



March 1, 2005

RE: The Decline and Fall of Fannie Mae

Dear Salutation,

The savings and loan industry disappeared due to unbridled lending practices. The government effectively reinvented this industry by centralizing it into two companies – Fannie Mae and Freddie Mac. Fortunately for the American public, Freddie Mac has been run in an efficient business like manner. On the other hand, Fannie Mae's ungoverned growth may very well result in a debacle similar to the savings and loan crisis.

If you look at Fannie Mae's balance sheet, it is alarming. The company has an investment grade credit despite having almost \$1 trillion of debt versus a meager \$60 billion of equity. The debt is real while the equity can disappear if the company catches the sniffles. Even more alarming is the fact that Fannie Mae has only \$1 billion of cash. This is a piggy bank reserve for a company of this size.

Fannie Mae has taken a few hits over the last several months; however, this could be just the tip of the iceberg. Fannie Mae's multi-family lending business is struggling with billions of dollars of troubled loans. These losses will consume valuable reserves putting the company in an even more precarious position.

Their home lending business is even scarier. Home buying has been unprecedented in the last five years. Many of these buyers have received virtually 95% financing. The last time money was that free and easy was during the height of the savings and loan industry. We all know how that story ended.

I'm not even sure that Fannie Mae knows the depth of its home loan problems. The company is still operating with 70 different manual accounting systems. How could they know if they were over or understating earnings?

Clearly, Group One is not the only real estate company concerned about this situation. It is interesting to see that after the board of directors of Fannie Mae replaced the chairman and CFO of the company, the federal government is now setting up an oversight regulator with receivership powers. Does Uncle Sam know something we don't?

As Fannie Mae's losses continue to mount credit will tighten. Investor's bullish outlook for the apartment sector will also wane. The result will create a better buying environment for those of us with a longer term outlook in this business.

Group One will keep you advised on all future developments affecting the multi-family market as we proceed through 2005. Should you have any questions regarding today's market place, please feel free to contact either of us at your convenience.

A handwritten signature in black ink that reads 'Robert H. Weitzman'.

Robert H. Weitzman

A handwritten signature in black ink that reads 'Robert Wolkoff'.

Robert Wolkoff