FHFA Supplement to 2021 Annual Reports Submitted by Freddie Mac

The following summaries were prepared by FHFA and provide additional information on selected objectives in Freddie Mac's 2021 Underserved Markets Plan. Discussions with Freddie Mac took place during virtual meetings held the week of June 27, 2022.

Affordable Housing Preservation Market

AHP_MF Rental_E: Develop Offering for Loan Credit Enhancement for Secondary Market Transactions "SMART CE" (Outreach)

Freddie Mac provided additional detail on its SMART Credit Enhancement (SMART CE) product, which it introduced in 2021 to round out a suite of products for small financial institutions. Smart CE enables smaller lenders to transfer multifamily loans off their balance sheet to a custodian; the custodian issues senior class A custodial receipts that Freddie Mac guarantees and junior or subordinate class B custodial receipts that are not guaranteed by Freddie Mac. (The lender retains the "B piece," or first-loss position.) In response to a question from FHFA, Freddie Mac explained differences between SMART CE and a related product, the Seasoned Loan Pool Credit Enhancement, through which Freddie Mac shares credit risk on pools of multifamily loans but the loans stay on the lender's balance sheet. SMART CE provides additional capital relief and creates liquidity through monetization of the loans. The optimal loan pool or deal size of $75 million is designed to limit the cost of securitization and meet the needs of small financial institutions, community banks, and CDFIs. Freddie Mac noted that the SMART CE product is intended for use with workforce or affordable developments.

AHP_Sec. 8_A: Provide Liquidity and Stability Through Section 8 Loan Purchases (Loan Purchase)

Freddie Mac confirmed that its Section 8 loan purchase baselines, targets, and quarterly and annual reports have consistently included units in properties with project-based assistance (Housing Assistance Payments contracts) and units with tenant-based assistance (Housing Choice Vouchers). Units with only tenant-based assistance account for roughly one-third of the units counted under this objective, and approximately 10 percent of units have both tenant-based assistance and project-based assistance. Freddie Mac described how its engagement in the affordable housing preservation space expanded in 2014 and noted that financing for properties with Section 8 assistance is a "core product" that has performed well, even during the COVID-19 pandemic.

AHP_Sec. 515_A: Develop a new offering to preserve properties with USDA Section 515 debt (Loan Product)

Freddie Mac provided more detail on its efforts to help preserve Section 515 properties. In 2021, Freddie Mac finalized a loan subordination agreement with USDA, published a term sheet, and purchased one Section 515 loan. (While Freddie Mac has a Section 515 term sheet, it is able to finance these properties across a variety of multifamily products. This is reflected on various term sheets.) This first transaction was atypical in that the loan fell comfortably within Freddie Mac's credit parameters, and it was relatively large ($4.3 million). Many loans on Section 515 properties have less favorable risk characteristics, such as higher loan-to-value ratios and lower debt coverage ratios. Freddie Mac would likely need to grant a credit policy exception for these deals, especially if the properties don't have Low-Income Housing Tax Credits. In addition, many Section 515 loans are smaller (less than $1 million) and would need to be bundled with other transactions to attract lenders in Freddie Mac's network.

Freddie Mac described efforts to raise awareness of its interest in Section 515 transactions among lenders within and outside of its network. Freddie Mac noted that it has encouraged lenders to reach out with all possible transactions—including those that might need a credit policy exception—and emphasized its goal of supplementing, not replacing, existing executions. It also described direct outreach to borrowers and local nonprofit organizations. Freddie Mac attended industry conferences and met with over 20 borrowers where they discussed their interest in providing financing for properties with USDA 515 loans.

AHP_Sustainability_A: Conduct and Publish a Report on Resiliency Efforts within Multifamily Housing (Outreach)

Freddie Mac described efforts to promote its white paper, *Resiliency Efforts in Affordable Multifamily Housing*, which it published in December 2021. Outreach activities include social media posts, issuing a press release, and including links to the report in external newsletters. Pandemic-related restrictions on travel and in-person meetings have limited the amount of informal feedback Freddie Mac received on the paper. Looking ahead, Freddie Mac plans to analyze ways to align private capital with public incentives to support resiliency in affordable multifamily housing, including through a report on incentives and requirements in state Low-Income Housing Tax Credit Qualified Allocation Plans. Freddie Mac also included in its 2022-2024 Plan a loan product activity to develop an offering to further property-level climate resiliency. This objective builds upon both the 2021 research project and the 2022 project.

Manufactured Housing Market

MH_Comm Govt_C: Purchase Resident-Owned Community Loans (Loan Purchase)

In response to a question from FHFA, Freddie Mac indicated that it provided formal quotes on three Duty to Serve-qualifying manufactured housing resident-owned community (ROC) transactions in 2021 but had informal discussions with the lending community about many more potential ROC transactions. The timeline for a ROC transaction can be lengthy, as the sponsors often have limited experience and may need extra time to provide all of the information Freddie Mac needs to issue a formal quote. Once a formal quote has been issued and the loan is under application, the project sponsor must provide additional information and due diligence that allows Freddie Mac to fully underwrite the loan. For its 2021 loan purchase, the COVID-19 pandemic resulted in additional delays securing necessary approvals from city and state officials.

Rural Housing Market

Rural_LIHTC (Rural)_A: Engage in LIHTC Equity Investment in All Rural Areas (Investment)

Freddie Mac explained why it uses proprietary funds rather than multi-investor funds to invest in Low-Income Housing Tax Credit properties. Using proprietary funds allows Freddie Mac to individually evaluate deals from a risk and return perspective and then determine which deals to include in an investment fund. A proprietary fund approach also allows Freddie Mac to contribute more to individual projects.

Rural_Small MF_Rental_A: Develop a New Offering to Preserve Properties with USDA Section 515 Debt (Loan Product)

See notes on *AHP_Sec. 515_A: Develop a new offering to preserve properties with USDA Section 515 debt (Loan Product)*.

Rural_Small MF_Rental_E: Increase LIHTC Investment in 5- to 50-unit Properties (Investment)

Freddie Mac invested in seven small (5- to 50-unit) LIHTC properties in rural areas in 2021, accounting for approximately 20 percent of its LIHTC transactions This is generally in line with Freddie Mac's typical share of allocations to the rural small multifamily segment. Approximately half of Freddie Mac's rural LIHTC deals were 5-50 unit properties historically. The LIHTC properties supported in the rural market were evenly split between new construction and rehabilitation/preservation.

In response to a question from FHFA, Freddie Mac described challenges to achieving its investment target under this objective. Some of these challenges are specific to the rural market, including a shallow labor pool and workers' difficulty finding a place to live during the construction period. In addition, small developers in rural areas may be more vulnerable to supply chain disruptions than larger developers. In the LIHTC market generally, the recent rise in interest rates has caused significant gaps in deals' capital structure that take time to fill. These delays can significantly extend project timelines.

Rural_HN Populations_B: Increase Technical Expertise in Indian Areas (Outreach)

Freddie Mac explained how the outreach and relationship-building it pursued under this objective in 2021 laid the groundwork for product development and a successful product launch in future years. Freddie Mac focused on educating stakeholders in Indian Areas about its existing conventional loan products. With that background, these stakeholders are better positioned to identify gaps in current offerings and suggest ways that Freddie Mac's products could be tailored to work efficiently and, eventually, at scale on tribal trust land.

Freddie Mac also took steps to begin addressing other challenges that constrain potential homebuyers' ability to get mortgage loans in Indian Areas. These steps include identifying lenders who will aggregate loans on tribal land and subservicers who will take on mortgage servicing in the event of a default and developing an appraisal curriculum. Freddie Mac is also seeking to stand up and support coalitions and advisory groups in 2023, similar to the South Dakota Native Homeownership Coalition, that can help advance any future loan product offering.