

FINAL TRANSCRIPT

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FRE - Q4 2007 Freddie Mac Earnings Conference Call

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CORPORATE PARTICIPANTS

Ed Golding

Freddie Mac - Sr.VP of Investor Relations

Dick Syron

Freddie Mac - Chairman, CEO

Patti Cook

Freddie Mac - Chief Business Officer

Buddy Pizel

Freddie Mac - CFO

CONFERENCE CALL PARTICIPANTS

Ken Posner

Morgan Stanley - Analyst

Annette Frank

Friedman Billings Ramsey - Analyst

David Hochstim

Bear Stearns - Analyst

Brad Ball

Citi - Analyst

Howard Shapiro

FPK - Analyst

Eric Wasserstrom

UBS - Analyst

Moshe Orenbuch

Credit Suisse - Analyst

Bruce Harting

Lehman Brothers - Analyst

Robert Lacoursiere

Banc of America Securities - Analyst

Fred Cannon

KBW - Analyst

Thomas Mitchell

Miller Tabak - Analyst

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to the Freddie Mac fourth quarter and full-year 2007 financial results conference call. (OPERATOR INSTRUCTIONS) As a reminder, today's call is being recorded. At this point, I would like to turn the conference now to the Senior Vice President of Investor Relations, Mr. Ed Golding. Please go ahead, sir,

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Ed Golding - Freddie Mac - Sr.VP of Investor Relations

Thank you, John. Good afternoon and welcome to our investor presentation and conference call where we present to you our financial results for the fourth quarter and full-year 2007. Speaking today are Freddie Mac's Chairman and Chief Executive Officer, Dick Syron, our Chief Business Officer, Patty Cook and our Chief Financial Officer, Buddy Pizsel. Before we begin, let me make two important points. First we have posted on our Web site a slide representation and core tables, which include additional details on our results. You may want to have these available as Buddy walks through the numbers. We have also released additional information on several significant topics, including house price appreciation, our ABS portfolio and a description of our new financial metric "Adjusted Operating Income." We understand it's a bit overwhelming to try to digest all of this in one day, so today we're covering the most relevant topics and we'll provide more detail at our March 12th Investor Analyst Day in New York.

Second, please note that today we make certain forward-looking statements regarding our business results. These statements are based upon a set of judgments, estimates and assumptions about our key business drivers and other factors. Changes in these factors could cause our actual results to vary materially from our expectations. You'll find a discussion of these factors in today's Information Statement and 2007 Annual Report which is also posted on our Web site. We strongly encourage you to review those factors carefully. One final note, we would like as many people as possible to be able to ask a question. Therefore, if you would please limit yourself to one question and a follow-up, I would be grateful. Time permitting, we will come back for second round. Thanks and now let me introduce our Chairman and CEO, Dick Syron.

Dick Syron - Freddie Mac - Chairman, CEO

Thank you, Ed. And thank all of you for joining us this afternoon. This is a momentous time for Freddie Mac in two dimensions. One is good and one is bad. After many years of effort, we're finally delivering timely financial reports. The entire Freddie organization, but especially Buddy Pizsel, deserve great credit for that.

Unfortunately the financials we're delivering are far from pretty. As we indicated in our call in November, continuing adverse trends in house prices, mortgage credit and fixed income markets contributed to significant losses in the fourth quarter. For the fourth quarter and full year, Freddie Mac recorded a net loss of \$2.5 billion and \$3.1 billion, respectively. I'll ask Buddy to take you through these results in detail in a couple of minutes but first I want to make a few general points on our position.

First on capital. No one could have lived through the last six months in the financial markets and missed the fact that access to capital is absolutely crucial in investor's minds. Freddie Mac recognized our need to address capital in the fourth quarter of 2007, and took a positive step to issue \$6 billion in preferred stock. As it turned out, we were the first in a long parade of companies to do so.

Giving effect to the impact of adopting the fair value option at the beginning of '08, our capital stood at approximately \$39 billion, with an estimated surplus of about \$4.5 billion over the 30 percent mandatory surplus target. This is about where we expected to be at the point following our preferred deal last year. At the current level and surplus, management believes that we have sufficient capital to provide for modest growth in our business and to weather the downturn in the absence of significant further disruptions. I should note that we are currently assessing how we plan to increase - how we plan to address the increase in conforming loan limits that was included in the fiscal stimulus package. We'll keep the market apprised of our intentions in this area as we formalize our plans - which will depend in part on how many MSAs are designated by HUD. But make no mistake, we'll be there to meet the responsibilities Congress has assigned to us.

In addition to being timely, Freddie has taken a big step forward in enhancing the presentation of our financial results. As we have committed in the past, and many of you have asked, we'll continue to improve our financial reporting package by providing expanded disclosures and updating existing data with new information. Both Patti and Buddy will address these items in greater detail. We hope today's release of new information about our ABS portfolio and business segment information under our Adjusted Operating Income metric will be useful to investors. Third, as we disclosed in our release, we have made significant

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progress towards fixing our internal control matters. To summarize, as of today, we've remediated three of the identified six material weaknesses and we've implemented controls, which we believe will be sufficient to remediate the remaining items in the near future. Along with returning to timely reporting, this step is crucial for the purpose of becoming an SEC registrant - a process we expect to initiate in the first half of this year.

Finally we've taken tangible steps to improve the profitability of our new guarantee business by implementing several pricing increases and adjusting things more on a price-to-risk basis in our single-family business as well as tightening our credit standards. In addition, we've taken steps to mitigate the impact of volatility on our financial results and on our capital levels. While these actions have taken a great deal of time and effort, our release today should underscore that Freddie Mac is a company that places a high value in keeping its commitments. Achieving these goals was crucial to the ongoing execution of our mission and success of our company for our shareholders. While the financial impacts of market volatility and credit deterioration have made our recent financial results suffer, real improvements in our company's infrastructure and profitability of new business makes me very optimistic about our future prospects when we emerge from the current downturn. Patti and Buddy will now take you through these items in more detail and I'll turn things over to Patti.

Patti Cook - Freddie Mac - Chief Business Officer

Thanks, Dick. The fourth quarter was clearly unprecedented from a housing and capital markets perspective. And as a result, our credit guarantee and investment businesses were significantly impacted by this turmoil. In my comments, I'll address the challenges we faced in the fourth quarter and the actions we took to improve the go forward outlook. Although difficult to see in our financial results, the long-term prospects for both of our businesses are bright.

There are six themes that I want to highlight that address these conflicting observations. First, house prices declined significantly in the fourth quarter at an estimated 4 to 5 percent value-weighted rate on our portfolio across the U.S. as a whole. Second, spreads on mortgage assets widened significantly in the fourth quarter and expectations for future credit losses in our guarantee business increased, producing significant losses. However, the majority of the mark-to-market losses are not expected to be realized. Third, Freddie Mac and GSE share as a whole continued to gain in the single-family and multifamily markets during the fourth quarter. Fourth, Freddie Mac continued to tighten credit, raise fees and widen spreads in our single-family and multifamily businesses. Fifth, while the 2007 single-family book is clearly worse than the 2006 book, it appears that beginning late in the fourth quarter the underlying credit quality of new single-family mortgage originations began to improve. Finally, following our preferred issue in December, and the recent announcement by OFHEO that the portfolio cap will no longer be in place as of March 1st, we continue to manage our capital prudently to provide for reasonable growth in our business as well as maintain capital sufficiency through the current credit downturn.

So first, the decline in house prices in the fourth quarter and the impact on credit. The large decline in house prices in the fourth quarter has led us to increase the expected decline in our median house price path to approximately 15 percent peak to trough, causing us to increase our expectations for expected default costs. While the relationship between house prices and defaults is clear, the forecast for expected defaults is not precise. This is particularly true in this environment as the rate of decline nationally is without recent precedent and the lack of correlation between unemployment and declining house prices is also unusual. Recognizing the challenges in forecasting defaults and losses, our best estimate is that the net present value of total expected default costs will range between \$10 and \$15 billion given these assumptions. This compares to our prior guidance of \$10 to \$12 billion. This estimate of expected default costs is about half of the GO on our fair value balance sheet. To realize default costs of this magnitude, you would need 3.5 percent defaults with 25 percent severities. To put this into historical perspective, our worse book in the early '90s realized about 2.5 percent defaults. While house prices nationally may decline further this time, the unemployment picture is much better. It is also worth noting that our current serious delinquencies are 65 basis points, well below a level needed to reach 3.5 percent defaults and well below the level of other prime market benchmarks.

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Next, fair value. Fair value declined significantly during the fourth quarter, about \$17 billion after tax, bringing the year-to-date decline to approximately \$25 billion after tax. This markdown is split about evenly between the guarantee business and the investment business. I will address both.

While the credit quality of our retained portfolio remains very high, with 57 percent in agency securities and 33 percent in non-agency securities, of which 96 percent is currently AAA-rated, spreads widened dramatically. This resulted in a pre-tax mark-to-market loss of \$14 billion during the quarter, almost \$10 billion of which was associated with our ABS portfolio, which sustained a 200 basis point widening of spreads.

During 2007, the ABS portfolio widened from a spread of 28 basis points to 335 basis points. However, given the structure of these securities and the resulting subordination, we do not believe any significant realized losses are likely and therefore have not recorded any impairments. Similarly, for the agency and CMBS components of the portfolio, we do not expect to realize these OAS losses. Since we do not expect to realize any meaningful losses, the reversal of these marks will, over time, emerge as higher core spread income in fair value.

During 2007, the overall spread on the retained portfolio therefore increased from 27 basis points to 104 basis points. In addition, the wider spreads are also creating expanded purchase opportunities in the agency mortgage securities market. Let me just remind you that all of these prices that we use for the portfolio are reflective of third party marks obtained from pricing services on the street.

I want to address the ABS portfolio in a little more detail. The non-agency ABS were critical to our efforts to meet our affordable lending objectives and allowed us to invest in nonprime markets with substantial credit enhancement. Despite the continued deterioration of the housing market and increases in non-prime delinquencies, we remain comfortable with our risk position on these assets. In order to provide a better understanding of how we come to this view, we have posted an extensive write-up of the ABS portfolio on the Web site with this release. Remember, all of the bonds held in this portfolio are plain passthrough securities and contain no CDO exposure. A couple of quick points. Look at slide eight. The circled items show the results of three stress test scenarios we run on the subprime portfolio. The results show that at a 50 percent default, 50 percent severity experience, our projected losses on that position are less than \$1 million. We even included two more onerous scenarios, not because we think they are likely but to show that even in these severe cases anticipated losses are far below the severe market estimates we have seen.

Let's move to the decline in fair value of the guarantee business. The g-fee business was affected by declining house prices which resulted in the current loan-to-value ratio of our portfolio increasing as delinquency rates increased and mortgage-related credit spreads widened further. The combination of these factors led to an expectation of higher expected default costs and significantly higher risk premiums.

The result is a decline in the fair value of the g-fee business of about \$9 billion for the quarter and \$13 billion for the year, after tax. About half of the increase is a function of higher expected default costs. The other is the result of market illiquidity in higher risk premiums which we capture in our third party mark-to-market process. Said another way, if we were relying solely on our own models to price our GO, our mark-to-market change for the year would have been about half as much. Remember in the fourth quarter of 2005, we moved to third party pricing for this portfolio and as a result, are picking up the risk premiums in the same manner as we do in the retained portfolio. If our expectations for default costs are close to what we ultimately realize, the portion of the mark-to-market loss associated with wider spreads will come back to fair value. This volatility in fair value raises the question of its usefulness as an earnings measure. We believe fair value is a useful measure for evaluating the business over longer term periods. It's not as useful over short time periods when spread volatility can dwarf the economic spread being earned in both businesses. This is particularly true for Freddie Mac as we have both the intent and capability to hold to maturity. As a result, we believe the additional non-GAAP measure of Adjusted Operating Income will help in evaluating the business.

Now let's move on to the brighter portion of my comments, GSE share. During the fourth quarter, as other mortgage investors pulled back from the market, Freddie Mac continued to support our customer's liquidity needs and provided needed stability

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to the single-family and multifamily mortgage market. As a result, volumes in the multifamily business doubled for the year and the growth rate of the single-family business rose to 18 percent, significantly out pacing the growth of MDO. Single-family GSE share also increased to approximately 72 percent in January 2008, from about 40 percent in 2006. We would expect the GSE share to remain high in 2008. While this growth bodes well for long term prospect it does entail some near term risks due to the adverse credit environment. However, in this environment we have improved fees and tightened our credit box, which is my next theme.

We've made four changes to our prices in credit guidelines beginning in August of 2007. Our most recent price increase was announced for implementation June 1st. The intention of the changes was to address the increase in the riskiest component of our deliveries by introducing risk-based pricing and by tightening credit terms. We believe these actions will have a material impact on returns in this business. In fact, we have begun to see the improvement in the credit quality of our deliveries in the last couple of months. Some highlights of the changes include: we reduce the maximum LTV/TLTV to 97 percent on all standard and affordable products with FICOs below 700; we eliminated NINA, NIVA and no ratio loans in October and we introduced new risk-based pricing fees in November, effective in March. For example loans with LTVs greater than 70 percent have an additional fee determined by FICO ranging from 75 to 200 basis points. This is the first time Freddie Mac has initiated changes of this magnitude. The combined effect of these price actions means that going forward, Freddie Mac will benefit from significant better pricing that should approach the mid-30s in basis points for new guarantees in the second quarter. This projected increase is dependent on the mix of business it has received.

Nonetheless, it remains true that the overall credit quality of our 2007 deliveries was worse than 2006 and the result of the GSE share, the overall market increasing primarily through the delivery of riskier loans. We believe this trend peaked in November. While it is too early to claim victory, we have seen a meaningful improvement in the quality of our deliveries.

We have observed the improvement in our underlying loan quality by examining improvements in the worse quintile where a majority of the expected losses exist. Examples of these changes include, in January, loans with total LTVs greater than 90 percent declined 13 percent from the peak, FICOs less than 620 declined five percent and low and no dock loans declined 14 percent.

Lastly, we must continue to manage capital responsibly as we consider various growth opportunities, particularly without the portfolio cap. We expect the single-family and multifamily businesses to grow in 2008, as the markets need for liquidity remains. We're also taking steps to help maximize the returns in the retained portfolio, beginning with the redeployment of our monthly runoff. Net increases in the retained portfolio will be weighed against the availability of regulatory capital in the market environment. We always look for opportunities to increase shareholder value through highly profitable investments and believe that we can manage our capital position to execute on those opportunities.

So there you have it - from a business perspective, even in this difficult business environment, with house prices declining, expected default costs rising and risk premiums widening, we are increasingly able to improve the franchise value of the firm. We continue to benefit from a relatively strong credit risk position and market position. Our ABS portfolio has continued to demonstrate its resiliency to underlying subprime losses. We have taken steps to continue our mission and improve our business and we are experiencing pricing power and credit standard tightening in our g-fee and multifamily businesses. All of these business drivers will contribute to improved returns over the long term. With that, I'll turn it over to Buddy.

Buddy Pizel - Freddie Mac - CFO

Thanks, Patti, and good afternoon, everyone. As Dick said, we intend to be a company that does what it says. From the finance side we've begun to demonstrate that in 2007 - we've improved our GAAP reporting and introduced our new non-GAAP framework, we've sunset the bulk of our control issues, we significantly expanded our disclosures, we don't have impairments on the ABS portfolio, and even with all of the additional work, we've returned to timely reporting. Lastly, our capital is about where we expected it following our preferred issuance in December. That's a lot of progress in one year and we'll continue

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down this track in 2008. We'll continue to accelerate our financial reporting timelines. We'll complete the strengthening of our control environment and become an SEC registrant. We said before that we aim to be a leader in disclosure and transparency and we've taken a number of actions today to continue our delivery on that commitment. We posted an enormous amount of information this morning with our release. Specifically, we provided new information on the house price path, our ABS portfolio and our new Adjusted Operating Income metric and results.

Another important piece of our story is the evaluation of our counterparty exposures with a focus on the MI companies and the monoline insurers. We intend to publish that analysis of this risk prior to our investor day and then discuss all of these materials at the investor meeting on March 12th. Given the intense focus on capital, and the significance of the changes we've made, I will emphasize our GAAP results today. And remember, all current and historical GAAP numbers presented reflect our accounting changes. A high-level GAAP take away from our release are one, net loss for the fourth quarter was \$2.45 billion, roughly double the loss of the third quarter. Two, adverse long term interest rates and credit spreads experienced in the third quarter actually worsened through year-end, producing greater mark-to-market effects than we had estimated on our third quarter call. Three, as we expected, we have not seen any impairments on our ABS portfolio. Four, our provision for credit losses remain substantial. And lastly, given all of that, as of the first of the year, Freddie Mac had an estimated core capital level of \$38.9 billion, that's \$12.4 billion greater than our regulatory minimum so we remain well capitalized for our risks.

So, let's start with capital, and if you'd please turn to slide two. Line seven at the bottom of the slide shows that after January 1, 2008, Freddie Mac had an estimated core capital level of \$38.9 billion, which translates into an excess of about \$4.5 billion over the 30 percent mandatory target capital surplus requirement.

As you can see, we did benefit from the adoption of FAS 159, the fair value option. While we originally estimated that FAS 159 adoption would have little to no impact on our capital position, the significant interest rate move we experienced in late 2007 created a one-time adoption adjustment upwards of \$1 billion in our core capital. So all in all, our capital position at January 1, 2008 is about where we expected it to be following our preferred issue. That gives us sufficient capital to provide for modest growth in our core businesses and certainly any relief on the 30 percent will give us greater flexibility.

Now let me take you briefly through slide three that shows the effects of our accounting policy changes and then we'll turn our attention to our GAAP results. As we discussed from early 2007, while our previous accounting policies are acceptable under GAAP, many investors struggle to understand our business results on an absolute basis and also struggled with our comparability to Fannie. Slide three displays the effect of changing two accounting policies for our guarantee business that should improve both these issues. The main revenue impact from changing the policy is that we now report our guarantee fees in one line, irrespective of whether the credit risk is on- or off-balance sheet. To make that change from our previously reported numbers, we transferred guarantee fee revenues out of net interest income and into the management and guarantee income line shown on lines one and two respectively.

On the credit side, two big changes. We no longer record mark-to-market credit adjustments to the on-balance sheet Freddie securities. The elimination of that mark is shown on line three. And instead, we will provide for incurred losses for those holdings through our FAS 5 provision. This increased provision is shown on line seven. While these changes reduce the magnitude of our year-to-date third quarter loss, they did not increase our capital as of September 30, because 2006 and prior years net income were cumulatively adjusted downward by approximately the same amount. Turning to slide four, let's go through our GAAP results. Revenues from our investment and guarantee activities shown on lines one and two were essentially consistent with those of the third quarter.

Let me take you quickly through the major mark-to-market items behind lines three and line eight and describe our exposure to future volatility. Line three, which includes most of our interest-rate related marks, worsened in the fourth quarter as a 51 basis point decline in long-term interest rates produced net mark-to-market loss of \$2.3 billion on our portfolio of derivatives. This also caused a reduction in the fair value of our guarantee asset of \$843 million. For the full year, these uneconomic marks reduced our GAAP results by over \$4 billion pretax, or close to \$2.6 billion after tax. For this exposure going forward we've taken two steps. First, as of the first of the year, we implemented FAS 159, the fair value option for a subsegment of our securities

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portfolio. By doing this, going forward, gains and losses experienced in the GA will be significantly offset by market value changes in the mortgage portfolio. Also, we are reinitiating hedge accounting to begin associating interest-rate hedges with underlying debt and the assets they economically hedge.

As we continue to implement this change throughout 2008, the amount of the derivatives portfolio that are subject to mark-to-market through our income statement will decline, somewhat reducing the potential for the disruptive marks. Turning to credit marks included in line eight. In the fourth quarter, mark-to-market items increased as continued widening in the credit market spreads on new mortgage securitizations produced a day one loss of \$1.3 billion and a mark-to-market loss of \$736 million on the delinquent loans we purchased out of securities. For these two items, we've taken several steps. First, as we previously disclosed, starting December 1st, we no longer automatically purchase loans out of securities that are 120 days delinquent. As a result, December delinquent loan purchases fell to \$4 million in UPB, that compares to October and November purchases of more than \$1 billion per month. So mark-to-market losses on significantly lower future purchases will decrease accordingly. However, I should reemphasize, these estimates for - estimates for incurred credit losses on these delinquent loans are already included in our loan loss provision.

The second change we made is one that Patti spoke to, which is to tighten underwriting and improve our guarantee fees. The fee increases take effect in March and in June so as they leg in, we will get some relief on the day one losses. However, these actions are not enough to overcome today's extremely wide market, not model based credit spreads, so we continue to explore other solutions to this issue. Based on all of these actions, we go into 2008 with reduced volatility in our GAAP earnings, which allows us to better manage our capital levels. Finally, I want to draw your attention to line seven. Credit-related expenses and this is our credit provision. While this amount actually declined from the third quarter of 2007 to the fourth quarter of 2007, it's important to remember that the third quarter provision amount was boosted by changes we made in our reserve practices specifically related to the '06 and the '07 book years. As a result, the change from the third quarter to the fourth quarter should not be viewed as a provision that has turned or is trending downward. At year-end, our credit reserve totaled \$2.8 billion which covers approximately the next year and a half of our disclosed, expected charge-offs.

We anticipate that the provision for credit losses will remain high in comparison to recent periods as the U.S. housing market remains under pressure. If you now turn to slide five - earlier Patti walked you through the updates on our credit guarantee portfolio characteristics and our views of house price paths, expected defaults and severities. All of these have worsened from third quarter to fourth quarter and accordingly our overall expected credit losses have gone up. The same factors that influence this increase drove increases in our expected charge-offs in 2008 and 2009 and our fourth quarter provision. On slide five, you can see that our estimated credit losses from '08 and '09 are now 12 and 14 basis points respectively, which combined have increased by \$1.5 billion from our third quarter disclosure.

So in summary, fourth quarter and full-year GAAP results continue to bear a lot of weight from credit expenses and mark-to-market items. On the positive side, our capital is in tact and we've taken a number of important steps to relieve some of the pressure in '08. While we've tried to give you some idea for how these items will move in '08, we'll give you a fuller treatment to 2008 on our investor day in March. And that completes my discussion on fourth quarter and full year GAAP results.

While we've included the Adjusted Operating Income results in our press release, ISS and the Web materials, because they're so new and in the interest of getting to your questions, we would not cover them today. Leave it to say, we're very pleased to introduce what we believe is a much more understandable framework for measuring our business performance and we'll cover AOI in detail at our investor day. So in closing, you put all of that together and we believe we have an excellent long-term franchise and we are all proud and committed to deliver on that future. By year-end, from a financial standpoint, we'll be as well run as any financial institution out there and you have our commitment on that. And with that, let me return things to Dick.

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Dick Syron - Freddie Mac - Chairman, CEO

Thanks, Buddy. You've listened a long time to us, so I'll be hopefully quite brief. First, no one knows how long a house - the housing downturn will be. We've been pretty cautious on our expectations. But clearly our sector is in a rough period that for anyone that is likely on this call is totally unprecedented in our lifetime.

Given this tough environment, we've done a number of what we think are necessary and appropriate things. We took early and decisive steps to raise capital, hopefully in a common shareholder friendly way. We adjusted our pricing and credit requirements to align more closely with risk. Importantly, we've finally become timely in our financial reporting and we're increasing its transparency, usefulness and comparability with other financial institutions. We've grown volume and market share in the guarantee business as the market has begun to come back to us. And now, our regulator, with whom we have a mutually respectful and professional relationship, has announced that they'll be lifting our portfolio cap as of March 1st and we'll be considering the approach they're going to take to the 30 percent surplus over time.

I think maybe, most importantly, we think we're dealing with the situation in a prudent and responsible way. We're not at all claiming that the housing downturn is mostly done. On the contrary, we're assuming that house prices have fallen about one-third as far as they're going to go, peak to trough. That may see pretty cautious or even pessimistic but I think cautious is exactly where you ought to want us to be right now. For all of these reasons, we believe that we will come out of the downturn in a strong, successful form as a competitor and in a sector whose longer-term demographics and growth prospects remain very good. Now, we're very eager to take your questions. Thank you for listening. And we'll open it up to questions.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS) And first line we'll go to is Kenneth Posner with Morgan Stanley. Please go ahead.

Ken Posner - Morgan Stanley - Analyst

Good afternoon and thank you for the disclosures and the Adjusted Operating Income. That's all great stuff that will take us a while to understand. I have a question about this pesky fair value number, which did fall substantially, particularly on a common equity basis for Freddie Mac in the quarter. And I wonder if you could just comment on how you're valuing the guarantee obligation. If I've done the math right, and maybe I didn't, you're valuing the guarantee obligation at 1.5 percent of the credit book and your competitor Fannie Mae seems to be valuing it, again if I did the math properly, at 75 basis points. How can that be and are these the right numbers?

Patti Cook - Freddie Mac - Chief Business Officer

Thanks for the question. I can't speak to how our competitor values their GO, but I can try and be as transparent as possible as to how we do it. And as you noticed in my prepared remarks, we come at that expectation of the present value or future expected default cost in the \$12 to \$15 billion range by looking at a median house price decline, peak to trough of about 15 percent. We look at a Monte Carlo simulation around that in terms of trying to estimate what default probabilities would be on that portfolio.

And that's sort of the interesting statistic I think you need to focus on. It suggested about a 3.5 percent default rate with 25 percent severity. So you in your own mind need to decide whether or not you think that's reasonable. What we do when we go to the market is we go beyond just an assessment of expected default costs with maybe a modest risk premium and actually capture the risk premiums that are in the marketplace in terms of a wider spread on mortgages and mortgage-related assets

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as we ask dealers for a price, for a spread. So the difference between what is on - what is in our fair value balance sheet and our estimate, is that difference in risk premium, which as I said in my comments, we would expect to earn back over time.

Ken Posner - Morgan Stanley - Analyst

That's helpful, thank you.

Patti Cook - Freddie Mac - Chief Business Officer

The other thing that is significant is to look at the delinquencies. Currently we have delinquencies of 65 basis points. So again I think you need to look at 65 basis points of delinquencies and an expectation of 3.5 percent defaults, get used to the \$12 to \$15 billion, then I think you can put the GO on the fair balance sheet in context.

Ken Posner - Morgan Stanley - Analyst

It sounds like is the difference is in the risk premium. Thank you.

Patti Cook - Freddie Mac - Chief Business Officer

Your welcome.

Operator

Our next question from the line of Paul Miller with Friedman Billings Ramsey. Please go ahead.

Annette Frank - Friedman Billings Ramsey - Analyst

Good afternoon. This is Annette Frank from Friedman Billings Ramsey. On your credit loss forecast for 2008 and 2009, the 12 and 14 basis points - could you talk about your underlying assumptions in terms of what you expect for house price declines nationwide and also on your severity of losses.

Dick Syron - Freddie Mac - Chairman, CEO

I think we said for housing price declines, we expected about another 10 percent from what we've experienced so far.

Patti Cook - Freddie Mac - Chief Business Officer

And, I think the other thing to conclude, is that there is a connection between that 12 and 14 basis points over time with the net present value of EDC that we alluded to, which is in the 12 to 15.

Annette Frank - Friedman Billings Ramsey - Analyst

And um --

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Patti Cook - Freddie Mac - Chief Business Officer

Go ahead.

Annette Frank - Friedman Billings Ramsey - Analyst

No, just a quick follow-up. On the cure rates you're seeing now on the delinquent loans, could you give us some indication on where this is right now versus where it was in 2005 and 2006?

Buddy Pizel - Freddie Mac - CFO

When we looked -when we look at the first year of cure rates, historically, they were trending about 45 percent and the first year cure rates on the '07 book have trended downward a little bit, so it's lagging where we've seen historically and we'll see where that goes in the second year, whether it rebounds or whether it continues.

Annette Frank - Friedman Billings Ramsey - Analyst

Okay. Thank you very much.

Operator

And next we'll go to the line of David Hochstim with Bear Stearns. Please go ahead.

David Hochstim - Bear Stearns - Analyst

Two questions. One is, could you just talk about how you would allocate capital between growing the retained portfolio and growing the guarantee business. I mean it seems that returns are very attractive in the guarantee business with higher fees and yet you have massively wider spreads on a range of mortgages available for purchase. Obviously you had some capital constraints but if you can buy mortgages from the retained portfolio without having to take additional credit risk, wouldn't that be a good thing and wouldn't that have a secondary benefit of causing mortgage spreads to tighten and help solve some of the problems with the marks and the balance sheet.

Patti Cook - Freddie Mac - Chief Business Officer

Good question, David. Thank you. First of all, ROEs in all three businesses really, the single-family business, the retained portfolio and the multifamily business have all improved dramatically since the last time we all spoke. I think when we think about the g-fee business it is front and certain to the core of our mission, which are liquidity, stability and affordability. And we think with our new price increases we are pricing appropriately for the risk imbedded in that portfolio. It's off balance sheet, the capital requirement is relatively low, we're comfortable that we're in a position to accommodate 10 percent growth rate in that business and similar increase in multifamily.

I think on the retained portfolio, that issue is a little bit harder. From two perspectives. First of all, it uses more capital than the other two from a regulatory perspective. And second while there are really good opportunities right now in agency mortgages, some of the widening and spreads we've seen on the retained portfolio have constricted the origination of agencies - of non-agency mortgages, namely ABSs in a way they're not readily available. So I think as we go forward, we have got to consider and continue to evaluate the opportunity, relative to the amount of regulatory capital, relative to the timeliness in the amount of 30 percent roll back.

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David Hochstim - *Bear Stearns - Analyst*

Aren't there opportunities in the market where you could in fact provide more valuable liquidity by buying I guess pools from other holders or investors, even if it's not new production. There is no liquidity in the market except in the agency securities market and that's a fundamental part of the problem.

Patti Cook - *Freddie Mac - Chief Business Officer*

We are active though, in sort of even in bulk space, so away from flow. Our bulk purchases last year were probably about \$100 billion. So we did a lot of that last year in terms of trying to provide liquidity in non-flow space to loans that were on balance sheets and we'll continue to do that where we see mortgages that are consistent with our charter, that are in the conventional conforming space.

Buddy Pizsel - *Freddie Mac - CFO*

But David, one of the things that we're - the way we're approaching the business, is we're going to be a little cautious with our capital at the beginning of the year. We have the amount of capital that is - will allow us to manage the growth in the g-fee business and be careful with the growth in the retained portfolio because we want to see where credit goes. So we're actually deploying capital on a fairly prudent basis as we get out of the blocks early in the year.

David Hochstim - *Bear Stearns - Analyst*

Could you clarify, Patti, what you said about the increase in fees, delivery fees and guarantee fees, that the increase to 30 basis points, that includes the delivery fee amortized over the life of the security? And are you going to take any of those upfront or just enough to manage the loss on an origination?

Patti Cook - *Freddie Mac - Chief Business Officer*

I'm not sure I fully understand your question. The fee increases were a combination of delivery - they were in delivery fees as opposed to in core guarantee fee.

David Hochstim - *Bear Stearns - Analyst*

But haven't you raised guarantees fees also for certain types of product.

Patti Cook - *Freddie Mac - Chief Business Officer*

Yes.

David Hochstim - *Bear Stearns - Analyst*

Okay. So you mentioned an increase in the beginning of the second quarter I guess.

Patti Cook - *Freddie Mac - Chief Business Officer*

Oh, yes. Yes.

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David Hochstim - *Bear Stearns - Analyst*

I just wanted to clarify that.

Patti Cook - *Freddie Mac - Chief Business Officer*

Yes. I see. In that target are - is the amortization of delivery fees. They're not taken upfront.

David Hochstim - *Bear Stearns - Analyst*

Would you take some of them upfront to offset the loss that you've been booking every time you create a security?

Buddy Pizel - *Freddie Mac - CFO*

No, our accounting, David, requires us to amortize that - so it comes in on an amortizing way. When we think about the economics of negotiating or transacting a fee we think of it on an amortized basis even though the cash comes in the door right away.

David Hochstim - *Bear Stearns - Analyst*

Okay. Thanks.

Operator

Our next question is from the line of Brad Ball from Citi. Please go ahead.

Brad Ball - *Citi - Analyst*

Thanks, Buddy, I appreciate given the time constraints that you do not want to delve too far into AOI, but I wonder if you can give us some high-level views on what you're accomplishing with AOI. If you look at your presentation, it looks like the bottom line differences between your AOI earnings and your GAAP earnings are substantial. It looks like \$5 billion differential.

Just at a glance, it looks like you're essentially eliminating from Adjusted Operating Income, all of the stuff that's bad, and keeping all the stuff that's good - so if you could clarify if that's actually the case. But it really does look like what you're doing is recognizing in AOI, the things in your business that are not economically hedged and basically amortizing those things that are. Could you give us just at least some color on that? Thanks.

Buddy Pizel - *Freddie Mac - CFO*

Yes, I mean this all goes to the timing of when we implemented this and the presentation years that we're giving you. If you go back - because the way we apply this, Brad, we went all the way back to 2001. And in those earlier years, its results are negative compared to what we reported and then as you get closer, to the '06 and '07 time frames, '06 is about a push and '07 gets better. So we committed to do this back in November of '06 when the market had not melted down. So the objective was not to make the results look better, the result - the objective was to make the results clearer.

I would take exception to the point that we're amortizing only certain items. We're looking at items that just from an emergence standpoint drop into a quarter and represent a cumulative effect of an approach to the portfolio that is really is thought of on a

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long-term basis and then amortizing that over its intended time frame. So I think you'll see when we go through a better - and more extended discussion of what we're trying to accomplish here, we basically look at both of these business as accrual-based emergence of earnings. The current GAAP framework creates a lot of marks that either accelerates forward or pushes out maybe in an inappropriate time frame the recognition of the emergence of those earnings and what we've tried to do is create a way so that accrual based earnings would emerge from both of the business. To us that makes sense. You guys can get into it and make your own calls but we find it useful in looking at the periodic performance of the business.

Brad Ball - Citi - Analyst

Okay. That's very helpful. Just as a follow-up, can you run this approach by your regulators, either past OFHEO or the SEC, and what have their impressions been and can we hope at the some point, maybe down the road, we could use the AOI income as the basis for establishing an AOI or AOE, adjusted operating equity, and that maybe regulatory capital will come off of that as a base, as opposed to a GAAP equity which is obviously skewed by the volatility in GAAP earnings.

Buddy Pizel - Freddie Mac - CFO

First we have run this presentation by the SEC to make sure that they didn't take exception to either the concept or the disclosure that we provided in the ISS because this will be included in the annual report that we use to start registration. And secondly, we've shared it with OFHEO. I think it's premature to even imply how it will be utilized by our regulator for purposes of capital and quite frankly we're looking at it more from an emergence of earnings than a capital management tool at this point.

Brad Ball - Citi - Analyst

Okay, thanks.

Operator

Our next question is from the line of Howard Shapiro with FPK. Please go ahead.

Howard Shapiro - FPK - Analyst

Hi. Thank you very much. One question for Buddy and one question for Dick, if I could? Buddy, on slide number four, GAAP financial results in the side pack, your line item number three, can you talk to us about how much of that volatility or how much of that Q4 loss would have been eliminated by the prospective adoption of FAS 159? As I understand it, that was not a component in reducing the mark-to-market in fourth quarter.

Buddy Pizel - Freddie Mac - CFO

That's true. And the difficulty with trying to give a sensitivity to where rates move when you put your hedges in place is that it changes as the market conditions change. So from the beginning of '07 until the end of '07, to the first quarter of '08, the sensitivity to interest rates change. They are at this point less than half of what they were in 2007 and that's only giving effect to the GA. And if we continue to implement hedge accounting we would hope to limit that exposure even further.

Howard Shapiro - FPK - Analyst

Okay. That's less than half sounds pretty significant, is that correct?

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Buddy Pizsel - Freddie Mac - CFO

Yes.

Howard Shapiro - FPK - Analyst

Okay and then Dick can I just ask you a question on the 30 percent OFHEO surcharge. What is the legal or regulatory right of OFHEO to keep the surplus in place at this point, now that you're current?

Dick Syron - Freddie Mac - Chairman, CEO

Well I think that the legal or regulatory right comes around to - we have a voluntary agreement with OFHEO.

Howard Shapiro - FPK - Analyst

Right.

Dick Syron - Freddie Mac - Chairman, CEO

As meeting certain elements of these agreements, and material weaknesses would be a consideration. While it's not explicit in it, I would expect where we are with SEC registration would be a consideration. And then we have some, what I would call, mechanical issues such as the exact timing of the separation of the chairman and CEO.

Howard Shapiro - FPK - Analyst

Okay. But once you resolve some of these mechanical issues and SEC registration, do they have any right, considering it's a voluntary agreement, to mandate a continued 30 percent surcharge.

Dick Syron - Freddie Mac - Chairman, CEO

Well I should be clear on some of this. I mean we agree to it, so I suppose it's to a degree voluntariness is debatable. But, to answer your question directly, we think OFHEO has taken the right steps by removing the caps obviously on the portfolio. And by raising the question that it's looking at the 30 percent, we think that's the right approach to take actually for the U.S. economy and the U.S. housing market because as I think was noted earlier in the conversation, the more that we're able to do in some of these markets, the better done right it's going to be for the economy. So I think OFHEO is approaching it in the right way. At the same time they're trying to balance, I think, the current kind of credit condition and be sure that we have sufficient capital. I will tell you, as an institution, in the environment that we're in, we're treating capital a little bit like a scuba diver treats oxygen. We look at it as very important and we're being very cautious on how we approach things, independent of OFHEO's approach.

Howard Shapiro - FPK - Analyst

Fair enough. Thank you very much.

Operator

Our next question is from Eric Wasserstrom from UBS. Please go ahead.

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Eric Wasserstrom - UBS - Analyst

Thanks very much. If I could just follow-up on the question of capital? On slide two you have the pro forma as of January 1st. But as I think about what spread behavior has done between then and today, February 28th, it would suggest that actually the existing capital today would be much lower than that \$4.5, is that not correct?

Buddy Pizel - Freddie Mac - CFO

That's actually not correct. By virtue of what we've done with the GA, we've muted some of that down rate pressure and actually, the way the position - the portfolio's positioned, we actually do much better in a steeper, yield curve environment, so the steepening has actually helped us. So coming out of the blocks as we sit here today, we're ahead of the game to some degree. Now we've seen how fleeting this can be so we're not banking that. But we're certainly in a better position today than we were on January 1.

Eric Wasserstrom - UBS - Analyst

Okay. So if I can just maybe repeat that back to you. Basically it's the benefit of the steepening on the yield curve on interest spread has offset the pressure that would result from credit spread or trading spread.

Buddy Pizel - Freddie Mac - CFO

Yes.

Eric Wasserstrom - UBS - Analyst

Okay. And then just in terms of the loss expectations, can you talk a little bit about the expectation for reserves and whether more is needed as you look across your delinquency pipeline?

Buddy Pizel - Freddie Mac - CFO

Well, when you think about more is leading. GAAP is not providing for the reserves through the end of time. Our reserves cover right now about a year and a half worth of expected losses. The way those - we've laid out what the charge-offs are going to be, net of recoveries. You can see '08 is \$1.7 billion, it goes up to \$2.2 billion in 2010, pretty much the way we've modeled it so far, plateaus.

So from a provisioning standpoint, our estimate would be that '08 should be the high point for provisioning and then it will start to come down on the other side. If you just think about that we're providing for a forward look of about a year and a half or so, that's the way that that would work. So you're not going to see a quick reduction in provisioning, as long as we're seeing this trend. But the one thing I would caution everyone is that it's still very early in seeing what the real charge-offs are going to be. Just look at the ramp from '07 to '08 to '09. That's a lot of uncertainty and it could break either way for us. So we'll have to take this one a quarter at a time and we'll see how it goes.

Eric Wasserstrom - UBS - Analyst

So in other words - let me just make sure I understand you correctly, you would expect your loss experience to be plateauing around 2010 but the peak of provisioning could be this year.

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Buddy Pizel - *Freddie Mac - CFO*

Yes.

Eric Wasserstrom - *UBS - Analyst*

Okay. Thanks very much.

Operator

Our next question is from the line of Moshe Orenbuch with Credit Suisse. Please go ahead.

Moshe Orenbuch - *Credit Suisse - Analyst*

Great, thanks. Could you, Buddy, maybe talk a little bit about how long it might take to get through the SEC registration process and besides the separation of chairman and CEO, what other conditions exist within the consent agreement.

Buddy Pizel - *Freddie Mac - CFO*

For all practical purposes, Moshe, we've already started the process. So we've engaged the SEC in reviewing the accounting changes that we put in. We've engaged the SEC in the introduction of our Adjusted Operating Income and our segment determination so they're getting good coverage on us already. Our intention would be - with the release of our annual report today, we would immediately start the process on a pre-clearing process for them to go through our entire annual report disclosures that would be the basis - the foundation upon which we go through the registration process.

Once we get the feedback on that, and that's - you can't really judge how long that's going to take. Then the literal process we go through - is literally you submit a Form 10 and 60 days from that you're an effective SEC registrant. So, it's really the time it will take for us to engage the SEC and get their feedback on our reporting and disclosures and then start the process. So it's not as long and torturous as some might think.

Moshe Orenbuch - *Credit Suisse - Analyst*

But three to four months would seem reasonable?

Buddy Pizel - *Freddie Mac - CFO*

We've said that we wanted to start the process by mid-year. Three or four months would be in that time frame and then 60 days from that time frame we would be an SEC registrant.

Moshe Orenbuch - *Credit Suisse - Analyst*

Great. Just a quick follow-up. Earlier questioner asked whether your new non-GAAP measure would be used kind of for regulatory capital. About three weeks ago the chair of OFHEO actually used your current non-GAAP measure as part of capital metric and I'm just wondering is that realistic. Does OFHEO look and how do they use that fair value in the capital process.

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Dick Syron - *Freddie Mac - Chairman, CEO*

Under the law, our capital is determined by GAAP. We follow GAAP regulations in a number of areas. It's statutorily specified, so GAAP is the relevant name.

Moshe Orenbuch - *Credit Suisse - Analyst*

I understand that. He did, however, in Congressional testimony use some slides that included leverage measured on a fair value basis.

Buddy Pizel - *Freddie Mac - CFO*

And we provide information to OFHEO and we use it internally to look at fair value, as Patti discussed, and we also have our own economic capital frameworks that gear off of fair value. They're not fair value on a pure unadjusted basis. So we share that information with OFHEO, it's helpful in some respects and they consider it in looking at the overall adequacy of our capital.

Moshe Orenbuch - *Credit Suisse - Analyst*

Thanks.

Operator

Next to the line of Bruce Harting with Lehman Brothers. Please go ahead.

Bruce Harting - *Lehman Brothers - Analyst*

Hi. On the Adjusted Operating Income, I'm just wondering - the investments have the largest contribution from net interest income but not any provisioning or credit costs associated with them. The single-family business has the credit costs less interest income. How are you picking up interest income versus guarantee and other - and what are the separations you're making there? And then another question would be - if you do go back to hedge accounting for GAAP purposes, can you just remind us of some of the issues regarding effectiveness and what will be different from say a couple of years ago before you discontinued hedge accounting, just in terms of potential pitfalls of going back to that? Thanks.

Buddy Pizel - *Freddie Mac - CFO*

Sure. Bruce, as far as the way investment income is allocated across the segments. The amount of investment income that is in the credit guarantee segment is really driven by the amount of capital that is supporting the segment and the free funds associated with that capital. So that's why there is investment income in there and then the balance of the investment income is really the net spread generated by the retained portfolio plus the capital supporting the retained portfolio business. That's the way we've set it up.

On the hedge accounting, we're actually going to enter into our first hedge next week. And we're keeping this very simple and straightforward. We've learned a lot of lessons from the past - in the ways not to do this and we are very, very diligent and we've already had external reviews of the adequacy of documentation, the nature of the hedges that we're going to enter into, will by their nature be extremely effective and we are going to be very, very diligent to make sure we're complying with all aspects of GAAP. And we're going to go into this slowly. So we're not going to, in one shot, lay on massively extensive or complicated hedges. We're going to walk before we run and move into this gradually with a lot of oversight.

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Bruce Harting - *Lehman Brothers - Analyst*

And in terms of net interest income, one last one, Buddy, on, what can we foresee? On the last quarterly conference call I think you highlighted a bottoming in the net interest margin on both a GAAP and perhaps on an adjusted basis. Anything you can comment about cost of funds versus the widening you're seeing on the asset side. And also following up, I think on David's earlier question about the tradeoff between MBS and on-balance sheet. Is there anything you can say to us about how we should be modeling '08 or '09 for how much jumbo you might be putting on the balance sheet at those higher spreads and the remixing of the asset side? Thanks.

Buddy Pizel - *Freddie Mac - CFO*

Yes, Bruce, I would prefer to deal with '08 expectations at our investor day. First of all, that will give us something to talk about. But there are some things that are going on in NIM. If you think about it we put on business in a couple of years in a relatively flat yield curve environment. As that moves forward, you don't - the new business is at a wider, because with the steepening you're getting little benefit for new business, so there are a couple of elements that have to be consider before you think about directional. And then on the question around jumbos, I didn't quite get your question.

Patti Cook - *Freddie Mac - Chief Business Officer*

If we put it on - I think the issue as it relates to jumbo would be, first of all, whether or not its on- or off-balance sheet. I think the suggestion you were maybe making is if we bought jumbo and it were on the balance sheet and how it would that contribute to NIM. And if the spread were wider it would have a positive impact on NIM. I think just to echo what Buddy was saying, The key difference is - the nuance of how the yield curve affects NIM, which is absent when we think of economic margin - the economic margin on these transactions is clearly wider than it has been in some time. But because of the way it's recognized in GAAP, the effect of the yield curve is not giving that transparency.

Buddy Pizel - *Freddie Mac - CFO*

And Bruce, just one last point there. While we've made a lot of judgments in Adjusted Operating Income, we decided it would be impossible to try to adjust out the early spread advantage you get in GAAP versus you get in an OAS basis. So we didn't try to do that. So, it will have an impact on the way that trends.

Bruce Harting - *Lehman Brothers - Analyst*

Just a clarification. When we look back a year from now, will the jumbo opportunity be mostly one that you put in the MBS pools or partly on balance sheet or mostly on balance sheet? Thanks and that's it.

Patti Cook - *Freddie Mac - Chief Business Officer*

Bruce, right now we haven't come to that decision. When you look at jumbos, theoretically there were three options. One it could have gone into TBA but SIFMA as of right now is saying it's not good delivery. We could choose to securitize it in its own security or we could put it on balance sheet and I think it's going to depend on the size of the opportunity, where the securitization of jumbos would actually trade so at this point we haven't made that decision. The other thing we don't know for sure is the MSAs that are going to be eligible and therefore the size of the opportunity at this point is also a bit unclear.

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Bruce Harting - *Lehman Brothers - Analyst*

Okay. Thank you.

Operator

Our next question is from the line of Robert Lacoursiere from Banc of America Securities. Please go ahead.

Robert Lacoursiere - *Banc of America Securities - Analyst*

Thank you. Wonder if you could discuss a little bit about the implications of New York Attorney General's lawsuit against First American in that there maybe, perhaps, widespread problems in terms of appraisals. Have you - what have you been doing to review the loans you have purchased. I imagine you have a rep and warranty issue that you can put these loans back to the original seller if you find they were inaccurate in terms of their appraisals. And in that, could you also give us a - disclose if you actually are and have been, what level of request for repurchases that you're requesting somebody else buy back from the pool?

Dick Syron - *Freddie Mac - Chairman, CEO*

Well one, our level of request for repurchases I believe has gone up. Two, we do have reps and warranties that we can use. Three, we have increased the resources and efforts that's we're putting towards quality control and looking at things. And four, not surprising you, I can't comment at all about our discussions with the attorney general.

Robert Lacoursiere - *Banc of America Securities - Analyst*

Can I follow-up. Could you put some meat around what it means by increasing your purchases. You can give us any numbers whatsoever?

Patti Cook - *Freddie Mac - Chief Business Officer*

Hang on. A couple of things on repurchases. Clearly, as you might expect, they are going up and we've taken a variety of actions that all relate around sort of adding staff so that we're able to review more loans than we've reviewed in the past. So we would expect the repurchase activity similar to within REO, our efforts around modifications to be enhanced during this time period.

Robert Lacoursiere - *Banc of America Securities - Analyst*

If I could bother with a small follow up on that. If you do result in a substantial increase of repurchases, how do you deal with it? Would you deal with it that there would be a loss sharing agreement rather than asking them to repurchase it?

Dick Syron - *Freddie Mac - Chairman, CEO*

In all due respect, you're getting into - you're getting into complex questions that deal with legal issues that deal with how we interact with specific customers and how we also - it's perfectly reasonable for you to try getting an answer to the question where we stand with Attorney General Cuomo, but it's really not appropriate for us to say any more than we've said.

Robert Lacoursiere - *Banc of America Securities - Analyst*

Thank you.

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Operator

Our next question is from Fred Cannon on KBW. Please go ahead.

Fred Cannon - *KBW - Analyst*

Thanks. Just going back to some of the earlier statements, I wanted to square your discussions on credit losses. I believe Patti said on the GO that you're assuming 25 percent default and 25 percent severity, which suggests a 87.5 basis point cumulative loss. On your slide where you show the expected credit losses in '08 and '09, you have 12 basis points in '08 and 14 in '09. I'm wondering is that 87.5 basis points going to be consistent with your expectations with your losses looking forward.

Buddy Pizel - *Freddie Mac - CFO*

Yes. These things do square. Included in Patti's number are three things. One are charge-offs, two is REO expense and three is lost interest. What is represented on the slides are just the charge-offs and the lost interest then there is a present value, future value disconnect between the two but they all do add together and they do reconcile.

Fred Cannon - *KBW - Analyst*

Okay. Thank you.

Dick Syron - *Freddie Mac - Chairman, CEO*

Operator, can we please have one more question.

Operator

Absolutely. And that will be from the line of Thomas Mitchell with Miller Tabak. Please go ahead.

Thomas Mitchell - *Miller Tabak - Analyst*

I guess the larger question I have is looking at your overall book of business, and looking at how much trouble the American homeowner appears to have gotten themselves into or has been pushed into, it's hard to reconcile in a way your mandate or your fulfillment of mission with how much people seem to need and how little the federal government is doing and essentially the kind of growth rates you've had. Can you address why you think that we're going to get out of this without a whole lot more help than we've had, please?

Dick Syron - *Freddie Mac - Chairman, CEO*

Well I'm not running for anything. But, look; I think we had a situation clearly where we did have a bubble in the housing market. That's why we've seen these corrections not generated by exogenous economic factors outside of housing. I think we probably were a little too aggressive in our ambitions on home ownership overall and affordable home ownership. But if you look at this over the longer run, there is growth in population, there is growth in immigration, Americans basically like to live indoors and there is going to be in the longer term a growth of demand for housing once we get through this correction.

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And the final point is, I would say, that one thing that this sure has demonstrated to me, and I think have increasingly demonstrated to a lot of other people, is the importance of having institutions such as the GSEs that provide what stabilization there is. This is a very ugly situation we're in in the United States housing market now. I would not want to contemplate how much more ugly it would be if there were not GSEs.

Thomas Mitchell - *Miller Tabak - Analyst*

That's a good point. The other question I had was on this fair value \$14 billion or whatever it was on the fourth quarter. I think I'm close on that. And the question is, what would it take to move that from essentially an observation to having to take a markdown? What would be the threshold on that?

Patti Cook - *Freddie Mac - Chief Business Officer*

The change would be our expectation that losses are probable. So if the housing market were to deteriorate significantly from here so you could begin to contemplate 50 percent defaults and 50 percent severities or 60 percent defaults and 50 percent severities then we might be in a position to consider some impairments, but even at that level the realized losses are modest. So it's really how, if it becomes more likely that those scenarios are realized and right now we're a long way away from those.

Dick Syron - *Freddie Mac - Chairman, CEO*

This is Dick Syron. I just want to rush things to a close to say we've taken an hour and 15 minutes of your time during a day when probably a lot of things are going on. We hope we presented rather, clearly and hopefully with great transparency what is going on with us. These are complicated issues. There were a number of good questions and we look forward to seeing many of you in New York at our investor day on March 12th when we can get into these things in even greater detail if you like. So thank you very much for your patience and your interest.

Ed Golding - *Freddie Mac - Sr.VP of Investor Relations*

Thank you. That concludes our call. Operator can you please tell about the replay number. Thanks.

Operator

Certainly. And ladies and gentlemen, this replay started today at 3:30 p.m. eastern and will last until March 13th at midnight. You may access the replay at any time by dialing 1-800-475-6701, international parties please dial 320-365-3844. The access code is 909706. Those number again is 1-800-475-6701 or 320-365-3844 and the access code, 909706. That does conclude your conference for today. Thank you for your participation. You may now disconnect.

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