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Via Email

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Federal Housing Finance Agency
Multifamily Housing Policy
400 7th Street S.W., Room 9-261
Washington, DC 20024

Re: Public Input on Reducing Fannie Mae and Freddie Mac Multi-Family Business

Dear Corinne Russell and Stefanie Johnson:

This letter is in response to your request for public input on the above referenced topic. My name is Dave Henderson. I am the Co-Head of Commercial Real Estate ("CRE") for PPM Finance, Inc. I oversee the commercial mortgage lending group. PPM is a related company and serves as the investment advisor to Jackson National Life Insurance Company. Jackson is the largest annuity seller in the United States and consistently ranks in the top 15 largest U.S. life insurance companies.

PPM has been focused on lending on multi-family projects since our group was formed in 1995. Currently PPM has a $6 billion commercial mortgage loan portfolio and a $6 billion real estate securities portfolio (made up of CMBS and investment grade REIT debt that PPM purchases). 29% or $1.75 billion of the PPM commercial mortgage portfolio is multi-family. PPM has originated $591 million of apartment loans so far in 2013. 43% of our total PPM commercial mortgage originations in 2010-2013 have been multi-family. PPM has been able to compete effectively with Freddie and Fannie, so my perspective is not one of "complaining about an uneven playing field".

I appreciate the fact that you have opened up this critical question to public comment. I have done this letter in a narrative form that does not specifically address each of the questions you asked in your News Release. However, the narrative does touch on many of the questions. If you need a response that directly addresses the questions, let me know.

I will provide some brief historical perspective before offering my thoughts and suggestions going forward. One key statistic that I recently saw was the percentage of overall multi-family loans held by Freddie and Fannie. The numbers were 29% at EOY 2005 and 43% at EOY 2012. I am not sure these numbers are precise, but I do feel the trend line is accurate.

From my perspective, most of the concerns with the Agencies have come in the last eight years. From 1995-2004, my sense was Freddie and Fannie seemed fine with being a meaningful player in the multi-family capital markets. Since 2005, the objective seems to be that each Agency should be a/the dominant player in the market. With the significant growth of CBMS in the middle of the last decade, the Agencies expanded product offerings to offer interest only, future advances, resizing of loans, flexible lines of credit, underwriting proforma income, competing on the highest quality 'A' product, etc. While some of these offerings have been scaled back, Freddie and Fannie continue to prioritize financing higher quality conventional apartment projects.

Also in the last five years, there has been an even stronger focus to compete Freddie vs. Fannie. In 2009, agency pricing was 200-300 basis points inside of life companies. When asked the question, their rationale was that the other agency was the main competitor rather than the broader market. I believe both agencies still view that the other agency is their biggest competitor.

I feel the reduction in new origination capacity by 10% for 2013 was a prudent first step. I believe an expansion of this approach going forward would be appropriate. The strongest argument for "business as usual" from Freddie and Fannie is that the apartment capital markets could fall apart and that apartment values could crash. I do not believe this would occur for the following reasons:

1. The multi-family product type has been the best performing property type over an extended period of time. It is less cyclical and has offered better returns. Market participants understand this and most would like to expand their multi-family portfolios.

2. Life companies are generally under allocated to apartments. The ACLI industry average is 16.7% of CRE mortgages as of 6/30/13. PPM's current level at 29% would be likely the highest in the industry (or in the top 3). Most life companies would be comfortable expanding to 20-35%. Many life companies have given up trying to originate apartment loans because they believe they cannot compete with the Agencies.

3. CMBS lenders also have trouble originating new apartment loans. CMBS buyers like PPM would love to see a greater percentage of apartment loans in newly originated pools. I believe there is plenty of unused capacity in the public debt markets that could be tapped.

4. I am less familiar with the banking sector, but based on my conversations with bank lending officers, banks desire to have more stabilized apartment loans in their portfolios.

My specific suggestions going forward are as follows:

1. Segment Freddie and Fannie's new activity and portfolios into two categories. One category would be loans where there is believed to be "Significant Liquidity" from other lending segments. The other category would be loans where there is some question on the amount of liquidity ("Not Significant Liquidity") from other sources. You can determine what falls into each category, but my suggestions are as follows:

I. Significant Liquidity:

- Class A and Class B multi-family products with no income restrictions or modest income restrictions (such as the 20/80 guidelines) that are located in first tier and second tier markets (I would suggest MSA's with greater than 300,000 people be the guideline).

II. Not Significant Liquidity:

- Projects in smaller markets (which do not meet the population limits established above) or
- Projects of C quality or below or
- Affordable housing projects. You can define, but would likely include projects with income restrictions on all units, or a meaningful percentage of units. (Would include section 8 and many LIHTC projects).

Senior housing and student housing should also each be put in one of these categories.

Any equity investments, entity level investments or secured or unsecured lines of credit should be prohibited immediately if these programs still exist.

A starting point would be to determine what percentage of overall Freddie and Fannie 2012 and 2013 new business activity falls into each category. Specific new business activity limits on one or both categories could then be established going forward. The key would be to set limits on the Significant Liquidity segment that allows for a systematic wind down of this segment. Let's assume for this example that 2013 activity for both agencies is $57 billion. Assume $40 billion is in the Significant Liquidity category. A sample wind down might be as follows for the Significant Liquidity category:

2013: Limit new activity to $40 billion
2014: Limit new activity to $30 billion
2015: Limit new activity to $20 billion
2016: Limit new activity to $10 billion
2017: Allow no new activity

I believe the other major lending segments (Life Companies, CMBS and Banks) could easily absorb approximately $10 billion of additional capital each year (growing to $40 Billion/year) without any meaningful stress in the multi-family capital markets. This does not even consider the impact of more capitalization from bridge lenders, mezzanine lenders or equity investors.

If it was determined later on that other segments were not picking up the appropriate demand of the Significant Liquidity sector, you could extend the time frame to reduce limits or establish permanent limits at a lower level.

There would not need to be strategic goals to reduce activity in the Not Significant Liquidity category. Limits at the current levels of activity or with measured increases each year (3% or so or on some other formula) would likely make sense.

Long-term it would definitely make sense to have only one agency providing financing in the Not Significant Liquidity area. This system should be in place by 2017 (or whenever the wind down of the Significant Liquidity segment has occurred). I also would suggest that all government or quasi-government real estate groups be folded into one entity that focuses on the Not Significant Segment of the multi-family financing. I see no reason for having a separate HUD/FHA operation.

My proposed approach focuses on the big picture issue of what should be the agency focus in multi-family financing and how we get there (Questions 3 and 4 in your News Release). I would be less concerned about scrutinizing specific lending guidelines or parameters during the transitional period (Questions 1 and 2 in your News Release) if the strategic wind down is on track.

Please feel free to contact me via e-mail at dave.henderson@ppmamerica.com or telephone at 312-634-2555.

Sincerely,

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Senior Managing Director – Commercial Mortgage Lending
PPM Finance, Inc.

Cc: George Green - MBA