, Los Angeles, San Antonio and Orlando, where representatives of more than 1,000 community-based organizations gathered to learn how to combat predatory lending practices in their communities.

## **Increasing Financial Literacy**

Freddie Mac has taken a leadership role in the development of innovative outreach initiatives designed to provide consumers information on the use of credit, to make them aware of their financial options and to help them avoid borrowing pitfalls. Freddie Mac also is working diligently to provide needed resources and assistance to front-line homebuying and credit counselors.

### **CreditSmart<sup>SM</sup>**

CreditSmart is an innovative financial education curriculum that helps consumers understand, obtain and maintain good credit, thereby preparing them for homeownership and other personal financial goals. The CreditSmart curriculum is being distributed to consumers through several community-based organizations, including the National Urban League and Rainbow/PUSH's "1,000 Churches Connected" initiative. The curriculum was developed in conjunction with several Historically Black Colleges and Universities (HBCUs), which are helping administer it along with several professional real estate broker associations across the country.

Rainbow/PUSH recently recognized Freddie Mac at its sixth annual Rainbow/PUSH Wall Street Project Conference and presented Freddie Mac with an award for demonstrating vision and leadership in providing financial education and supporting the organization's mission of economic empowerment and equality for all. Through its 1,000 Churches Connected initiative, Rainbow/PUSH has organized CreditSmart classes with more than 80 churches across the nation, reaching more than 2,500 congregants. In 2003, 350 new churches will be added, benefiting an additional 12,000 congregants.

CreditSmart also is being distributed in a bilingual format (English and Spanish) as CreditSmart Español, in collaboration with seven national organizations dedicated to enhancing the well-being of the Hispanic community. These organizations are: Cuban American National Council, Hispanic Association of Colleges and Universities, League of United Latin American Citizens, National Association of Hispanic Real Estate Professionals, National Council of La Raza, National Puerto Rican Coalition and United States Hispanic Leadership Institute.

The bilingual curriculum, launched in December 2002, will help Spanish-speaking families or those with limited English proficiency understand the importance of good credit and the U.S. financial system. Since the national launch, several of our partners have begun implementing the curriculum with their constituents.

Both CreditSmart and CreditSmart Español are part of Freddie Mac's *Catch the Dream* initiative.

### **National Urban League CreditSmart/Homeownership Development Initiative**

Freddie Mac and the National Urban League launched the CreditSmart/Homeownership Development Initiative to increase homeownership among minorities by combining borrower education and flexible mortgage products. This effort launched with seven Urban League affiliates located in Birmingham, AL; Charlotte, NC; Louisville, KY; Greenville, SC; Oklahoma City, OK; Springfield, IL and Washington, DC.

The path to homeownership begins with free financial literacy workshops at the Urban League affiliates using Freddie Mac's CreditSmart curriculum. After successfully completing the CreditSmart program, those interested in taking the steps to homeownership receive financial counseling at the Urban League affiliate sites. The counseling program includes information about the entire home-buying process; including money management, wise use of credit, what to expect from lenders and realtors, affordable loan products and home maintenance responsibilities. Each affiliate caters programs to the needs of the local community by providing homebuyer education and counseling and/or developing and constructing affordable housing.

Since the initiative's launch in early 2002, 41 CreditSmart financial literacy workshops have been presented to more than 600 minority participants. Those participants are proceeding to take the next steps to achieving homeownership through homeownership education and qualification for mortgage financing.

### **Targeted Initiatives**

Freddie Mac primarily serves the housing finance needs of low- and moderate-income families, families living in underserved areas and minority families through our standard mortgage programs and products. In addition, Freddie Mac undertakes numerous targeted efforts to expand homeownership opportunities for these families. These various efforts are listed in Appendix 2.

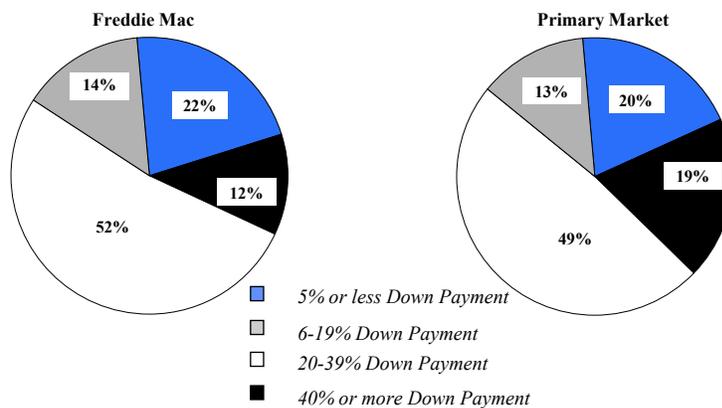
A number of Freddie Mac's efforts, including a variety of mortgage products, special initiatives and targeted investments, are designed specifically to serve very-low-, low- and moderate-income homeowners. Central to our efforts to reach these families has been the introduction of a wide variety of lower down payment mortgage products, some requiring as little as 3 percent down from the borrower. Notable initiatives in 2002, discussed in Appendix 2, include purchasing mortgages under HUD's Section 8 to Homeownership program and implementing changes in our underwriting guidelines aimed at improving the homeownership rate among immigrants.

Freddie Mac's efforts to meet the down payment needs of America's families have proven successful. Although Freddie Mac is required by law to obtain credit enhancements on mortgages with down payments under 20 percent, the distribution of our fundings of such mortgages in 2002 closely matched the distribution observed in the

primary market. As shown in Exhibit 17, about 22 percent of the home purchase mortgages we financed were for households making down payments of 5 percent or less, and 36 percent were for households making down payments of less than 20 percent. Indeed, Freddie Mac's share of lower down payment home purchase loans (36 percent) exceeded the share of such loans originated in the primary market in 2001 (33 percent).

**Exhibit 17**  
**Freddie Mac Purchases Loans with a Wide**  
**Range of Down Payments**

*One-Family, purchase-money fundings by down payment, 2002*



Sources: Freddie Mac, Federal Housing Finance Board's 2002 Mortgage Interest Rate Survey

Freddie Mac also takes a multifaceted approach to community development lending, which includes establishing public-private collaborations that increase access to mortgage credit for very-low-, low- and moderate-income and minority households and eliminate barriers to homeownership in targeted underserved communities. Working with affordable housing lenders, Freddie Mac designs creative solutions to meet the homeownership needs of specific populations in targeted market areas; explores efficient use of public subsidies to make homeownership more affordable; and helps develop effective homebuyer education/counseling and debt management assistance programs.

### Helping Community Lenders

Freddie Mac is committed to meeting the needs of community lenders and their customers. During 2002, Freddie Mac introduced several initiatives and alliances designed to increase the benefits of secondary market financing to community lenders.

Freddie Mac teamed with mortgage technology developer MortgageBot in February 2002 to offer small- to mid-size lenders the ability to affordably enhance their websites to deliver online mortgage loan approvals with Freddie Mac's Loan Prospector automated underwriting service. MortgageBot custom-builds, hosts and maintains a lender-controlled and branded website, and links it to Loan Prospector. This service enables lenders to cost-effectively tap an additional loan origination channel while maintaining control of their brand. Borrowers visit a lender's website, complete an online mortgage application and receive an online loan decision from the lender within minutes. Borrowers also can use the lender's website to access additional services such as a rate sheet with the lender's pricing and city-specific closing costs estimates.

In April 2002, Freddie Mac launched an initiative that makes it simpler for community lenders to securitize small amounts of mortgages held in their portfolios. The "mini-bulk" initiative enables lenders to pool as little as \$10 million of single-family mortgages, providing another tool for community lenders.

In February 2002, Freddie Mac and America's Community Bankers (ACB) joined in a strategic alliance to better enable community banks to serve the housing needs of their communities. Community banks will receive enhanced access to Freddie Mac's technology services, including the online origination tools custom-built by MortgageBot. In addition, ACB members and Freddie Mac will work closely to increase cash sales of mortgages into the secondary market. The alliance also provides ACB members with exclusive training opportunities on many Freddie Mac products and programs, especially in the areas of technology and affordable housing.

At the end of 2002, Freddie Mac entered into an alliance with the Credit Union National Association and CUNA Mutual Mortgage Corp. to give credit unions unprecedented access to the secondary market and Freddie Mac's technology. The alliance provides credit unions with enhanced access to Loan Prospector, the ability to develop branded online sites, simplified requirements for selling seasoned mortgages to Freddie Mac and enhanced ability to sell small amounts of mortgages to Freddie Mac.

## **Conclusion**

Freddie Mac during 2002 purchased record numbers of mortgages for both home purchase and refinancing. Our \$578 billion of single-family purchases met unprecedented demand for liquidity to the origination market and helped stabilize the national economy. Freddie Mac also continued our longstanding efforts to expand markets and bring the benefits of the secondary market to more families.

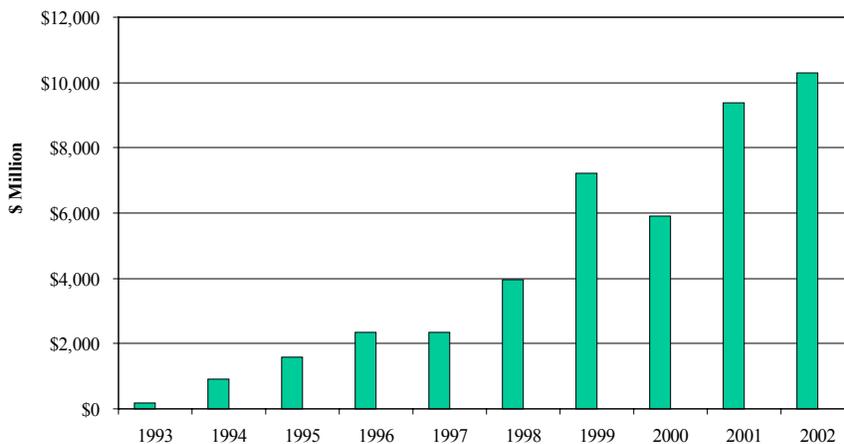
### Chapter 3: Opening Doors to Affordable Rental Housing

In 2002, Freddie Mac's multifamily mortgage program provided a major source of credit to the nation's rental housing market and substantially assisted in the achievement of our affordable housing goals. In 2002, multifamily business activities at Freddie Mac totaled a record \$13.3 billion. Through multifamily mortgage purchases and other activities, Freddie Mac helps make rental housing affordable to all segments of the low- and moderate-income markets, including very-low-income households.

Our multifamily activities financed rental housing for 333,000 families in 2002, 93 percent of which were affordable to very-low-, low- and moderate-income renters. In a year marked by a continuing slow economy, historically low interest rates and weakening multifamily economic fundamentals, Freddie Mac's high volume of purchases provided stability and liquidity to the multifamily market. Freddie Mac's multifamily loan products and pilots enabled a greater number of multifamily borrowers to take advantage of historically low interest rates to provide rents affordable to very-low-, low- and moderate-income families.

Freddie Mac has become a key source of financing for affordable rental housing. In the ten years following the launch of our new generation multifamily program in 1993, Freddie Mac has purchased \$53.9 billion in multifamily mortgages, which financed housing for more than 1.6 million families. As indicated in Exhibit 18, the dollar volume of our purchases has increased substantially over the years.

**Exhibit 18**  
**Freddie Mac's Multifamily Mortgage Purchases, 1993-2002**



Note: CMBS purchases not included  
Source: Freddie Mac.

Freddie Mac's support of the multifamily market extends beyond the loans we purchased through our traditional multifamily programs and beyond our activities that qualify toward meeting the housing goals. We are major investors in properties qualifying for low-income housing tax credits (LIHTCs) and in mortgage revenue bonds (MRBs).

## **The Multifamily Market in 2002**

Multifamily lending activity in 2002 was strong due to the historically low interest rates that spurred multifamily refinancing activity combined with normal acquisition and construction financing needs. In fact, multifamily mortgage debt grew by \$43.3 billion during 2002, the second largest increase in history (the 2001 increase was \$48.3 billion).<sup>34</sup> Low rates were reflected in a 56 basis point decline in the contract interest rate on multifamily fixed-rate loan commitments in the market from third quarter 2001 to third quarter 2002 (from 6.84 percent to 6.28 percent).<sup>35</sup>

Lending was strong despite the weakening of the multifamily market that began at the end of 2001 and continued throughout 2002. Apartment demand fell as a result of the soft economy and extremely low mortgage rates that encouraged an exodus of renters to homeownership. As a consequence, overall occupancy levels and effective rents dropped. This weakness in the market has been widespread, with most metropolitan markets experiencing higher vacancy rates and zero to negative rent growth. The average vacancy rate for 60 major metro markets rose from 4.8 percent in fourth quarter 2001 to 6.2 percent in fourth quarter 2002.<sup>36</sup> In addition, effective rents in U.S. metropolitan markets in fourth quarter 2002 dropped about 1 percent from fourth quarter 2001.

Still fearful of repeating the excesses of the late 1980s, the multifamily development and financial markets have exercised considerable discipline in the development of new projects. Multifamily starts rose only slightly in 2002 to 306,300 units, compared to 292,800 units in 2001.<sup>37</sup>

In addition, multifamily credit quality remained strong in the market despite flat property values, flat rents and increased vacancies. Typical apartment investment portfolios are continuing to experience historically low delinquency levels. For example, the American Council of Life Insurers reported that as of the end of the third quarter of 2002, 60-day delinquency rates on its member's multifamily portfolios of 23 basis points, up only 14

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<sup>34</sup> Federal Reserve Board, March 2003.

<sup>35</sup> American Council of Life Insurance.

<sup>36</sup> Reis, Inc.

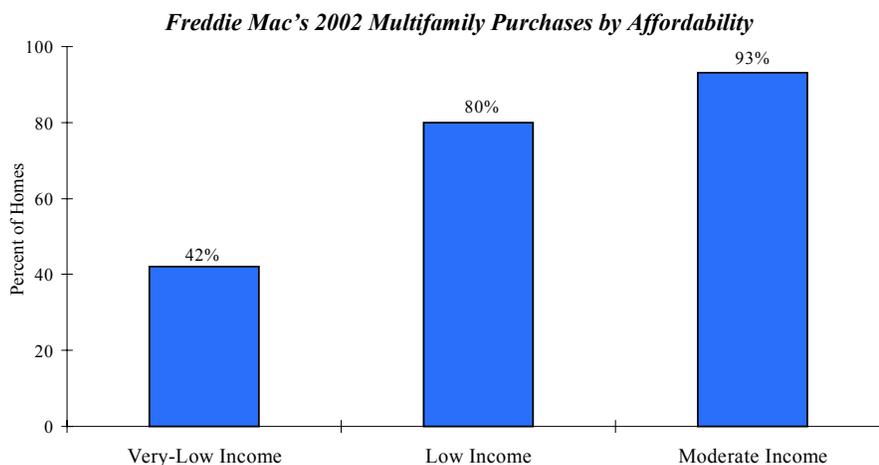
<sup>37</sup> U.S. Census

basis points from the same time the previous year. The strong rent growth of the late 1990's and the low interest rates on mortgage debt have provided the multifamily sector with financial strength to weather the current vacancy increases and downturns in property income.

## Multifamily Initiatives

Freddie Mac's multifamily programs play a vital role in our service to very-low-, low- and moderate-income families. As illustrated in Exhibit 19 below, 42 percent of the multifamily units we financed in 2002 were affordable to very-low-income families. Our multifamily financing activities included \$5 billion in mortgages meeting the criteria for the special affordable housing target (loans serving very-low-income families or low-income families living in low-income neighborhoods). Since 1993, Freddie Mac has funded \$21 billion in mortgages that meet this target.

**Exhibit 19**  
**Nearly All of Freddie Mac's Multifamily Housing Is**  
**Affordable to Moderate-Income Families**



Source: Freddie Mac

During 2002, we used innovative financing structures combined with prudent, flexible multifamily lending practices to reach our record level of multifamily mortgage purchases. We also adjusted our lending practices to ensure responsible lending in the softening apartment markets and declining interest-rate environment in 2002. This strategy results in financially viable, well-managed properties that are assets to their communities.

Freddie Mac maintained our focus on our targeted affordable initiatives in conjunction with our Program Plus® network of lenders in 2002. We continued to test initiatives

through pilot programs and implement enhancements to our existing multifamily mortgage products. Our wide range of mortgage programs, products and pilots supported the acquisition, refinance or rehabilitation of existing apartment buildings as well as new construction. Our lending programs covered a broad array of eligible mortgage products such as tax-exempt bond credit enhancement, cash products including fixed-rate, interest-only, adjustable-rate, streamlined refinance and second mortgages, and also securitization activities.

### **Bond-Financed Credit Enhancement**

In 2002, Freddie Mac provided credit enhancements of \$1.6 billion for newly constructed and existing affordable multifamily properties. Under this initiative, Freddie Mac works closely with state and local housing authorities to credit enhance the agencies' tax-exempt bond and related taxable issuances. By providing our credit enhancement to these bonds, as well as purchasing the related conventional cash loans, Freddie Mac lowers the cost of borrowing and thereby assists the borrower in maintaining affordability into the future.

*Duval County, FL* – In 2002, Freddie Mac's credit enhancement of \$29.5 million of 501(c)(3) bonds issued by the Duval County HFA in Jacksonville, FL facilitated the preservation of more than 1,000 critically needed affordable mixed income units by an experienced nonprofit. Forty percent of the units are restricted to families with incomes of less than 60 percent of area median income (AMI), and 75 percent are restricted to families with incomes of less than 80 percent of AMI.

### **Tax Credit Forward Commitment Pilots**

We also support the construction of new affordable rental housing and substantial rehabilitation through our Forward Commitment pilot. This initiative provides financing for loans or credit enhancement for bonds with use agreements that preserve the affordability of units into the future. This tool has enabled us to respond to market needs by providing refinancing for properties originally financed with LIHTC equity.

In 2002, Freddie Mac successfully converted our first five forward commitments to permanent financing. In 2002, Freddie Mac also provided a record \$94 million in new forward commitments and provided a variety of innovations to reduce the cost of financing and increase affordability, including variable-rate construction financing, forward starting swaps, forward rate locks and take-outs. Innovative transactions under the Forward Commitment pilot include:

*Belmont Heights* – Using our forward commitment tool, Freddie Mac was able to provide \$5.5 million to assist in the rebuilding of a public housing project in Tampa, FL, under the HUD HOPE VI program.

*Medford Landing* – Medford Landing, located in Suffolk County Long Island, NY, whose sponsor includes a 501(c)(3) not-for-profit and for profit entities, successfully completed its construction and lease-up under its forward commitment issued in 2001. This project's 112 units, located in a HUD-defined underserved area, will maintain their affordability for an extended period of 50 years, and will be restricted to senior citizens with incomes less than 60 percent of area median income. One-quarter of the units will be further restricted to those with incomes less than 30 percent of area median income. In addition to Freddie Mac financing, the property benefited from both LIHTC equity and soft second mortgage funds provided by the New York State Housing Trust Fund.

### **Conventional Mortgage Financing Innovations**

Responding to the needs of the multifamily borrowers, Freddie Mac has initiated several underwriting innovations including the Fixed-to-Float Option and the Conventional Forward Commitment pilot.

*Fixed-to-Float Option* – In 2002, Freddie Mac enhanced our fixed-rate mortgage products under both the popular early rate-lock delivery option and the standard delivery option. The new Fixed-to-Float option provides borrowers with a reduced interest rate and an optional one-year extension of the mortgage term (at a floating rate) in exchange for a yield maintenance provision requiring certain payment upon prepayment that applies during the full mortgage term. In 2002, borrowers used the Fixed-to-Float option for more than \$1.4 billion in mortgages.

*Conventional Forward Commitment pilot* – We expanded our forward commitment pilot to include a conventional forward commitment execution. The Conventional Forward Commitment enables owners and builders to finance the construction and substantial rehabilitation of properties that are funded with conventional mortgages.

### **Seniors Housing**

Freddie Mac finances properties that offer resident and congregate services for senior citizens. In 2002, Freddie Mac purchased \$231 million of seniors housing mortgages. Our 2002 purchases brought our total senior citizens housing portfolio to \$1.2 billion. The vast majority of these units are affordable to low- and moderate-income residents.

*Coraopolis Towers* – Freddie Mac's seniors housing program preserved affordable housing for low-income tenants living in Coraopolis Towers, in Coraopolis, PA. Residents of this independent living/congregate care seniors apartment building benefit from Section 8 rent subsidies and the amenities and services provided in this seniors property. A community room, library, cafeteria, planned shopping trips and personal care seminars are available to tenants. The borrower utilized the Early Rate-Lock and Fixed-to-Float options for this mortgage. The apartments serve households of various low-income levels, ranging from 0 to 60 percent of area median income.

### **Five- to 50-Unit Properties**

Freddie Mac has an increasing presence in the market for five- to 50-unit multifamily properties, which HUD has identified as historically underserved by the secondary market. Our 2002 purchase volume of \$1.8 billion represents more than 44,000 apartment units. Freddie Mac purchases small multifamily mortgages through both flow and portfolio purchases. We expect that, over time, our growing presence in this market segment will bring increased standardization and liquidity to mortgages on these small multifamily properties.

### **Leveraging Public Resources**

Freddie Mac also engages in other multifamily activities that leverage public resources as a means of making affordable apartments available to very-low-, low- and moderate-income renters.

### **Low-Income Housing Tax Credit Investments**

LIHTC investments are an effective tool that combines private sector capital, government incentives and community-based housing expertise for the benefit of low-income renters. Our participation in tax credit investments supports the creation or rehabilitation of rental housing for America's lowest income families. In 2002, Freddie Mac continued to be a market leader. We made the largest single-year commitment in our history to low-income housing tax credits by committing to invest more than \$883 million. As a result, our total investments surpassed the \$2.7 billion mark. Altogether, Freddie Mac's investments have financed the construction or rehabilitation of more than 180,000 rental units for very-low- and low-income families in 2,500 projects in all 50 states, the District of Columbia, Puerto Rico and the Virgin Islands. Although these rental units do not count toward Freddie Mac's affordable housing goals, these investments contributed to meeting the needs of the nation's low-income renters.

In 2002, Freddie Mac continued to expand our investment efforts by establishing additional separate investment funds, Equity Plus® Low-Income Housing Tax Credit Funds. Through these funds, Freddie Mac will provide up to 100 percent of the tax credit equity in qualified affordable multifamily projects. This level of investment is evidence of our deep and ongoing commitment to the financing of low-income rental housing. Freddie Mac will underwrite each project along with the equity fund and manage our investment at the project level.

### **Tax-Exempt Bond Investments**

Freddie Mac purchased \$433 million in newly issued multifamily mortgage revenue bonds in 2002. These bonds, which are issued by state, county or city government

agencies, finance mortgages for nonprofit borrowers or property owners who agree to keep rents at affordable levels. Freddie Mac's investment enables borrowers to maintain affordable rental rates. Freddie Mac's 2002 multifamily bond purchases will finance estimated 7,900 units of affordable housing. We estimate that 58 percent of those units will be affordable to very-low-income families.<sup>38</sup>

### **Financing Multifamily Housing Through Securitization**

Freddie Mac issued a record \$1.9 billion of securities backed by multifamily mortgages through negotiated transactions in 2002. More than 92 percent of these securities financed mortgages for affordable housing, making apartments available to 43,000 very-low-, low- and moderate-income families.

Also in 2002, Freddie Mac provided additional liquidity to the residential rental market by investing in CMBS, which increases the supply and lowers the cost of multifamily mortgage financing, and helps provide more affordable rents.

### **Conclusion**

In 2002, Freddie Mac demonstrated our commitment to the multifamily market by financing a record \$13.3 billion in mortgages. In a year marked by a slow economy and softening markets, we provided a reliable source of funds and liquidity for multifamily lenders while retaining appropriate credit standards. We funded 152,000 apartments that met the special affordable housing goal. Because the vast majority of multifamily units we finance are affordable to low- and moderate-income renters, our multifamily program plays a key role in Freddie Mac's service to low- and moderate-income families.

In a year of historically low interest rates, Freddie Mac enabled affordable housing lenders and borrowers to take advantage of the low interest rate environment, thus reducing rental costs to tenants.

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<sup>38</sup> *State HFA Factbook: 2000 NCSHA Annual Survey Results*. Estimates are based upon data reported by each of the state housing finance agencies from which Freddie Mac purchased mortgage revenue bonds issued in 2002.

## **Chapter 4: Miscellaneous Reporting Requirements**

Freddie Mac's use of automated underwriting makes the mortgage finance system more efficient, objective and fair. In addition, our business practices, such as our credit policies and underwriting standards, quality control processes, pricing and other activities, contribute to an efficient and fairer mortgage finance system that opens doors to housing for more families.

### **Opening Doors to a Fairer System**

Freddie Mac is committed to equal opportunity and fair lending. Each year, we dedicate significant resources to ensure that our business practices help make the housing finance system fairer, more efficient, and less costly. The following provides an assessment of the steps we take to ensure that our underwriting standards, purchase requirements, pricing and fees promote access to low-cost mortgage credit for all borrowers, including minority families.

#### **Automated Underwriting**

Freddie Mac continues to use technology, such as automated underwriting, to make the mortgage finance system more objective and fair. We also take specific, additional steps to ensure that our automated underwriting technologies and other recommended statistical tools are used in a way that promote fairness and access to credit in the mortgage process.

Freddie Mac periodically reviews Loan Prospector to ensure that it continues to predict mortgage loan performance in a fair and unbiased manner. Ongoing review of Loan Prospector confirms that, in comparison to traditional manual underwriting, Loan Prospector:

- More accurately predicts default risk for all groups of borrowers
- Increases fairness in the mortgage underwriting process
- Better extends homeownership opportunities to traditionally underserved borrowers

Each of these findings is discussed below.

#### *Increased Accuracy*

Loan Prospector uses a statistical model that predicts mortgage default based upon the actual performance of millions of mortgages Freddie Mac has purchased over many years. By using Loan Prospector, lenders can effectively incorporate the experience of

thousands of loan originators and millions of borrowers into their lending decisions, which vastly improves accuracy.

Loan Prospector does not “reject” any loans eligible for purchase by Freddie Mac. Rather, for each loan reviewed, Loan Prospector provides a risk assessment of “accept” or “caution.” An “accept” classification represents Freddie Mac’s promise to purchase the mortgage if it is offered to us for sale. Freddie Mac also will purchase caution mortgages if the lender identifies factors that offset the risks identified by Loan Prospector.

A recent analysis of mortgages Freddie Mac purchased in 1994 and 1995 found that Loan Prospector accurately predicts mortgage default.<sup>39</sup> The analysis compared the actual performance of loans to the performance that Loan Prospector would have predicted for those loans. Loans rated by Loan Prospector as the most risky defaulted at four times the average rate of all loans. Loans identified by Loan Prospector as the least risky defaulted at only one-fifth the average rate. Loan Prospector also accurately predicted defaults across all income and racial groups.

Loan Prospector’s higher level of underwriting accuracy results in higher borrower “accept” rates. For example, Freddie Mac analyzed about 1,000 loans originated in 1993 and 1994 as part of an affordable housing initiative. Of the 1,000 loans, manual underwriters rated 52 percent accept, compared to a Loan Prospector accept rate of 87 percent. This analysis suggests that Loan Prospector does a better job of distinguishing between high- and low-risk loans than manual underwriters and that low- and moderate-income borrowers are more likely to obtain a mortgage through automated underwriting rather than through manual underwriting.

#### *Increased Fairness*

By bringing greater accuracy to the mortgage underwriting process, Loan Prospector promotes greater fairness in mortgage lending. Loan Prospector provides an underwriting tool that facilitates underwriting decisions based upon objective criteria that are applied the same way to every borrower, every time.

#### *Expanding Markets*

Loan Prospector’s ability to provide increased accuracy and fairness, along with its faster loan processing and reduced costs, has expanded the nation’s mortgage markets in several respects.

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<sup>39</sup> Susan Wharton Gates, Vanessa Gail Perry and Peter M. Zorn, “Automated Underwriting in Mortgage Lending: Good News for the Underserved?” *Housing Policy Debate*, vol. 3, issue 2, 2002.

Increased accuracy has led to the development of new mortgage products that a few years ago would have been deemed to be too risky. Loan Prospector can assess mortgages with very low (or no) down payments, A-minus mortgages and alternative-A loans (which generally have nontraditional documentation). Since introducing Loan Prospector in 1995, Freddie Mac has doubled the share of our purchases of mortgages with loan-to-value (LTV) ratios of 95 percent or above. By reducing down payments, Loan Prospector helps more families achieve homeownership.

Loan Prospector's ability to differentiate clearly among mortgage risks has made the approval process more objective. Lenders can now routinely originate loans to borrowers they were less likely to serve in the past, such as borrowers with relatively high debt-to-income ratios and the self-employed. This creates more business for lenders and greater access to mortgage credit for traditionally underserved groups.

Loan Prospector also reduces the average time lenders spend underwriting most loans, permitting more time to be spent evaluating other loans. It also reduces origination costs, which may be lower by about an average of \$650 or more per loan.

Automated underwriting systems such as Loan Prospector are increasing housing opportunities by significantly reducing costs and bringing a level of fairness and consistency to lending processes that traditional manual underwriting cannot match and by expanding markets to new borrowers through their superior predictive power.

## **Credit Policies/Underwriting Standards**

Freddie Mac assesses the likely impact of proposed changes to our underwriting standards on low-income and protected-class borrowers. We also solicit feedback from lenders and others in the housing finance system. In addition, we undertake affordable lending initiatives that explore alternative approaches to expand access to lower-cost mortgage credit to more underserved households. For a description of these affordable lending initiatives, see Appendix 2.

Freddie Mac develops marketing and customer support materials for each credit policy. In addressing fair lending or other compliance questions, these materials assist our customers to serve underserved families and neighborhoods and to avoid misconstruing credit policy standards.

Freddie Mac's guidelines are crucial to our ability to maintain credit quality. However, the potential exists that our lender customers may misinterpret or have an incomplete understanding of the guidelines. To guard against any such misinterpretations or misunderstandings, we discuss our guidelines with industry participants and community groups to ensure they are not misinterpreted to create arbitrary barriers for creditworthy borrowers.

In 1991, Freddie Mac created Underwriting Barriers Outreach Groups (UnBOG) to review our underwriting guidelines and identify aspects of them that might be misinterpreted in ways that limited lending opportunities. This successful ten-year initiative resulted in numerous clarifications to Freddie Mac's underwriting guidelines.

Currently, Freddie Mac's Affordable Housing Advisory Council, which we created in 1992, provides Freddie Mac with expert advice regarding possible methods for advancing affordable housing. Members are leaders in the affordable housing field, including representatives of community-based and other nonprofit and for-profit organizations and state and local government agencies actively engaged in the promotion, development or financing of housing for very-low-, low- and moderate-income families, minority families and families living in underserved areas. The Advisory Council discusses a range of topics, including loss mitigation services, expanding opportunities via Loan Prospector, new mortgage products and initiatives, priorities for affordable lending and community development lending, and technology alternatives for enabling and maintaining homeownership.

The feedback we receive from the Advisory Council and other industry groups has assisted us in the continuous process of clarifying our guidelines, which enhances our service to very-low-, low- and moderate-income families, minority families and families living in underserved areas.

## **Managing Mortgage Performance**

Freddie Mac manages the servicing of approximately 10 million mortgages, and is constantly searching for new information that will help accurately assess risk of default and help families avoid mortgage foreclosures. The consequences of poor risk assessment include the origination of mortgages that end up in foreclosure, which can be disastrous for the families and their neighborhoods. Low- and moderate-income families and neighborhoods are particularly vulnerable to the harmful effects of poor lending practices. Freddie Mac is committed to providing tools to lenders that enable appropriate risk assessment, helping to ensure that families can use their homes to build wealth and achieve their long-term financial objectives. The development of Freddie Mac's Loan Prospector represents a substantial improvement in this regard.

During the past few years, foreclosure rates on mortgages purchased by Freddie Mac have dropped significantly for all borrower groups. While partly attributable to the economic expansion of the past decade and continued house price appreciation, Freddie Mac's success in reducing foreclosures also evidences our use of better risk assessment tools in underwriting mortgages, as well as innovative tools to assist families who encounter problems in making their mortgage payments. These tools have been developed based on our increased understanding of mortgage risk. Active management of mortgage risk enables Freddie Mac to offer more borrowers access to lower-cost mortgage financing, helping families purchase homes they can afford to keep.

### **Using Automated Tools to Preserve Homeownership**

In addition to providing automated tools for underwriting, Freddie Mac provides automated tools for lenders to identify and work with borrowers most likely to encounter problems making their mortgage payments. In 1997, Freddie Mac introduced *EarlyIndicator*<sup>SM</sup>, a state-of-the-art, statistically based delinquency management tool that assists the mortgage industry in helping more borrowers avoid foreclosure, making delinquency management more effective and efficient for mortgage servicers and reducing credit losses for investors.

*EarlyIndicator* features two distinct model types: collections and loss mitigation. Collection scores measure the likelihood that a mortgage that is late for one payment will become late for two payments. Loss mitigation scores measure the likelihood that a mortgage two or more payments late, including mortgages in foreclosure, will result in a loss to the investor. *EarlyIndicator* helps lenders identify and focus on high-risk borrowers and begin working with them earlier in the delinquency process. Early intervention by lenders is crucial to helping delinquent borrowers – the longer a loan is delinquent, the greater the likelihood of foreclosure. *EarlyIndicator* thus promises to help more homeowners avoid foreclosure, while reducing industry credit losses. At the end of 2002, 66 mortgage servicers, servicing an estimated four-fifths of Freddie Mac's seriously delinquent loans, had been licensed to use *EarlyIndicator*.

In 2001, Freddie Mac released a new version of *EarlyIndicator*, Version 4.0, which enhances the predictive power of this default management tool. Key upgrades include the addition of collections and loss mitigation models for subprime and government loans, as well as an updated loss mitigation model for conventional loans. Version 4.0 was the first such commercially available tool for subprime mortgages, enabling servicers to more effectively manage increasingly complex mortgage portfolios and helping borrowers who traditionally have been at a high risk of default to avoid foreclosure. To date, 16 subprime servicers are licensed to use *EarlyIndicator*. These additional enhancements represent Freddie Mac's continued leadership in providing comprehensive and predictive delinquent loan scoring models. *EarlyIndicator* continues to be the mortgage industry standard for default management technology.

*EarlyIndicator* can reduce the consequences of mortgage delinquency for borrowers, servicers and investors. Through continuing research on the drivers of mortgage performance and through the use of innovative statistical tools to identify at-risk borrowers earlier in the delinquency cycle, Freddie Mac is leading the way to help more homeowners obtain mortgages they can afford and homes they can keep.

## **Conclusion**

For more than 30 years, Freddie Mac has fulfilled our public mission by opening doors for 30 million families. Today, due to Freddie Mac's efforts, America has the best housing finance system in the world. Every day we strive to extend the benefits of the mortgage finance system to reach an even broader diversity of our nation's homebuyers and renters.

2002 was an extraordinary year for Freddie Mac and the families we serve. We financed housing for an unprecedented 4.6 million families in communities across the country. Our mortgage purchases brought strength to the housing sector in an otherwise weak economy. In a challenging environment, we met all of the affordable housing goals established by HUD.

In 2002, Freddie Mac continued to ensure the continuous availability of mortgage credit and fulfill our charter purposes of providing stability and liquidity in the residential mortgage market. Because of Freddie Mac's leadership in attracting global capital to finance America's homes, borrowers in the mortgage market served by Freddie Mac enjoy uninterrupted access to mortgage credit at low cost.

Freddie Mac's leadership in providing tools to lenders to improve the mortgage finance system and in promoting responsible lending practices and financial literacy helps put families into homes they can afford and keep. We are using these tools to purchase a broader range of mortgage products and provide lower-cost mortgage financing to more families.

Freddie Mac looks forward to making the world's best housing finance system even better for America's families.

## Appendix 1: Cross-Reference Index

The following provides a cross-reference to the pages of Freddie Mac's Annual Housing Activities Report that provide the information that meets the specific reporting requirements set forth in Section 307(f)(2) of the Freddie Mac Act (12 U.S.C. §1456(f)) and the Secretary of HUD's implementing regulations, 24 U.S.C. §81.63:

<b>Reporting requirement: The Annual Housing Activities Report shall</b>	<b>Pages</b>
(A) include, in aggregate form and by appropriate category, statements of the dollar volume and number of mortgages on owner-occupied and rental properties purchased which relate to each of the annual housing goals	6-10
(B) include, in aggregate form and by appropriate category, statements of the number of families served by the Corporation, the income class, race, and gender of homebuyers served, the income class of tenants of rental housing (to the extent such information is available), the characteristics of the census tracts, and the geographic distribution of the housing financed	3-10, 16-17, 31-33, 41, 43-44
(C) include a statement of the extent to which the mortgages purchased by the Corporation have been used in conjunction with public subsidy programs under Federal law	28-31, 46-48, 59-60
(D) include statements of the proportion of mortgages on housing consisting of 1 to 4 dwelling units purchased by the Corporation that have been made to first-time homebuyers, as soon as providing such data is practicable, and identifying any special programs (or revisions to conventional practices) facilitating homeownership opportunities for first-time homebuyers	4-5, 27-40, 57-78
(E) include, in aggregate form and by appropriate category, the data provided to the Secretary under subsection (e)(1)(B) [the loan to value ratios of purchased mortgages at the time of origination]	38-39
(F) compare the level of securitization versus portfolio activity	12-13, 47-48
(G) assess underwriting standards, business practices, repurchase requirements, pricing, fees, and procedures, that affect the purchase of mortgages for low- and moderate-income families, or that may yield disparate results based on the race of the borrower, including revisions thereto to promote affordable housing or fair lending (24 C.F.R. §81.43	17-19, 49-54

<b>Reporting requirement: The Annual Housing Activities Report shall</b>	<b>Pages</b>
requires such assessment with respect to the race, color, religion, sex, handicap, familial status, age, or national origin of the borrower).	
(H) describe trends in both the primary and secondary multifamily housing mortgage markets, including a description of the progress made, and any factors impeding progress, toward standardization and securitization of mortgage products for multifamily housing	5, 42-43, 47-48
(I) describe trends in the delinquency and default rates of mortgages secured by housing for low- and moderate-income families that have been purchased by the Corporation, including a comparison of such trends with delinquency and default information for mortgage products serving households with incomes above the median level that have been purchased by the Corporation, and evaluate the impact of such trends on the standards and levels of risk of mortgage products serving low- and moderate-income families	26-27, 42-43, 52-53
(J) describe in the aggregate the seller and servicer network of the Corporation, including the volume of mortgages purchased from minority-owned, women-owned, and community-oriented lenders, and any efforts to facilitate relationships with such lenders	15, 39-40
(K) describe the activities undertaken by the Corporation with nonprofit and for-profit organizations and with State and local governments and for housing finance agencies, including how the Corporation's activities support the objectives of comprehensive housing affordability strategies under section 105 of the Cranston-Gonzalez National Affordable Housing Act [42 U.S.C. § 12705]	28-40, 44-48, 57-77

## **Appendix 2: Targeted Initiatives**

Freddie Mac serves the housing finance needs of very-low-, low- and moderate-income families, families living in underserved areas and minority families primarily through our standard mortgage products. Additionally, Freddie Mac undertakes numerous targeted efforts to expand homeownership opportunities through the development of innovative affordable housing loan mortgage products specifically designed to overcome barriers to homeownership. Provided below are examples of the broad range of creative initiatives and loan products that Freddie Mac has developed to assist families achieve the dream of homeownership.

### **Addressing the Housing Finance Needs of Very-Low-, Low- and Moderate-Income Families**

Freddie Mac offers a variety of products, undertakes numerous special initiatives and makes targeted investments to increase homeownership opportunities for very-low-, low- and moderate-income families.

#### **Expanding Immigrant Homeownership**

During 2002, we provided specialized training for mortgage originators and brokers to implement changes in our guidelines aimed at improving the homeownership rate among immigrants. These changes, announced in 2000:

- Removed all specific underwriting and documentation requirements for resident aliens. Freddie Mac now purchases loans made to resident aliens under the same guidelines used for U.S. citizens. Resident aliens previously were required to provide additional documentation and higher down payments. This change enables resident aliens to take full advantage of Freddie Mac's low down payment products.
- Allow cash on hand to be used as borrower funds when borrowers do not maintain checking, savings or other similar accounts. People in certain immigrant groups may keep their funds in currency instead of using banking services. This policy change extends the benefits of the secondary market to this underserved borrower segment.
- Allow rental income received from family members residing in the home to be counted as income for underwriting purposes. To pool their financial resources, some families combine extended family members in the same home, and relatives often pay rent to the homeowner. This policy change enables more households to qualify for homeownership and helps finance housing that is more suitable for the size of the family.

### **Freddie Mac 100**

For many families, the largest barrier to homeownership is lack of funds for a down payment. To help alleviate this problem, Freddie Mac introduced the Freddie Mac 100 mortgage product in 2000. It allows a 100 percent LTV ratio and requires only that the borrower has sufficient funds to pay closing costs. Freddie Mac 100 has been well received in the marketplace.

### **Affordable Gold<sup>®</sup> 97**

Available since 1996, Freddie Mac's Affordable Gold 97 product permits borrowers to make 3 percent down payments from personal cash and to use other sources to cover their closing costs. It also offers flexible ratio and reserves guidelines. Affordable Gold, along with our other low down payment offerings, provides opportunities for homeownership for first-time homebuyers or others who have limited savings to use toward the purchase of a home.

### **Affordable Gold<sup>®</sup> 100**

Freddie Mac, the California Housing Finance Agency Loan Insurance Fund, and several national and local lenders offer Affordable Gold 100, which provides 100 percent financing of the purchase price of a home to low- and moderate-income borrowers in California. Borrowers pay the closing costs associated with the home purchase, which can come from a variety of sources, including a grant from a qualified institution, gift from a relative or an unsecured loan. Affordable Gold 100 is the first program of its kind to combine mortgage insurance benefits provided by a state insurance fund, the secondary mortgage market and a team of the nation's top mortgage lenders.

### **Alt 97<sup>SM</sup>**

Alt 97 is a product that can help reach borrowers who have good credit but limited cash for a down payment. It incorporates many of the underwriting flexibilities of Affordable Gold, including expanded debt ratios. The 3 percent down payment can come from a combination of sources, such as gifts or grants. It is an ideal product for first-time homebuyers with limited funds.

### **Two-Family 95 Percent LTV Program**

Freddie Mac offers Loan Prospector customers the ability to make low down payment loans to purchasers of two-family properties when the borrowers occupy one of the units as their primary residence. Under this program, rental income from the other unit further helps many homebuyers afford their homes.

## **Section 8 Rental to Homeownership**

In September 2002, Freddie Mac completed the first of several transactions using Section 8 vouchers for homeownership. This innovative HUD program allows people currently receiving Section 8 rental subsidies to use them toward mortgage payments. Freddie Mac allows lenders to deduct the full amount of the voucher from the mortgage payment or add it to stable monthly income to determine if a borrower qualifies for a mortgage. Under this program, borrowers receive extensive credit and homeownership counseling.

## **Individual Development Accounts**

Under all of our Expanding Markets mortgage products, Freddie Mac purchases loans in which the borrower's down payment consists of funds that have been matched through an Individual Development Account (IDA) homebuyer savings program. IDA homebuyers' savings programs, considered as borrower cash, require that a borrower make regular deposits to a savings account established to save toward the purchase of a home. A public agency, nonprofit organization, lender or employer matches the savings.

## **Builder Grants for Down Payment**

Freddie Mac continues to explore new options to reduce the amount of funds needed for down payments. Working with the National Association of Home Builders (NAHB) and selected lenders, we made available the option to use a grant from a builder for a down payment. This option allows new homeowners additional sources of down payment and allows homebuilders to sell their homes more quickly, which reduces inventories and financing costs.

## **Designing and Financing Affordable Homeownership Programs**

Freddie Mac sponsors forums and workshops designed to assist lenders and practitioners in affordable housing to exchange information and learn about best practices in the design and implementation of programs that meet local needs. For example, we sponsor "Financing Affordable Homeownership" workshops throughout the country to give local housing practitioners basic information on mortgage credit, program design, funding and financing resources, effective use of limited local subsidy resources and recent developments in homebuyer education and counseling. Workshops were presented in Savannah, Dallas, St. Louis and Boston during 2002.

## **Mortgage Revenue Bonds**

Freddie Mac provided increased liquidity to the affordable housing segment of the market in 2002 through a series of targeted investments in MRBs containing state and local housing finance agency (HFA) mortgages.

State and local government HFAs issue tax-exempt and taxable bonds specifically designed to finance mortgage loans to very-low-, low- and moderate-income first-time homebuyers. Working with the HFAs, Freddie Mac purchases and/or securitizes the bond issues. The proceeds are used by the HFAs to make low-rate mortgage loans for first-time homebuyers.

Freddie Mac's MRB purchases make a significant contribution to the liquidity of these bonds and the continued availability of lower-cost financing for first-time homebuyers of limited income, as well as to neighborhood stability and revitalization. Freddie Mac's MRB purchases over the past five years financed housing for an estimated 48,000 low- and moderate-income first-time homebuyers, 27 percent of whom were minority families and 65 percent of whom were very-low- and low-income families.<sup>40</sup>

### **CRA Portfolios**

In 2002, Freddie Mac continued purchasing seasoned affordable mortgage portfolios originated by depositories to meet their Community Reinvestment Act (CRA) objectives. Freddie Mac developed credit enhancements that offer depositories the means to profitably sell these loans to us. These transactions provide immediate liquidity to facilitate new targeted affordable lending activity. Freddie Mac also increased our ability to purchase smaller portfolios opening this option to many community banks that otherwise would not have an outlet for their portfolios.

As part of this initiative, Freddie Mac also works with lenders to create Freddie Mac Gold PCs that are backed by loans meeting CRA income and targeted geographic guidelines. Under guidance from banking regulators, such securities are eligible for credit under the CRA's "Investment Test."

### **Help for Underserved Communities**

Freddie Mac lifted the income restrictions on our affordable mortgage products in all underserved communities. This change makes more financing available for borrowers purchasing homes in underserved markets and should bring more economic diversity and resources to areas with the greatest need.

### **Helping National Lenders Reach Underserved Borrowers**

In 2002, Freddie Mac worked with several national lenders to structure innovative products aimed at meeting the borrowing needs of their underserved customers. These efforts resulted in the origination of more than \$2.5 billion in mortgages. Compared to

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<sup>40</sup> *State HFA Factbook: NCSHA Annual Survey Results, 1997-2002*. Estimates are based upon average mortgage balances and average percent of minority borrowers as reported by each of the state housing finance agencies from which Freddie Mac purchased mortgage revenue bonds.

standard affordable lending products, very-low-income, low-income and minority borrowers comprised a higher share of the homebuyers served.

## **Enhancing Community-Based Lending**

Freddie Mac's multifaceted approach to community development lending includes establishing public-private collaborations to increase access to mortgage credit for very-low-, low- and moderate-income families, minority families and families living in targeted underserved communities. Our community development lending initiatives typically incorporate these essential ingredients:

- The formation of national, regional and local alliances and initiatives between Freddie Mac Seller/Servicers, national organizations with local affiliates throughout the country, nonprofit housing organizations, state and local governments, community groups, faith-based organizations, real estate professionals, mortgage and property insurers, and developers.
- New affordable lending products designed to reach underserved borrowers and communities that offer solutions to the most common problems that very-low, low- and moderate-income borrowers face, such as lack of funds for down payments or rehabilitation; poor, nontraditional or no credit history; and lack of knowledge about the responsibilities of homeownership
- New ideas and creative ways to increase homeownership opportunities in underserved communities

In 2002, Freddie Mac launched more than 30 new alliances and initiatives and continued working with existing alliances. Set forth below are examples of activities that address meeting the needs of cities and revitalizing neighborhoods:

### **Community Gold<sup>SM</sup>**

This versatile loan product is designed to reach more very-low-, low- and moderate-income and minority families and those in underserved communities participating in one of our community development lending initiatives or alliances. Community Gold is ideal for households with limited resources for a down payment, including first-time borrowers, and for people with credit-related concerns that might have limited their homebuying options in the past.

Community Gold can be used for both purchase and purchase/rehabilitation. Borrowers can contribute as little as \$1,000 or 2 percent of a home's value from personal cash. The ability to offer this flexibility is due in large part to the existence of high-quality pre- and post-purchase homebuyer counseling.

## **En Su Casa**

*En Su Casa* (In Your House) is a \$200 million homeownership initiative that combines technology tools with flexible mortgage products to meet the needs of Hispanic borrowers. Designed to help dismantle key barriers to homeownership and provide Hispanic homebuyers with greater access to mortgage financing, *En Su Casa* is a vital component of Freddie Mac's *Catch the Dream* initiative.

En Su Casa brings together organizations committed to increasing homeownership among the nation's Hispanic families. Participants include Freddie Mac, the National Council of La Raza (NCLR), 20 community-based NCLR-affiliated housing counseling organizations, the National Association of Hispanic Real Estate Professionals (NAHREP), EMT Applications and participating Freddie Mac Seller/Serviceicers, including Bank of America, U.S. Bank and Wells Fargo Home Mortgage. Freddie Mac has underwritten the initiative over a three-year period. Our funding supports technology development, basic start-up costs and implementation in more than 20 Hispanic communities across the country.

The initiative provides participating counseling organizations with CounselorMAX, a web-based tool that enables counselors to analyze client qualifications and match their clients with the most affordable loan products and services. Through CounselorMAX, homebuyers will have access to a broad range of flexible mortgage loan products provided by participating Freddie Mac Seller/Serviceicers.

Participating counseling organizations provide services that include:

- Educating the borrower in the homebuying and financing process
- Assisting the borrower in understanding and clearing credit problems
- Analyzing the borrower's income and debt and credit history to determine the maximum mortgage that the borrower can afford
- Providing borrowers with sufficient information to enable them to compare mortgage products from a variety of lenders and select the product that most closely suits their needs
- Assisting the borrower through the application and closing process

Mortgage products provided by participating lenders include low down payments, flexible credit underwriting and debt-to-income ratios, and streamlined processing for resident alien borrowers. Borrowers will be able to use cash for paying closing costs.

## **With Ownership Wealth (WOW)**

Freddie Mac and the Congressional Black Caucus Foundation have launched an initiative aimed at increasing African-American homeownership with one million new families by 2005. The "With Ownership Wealth," effort recognizes that homeownership helps build

family wealth and strong neighborhoods. Education and communication, in the form of targeted television and radio campaigns and homeownership seminars, are key components of the initiative.

### **Rainbow/PUSH Minority Homeownership Initiative**

Freddie Mac and the Rainbow/PUSH Coalition's Wall Street Project are operating a joint campaign to increase homeownership among minority families. The campaign provides information about the benefits of homeownership, the mechanics of the homebuying process and specific mortgage products. Freddie Mac also is working with Rainbow/PUSH, participating lenders and financial ministry counselors of several local churches to increase mortgages made to minority families in selected locations over the next five years.

### **Expanding the Dream<sup>®</sup> DeKalb**

Expanding the Dream DeKalb is a unique suburban minority homeownership outreach initiative in DeKalb County, GA between Freddie Mac, Wal-Mart, the South DeKalb Mall, DeKalb County, Green Forest Community Development Corporation and two minority-owned lending institutions – Citizen's Trust Bank and Infinity Mortgage Corporation. Wal-Mart and the South DeKalb Mall provides space for educational ATM-style kiosks featuring interactive computer-based programs that direct potential homebuyers to homebuyer-education classes, financial counseling assistance and down-payment assistance from the county. The kiosks, open seven days a week, features Freddie Mac's credit education brochure and offers information on Freddie Mac loan products available through participating lenders.

### **HomeFree USA, Washington, DC**

Freddie Mac and HomeFree USA have engaged in a successful alliance to increase minority homeownership in the Washington, DC metropolitan area since 1996. HomeFree USA is a minority-led nonprofit organization created to increase homeownership opportunities among minority and low- and moderate-income families in the Washington, DC metropolitan area. With support from Freddie Mac and other housing organizations, HomeFree USA has successfully counseled hundreds of people over the past five years. Freddie Mac's Loan Prospector assists HomeFree USA's clients in pursuing homeownership opportunities using an innovative offering, the "Freedom Fund," that features a 97 percent LTV ratio and requires only \$500 from borrower funds with flexible underwriting.

### **NAACP-Atlanta**

A \$20 million affordable housing initiative launched by the Atlanta branch of the National Association for the Advancement of Colored People (NAACP), Freddie Mac and Bank of America are expanding homeownership opportunities for very-low-, low- and moderate-income families, minority families and families living in historically underserved Atlanta neighborhoods. The initiative is helping hundreds of families become homeowners by combining aggressive outreach and borrower counseling from NAACP-Atlanta with affordable mortgage products that Bank of America is originating and Freddie Mac is purchasing. NAACP-Atlanta is providing a wide range of borrower services, including one-on-one counseling, telephone counseling, and housing and mortgage information through its network of local partners. The effort builds on Freddie Mac's \$1 billion Select Atlanta Homeownership Alliance, which is described below.

### **New Cities Community Development Corporation & Metropolitan Alliance of Congregations Homeownership Initiative**

Freddie Mac launched a \$75 million, three-year initiative with the New Cities Community Development Corporation and the Metropolitan Alliance of Congregations (MAC) that is expected to help hundreds of families in the Chicago area prepare for and successfully achieve homeownership. An interfaith organization of 300 congregations, MAC increases homeownership opportunities in multicultural communities, particularly among Latinos, immigrants and African-Americans.

The newest element of MAC's Rebuilding America's Communities Campaign, the New Cities Homeownership Initiative, combines flexible, low down payment mortgages with comprehensive pre- and post-purchase borrower education support services to help participating families weather unexpected problems and remain in their homes. Freddie Mac has committed to purchase \$75 million of mortgages under this initiative.

### **HomeSteps<sup>®</sup>**

HomeSteps, a unit of Freddie Mac, sells foreclosed homes in a manner that benefits first-time homebuyers and low- and moderate-income families. Homes sold by HomeSteps are affordable and desirable. Many of the homes are in move-in condition, with necessary repairs already performed.

HomeSteps works closely with community and state organizations that provide instruction and assistance for every step in the home-buying process, including mortgage assistance programs. The unit also works with community participants that can help potential buyers repair a weak credit history. Potential buyers can also learn how to qualify and apply for a mortgage loan. HomeSteps provides other valuable services for homebuyers, including negotiating decreased settlement costs.

## **Neighborhood Reinvestment Corporation**

Since 1994, Freddie Mac and Neighborhood Reinvestment Corporation (NRC) have worked together to revitalize communities through NRC's NeighborWorks® network organizations. Freddie Mac is a key supporter of NRC's successful homeownership campaigns that support the development of homeownership centers throughout the nation to dramatically increase the number of new homeowners in underserved communities. We develop numerous local lending initiatives with NeighborWorks network organizations to expand homeownership opportunities, as well as to combat predatory lending practices. As a collaborative partner with Freddie Mac, NRC is working with us to make our minority homeownership initiative, *Catch the Dream*, a wide-reaching success.

## **New England Initiative**

In a multistate effort, Rhode Island, Connecticut, Massachusetts and New Hampshire residents benefit from a comprehensive initiative that combines homeownership counseling and education. The initiative increases access to affordable mortgage financing and promotes the preservation of homeownership. The Consumer Credit Counseling Services of Southern New England provides consumer credit counseling and homebuyer education through 35 service outlets in these states. Freddie Mac will purchase up to \$100 million in eligible mortgages originated from participating lenders. This initiative compliments and strengthens current community outreach efforts already in place through CreditWorks and the Good Neighbor Program in Connecticut.

## **California NeighborWorks**

A landmark \$25 million private-sector initiative is helping more California families overcome income, credit and savings barriers to affordable homeownership without public subsidies. The new statewide effort – as a result of a collaboration between Freddie Mac, California Bank & Trust, Impact Community Capital, the California Housing Loan Insurance Fund and the California NeighborWorks organizations – combines an affordable 30-year fixed-rate mortgage with a low rate second loan that families can use to finance the down payment or closing costs. The program also combines low-cost mortgage insurance, flexible underwriting and minimal borrower contributions with a grassroots marketing and counseling effort spearheaded by the NeighborWorks organizations.

Other key benefits include flexible treatment of credit issues and expanded debt-to-income ratios so that more low- and moderate-income families can qualify for an affordable market-rate, conventional mortgage.

### **Mississippi Lease-Purchase Plus**

A lease-to-own program called "Get on Track Mortgage" is a collaborative effort between Freddie Mac and the Mississippi Home Corporation that offers a distinctive homeownership opportunity for very-low-, low- and moderate-income area residents. An eligible family selects a new or existing home to purchase and then enters into a lease-agreement. After 39 months, the family takes ownership of the home and assumes the mortgage. The family must consistently demonstrate on-time lease payments and address any outstanding credit issues.

More than 250 Mississippi families will benefit from this \$25 million initiative. Mississippi residents can acquire a home at today's prices and benefit from the built-up equity during the lease period.

### **California Teachers Mortgage Program**

This groundbreaking program permits the use of a second loan for the entire down payment. After only two years, this California Teachers Mortgage Program has enabled 1,600 teachers and other school employees to become homeowners. The California State Teachers' Retirement System (Cal STRS) is becoming the nation's first public pension fund to become a Freddie Mac Seller/Servicer so that it can sell mortgages to Freddie Mac more easily and use the proceeds of the sale to finance new mortgages for more teachers.

The program is part of a collaborative effort between Cal STRS, the Sacramento Housing and Redevelopment Agency, the California State Treasurer's Office, Bank of America and Freddie Mac. The purpose of the program is to provide affordable mortgage financing to assist teachers in overcoming the high cost of homeownership in California. The program also supports teacher recruitment and is being used as a non-salary incentive to recruit qualified teachers to California. Freddie Mac also sponsored the creation of a website ([www.homesforteachers.com](http://www.homesforteachers.com)) which acts as a one-stop information source for teachers wanting to purchase a home in California.

### **Employer-Assisted Homeownership Program – Black and Decker**

To expand homeownership opportunities for Black and Decker employees in Cumberland County, NC, the company allows its contributions to employee 401(k) accounts to be used toward a down payment or for closing-cost assistance. This \$20 million effort in conjunction with Kingdom Community Development Corporation, Black and Decker, BB&T and local community-based organizations offers employees access to homebuyer education and financial counseling, affordable mortgage products, public subsidies, post-purchase counseling and default intervention.

### **Pacific Housing and Finance Lease-Purchase Initiative**

The Pacific Housing and Finance Agency, Freddie Mac and several local lenders have launched an innovative \$70 million lease-purchase initiative designed to help families with impaired credit become homeowners. The new program is available in 35 different California cities through five different lenders. The program provides an exceptional opportunity for families to rebuild their credit reputations while living in and preparing to purchase affordable homes. Families with up to 140 percent of their community's median income can participate. The program is a major expansion of the Southern California Lease-Purchase Initiative begun in 10 cities in 1998. A similar initiative has been launched in the East Bay-Delta communities in California.

### **Revitalizing Neighborhoods**

Homeownership is one of the key ingredients to building vibrant neighborhoods. Freddie Mac also focuses on renovation, rehabilitation and revitalization to stabilize and strengthen neighborhoods. We contribute new and innovative loan products, purchase-and-rehabilitation products, refinance-and-rehabilitation products, new in-fill home construction products, and borrower outreach and support services to help people become homeowners and revitalize neighborhoods.

Most of Freddie Mac's Community Development Lending initiatives are developed with specific neighborhoods in mind. On occasion, however, Freddie Mac designs initiatives to increase homeownership communitywide. Selected communities receive an array of flexible mortgage products, technical assistance and grant funding for marketing and other costs.

### **San Diego**

The *Dueño de Mi Casa, Dueño de Mi Comunidad* initiative is a dynamic homeownership campaign designed to expand access to mortgage credit to low- and moderate-income residents and to support neighborhood revitalization in the Logan area of San Diego and in its suburb National City. Participants include Freddie Mac, the Metropolitan Area Advisory Council (MAAC), Wells Fargo Bank and its subsidiary Wells Fargo Home Mortgage, and NAHREP.

Residents in the targeted neighborhoods are predominantly low-income, Latino families. The neighborhoods suffer from poor land use, an aging housing stock, few community services, a lack of affordable housing and limited economic opportunities. Homeownership rates are only 30 percent, and a substantial portion of the single-family housing stock consists of rental units, many of which are in poor condition and owned by individuals living outside of the community. The goal of the initiative is to improve neighborhood stability and safety by upgrading the quality of the housing stock and increasing homeownership opportunities.

Many homes targeted for renovation are small and do not meet the needs of larger families. These homes will be both renovated and enlarged by bedroom and bathroom additions. Renovated rental units will be converted into owner-occupied units, and deed restrictions will be placed on two- to four-unit dwellings to require owner occupancy.

To help residents become homeowners, the initiative will offer flexible mortgage products and subsidies for very-low-, low- and moderate-income borrowers, grassroots outreach and marketing, comprehensive homebuyer education and counseling, and access to public subsidies.

### **Atlanta, GA**

A long-term, \$1 billion public-private-nonprofit alliance between Freddie Mac, the City of Atlanta, Bank of America, the Atlanta Center for Homeownership, Atlanta employers, the Consumer Credit Counseling Service and other local nonprofit groups is designed to expand affordable homeownership opportunities in the city.

Bank of America's Neighborhood Advantage Credit Flex<sup>TM</sup> and Zero Down<sup>TM</sup> are the featured mortgage products offered through the alliance. Freddie Mac will purchase eligible loans. For borrowers with impaired credit, Freddie Mac's CreditWorks mortgage loan product will be available. CreditWorks helps people burdened with excessive debt and impaired credit to become eligible for a prime market rate mortgage faster than would otherwise be possible.

Another goal of the alliance is to stimulate the construction of new homes as well as bring more of the city's older housing stock up to livable standards. Overall, the alliance will seek to create more than 450 units of new housing in targeted neighborhoods. This initiative is combining resources from the City of Atlanta, the Atlanta Empowerment Zone Corporation, and the Atlanta Housing Authority with Freddie Mac's low down payment mortgage products.

A key component of this outreach effort is the Center for Homeownership, which provides comprehensive, one-stop homebuying assistance that covers all aspects of the homebuying process.

### **Jacksonville, FL**

The Jacksonville Homeownership Alliance is a \$250 million public-private-nonprofit alliance designed to help 2,500 Jacksonville families buy homes with cash down payments as low as \$500. The alliance was created to increase homeownership opportunities in Jacksonville, promote economic growth in key underserved neighborhoods, and encourage new housing construction while promoting historic preservation.

Freddie Mac's Community Gold<sup>®</sup> and Affordable Gold<sup>®</sup> products are available, permitting low down payments, flexible underwriting guidelines and a variety of loan options, including purchase and rehabilitation. The alliance also launched an Employer's Assistance Homeownership Program that encourages Jacksonville hospitals and businesses to promote homeownership to their workforces by providing down payment and closing cost assistance.

To preserve aesthetically appealing older homes, the alliance is also providing affordable mortgage financing to help families acquire and rehabilitate distressed properties in Jacksonville's Historic Springfield and Urban Core neighborhoods.

### **Oakland, CA**

Mayor Jerry Brown, Bank of America, Wells Fargo Home Mortgage and Freddie Mac launched a \$1 billion homeownership campaign in late 1999. The collaborative effort also includes such prominent organizations as the Home Buyer Assistance Center, the Low Income Housing Fund, the Local Initiatives Support Corporation and other local nonprofit groups. Up to 10,000 families are expected to directly benefit, which will raise the citywide homeownership rate a full five percentage points over a five-year period.

Key features of the campaign include the following:

- Flexible mortgage offerings
- Lease-purchase option to enable families to move into a home and use a three-year lease period to establish or re-establish their credit
- Acquisition-rehabilitation component to allow financing for non-profit housing developers to acquire distressed properties and rehabilitate them into attractive new homes for purchase
- Debt-management program, allowing borrowers with serious credit difficulties to re-establish their credit reputation in a short period of time through successful participation in the program

### **Quad Cities, IL & IA**

The Rock Island Economic Growth Corporation the Quad Cities Housing Center, the Bi-State Regional Commission and Freddie Mac formed a \$60 million, three-year alliance to increase the homeownership rate and promote revitalization in the Quad Cities: Rock Island and Moline, Illinois, and Davenport and Bettendorf, Iowa. This is an example of a broad-based lending alliance that encompasses multiple cities interested in coordinating their homeownership efforts.

The alliance brings together the Illinois Housing Development Authority, not-for-profit housing organizations and lenders. Freddie Mac's Community Gold and Affordable

Gold mortgage products will permit low down payments, expand the sources of funds borrowers can use in buying a home and offer a variety of loan options.

### **New Orleans, LA**

Freddie Mac and Wells Fargo Home Mortgage have introduced the *Doubles* program, an initiative to promote the renovation and purchase of duplex housing in New Orleans. The *Doubles* program is designed to help lower the cost of homeownership by allowing duplex borrowers to make their monthly mortgage payment using rental income from the second unit. With down payments as little as \$1,000, qualified borrowers can finance the purchase, purchase-and-rehabilitation or refinance-and-rehabilitation of one- to two-unit properties. The program further reduces financial barriers to the borrower by offering flexible ratio guidelines and alternative down-payment options.

Freddie Mac is working with the Congressional Black Caucus' WOW Campaign, as well as with state and local government leaders and other organizations to make the dream of homeownership a reality for more residents of New Orleans. Freddie Mac has committed to purchase \$25 million in eligible affordable mortgage products from Wells Fargo Home Mortgage.

A unique element to the *Doubles* program allows extended families the opportunity to live together and have the comfort and security of grandparents, parents, children or other family members living next door. In addition, the *Doubles* program includes comprehensive homeownership education, credit and landlord counseling. The Neighborhood Development Foundation, a local nonprofit housing organization, provides counseling and educational services along with consumer outreach.

### **Augusta, GA**

Freddie Mac joined forces with the Augusta Neighborhood Improvement Corporation (ANIC) to launch a \$60 million effort to revitalize the city's Laney-Walker neighborhood by making homeownership in this historic community more affordable for minority and low- and moderate-income families. Other participants include Bank of America and SouthTrust Mortgage, the City of Augusta and the State of Georgia.

The revitalization package includes \$30 million from the State of Georgia with \$10 million targeted to housing rehabilitation and homeownership programs. The City of Augusta has committed \$1 million toward a down payment assistance program. Freddie Mac will invest \$30 million in affordable, low down payment Community Gold mortgages for Augusta families. Bank of America has provided \$250,000 to ANIC to support its operations and housing activities. ANIC will coordinate the initiative and provide essential financial support services for homeownership, including a full range of outreach efforts, down payment assistance and homebuyer education.

### **Eastern North Carolina**

A collaborative effort to increase and sustain affordable homeownership opportunities in Eastern North Carolina was launched by Freddie Mac and a group of organizations, including the North Carolina Fair Housing Center. The public-private collaboration, CarolinaGold, brings a full range of products and services to bear against obstacles to successful homeownership. Freddie Mac will purchase up to \$100 million of qualified mortgages from participating lenders. The initiative includes flexible, low down payment mortgage products, pre- and post-purchase counseling and financing for home rehabilitation.

### **Bainbridge Township, OH**

The first phase of a \$25 million, three-year initiative to revitalize the traditional African-American community of Chagrin Falls Park commenced in 2002. Under the initiative, Chagrin Falls Park Community Development Corporation is securing vacant land parcels for development, providing marketing services and recruiting eligible families. Construction is complete on the first group of houses, including up to 90 newly built homes. This effort also helps families buy homes with flexible down payment mortgages made by participating lenders and purchased by Freddie Mac. To qualify, borrowers must participate in comprehensive pre- and post-purchase homeownership education and counseling. The complete neighborhood revitalization plan will also leverage this effort to make financing available for property renovation by homeowners.

### **Chicago, IL**

Chicago's *Choose to Own* initiative gives families the ability to turn their Section 8 federal housing vouchers into monthly payments toward owning their own home. Participants include HUD, the City of Chicago, the Chicago Housing Authority and Freddie Mac.

Under the initiative, voucher holders use their federal subsidy payments to cover the monthly mortgage costs on a 30-year fixed-rate conventional conforming mortgage instead of using the payments for rent. To ensure borrowers do not pay more than 28 percent of their monthly income on the mortgage payment, some borrowers may be able to qualify for a 15-year below-market-rate second mortgage through the Neighborhood Housing Services of Chicago. To make homeownership more accessible, the City of Chicago Department of Housing provides down payment and closing cost assistance to eligible borrowers through its City Mortgage Program.

Various housing organizations will provide counseling, and the Lawyers Committee for Civil Rights will offer legal services. Harris Bank, Mid-America Bank, Citibank and Shorebank will provide 30-year fixed-rate mortgages to qualified families.

### **Baltimore, MD**

Through an extensive effort by Freddie Mac and Key Bank and Trust, scores of empty foreclosed houses in Baltimore and suburban Baltimore County are being rehabilitated through collaboration with the city and county governments, the St. Ambrose Housing Aid Center and the Govans Economic Management Senate. The initiative is expected to stimulate homeownership and economic growth in key neighborhoods across the metropolitan area. Participants will acquire, rehabilitate and sell at least 50 homes to low- and moderate-income families.

St. Ambrose will acquire foreclosed federally owned properties for as little as \$1 each through a HUD program. Baltimore City and Baltimore County will provide St. Ambrose with access to the HUD properties, which have been empty for at least six months. The Baltimore County Office of Community Conservation will provide federal Community Development Block Grants and HOME funds to stimulate additional in-fill housing in several county neighborhoods targeted by St. Ambrose. Key Bank and Trust will provide mortgage financing for qualified borrowers. Freddie Mac has committed \$5 million to purchase the mortgages to ensure a continuous supply of mortgage funds for additional homebuyers.

### **Syracuse, NY**

As part of the Syracuse Neighborhood initiative, the Syracuse Home Ownership Program combines many outreach activities including technology support, homebuying counseling and education services, and greater access to affordable mortgage products. CounselorMAX provides a state-of-the-art tool to conduct housing outreach, client tracking and homebuyer education. Home HeadQuarters provides pre- and post-purchase counseling, and HSBC Mortgage Corporation (USA) offers program participants reduced banking fees and other banking services.

This initiative will provide a minimum of \$25 million in new mortgage capital and stimulate the origination of hundreds of affordable home mortgages. Mortgage products and services integrated into the program include HSBC's Community Works Mortgages for Section 8 and Freddie Mac's Community Gold, Affordable Merit Rate and 100 Mortgage.

Additional program elements include credit flexibility, incentives for property renovation and a pilot home equity protection plan to encourage people to move back into urban Syracuse neighborhoods and create stronger communities.

HSBC Mortgage Corporation (USA), HSBC Bank (USA), Home HeadQuarters and Neighborhood Reinvestment Corporation join Freddie Mac to generate homeownership growth in Syracuse

## **Racine, WI**

The Corporate and Community Partnership Program (CCPP) of Racine, WI is a multi-faceted housing and neighborhood revitalization strategy designed to serve the City of Racine by bringing together, in a single, concerted effort, the community's nonprofit, government, and for-profit resources and expertise. The primary goal of the program is to promote safe, decent affordable housing throughout Racine, and in particular to promote the vitality of select neighborhoods where new construction and rehabilitation are most needed.

CCPP represents a true public-private partnership. SC Johnson Corporation has taken a leadership role in providing funds to a premier affordable housing nonprofit organization in the area, NHS of Southeast Wisconsin, to allow the renovation of existing homes and the construction of new ones. HUD's Section 8 for Homeownership program is being utilized through the local Section 8 administrator, the Housing Authority of Racine County, to allow renters with Section 8 vouchers to purchase homes. The City of Racine has made available funds to support down payment and closing costs for new homebuyers. Freddie Mac is working closely with its lender partner, Johnson Bank, to make available flexible and affordable mortgage products that help homebuyers realize their dream of homeownership, and help first-time homebuyers avoid predatory lending practices.

Freddie Mac believes this initiative can serve as a model for other similar sized communities that want to bring together local business interests with the needs of the municipality.

## **Pathways to Homeownership**

Pathways to Homeownership is a unique collaborative effort between Freddie Mac and Central Piedmont Community College (CPCC) in North Carolina to increase homeownership opportunity for very-low-, low- and moderate-income and minority individuals that are moving from welfare to work.

Pathways to Homeownership is targeted to current and previous students of CPCC's Pathways to Employment program, a proven Welfare-to-Work program for residents of Charlotte, NC. Freddie Mac's CreditSmart financial literacy training has been integrated into the Pathways to Employment curriculum. Each student is required to participate in the CreditSmart training and earn a certificate of completion. After successfully completing the CreditSmart program, those interested in taking the steps to homeownership receive counseling at Ujamma, a local nonprofit housing organization.

Lender participants in the program offer flexible mortgage products that are designed to help borrowers overcome traditional homeownership hurdles such as insufficient credit and down payment savings. These affordable mortgage products will enable qualified

borrowers to finance a home with very little of the down payment coming from their own funds. To help borrowers cover the rest of the down payment, Ujamma will help borrowers obtain funds for down payment assistance available through the City of Charlotte.

Freddie Mac plans to buy eligible mortgages made as part of Pathways to Homeownership to ensure a steady supply of mortgage credit for additional homebuyers. Pathways to Homeownership is the latest Freddie Mac effort to expand affordable homeownership opportunities in Charlotte. Over the past five years, Freddie Mac has purchased \$9.5 billion in mortgages made to an estimated 82,000 Charlotte area residents.

### **Rebuilding Chinatown in New York City**

Freddie Mac and the Asian Americans for Equality joined to launch an intensive, 90-day planning initiative to collect and share ideas, opinions and suggestions from a broad cross-section of the Chinatown community on how to address many of the issues affecting this historical and cultural hub of New York City. The information will be analyzed and developed into what will be a blueprint for Chinatown's resurgence over the next few years. This blueprint will address many areas of concern, such as employment, economic development, transportation and housing. Freddie Mac contributed \$100,000 to support this community planning process.

### **Revitalizing Boston's Chinatown**

To increase homeownership for the Asian community in Boston's Chinatown, Freddie Mac and the Asian Community Development Corporation (ACDC) developed the Comprehensive Homeownership Program, an initiative that provides homeownership education to prepare local residents for the homebuying process. Freddie Mac provides financial support and training for counselors on our affordable mortgage products and best practices of other successful initiatives. We also connect ACDC to participating Freddie Mac lenders. All Affordable Gold and Community Gold mortgages are offered through these lenders. CreditSmart and CounselorMAX are also available.

Under this initiative, Freddie Mac will purchase up to \$10 million in eligible mortgages. ACDC and Freddie Mac plan to extend this initiative to four additional communities in the greater Boston area.

### **Building Capacity through Technology; Promoting Education and Training**

Freddie Mac has expanded our efforts to provide capacity-building support to lenders and to affordable housing advocates – including local governments and national and local community-based organizations. We provide direct funding, technical assistance, leveraged resources and collaboration with participants in our national and local alliances

and initiatives. We assist in the development of programs designed to meet specific, locally identified needs. We provide loan products focused on the needs of specific borrower populations. We offer strategies to encourage the optimal use of federal funds. We also provide our consumer credit education curriculum aimed at explaining the role that good credit plays in obtaining affordable mortgage credit.

### **Housing Counseling Capacity Assistance**

America's housing counselors will now be able to devote more time to clients, rather than on tedious administrative tasks, thanks to the creation of CounselorMAX, a web-based marketing application owned and operated by Emerging Market Technologies Applications (EMT Applications) and underwritten by Freddie Mac. Designed specifically for – and in conjunction with – housing counselors, CounselorMAX integrates the processes used most by housing counselors with unique timesaving tools to assist with client education and communication. Use of CounselorMAX is allowing housing professionals throughout the nation to realize greater time and cost efficiencies than ever before, and permitting more of America's families to benefit from homeownership counseling.

With the touch of a few buttons, the easy-to-use CounselorMAX system can:

- Manage the homebuying process
- Reduce the time spent on administrative tasks by nearly 70 percent
- Speed the determination of borrower eligibility
- Build, track and transfer client files electronically to the lender, reducing valuable time and resources from counselors and lenders

For additional flexibility, remote users can access CounselorMAX through the World Wide Web at [www.counselormax.com](http://www.counselormax.com).

### **McDonald's Computer Technology Centers**

Freddie Mac and McDonald's have a joint agreement to operate Computer Technology Centers in local McDonald's stores in the southeastern United States. This collaboration focuses on increasing access to Web-based information on topics such as financial literacy, mortgage financing and how to buy a home.

As part of the relationship, Freddie Mac equips select McDonald's restaurants in minority and low- and moderate-income neighborhoods with state-of-the-art personal computers and "quick click" access to comprehensive Internet-based homeownership and credit management information. The information made available at the centers can be found at [www.freddiemac.com/homebuyers](http://www.freddiemac.com/homebuyers). Participating lenders will also have web links at the McDonald's centers.

### **MC Vision Ministries**

Freddie Mac works with various faith-based organizations that assist local residents with the homeownership process. MC Vision Ministries, with financial support from Freddie Mac, works with faith-based entities and other community-development organizations to improve their overall knowledge of the homebuying process, including workshops and training on counseling, personal finance independence and responsibility, predatory lending practices and affordable housing opportunities.

A nine-month training series allows continuous education to community organizations provided by MC Vision Ministries. The participating cities include Chicago, Milwaukee, San Antonio, Oakland, Little Rock and Bridgeport, CT.

### **Faith to Home**

The faith-based community initiative, Faith to Home, reaches out to over 5,000 New York, New Jersey and Pennsylvania parishioners and provides financial literacy and homebuyer educational services. These broad efforts include homebuyer outreach, education, counseling, prequalification and access to a range of affordable mortgage products that include flexible underwriting, low down payment requirements and reduced closing costs.

The initiative combines a two-phase approach. The first phase employs staff development, volunteer recruiting and training, community outreach, client education and loan referral directly to the lender. The second component builds upon the first phase and expands to targeted marketing, loan production and tracking, one-to-one counseling and post-purchase education.

Wells Fargo Home Mortgage and Faith Fellowship Community Development Corporation join Freddie Mac in this tri-state outreach effort. Some of the specific program features include development of 30 training volunteers for financial and homebuyer education; integrating the CreditSmart curriculum, down payment and closing cost assistance by leveraging state and county resources; use of CounselorMAX; and creating and implementing a best practices guide for future faith-based programs.

Eligible mortgage products include Freddie Mac's Community Gold, Affordable Gold 5 and the 100 percent mortgage.

### **Financing Affordable Homeownership Workshops**

Freddie Mac sponsors forums and workshops designed to assist lenders and practitioners in the affordable housing arena to exchange information and learn about best practices in the design and implementation of affordable programs to meet the needs of their local communities. We also sponsor "Financing Affordable Homeownership Programs"

workshops throughout the country to provide local housing practitioners with information about the effective use of limited local subsidy resources and recent developments in homebuyer education and counseling. We also support smaller forums sponsored by other organizations, including a HUD-sponsored affordable housing workshop in Washington, DC, and homeownership forums sponsored by religious organizations.

### **Homebuyer Education on Wheels**

The Homebuyer Education on Wheels (HEW) Initiative expands current homebuyer education and counseling efforts by providing additional outreach to underserved California communities in the tri-county areas of Sacramento, Solano and Yolo. The HEW Initiative involves transforming a school bus into a classroom and private meeting spaces.

Freddie Mac provides support services for HEW in collaboration with Sacramento Valley Organizing Community, Consumer Credit Counseling Services of Sacramento, Neighborhood Housing Services of Sacramento, Mercy Services Corporation, Community College Foundation, Bank of America, California Bank and Trust, and Wells Fargo Home Mortgage.

Through this unique outreach, the newly redesigned bus brings mobile access to rural residents on homebuyer education, comprehensive counseling and flexible mortgage products. These services are literally driven directly to workers in the community, many of whom have limited homebuying knowledge and restricted access to mortgage lenders and education and counseling services. The HEW Initiative will help increase home-purchase preparedness and the homeownership rate of agricultural workers.

### **Homebuying Education Benefits**

A 2001 Freddie Mac study confirmed that pre-purchase homeownership counseling can significantly reduce 90-day delinquencies.<sup>41</sup> This groundbreaking research affirms Freddie Mac's leadership role in looking to the nation's housing-counseling practitioners to help expand homeownership opportunities for minority families, very-low-, low- and moderate-income families and other underserved communities. The study has helped launch an important dialogue about how to best use pre-purchase counseling to make homeownership more accessible to more families.

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<sup>41</sup> Abdighani Hirad and Peter Zorn, "A Little Knowledge Is a Good Thing: Empirical Evidence of the Effectiveness of Pre-Purchase Homeownership Counseling," Freddie Mac, May 2001.

## **Conclusion**

Freddie Mac has implemented a broad range of targeted initiatives and mortgage products designed to expand the benefits of the secondary market to very-low-, low- and moderate-income and minority families and to underserved communities. The result of these efforts is that Freddie Mac continues to open doors to homeownership for more of America's families.