

September 8, 2008

Fannie Mae and Freddie Mac Announcement

Over the weekend, the Treasury announced plans to place Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) into a conservatorship which will be overseen by the Agencies' newly appointed regulator, the Federal Housing Finance Agency (FHFA). Treasury had previously hoped that the Housing Bill, signed in July, would restore market confidence in the Agencies and allow them to raise the necessary equity capital to weather the current housing downturn. In the end, continued dislocation within debt markets threatened the integrity of the financial system and required the action taken over the weekend.

Key aspects of the announcement:

- FHFA takes control of the entities in an effort to conserve assets, calm markets, and fulfill their mission with respect to the housing market.
- Current management will be replaced with FHFA appointed individuals.
- Treasury will purchase \$1 billion of new Senior Preferred Stock issued by each Agency, paying 10% cumulative dividends (fact sheet attached).
- Treasury agrees to purchase additional Senior Preferred Stock in any period, where capital levels fall below zero, to restore the entities to a positive capital position. In aggregate, Treasury will purchase up to \$100 billion of Senior Preferred Stock per Agency.
- Treasury acquires warrants to purchase common stock totaling 79.9% on a fully diluted basis with an exercise price near \$0.

- Dividends on Common and existing Preferred Stock are suspended and may not be paid without Treasury approval.

Most importantly: Scheduled interest and principal payments on Senior and Subordinate Agency Debt and Agency Mortgage Backed Securities will continue to be paid on a timely basis.

The severity and duration of the housing decline will be key factors in determining the amount of losses ultimately realized by Fannie and Freddie, the amount of impairment to common and preferred stockholders, and the amount of capital investment required of the Treasury.

The biggest beneficiary of yesterday's action has been the agency mortgage passthrough market which represents approximately 40% of the U.S. Investment Grade bond market. This morning, spreads are 30 to 40 basis points tighter relative to Treasuries which translates into an approximately 2% increase in mortgage passthrough prices while prices of US Treasuries securities remain relatively unchanged. This spread movement is particularly significant because it results in an immediate drop in the prevailing mortgage rate of 30-40 basis points. In addition, while not quite as dramatic, Agency CMO spreads are tightening in line with the improvement in mortgage passthrough spreads.

Agency senior and subordinate debentures are also much tighter this morning, improving as much as 20 basis points in longer senior debt maturities and as much as 30 basis points in shorter dated maturities and subordinate debt is as much as 200 basis points tighter versus Treasuries. Government support has certainly been the basis for the tightening. However, the new financing arm for the agencies, which will allow them to fund future purchases of mortgage securities with the New York Fed, will lead to a reduction in future issuance of non-call and callable agency debentures.

With preferred and common stockholders situated below the Treasury investment point, markets have punished those assets. Existing preferreds have fallen in price to trading levels of 5-10% of par. And common stocks (FNM and FRE) are now trading near \$1/share, both significantly lower on the day.

Corporate spreads are relatively unchanged following the bailout of the Government Sponsored Enterprise (GSEs). The market continues to focus on fundamentals and technicals, which we believe remain weak despite valuations that appear compelling versus historical levels.

We'll continue to keep you apprised of developments within the financial markets as they take place.

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FEDERAL HOUSING FINANCE AGENCY



FACT SHEET

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*****EMBARGOED UNTIL 11AM*****

QUESTIONS AND ANSWERS ON CONSERVATORSHIP

Q: What is a conservatorship?

A: A conservatorship is the legal process in which a person or entity is appointed to establish control and oversight of a Company to put it in a sound and solvent condition. In a conservatorship, the powers of the Company's directors, officers, and shareholders are transferred to the designated Conservator.

Q: What is a Conservator?

A: A Conservator is the person or entity appointed to oversee the affairs of a Company for the purpose of bringing the Company back to financial health.

In this instance, the Federal Housing Finance Agency ("FHFA") has been appointed by its Director to be the Conservator of the Company in accordance with the Federal Housing Finance Regulatory Reform Act of 2008 (Public Law 110-289) and the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4501, et seq., as amended) to keep the Company in a safe and solvent financial condition.

Q: How is a Conservator appointed?

A: By statute, the FHFA is appointed Conservator by its Director after the Director determines, in his discretion, that the Company is in need of reorganization or rehabilitation of its affairs.

Q: What are the goals of this conservatorship?

A: The purpose of appointing the Conservator is to preserve and conserve the Company's assets and property and to put the Company in a sound and solvent condition. The goals of the conservatorship are to help restore confidence in the Company, enhance its capacity to fulfill its mission, and mitigate the systemic risk that has contributed directly to the instability in the current market.

There is no reason for concern regarding the ongoing operations of the Company. The Company's operation will not be impaired and business will continue without interruption.

Q: When will the conservatorship period end?

A: Upon the Director's determination that the Conservator's plan to restore the Company to a safe and solvent condition has been completed successfully, the Director will issue an order terminating the conservatorship. At present, there is no exact time frame that can be given as to when this conservatorship may end.

Q: What are the powers of the Conservator?

A: The FHFA, as Conservator, may take all actions necessary and appropriate to (1) put the Company in a sound and solvent condition and (2) carry on the Company's business and preserve and conserve the assets and property of the Company.

Q: What happens upon appointment of a Conservator?

A: Once an "Order Appointing a Conservator" is signed by the Director of FHFA, the Conservator immediately succeeds to the (1) rights, titles, powers, and privileges of the Company, and any stockholder, officer, or director of such the Company with respect to the Company and its assets, and (2) title to all books, records and assets of the Company held by any other custodian or third-party. The Conservator is then charged with the duty to operate the Company.

Q: What does the Conservator do during a conservatorship?

A: The Conservator controls and directs the operations of the Company. The Conservator may (1) take over the assets of and operate the Company with all the powers of the shareholders, the directors, and the officers of the Company and conduct all business of the Company; (2) collect all obligations and money due to the Company; (3) perform all functions of the Company which are consistent with the Conservator's appointment; (4) preserve and conserve the assets and property of the Company; and (5) contract for assistance in fulfilling any function, activity, action or duty of the Conservator.

Q: How will the Company run during the conservatorship?

A: The Company will continue to run as usual during the conservatorship. The Conservator will delegate authorities to the Company's management to move forward with the business operations. The Conservator encourages all Company employees to continue to perform their job functions without interruption.

Q: Will the Company continue to pay its obligations during the conservatorship?

A: Yes, the Company's obligations will be paid in the normal course of business during the Conservatorship. The Treasury Department, through a secured lending credit facility and a Senior Preferred Stock Purchase Agreement, has significantly enhanced the ability of the Company to meet its obligations. The Conservator does not anticipate that there will be any disruption in the Company's pattern of payments or ongoing business operations.

Q: What happens to the Company's stock during the conservatorship?

A: During the conservatorship, the Company's stock will continue to trade. However, by statute, the powers of the stockholders are suspended until the conservatorship is terminated. Stockholders will continue to retain all rights in the stock's financial worth; as such worth is determined by the market.

Q: Is the Company able to buy and sell investments and complete financial transactions during the conservatorship?

A: Yes, the Company's operations continue subject to the oversight of the Conservator.

Q: What happens if the Company is liquidated?

A: Under a conservatorship, the Company is not liquidated.

Q: Can the Conservator determine to liquidate the Company?

A: The Conservator cannot make a determination to liquidate the Company, although, short of that, the Conservator has the authority to run the company in whatever way will best achieve the Conservator's goals (discussed above). However, assuming a statutory ground exists and the Director of FHFA determines that the financial condition of the company requires it, the Director does have the discretion to place any regulated entity, including the Company, into receivership. Receivership is a statutory process for the liquidation of a regulated entity. There are no plans to liquidate the Company.

Q: Can the Company be dissolved?

A: Although the company can be liquidated as explained above, by statute the charter of the Company must be transferred to a new entity and can only be dissolved by an Act of Congress.



U.S. TREASURY DEPARTMENT OFFICE OF PUBLIC AFFAIRS

EMBARGOED UNTIL 11 a.m. (EDT), September 7, 2008

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FACT SHEET:

TREASURY SENIOR PREFERRED STOCK PURCHASE AGREEMENT

Fannie Mae and Freddie Mac debt and mortgage backed securities outstanding today amount to about \$5 trillion, and are held by central banks and investors around the world. Investors have purchased securities of these government sponsored enterprises in part because the ambiguities in their Congressional charters created a perception of government backing. These ambiguities fostered enormous growth in GSE debt outstanding, and the breadth of these holdings pose a systemic risk to our financial system. Because the U.S. government created these ambiguities, we have a responsibility to both avert and ultimately address the systemic risk now posed by the scale and breadth of the holdings of GSE debt and mortgage backed securities.

To address our responsibility to support GSE debt and mortgage backed securities holders, Treasury entered into a Senior Preferred Stock Purchase Agreement with each GSE which ensures that each enterprise maintains a positive net worth. This measure adds to market stability by providing additional security to GSE debt holders – senior and subordinated-- and adds to mortgage affordability by providing additional confidence to investors in GSE mortgage-backed securities. This commitment also eliminates any mandatory triggering of receivership.

These agreements are the most effective means of averting systemic risk and contain terms and conditions to protect the taxpayer. They are more efficient than a one-time equity injection, in that Treasury will use them only as needed and on terms that the Treasury deems appropriate.

These agreements provide significant protections for the taxpayer, in the form of senior preferred stock with a liquidation preference, an upfront \$1 billion issuance of senior preferred stock with a 10% coupon from each GSE, quarterly dividend payments, warrants representing an ownership stake of 79.9% in each GSE going forward, and a quarterly fee starting in 2010.

Terms of the Agreements:

- The agreements are contracts between the Department of the Treasury and each GSE. They are indefinite in duration and have a capacity of \$100 billion each, an amount chosen to demonstrate a strong commitment to the GSEs' creditors and mortgage backed security holders. This number is unrelated to the Treasury's analysis of the current financial conditions of the GSEs.
- If the Federal Housing Finance Agency determines that a GSE's liabilities have exceeded its assets under generally accepted accounting principles, Treasury will contribute cash capital to the GSE in an amount equal to the difference between liabilities and assets. An amount equal to

each such contribution will be added to the senior preferred stock held by Treasury, which will be senior to all other preferred stock, common stock or other capital stock to be issued by the GSE. These agreements will protect the senior and subordinated debt and the mortgage backed securities of the GSEs. The GSE's common stock and existing preferred shareholders will bear any losses ahead of the government.

- In exchange for entering into these agreements with the GSEs, Treasury will immediately receive the following compensation:
 - \$1 billion of senior preferred stock in each GSE
 - Warrants for the purchase of common stock of each GSE representing 79.9% of the common stock of each GSE on a fully-diluted basis at a nominal price
- The senior preferred stock shall accrue dividends at 10% per year. The rate shall increase to 12% if, in any quarter, the dividends are not paid in cash, until all accrued dividends have been paid in cash.
- The senior preferred stock shall not be entitled to voting rights. In a conservatorship, voting rights of all stockholders are vested in the Conservator.
- Beginning March 31, 2010, the GSEs shall pay the Treasury on a quarterly basis a periodic commitment fee that will compensate the Treasury for the explicit support provided by the agreement. The Secretary of the Treasury and the Conservator shall determine the periodic commitment fee in consultation with the Chairman of the Federal Reserve. This fee may be paid in cash or may be added to the senior preferred stock.
- The following covenants apply to the GSEs as part of the agreements.
 - Without the prior consent of the Treasury, the GSEs shall not:
 - Make any payment to purchase or redeem its capital stock, or pay any dividends, including preferred dividends (other than dividends on the senior preferred stock)
 - Issue capital stock of any kind
 - Enter into any new or adjust any existing compensation agreements with “named executive officers” without consulting with Treasury
 - Terminate conservatorship other than in connection with receivership
 - Sell, convey or transfer any of its assets outside the ordinary course of business except as necessary to meet their obligation under the agreements to reduce their portfolio of retained mortgages and mortgage backed securities
 - Increase its debt to more than 110% of its debt as of June 30, 2008
 - Acquire or consolidate with, or merge into, another entity.
- Each GSE's retained mortgage and mortgage backed securities portfolio shall not exceed \$850 billion as of December 31, 2009, and shall decline by 10% per year until it reaches \$250 billion.