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Thank you, Chairman Frank, Ranking Member Bachus, and members of the Committee for inviting me to this hearing on solutions to the subprime market turmoil. Fannie Mae is committed to being part of a solution that keeps people in homes, minimizes market disruption and improves practices and products for consumers. Congress chartered our company for times like these, to provide liquidity to the mortgage market in the bad times as well as the good. Today, a critical segment of the mortgage market and the families who depend on it need the kind of help we can provide. And we are going to help through a broad initiative we call "HomeStay."

Fannie Mae has a history of working with lenders to serve families who don't have perfect financial profiles. "Subprime" is, after all, simply the description of a borrower who doesn't have perfect credit. We see it as part of our mission and our charter to make safe mortgages available to people who don't have perfect credit. In the past several years, for example, we have designed mortgage options to give borrowers with blemished credit access to high-quality, low-cost, non-predatory loans. We also set conservative underwriting standards for loans we finance to ensure the homebuyers can afford their loans over the long term. We sought to bring the standards we apply to the prime space to the subprime market with our industry partners primarily to expand our services to underserved families.

Unfortunately, Fannie Mae-quality, safe loans in the subprime market did not become the standard, and the lending market moved away from us. Borrowers were offered a range of loans that layered teaser rates, interest-only, negative amortization and payment options and low-documentation requirements on top of floating-rate loans. In early 2005 we began sounding our concerns about this "layered-risk" lending. For example, Tom Lund, the head of our single-family mortgage business, publicly stated, "One of the things we don't feel good about right now as we look into this marketplace is more homebuyers being put into programs that have more risk. Those products are for more sophisticated buyers. Does it make sense for borrowers to take on risk they may not be aware of? Are we setting them up for failure?"

As a result, we gave up significant market share to our competitors. At the same time, we continued our careful entry into the subprime market, by and large supporting lenders, products and practices that met our standards, and which helped us meet our HUD affordable housing requirements. We also applied our strict, 11-point anti-predatory lending standards to our loan purchases. Under this policy we reject, for example, loans the borrower can't afford to pay from the start … loans with excessive points or fees … loans subject to mandatory arbitration … loans with abusive prepayment penalties … or loans with single-premium credit insurance or debt cancellation insurance. And, of course, any loans that are illegal.

Today, our exposure remains relatively minimal – less than 2.5 percent of our book of business can be defined as subprime. While our disciplined approach to the subprime market has helped to protect our company, our lenders and our borrowers from the turmoil, it has also given us some room to support the market, as Congress intended us to do. We are a secondary market mortgage company – we can't solve all the problems, but we can't wash our hands of them, either.

We want subprime borrowers to have a fair shot at homeownership. We think simple, straightforward, fixed-payment mortgages generally are the best products for these borrowers.

So Fannie Mae should not walk away and say the market turmoil is not our problem. We are concerned about a liquidity crunch in the subprime segment – the risk that as the turmoil shakes out, the flow of capital to finance subprime lending could slow to a trickle. Some may ask, why would that be a problem? Don't we want to cut off financing for this segment? The answer is no – that would only make it more difficult and costly for the least fortunate borrowers who depend on this lending to finance or refinance their homes. Robert Gnaizda of the Greenlining Institute said, "[A]rbitrary and artificial tightening of credit ... may be counterproductive – that is, it may dry up credit for members of minority groups, the poor, and the 70 percent of Americans who live from paycheck to paycheck." Economic history has a way of punishing the most vulnerable first and last – we should try to avoid that as the lasting effect of the subprime clean-up.

We should also seek to get ahead of the problem and help borrowers who are not yet in trouble. This is the more immediate problem of borrowers facing imminent "payment shock," homeowners with adjustable-rate loans that are scheduled to reset at higher rates. We want to help prevent further disruption of the subprime market, which would make it tougher for these borrowers to refinance into better, safer loans.

That is where we are concentrating our efforts today. We believe the best way to influence the subprime market, and be part of the solution, is to stay engaged and provide funding for conventional loans to these borrowers that are affordable over the long term.

Fannie Mae is committed to help through a new company initiative we call HomeStay, which has three basic parts.

First, we are working with our lender partners to help homeowners avoid immediate foreclosure. Several years ago, we created an operation at Fannie Mae that focuses solely on helping people who are falling behind on their mortgage payments to avoid default. If the mortgage is on our books, we work with our lenders or loan servicers to offer borrowers a range of workout solutions, and we offer lenders financial incentives to help borrowers avoid foreclosure. Last year alone, we worked out 27,000 loan modifications. We also provide lenders with systems that help them identify borrowers most likely to default so they can help out early in the process. If the mortgage is not on our books, we'll refer borrowers who call us to the right place.

Second, we are working with our lender partners to help homeowners avoid payment shock, and transition to safer products. We are expanding our lending options for subprime borrowers so that lenders can help them refinance out of high-reset ARMs or other loans that are a struggle for them. Our HomeStay initiative makes these products more flexible and broadly available. It includes our usual borrower-friendly options such as low down payments; long-term, fixed rates; low fees and points; a prohibition on pre-payment penalties and a ban on arbitration clauses. Right now, on a $200,000 mortgage, the monthly payment difference from a short-reset ARM to a safer, 30-year HomeStay loan is about $90 – significant, but not insurmountable. And to help with the current market needs, we are improving this loan option so that more lenders can qualify more borrowers for it. Briefly:

- We are adjusting our credit requirements so that more people can qualify. Essentially, homeowners facing imminent payment shock will be able to refinance into our loans without first having to clear up unpaid bills on their credit reports.

- We are using our experience with blemished credit by expanding the product set from a custom option available to 500 selected lenders, to HomeStay, which will make it available to about 2,000 of our lenders nationwide.

- And we're stretching the loan term from the maximum 30 years to 40 years. This will shave the monthly payment by about 5 percent, and it will allow many more borrowers to qualify.

Our message to lenders with borrowers facing resetting ARMs is this, "If your homeowner has managed his credit over the past 12 months, there's a good chance Fannie Mae can help."

Right now, we're getting at least 15,000 applications for subprime refinancing coming into our system per month. Because we have been adhering to our own prudent standards throughout, even before our new enhancements, 80 percent got a "yes." Altogether, we estimate that about 1.5 million homeowners who face resetting ARMs and potential payment shock this year and next could be eligible for our loan options. Certainly, lenders may choose someone else to buy or securitize the loans, but 1.5 million would be eligible for our options; we think this will also help establish a benchmark in the market for safe loans. These are also good alternatives for first-time homebuyers as the riskier "affordability" loans dry up.

Third, we are working with our housing partners to help counsel future homeowners. We are focusing especially on those who are most vulnerable, or for those whom a product modification alone will not save the day. We have to help people know what to do well before payment shock hits, and to avoid making the wrong mortgage choice in the first place.

- For example, we are providing $5 million in grants this year alone to support a national foreclosure prevention initiative being managed by NeighborWorks of America and the Homeownership Preservation Foundation. Such nonprofit organizations join with local governments, other nonprofit organizations, borrowers and lenders to help families overcome obstacles that could result in the loss of their homes.

- We also are launching a "Know Your Mortgage" effort, providing lenders with fact sheets with easy-to-understand descriptions of mortgage terms in English and Spanish for use with borrowers.

- In addition, we are expanding distribution of our Home Counselor Online system to lenders, organizations and agencies. This web-based application is designed to help people understand the home-buying process, how to protect or fix their credit, what to demand and what to avoid. We provide this system, free, to over 2,000 counseling agencies, and we'd like more to have it.

Finally, as we help the subprime market through this turmoil, Fannie Mae will continue to support better lending guidelines. When banking regulators finalize the new guidelines regarding teaser ARMs, which should be soon, we will work with our industry partners to comply with them. From the start, we said we believed the best course of action would be to follow the regulatory process to avoid further disruption of the subprime market and the borrowers who depend on it. That's what we're going to do. John Dugan, the Comptroller of the Currency, said of the proposed guidance, "We don't really want to unduly restrict credit to credit-worthy borrowers where the market is willing to extend that credit." We agree, and we stand ready and willing to extend that credit in a prudent and sustainable manner.

The actions I described today are first steps. Today and going forward, Fannie Mae can and will do more than our part to help lenders to protect homeowners, stabilize the subprime segment of the mortgage market, and keep affordable mortgage credit flowing to families who need it most. We look forward to working with this Committee and the Congress as we do.

Thank you, Chairman Frank and Ranking Member Bachus for giving me the opportunity to testify today.