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TESTIMONY OF
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BEFORE THE

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

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Chairman Frank, Ranking Member Bachus, Members of the Committee. Thank you for the opportunity to discuss legislative and regulatory options for mitigating mortgage foreclosure.

Since I last testified in April, the problems in the subprime market have worsened, and there are indications they are spreading to the broader economy.

Outside the market supported by Freddie Mac and Fannie Mae, mortgage money is either unavailable – or available only at high rates. Numerous lenders have closed their doors. Hundreds of thousands of subprime borrowers have entered the foreclosure process already this year – and many more will hit their interest-rate resets in the coming months.

Amid this turmoil, Freddie Mac is taking concrete steps to stabilize markets, support our lenders – and assist as many borrowers as possible.

In February we were the first investor to announce tightened lending standards to limit payment shock for subprime borrowers, and help ensure these borrowers can afford and keep their homes. We will invest only in securities backed by short-term adjustable-rate subprime mortgages that have been underwritten to a fully-indexed, fully-amortizing level.

In April we committed to purchase up to \$20 billion in more consumer-friendly mortgages that will provide better choices for subprime borrowers. We began delivering on that commitment this summer with our new mortgage offering, called SafeStep.

We are also working hard to ensure there is no disruption in the supply of mortgage funds. We have increased our purchases of mortgages and mortgage-related securities, which reached a high of \$40 billion in June. In August we offered needed support to the Alt-A market by providing a 90-day forward purchase commitment, which will allow borrowers to “lock in” their rate. We’re also seeing sizeable increases in our purchases of mortgages to borrowers with weaker credit.

Finally, we remain dedicated to helping borrowers avoid foreclosure. Year to date, we have helped more than 27,000 families find alternatives to foreclosure – for a total of 194,400 since the beginning of 2004.

These efforts will cushion the negative effects on borrowers and communities, but they are not a panacea. The problems in subprime are complex and long in the making. Following a lengthy period of strong house-price growth and a glut of liquidity, a major market correction is underway. Payroll job losses in August – the first reported decline in four years – should serve as a wake-up call that we’ve got real problems on our hands – particularly in some communities.

In considering how to respond to these challenges, I have a few thoughts.

First, solutions need to deal with both aspects of the crisis – borrower foreclosures and mortgage market liquidity. Not all families are in the same set of circumstances. We should carefully determine which borrowers can be helped – and by what mechanism.

Some efforts are already working. For example, we're hearing that mortgage servicers are acting proactively to contact subprime borrowers well in advance of the reset date. And there's greater flexibility on the part of investors to permit modifications, thanks to the SEC's recent clarification of this issue.

Second, solutions should avoid creating perverse incentives. Many lenders and investors bear responsibilities that must be taken into account. We need to help homeowners – not bail out investors.

Third, to avoid getting into this situation again, as a nation, we need to have an honest discussion about how much homeownership is actually sustainable – and how best to achieve it.

Finally, certain legislative and regulatory solutions would help alleviate the mortgage credit crunch, help borrowers and restore investor confidence. The President's plan for modifying FHA is a start, as well as enhanced borrower education and tax code changes that will help alleviate the strain on borrowers who have benefited from debt forgiveness.

But the problems loom large, and more needs to be done. The GSEs can play a larger role in this regard. Lifting the caps on GSE portfolio growth would provide a needed back-stop bid for mortgages, sending a positive signal to the markets.

Similarly, a temporary lifting of the conforming loan limit would enable us to provide needed liquidity to a segment of the jumbo market. As shown in the attached chart, jumbo mortgages have become significantly more expensive relative to those in the conforming market. The 92 basis point difference between rates on jumbo and conforming mortgages far exceeds any such spike in the past 20 years. In high cost areas in particular, a temporary lifting of the conforming loan limit might prevent declines in home prices that could lead to additional defaults.

In closing, let me say that a bipartisan Congress chartered Freddie Mac to keep mortgage markets stable and functioning, especially in a time like this. Freddie Mac can't solve the whole problem, but we are an important piece of a comprehensive solution. Our job is to provide stable and affordable mortgage financing for families in your cities, towns and rural communities. That is exactly what we are doing – and will continue to try to do.

Thank you again for the opportunity to appear before the Committee today on an issue critical both to homeowners and the broader economy.

