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CountryWide Fourth Quarter 2003 Earnings Call Transcript

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Company Name: Countrywide Financial
Company Ticker: CFC US
Date: 2004-01-27
Event Description: Q4 2003 Earnings Call

Market Cap: 2,479.21
Current PX: 4.25
YTD Change(\$): -4.69
YTD Change(%): -52.461

Bloomberg Estimates - EPS
Current Quarter: -0.409
Current Year: -1.592
Bloomberg Estimates - Sales
Current Quarter: 1329.667
Current Year: 5816.200

Q4 2003 Earnings Call

Company Participants

- Angelo Mozilo, Chairman and CEO

Other Participants

- Bob Napoli
- Angelo Mazilo
- Stanford L. Kurland
- Mike McMahon
- Keith McLaughlin
- Eric Wasserstrom
- Eric Wasserstom
- David Sambol
- Dave Sambol
- Brad Ball
- Angeloe Mazilo
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- Hai Vu

MANAGEMENT DISCUSSION SECTION

Operator

Good morning. Welcome to the Countrywide Financial Corporation's fourth quarter earnings conference call. At this time, all phone lines are muted or in a listen-only mode. However, after today's presentation, we will be taking questions and we certainly encourage your participation at that time. To queue up for a question, just press star, then 1, on your touchtone phone. You will hear a tone indicating that you have been placed in queue, and just as a note, you may remove yourself from queue at any time by pressing the pound key.

Once again, ladies and gentlemen, if there are questions or comments later in the conference, please queue up by pressing the star, then 1, on your phone keypad.

Also, should you require assistance during today's earnings report, you may reach an AT&T operator by pressing star, then zero.

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And as a reminder, today's call is being recorded for replay purposes. We ask that you stay online at the conclusion of today's meeting to receive the replay information.

With that being said, here now is your host, with our opening remarks, Countrywide's Chairman, Chief Executive Officer, Mr. Angelo Mozilo. Please go ahead, sir.

Angelo Mozilo, Chairman and CEO

Thank you. Good morning, and welcome to Countrywide's earnings teleconference for the fourth quarter and year end of 2003. We strongly encourage all participants to view the fourth quarter earnings and performance report while listening to this call. This report can be accessed on our website at www.countrywide.com by clicking on investor relations on the home page and then clicking on the supporting slide show text link for the fourth quarter 2003 earnings teleconference.

On Page 2 of the earnings and performance report, we provide an agenda for today's teleconference. First, I will provide a brief overview of our actual results. This will include a summary of some of our most noteworthy accomplishments during the year, as well as a tabular presentation of key financial and operational statistics for the three-month and 12-month periods just ended. Next, I'll provide you with an overview of current market conditions. And finally, we'll take a look at 2004 and beyond and how Countrywide has built a solid foundation for future growth.

Page 3 lists some of our 2003 operational milestones. We achieved total fundings of 435 billion, which substantially exceeds the total for the previous two years combined. Purchased fundings alone were 130 billion which nearly matched Countrywide's total fundings, purchase and refinance, from just two years ago.

Countrywide's servicing portfolio reached \$645 billion, which is more than two times the size of our portfolio at the start of the refi boom. Bank assets reached 19.3 billion, which is almost four times our total a year ago. And securities trading volume in our capital markets subsidiary was 2.9 trillion, nearly \$1 trillion more than the total for 2002.

Earnings accomplishments are highlighted on Page 4. Diluted earnings per share were \$12.47, which is greater than the last three years combined. I would like to emphasize that all numbers in this presentation reflect the 4-for-3 stock split completed in December.

Net earnings reached 2.4 billion, which nearly tripled last year's previous record of 842 million. Our diversification businesses combined to produce 894 million in pre-tax earnings, nearly 2 1/2 times last year's total and more than the entire company earned in any year before 2002.

The table on Page 5 focuses on our performance in the fourth quarter. Net earnings were 564 million, up 121% above last year's fourth quarter. Earnings per diluted share increased 89%, to \$2.74. Diversification pre-tax earnings increased 122% to \$246 million. Fundings were 76 billion, down 25% from the same quarter last year when refinance activity was much higher, but as will be noted later in this presentation, we became the number one mortgage originator during the fourth quarter.

The pipeline of applications in process fell significantly from December 31st, 2002 but remain a robust 33 billion. Later in this presentation, I will go into further detail about where we stand today.

The servicing portfolio grew 43%, concluding the year at 645 billion.

Page 6 compares our 12 month financial measures with the prior year. Net earnings rose 182% to 2.4 billion. Earnings per diluted share of \$12.40 were 156% higher than last year. Diversification pre-tax earnings, which were 368 million last year grew 143% to 894 million. And fundings increased by 73% to 435 billion.

In the wake of Countrywide's remarkable 2003 accomplishments, what happens next? Countrywide has gone beyond simply capturing the short-term benefits of refinance boom conditions. We view these environments as opportunities to build lasting foundations for future growth. This is reflected in our 2004 earnings guidance shown on Page 7. Guidance for 2004 is \$9 to \$12 per diluted share. This range falls below 2003 EPS of 12.47, but 2003 was obviously an

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extraordinary year. It is more informative to compare 2004 guidance with prior years.

Even at the low end of the range, \$9 per diluted share, the implied compounded annual growth rate from the beginning of the decade would be 40%. Management believes that a substantial portion of the growth achieved during the refinance boom was built upon a lasting foundation and can be sustained in the future. Investors who held our stock during 2003 were obviously well rewarded. As the chart on Page 8 indicates, Countrywide significantly outperformed both the S&P 500 index and the S&P 500 financials. Other major companies in the mortgage space did not keep pace with us. Countryside's stock price appreciated 90% during the year, versus 22% on average for the companies listed in the table on the right hand side of this page.

In a moment, I will describe the strategies we have in place to continue to deliver outstanding performance in 2004 and beyond. But first I'd like to provide you with a brief overview of current market conditions and how Countrywide is positioned to capitalize upon the opportunities they present.

Turning to Page 10, this table highlights something I mentioned earlier, that management believes Countrywide moved into the top spot amongst mortgage originators in the fourth quarter with 76 billion. This exceeded our closest competitors, Wells Fargo and Washington Mutual, who funded 71 billion and 70 billion respectively, per their recent press releases. Looking back to the previous quarter, it is notable that both companies funded more than Countrywide and refinance volume was still at extremely high levels. Countrywide held more of the market during the decline in the fourth quarter as a result of our reputation for quality, our solid operational foundation, and our ability to expand our salesforce in the changing market conditions. In the post-boom world, we believe the continuing industry consolidation is a great opportunity for Countrywide, as many high quality salespeople throughout the industry will see advantages in joining the winning team at Countrywide where the post-boom strategy is to continue to aggressively pursue market share.

There's been a great deal of interest in recent months in the status of origination margins in the industry and at Countrywide. Page 11 addresses this point. Margins achieved during the peak volume levels of the refinance boom are not likely to be sustainable as the market contracts, but Countrywide has consistently maintained that the market dynamics are such that margins will be sustainable at reasonable levels after the boom ends.

On the chart on Page 11, it shows the – during the fourth quarter, when Countrywide moved to the number one spot among mortgage originators, our margins remained healthy, despite a significant contraction in total market volume. Thus, the facts continued to support our belief in a rational post-boom environment.

But speculation about a greatly diminished mortgage market may be premature. Last week's MBA application indices indicated highly positive trends as shown on Page 12. The purchase index is shown on the left. This index hit 502, the highest level reported since the survey began in 1990. And there is even talk about a resurgence in the current refinance boom. The chart on the right shows a sudden spike in the refinance index to over 3300, as refinance applications hit their highest level in nearly 6 months. Immediately before that, the refinance index had reached its lowest level in recent times, at around 1700, which was still substantially above the range of 500 to 700 that would be expected in a normal purchase market.

For Countrywide specifically, as of the end of January – end of the day January 23rd, our month-to-date average daily applications were 1.7 billion, up from 1.4 billion month-to-date on December 23rd.

The next topic is Countrywide's future and how we have built a solid foundation for growth in the years ahead. Turning to Page 14, you can see some of the key foundational elements that have come out of growth during the boom.

Total originations grew more than sevenfold since the beginning of the boom. Much of this was refinance volume, which is not sustainable when rates rise, but note that purchase volume increased by 172%. This was driven by strategic expansion of our salesforce, which grew to 7500 people at December 31st, 2003. Our overall market share grew 112% during that same period. On the servicing side, our portfolio grew by 126%, representing a 63% growth in market share, and driving an increase of 117% in fee-based revenue. This, too, represents sustainable growth as the weighted average coupon of this production – on this production was reduced from 7.8% to 6.1%, meaning our servicing portfolio will be unlikely to experience high prepayments when rates rise again.

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The chart on Page 15 shows another perspective on sustainable growth. This chart plots Countrywide's origination volume and market share since 1990, and also breaks out the 13-year period in re – into refinance boom and purchase market cycles. Countrywide's market share rose during each of three refinance booms, and as this chart shows, this was lasting growth. In none of these cases did post-boom market share fall back to pre-boom levels.

The servicing side of our business has also achieved sustainable growth, as shown on Page 16. Our servicing portfolio shows consistent growth in all types of rate environments. During the most recent refinance boom, our portfolio, which generates an annuitous stream of cash, has grown substantially. At our quarter-end November 30th, 2000, which coincides roughly with the beginning of the refinance boom, the portfolio stood at 282 billion. Today, the balance is 645 billion. Just to put this into financial perspective, compared to fee-based revenue for the November 30th, 2000 quarter versus the fourth quarter of 2003, back then, fee-based revenue, servicing fee plus miscellaneous servicing portfolio fees before amortization, impairment, or hedging activities, was 288 million, or an annualized run-rate of about 1.2 billion. In Q4, that amount was 631 million, or an annualized run-rate of more than 2.5 billion. Please note that this analysis relates to revenue and does not necessarily translate directly into the bottom line, which is impacted by other factors such as amortization and impairment.

This is an example of what I mean when I talk about building a sustainable model or sustainable foundation. Now that – now let's look at some of our specific strategies for 2004 on Page 17.

As I mentioned earlier, we have very aggressive market share goals. These goals are supported by our salesforce that is financially incented to build businesses. Our salesforce numbers over 7500 today, and our plans are to grow that number to 10,000 by year end.

We want an active presence and a distribution capability to every material customer segment within each of our channels. In our retail division, for example, that means targeting the first-time homebuyer, the affluent homebuyer with jumbos, and the emerging market segment. We're also focusing on the consumers who prefer to transact business on the Internet as well as B2B customers like relocation companies and builders and realtors who want to form joint ventures. We have similar proactive strategies and focus across all origination channels. Another key component of our strategy is to maintain the industry's broadest product menu. Many of our competitors have limited product lines. Our strategy is to be able to offer a one-stop shop solution to our business partners, mortgage brokers, realtors, and builders, for example, so that if they have a customer who can qualify for a loan, we will have a product that meets their needs. And finally, we have a scalable infrastructure that can expand quickly to meet peak demand periods which we may see again soon through use of temps and commission-incented salesforce. Our broad product menu is supported by Countrywide Bank, which will specialize in ARM and hybrid products. We have 31 financial centers today, housed within our retail branches, and the plan is to bring that number to about 60 by the end of 2004. It is important to note that these centers average only 300 square feet in size and staffing is usually limited to two employees with low operating costs in comparison to conventional bank branches.

Taking into account the Bank's current pace of growth and business activities, Bank assets are estimated to be approximately \$35 billion by year end. The Bank's target ROA is 1.1%. And its 17% return on average equity is – I'm sorry. And its return on equity average is expected to be 18%.

Turning to Slide 18, and Capital Markets, the strategy is one of growth and diversification. While some of the subsidiary's profitability is tied to mortgage origination volume, it is branching out into new business segments and markets to reduce this reliance. One example is our recent announcement that Countrywide Securities Corporation is now a primary dealer of U.S. treasuries. This expands our access to institutional investors and allows us direct participation in the Fed's open market operations and securities lending. In addition, Capital Markets plan to expand its product and service offerings both within the residential mortgage arena and in other fixed-income securities. This will be supported by an expanded salesforce and by an international expansion as well. In our insurance business, one of the more recent developments was the hiring of a 25-year industry veteran as President and CEO of Balboa Life and Casualty. This will strengthen our management bench and enhance the growth and prospects of this very important subsidiary. In a non-refinance environment, the insurance business should not be negatively impacted as lender-placed business is insulated from the mortgage origination cycle, and reinsurance premiums historically have grown in line

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with the servicing portfolio – portfolio and we expect our portfolio to increase. Next, let's turn to Countrywide's longer term goals.

On Slide 19, you will see three of our most important five-year goals. As I've said many times before, the quality and execution capabilities of our time tested management team gives me great confidence that our 2008 target goals will be achieved. Our goal is market dominance, and we are targeting 30% origination market share by 2008. To support our macro hedge strategy, our goal is a servicing portfolio of at least 1 1/2 trillion by 2008. Growth in our diversification businesses should continue to be strong, with the Bank being a significant contributor. Based on the Bank's current pace of growth and business activities, assets are estimated to be \$120 billion by year-end 2008.

In summary, 2003 was an outstanding year on all fronts and I am proud of and grateful for the more than 34,000 employees who helped deliver these results for our valued investors. For Countrywide, 2003 was a year of opportunity where we enhanced our foundation for future growth.

We always emerge from boom times larger, stronger, and well prepared for the transition to normal market conditions. For 2004, we are reaffirming our earnings guidance, which is \$9 to \$12 per diluted share. This is significantly higher than any year before 2003, and it represents 40% compounded annual growth since the beginning of the decade.

To see the assumptions behind our earnings guidance, please refer to our third quarter 2003 earnings teleconference presentation. We are reaffirming these assumptions after adjustment for 4-for-3 stock split completed in December of 2003.

Beyond 2004, we are well-positioned for growth, as both our mortgage banking operations and diversified businesses have sound strategies and foundations in place.

I would like to now open the lines for any questions that you might have.

Q&A

Operator

And ladies and gentlemen, as a reminder, please queue up with any questions that you have at this time, by pressing star, followed by the 1. Thank you. Our first question is from the line of Bob Napoli with Piper Jaffray. Please go ahead.

<Q - Bob Napoli>: Good morning. I'll ask two questions, if I may. The first, the Bank \$120 billion bank by 2008, that's a pretty big bank in a pretty short period of time. With putting these targets out there, does it suggest that regulatory constraints are – are no longer an issue as far as the growth of the Bank?

<A - Angelo Mozilo>: No, these are all – all of that is put out there, Bob, on the basis that the regulators are comfortable with our growth plans.

<Q - Bob Napoli>: Okay. That's – and then secondly, on the – on the hedging for the quarter, just trying to understand the write up of the MSR and the hedging. It seemed like the hedge loss was a little bit higher than last quarter, although rates were less volatile. I was just kind of wondering what – why the hedge loss may have been what it was this quarter and kind of the outlook into early '04. And then lastly, would you care to venture a range for first quarter earnings, given the resumption of a refinance....

<A - Angelo Mazilo>: I'll take the last part. We don't give quarterly offerings. We're off of that, Bob.

<Q - Bob Napoli>: Okay.

<A - Angelo Mazilo>: Stan, you want to take this one.

<A - Stanford L. Kurland>: Yeah. With regard to the servicing hedge performance in the fourth quarter, we did have impairment and recovery, which offset the – more than offset the loss on the hedge instruments, although as you noted,

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the performance was not as great as it was in the third quarter. The third quarter, we had excellent performance. There was considerable volatility and opportunities created, and we – and the way that we operated the hedge resulted in excellent activity in the third quarter, and frankly very respectable performance in the fourth quarter as well. The fourth quarter had a little bit of mortgage tightening to treasuries and swaps, which is one of the reasons that the hedge didn't perform, you know, quite as well. We also had a couple of the strata of our servicing asset that was actually capped out and so we couldn't increase the impairment recovery any further on those strata. In other words, they were capped out at their cost. But all in all, it's – the hedge performed well, well within the targets that we provide, and, you know, we continue to operate it in the – you know, in the – pretty much the same fashion in the current – in the current year.

<Q - Bob Napoli>: Thank you.

Operator

And there's a question from the line of Mike McMahon, Sandler O'Neill & Partners. Please go ahead.

<Q - Mike McMahon>: Hi. My banking question was just asked, but a more minute question: The servicing fees as a percentage of the portfolio declined to around 47 BIPS annualized in the fourth quarter. I assume that came from the miscellaneous fees? And I'm just wondering, how volatile is the miscellaneous fee line on the servicing item?

<A - Angelo Mazilo>: Mike, Keith is going to answer that question.

<A - Keith McLaughlin>: Yeah, Mike. As you know, a portion of those miscellaneous fees contain prepayment penalties and other payoff-related fees, and the level of payoffs, as you know, declined in the fourth quarter, so we saw commensurate reduction in those fees. Also, in the fourth quarter we did see a reduction in income from our other retained interests, and if you think of those other retained interests, a portion of them are, in effect, squeezed IOs. You know, the portion that relate to our sub-prime securitizations where we're securitizing hybrid ARMs, and so perhaps somewhat counterintuitively, in a rising rate environment, the yields on those retained interests actually decline because of the squeeze effect and there being less projected future cash flow related to those.

<Q - Mike McMahon>: Very good. Thank you.

<A>: So it was a reduction in income from those sub prime retained interest and that was another drop there.

<Q - Mike McMahon>: Thanks, Keith.

Operator

We have a question from Eric Wasserstrom, UBS Warburg.

<Q - Eric Wasserstrom>: Great. Thank you. Two questions, please. The first is: Can you give any color about why there seems to be some very distinct disparity between your production margin results and maybe some of those in – also in the industry who have shown quarter on quarter reductions in, you know, 60, 70, 80 basis point range? And secondly, can you also comment, following up on the question that was just asked, of the Bank assets, how much of those are residual interests versus other kinds of assets?

<A - Angelo Mazilo>: The Bank, there's no residual assets. In so far as – and I don't mean to be curt here, but, you know, you're the analyst. You figure out what the – you know, what our competition is doing. We have no idea, you know, what – what drives their margins. I mean, we can tell you what drives ours but we can't – we're unable to tell you why there's a difference. I could speculate, but it would just strictly be speculation.

<Q - Eric Wasserstrom>: Okay. So perhaps said differently, are you seeing certain players price in a just -- perhaps not all but certain players -- price in a particularly competitive way or are all the large players....?

<A - Angelo Mazilo>: Yes.

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<Q - Eric Wasserstrom>: Yes?

<A - Angelo Mazilo>: Yes, we are. We're seeing – in particular, I mean, to be very specific here, we're seeing Chase be very aggressive on the correspondent side of the – of the business, and that would be the one that would stand out in my mind as – you know, as I review it with – with Dave Sambol and Stan. That's the one area that we've seen some aggressiveness and that would, again, be speculative but that would – you know, based upon what we know about the business, that would certainly tighten their margins overall on their production.

<Q - Eric Wasserstrom>: Great. Thank you.

<A - Angelo Mazilo>: Dave did you have a comment on that?

<A - David Sambol>: Yeah. I just want to point out that the, you know, operating structure makes a big difference in the overall composition of – of margins. You know, clearly as you come out of a refinance market, you're going to lose part of the pricing margin that you have, or pricing strength that you have, and that's something that we anticipate and expect – and expected. The other side of it is how you build the structure, how versatile is it to respond to changes in volumes and, you know, as we've indicated throughout this refinance market, we've been very careful in how we've built that structure in terms of hiring more individuals that are on variable comp and in terms of our processing staff, we've filled with many temps and dealt with – over time, and these things were very easy for us to contract the way that we had situated it. And so you're seeing, in our operations, you know, the results that we have been talking about for, you know, quite some time, that we think that the – first of all, the market is going to be very rational versus pricing, and in particular, versus the values attributed to servicing, and we're seeing basically that. And you're also seeing the success of the very versatile operations that we've built.

<A - Angelo Mazilo>: And the brand.

<A - Dave Sambol>: And the brand, yeah. And, you know, it is – you know, I think it's – you know, we have incredible technology and product, as we've mentioned, and clearly we're attracting salespeople from the industry and that's also shoring up activity as well. So, you know, we're – as Angelo said, we can't really take responsibility, nor do we really analyze what goes on with our competitors, but the market is very much, you know, acting in – in the most rational manner that I think we've ever seen in the history of mortgage banking.

<A - Angelo Mazilo>: I agree. And I think that's attributable to the consolidation and the fact that it's in the – the business is now in the hands of rational players who have responsibility to shareholders.

<Q - Eric Wasserstrom>: Thank you.

Operator

There's a question from the line of Brad Ball, Prudential Equities.

<Q - Brad Ball>: Thanks. Angelo, you mentioned an interest – or a capability of taking advantage of consolidation in the marketplace and I'm wondering if you have an appetite to acquire servicing, and whether or not there's any servicing out there at reasonable values that you may have an interest in.

<A - Angelo Mazilo>: Well, yeah, I think that, you know, our basis is always, can we buy it equal to or better than what it costs us to create it. That has been our guiding principle all these years. And so the answer to your question, one is that certain – we're always looking for opportunities to utilize the tremendous capacity that Countrywide enjoys today because of our technology. And – and what's happening, the disruption is a result of the fall off in applications and is providing us with at least some opportunities to look at, you know. Where it will go from here, I'm not sure but we certainly are looking to increase both our production capability and our overall servicing portfolio because the – there's no question about the tremendous economies of scale you get by a large servicing portfolio. And we have now the capability to really double – at least our technology has the capability of taking on double the servicing portfolio we have in place today. And so we have the ability, we have the intellectual assets, we have the technological capability and we have the financial capability to look at opportunities today and it's a long-winded answer to your question that,

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we'll look at it and we're seeing some. Some things happen in the industry which – which are interesting to us. Where it will go, I don't know.

<Q - Brad Ball>: Okay. And separately, in your press release, you talked about your – basically supporting your guidance given to us back in October, and in that guidance, you indicated that you would expect to recapture net impairments of about 800 million over the fourth quarter and '04 period. Do we still have roughly 800 million of net recapture available? Is that what you're?

<A - Angelo Mazilo>: Yeah. I think at that time we said it could be '03, it could be '04, it could be as late as '05, is my recollection of exactly what we said. But what is that balance of that impairment reserve?

<A>: Yeah. I think that number still holds. We have an impairment reserve at 12/31 of 1.2 billion. You know, and keep in mind, in a rising rate environment, we may recover the full amount of that reserve. There would also be some hedge loss that would offset that. So the net amount of 800 million, I think, is still a reasonable figure.

<Q - Brad Ball>: Okay. I mean your impairment reserve at the end of the third quarter was 1.7 billion.

<A>: It's down to 1.2 now.

<Q>: It's one two now but there's still 800 million of net impairment that you could recapture?

<A - Angelo Mazilo>: Well, that's the estimate.

<Q - Brad Ball>: Okay.

<A - Angeloe Mazilo>: Assuming that, you know, that you're going to have some hedge losses in that.

<Q - Brad Ball>: Okay. Fine. And then just finally, back on acquisitions, the – you know, the big number that you've thrown out for the Bank, would you consider doing anything in the Bank? Buying a bank or more of a branch-based delivery system? And are there any products that you don't have or can't build internally that you would want to add to that Bank?

<A - Angelo Mazilo>: I – well, to answer the first part of your question, it's no. That projection, 120 billion, is easily achieved, again, only conditioned upon the regulators being comfortable with both our infrastructure, you know, our governance and our management team, which we are comfortable with. And so we can do that internally. There is no model out there – remember, I described our model. It's very unique -- 300 square feet, one person, using our branch. These are microsites, by the way. These are not legal branches, so that means I don't need permission to open or close them. And at this juncture, management doesn't see any reason for us to enter into – to buy branches to get exposure. We have 550 branches to go yet that we can open in tremendous communities, well located, you know, that have been there for 15, 20, and 30 years with a brand. So I think all the growth plans we put out to you relative to the bank are organic and I think that's the way we're going to keep it.

<Q - Brad Ball>: Great. Thanks.

Operator

Mike Vinciguerra, Raymond James.

<Q - Mike Vinciguerra>: Thank you. Good morning. I want to follow up with another question or two on the Bank, if I may. One question I had is just looking at the balance sheet, your investments grew to about 26 billion on the balance sheet and we know that, you know, 19 billion or so are at the Bank. That was a big increase. I guess is it the holding company? Can you explain to me, is there a dynamic going on where they just haven't been transferred over to the bank at this point or how does that work out? And then second of all, as you grow to that \$120 billion, are there any thoughts to diversify your loan holdings away from home equity or mortgage, or is that going to be strictly where you guys focus? Thank you.

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<A - **Angelo Mazilo**>: Let me respond generally, and then I'll have Keith and – and Stan intervene, if they wish. In terms of product line, the – our core competencies rest within the home mortgage arena, so, you know, the single family – primarily single family related. Again, it's trying to get an asset/liability match so it will be – has to be a product that has – it's a variable product, and so I don't – you know, I don't see any major change in that strategy. In terms of your – the growth in the assets of the parent, that's purposeful and it's not a matter of assets yet to be transferred over to the bank. We have said in previous teleconferences that our objective is to create spread income within the parent. We have about \$30 billion net increase over the year in our – in our assets which are basically mortgage loans held for investment in the parent. So the – the growth of that – the balance sheet is that – is in the loan category held for investment. You want to comment on that?

<A>: Yeah. I would just expand. As you know, we haven't – we haven't sold our HELOC production for some time. The Bank at this point has not had the capacity to absorb all of these HELOCs, so a portion of those HELOCs have ended up on the mortgage bank's balance sheet. There's about 11 billion, I believe, in total on the mortgage bank's balance sheet as of December 31.

<Q - **Mike Vinciguerra**>: Great. Thanks, guys.

Operator

And we have a question from the line of Jonathan Gray, Sanford Bernstein. Please go ahead.

<Q - **Jonathan Gray**>: Yes. First of all, thanks a million for providing us with such a fantastically exciting business to follow and analyze. It's just breathtaking. I have to ask my usual picayune mechanical questions. Can you tell us the volume of HELOCs and sub-prime loans sold in the fourth quarter and perhaps give us some idea of what the gain on sale of those was?

<A - **Angelo Mazilo**>: Thank you for that comment, Jonathan. I'll turn it over. Keith, you want to take that or

<A - **Keith**>: Sure.

<A - **Angelo Mazilo**>: Yeah.

<A - **Keith McLaughlin**>: Jonathan, as I just mentioned, we didn't sell any home equity loans in the fourth quarter. We sold approximately 5 billion of sub prime mortgages in the fourth quarter, and realized a gain on sale of roughly 180 million related to that.

<Q - **Jonathan Gray**>: Okay. Thank you very much.

Operator

Thank you. Our next question is from Bruce Harting, Lehman Brothers.

<Q - **Bruce Harting**>: The – you know, competitive strengths of your business model coming at this business from, you know, starting with the mortgage bank and now building into a bank, can you just talk about that a little bit? I mean, it seems to me that you have, you know, much more streamlined operation to now build into the bank. And then, you know, the bank growing to 120 billion, how should we think about, you know, the company as it's growing to that size? Are you an institutional, you know, mortgage-oriented finance company with, you know, more of a capital markets investment banking tilt in the future? Should we think of you as a consumer bank that will be crossselling through your branch network other consumer banking products? And you said that you can do this organically. I'm just fascinated on how, you know, we should think about you. And it seems like the buildup of the capital markets area is going so successfully, it almost feels like, you know, you have as much a shot at becoming more of an investment banking business model than a, you know, traditional commercial bank business model. Thanks.

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<A - **Angelo Mazilo**>: Bruce, I – let me just tell you what – I think – we have a mission statement at Countrywide which we all share in this mission, and this vision. It is, you know, we're a financial services company that serves both consumers and institutions with mortgage banking at its core. And that's how we view ourselves. Now, we look at, for example, the capital markets separately. We don't merge it, you know, in the way you just described it, sort of investment banking entity. We look at it separately. It has a – certainly it's linked to the mortgage bank operation as well as to the Bank. It lends great efficiencies to both those operations and streamlines it, makes those operations seamless, but it is a – on its own, a very powerful capital markets operation. And at least in our minds, the management team, we look at it, although linked, separately. We look at ourselves as the – we view ourselves as the dominant force in mortgage banking, which primarily will be single family but it won't be limited to single family over the balance of this decade. And we look at the bank playing a major – more major role in terms of its participation in our mortgage banking activities. So you could view us as a – a – the bank emerging as a major player, and owning some of our mortgage banking activities which it does not own today. But it has to do with size, scope of the bank, and also, again, the regulators being comfortable with our business plan. But I would not – you know, as you described it, Bruce, are we an investment bank, are we this or that, I try to describe – we look at each of these businesses separately, we focus on them separately, we're very concerned about – always concerned about the quality of the management team in each of these entities, and at the end of the day, as I said, our mission has served us well to this point. And that is, again, a financial services company serving the consumers and institutions, but with mortgage banking at its core. Could that change in – at the end of this decade as we go into the next decade? Possibly. But that's how we view ourselves today. Is that a fair statement, Stan?

<A - **Stanford L. Kurland**>: Yeah. I think, you know, we're talking about two entities that fit, you know, very well into our strategic initiative. And when we talk about capital markets and we mention that our goal is to have 30% of the origination of mortgages by 2008, and so when you think about capital markets – or capital markets-type activity or investment banking niche, we have tremendous – and will have building control --of the distribution of mortgage investments, looking forward to, you know, an operation that basically controls 30% of the new investments and mortgage-backed, and clearly that, you know, generates customers and relationships and the ability to participate further in fixed-income. So it's a great addition, and synergistically fits very well with our operations and as Angelo mentioned, the bank is, you know, in terms of expanding our capabilities as a mortgage originator, particularly on the ARM side, adds a great dimension to the company, and we have the unique ability, given our – the ability to create assets and the customers that we have and the brand recognition, to continue to build a great bank.

<Q - **Bruce Harting**>: And is deposit growth – just in the quarter, I'm curious if you can comment on deposit growth? And then as you get to 120, is deposit growth keeping pace at, you know, half that rate? Two-thirds that rate? You know, a hundred percent of that rate? And also, just curious – and this is my last question – implications of, you know, a 30% market share on loan quality? You know, if you're capturing 30% of the market, you know, are you going to get your proportionate share of all types of loans by FICO score or are you just going to try to get the highest quality? And then implications on your relationships with loan brokers, GSEs and MIs, you know, in terms of pricing. Just kind of, you know, thinking through that. I would think that those are advantageous.

<A>: Yeah.

<Q - **Bruce Harting**>: As you gain share. Thanks.

<A>: Going for 30% mortgage share is totally unrelated to quality of loans we go after. We originate all types of loans today, from sub-prime, you know, all the way up to prime prime and jumbos and super jumbos, so we cover the entire marketplace today. There will be no compromise by this company in the overall quality of the product line, you know, which manifests itself in your delinquencies and foreclosures, but we don't compromise on that as we grow market share, nor is there a necessity to do that. I mean you're talking about a market that's going to be by 2008 very consolidated. There will probably be five players that will dominate it. In terms of going after the – and also, there's no deterioration in the relationship with each of our channels. We intend to grow that 30% market share through the channels that we have today, which is the Internet, which is mortgage brokers, which are correspondents, which are real estate brokers, consumers direct, call centers. So we're not – we're not going to give one up for the other. We – we need all of those channels to achieve the market share, so I think we'll become a better provider for all of those

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constituencies then than we are now. We'll have to be, in order to get that 30% market share. What was the other part of that question? What was the other part of it?

<Q - **Bruce Harting**>: Oh, you know, relationships with

<A>: Oh, GSEs?

<Q - **Bruce Harting**>: – brokers, GSEs and the like.

<A>: Yeah. I think the GSEs, you know, you have to first of all satisfy yourself that the GSEs are going to be okay, you know, with all the issues that have been surrounding them the last couple years. We believe they'll be okay, and we believe that they will still remain a major force and there's a lot of solid reasons for that justification that they'll be okay, you know, which I won't take your time now to enumerate. But if you go through it logically, they must exist and they must be vibrant and they must be healthy for the sake of this country. So based upon that, we believe that they will continue to be a very, very important partner of ours, as will the bank be – be an important partner of ours, as well as some unique and exotic securitizations for the super jumbos and other products that we're not very strong in today. So again that whole segment, I think, will be strengthened as we get to the 30% market share. The 30% market share is very achievable and let me just say this to you, that we have, for the 36 years, sat down and set five year goals for us, you know, seven times. In between those five years, maybe it didn't look so great, but at the end of every one of those five-year segments, we exceeded the goals that we set for ourselves and I'm confident we'll do it this time.

Operator

And there's a question from the line of Paul Miller, FBR [Friedman Billings Ramsey].

<Q - **Paul Miller**>: Yeah. Thank you very much. Two quick questions, Angelo. On your \$9.2 billion of deposits on the bank side, are they all deposit gathered from your micro branches or are they – any of them broker deposits in that number?

<A>: There's a little – there's a small broker deposit component.

<A>: Yeah. You know, it's a very small part of our deposits are brokers, as Angelo said. You know, the major portion of the deposits come from escrow balances that we control, about \$6 billion comes from escrow deposits. It's one of the great synergies that we have with our servicing operation. And then our retail deposits are about – almost – getting close to 3 1/2 billion dollars. And those are steadily growing, but one of the – you know, the – a great value that we achieve is with the synergy in our mortgage operations, both in our ability to move escrow balances to the bank and, as well as our future ability to solicit the portfolio for our retail deposits.

<A>: I might point out, also, that these – although this – you know, the model, in terms of a micro site for us, which is the two people, 1 1/2 persons and 300 square feet, is a very – has turned out to be a very effective model in gathering deposits. Our earlier branches, microsites that we opened up, had deposits in excess of \$90 million in that 1 1/2 person, 300 square foot branch, which exceeds that of the average commercial bank branch of 5,000 square feet and 7 people. So it is an extraordinarily effective model, and because it's working so well, we just continue to leverage off that model.

<Q - **Paul Miller**>: How many of these micro branches do you currently have in operation?

<A>: I just stated 30-31.

<Q - **Paul Miller**>: You have 30 and you're planning to go to 550. Is that what you said earlier?

<A>: No. What I said was for the balance of this year, of 2004, we're going to open up 60. What I said was we have now over 550 mortgage branches and that's where we locate

<Q - **Paul Miller**>: Gotcha. I gotcha.

<A>: So we have – you know, we have all of that potential to grow into.

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<Q - Paul Miller>: So the potential is 550. You plan to open 60 in '04?

<A>: We plan to have 60 at the end of '04.

<Q - Paul Miller>: End of '04. Thank you very much. And the other question is, and this might not – if it's immaterial, just tell me, Angelo. There's a lot of like SEC and FASB letters coming out on both how to account for mortgage production and also how to account for MSR's. The one letter I think came out – or I think SEC might come out soon, is that commitments have to be accounted for as a liability.

<A>: Right.

<Q - Paul Miller>: And secondly, I've read somewhere that hedging might have to be marked to market which might smooth out your MSR valuations. Can you just comment about those things?

<A>: Yeah. Absolutely. There – yeah, I don't think it's immaterial, I think that these are material issues. I'm going to have Keith comment on it. It's something that we've been watching, observing, and Keith has been in communication with a few people on it, so Keith, why don't you talk to him what you know about it.

<A>: Sure. As it relates to interest rate lock commitments, as most people probably know, the SEC recently came out with a – with some guidance, I guess, if you will, about how those should be accounted for and there's been significant diversity in practice in the industry about how to account for those interest rate lock commitments ever since FASB 133 came out and said that those were derivatives and had to be marked to market. The issue is how do you mark those things to market. So what the SEC has said, essentially, is that those things, in their eyes, are really written options, and as you know, when you have a written option, you never really – you never have an asset, you only have a liability. So the way they see it is, if you enter into an interest rate lock commitment and rates rise, you have to recognize the decline in value of that commitment to you. Conversely, if rates fall, even though economically there is a gain that we do realize in that event, the SEC has said you cannot recognize that gain until it's realized, ultimately when the loan is sold. So the FAS – the SEC has given, I think, a window for the industry and for the FASB to step in and attempt to modify their proposal and the industry is working actively with the SEC at this point on that. If at the end of the day, the SEC prevails in their thinking and it has to be accounted for as a written option, what that means to Countrywide, because Countrywide has not ever recognized the profit embedded in those locks, which some in the industry have, we've never done that, we've only recognized the changes in market value, be they positive or negative, the impact on us will not be as great. We would expect the exposure, given that we would not be able to recognize gains in any period, to be in the order of magnitude of about 50 million. Keep in mind that's very short-term, you know, because those gains will be realized ultimately when the loan is sold, so you're talking about an effect that lasts no more than a quarter in duration. All that said, we're hopeful that the SEC will see it our way and the industry's way, and essentially permit the accounting that we currently employ, which is not to recognize the profit that's embedded in the lock but to recognize the changes in value due to underlying changes in market rates that occur. So that's what we're looking forward to on the lock commitments. Now, in terms of mortgage servicing rights, the FASB has decided to take up the accounting for mortgage servicing rights, again, basically to determine whether they should be marked to market as opposed to the current accounting which is lower of cost or market. That would be a positive development for us, and for the industry, because as it stands now, given the lower cost of market constraint, the only way that you can recognize appreciation in the MSR's is if you apply hedge accounting, which is not impossible but difficult to do with respect to MSR's. So this would make it easier for us to reflect what we think is the economics of the business and to offset the economic effects of the MSR's in our hedging of the MSR's. So that's a positive development on the MSR's, and we're hopeful that the FASB will, in fact, change the accounting there.

<A>: What provoked the SEC issue was – we believe -- was some of the people participating in this industry recognized the gain on sale at the time of the loan application, which we have never practiced. We believe that you should recognize gain on sale when the loan is sold. That seems to be logical to us. And so because of the fact that certain of the participants in the marketplace were recognizing significant gains at the time loan application was taken, that created concern and, therefore, created this issue. We'll have to see how it comes out but we believe that it should be --that the logical way and the proper way to do it is the way we do it, have done it, and that is to recognize gain on sale upon sale of the loan.

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<Q - Paul Miller>: Thank you.

Operator

And we have a question from the line of Robert Hottensen, Goldman Sachs.

<Q - Robert Hottensen>: Hi, Angelo, it's Jason Nichols. Just two questions. One on the insurance business. Premiums earned growth looked pretty strong, but expenses, whether it was claims or operating, looked pretty well contained, so I just wanted to get your sense of how that should look in 2004. And

<A>: I think we're going to see – I'm sorry. Go ahead.

<Q - Robert Hottensen>: Just I'll give you question two.

<A>: Okay.

<Q - Robert Hottensen>: On the loan production sector statement breakdown, you guys used to break out loan origination fees and direct pricing costs but they're not on this quarterly statement, so I was wondering, first of all, if you could let us know what they were, and consider possibly including that in – in future releases.

<A>: Okay. Let me take the insurance and I'll have Keith and Stan address the other issue. In terms of 2004, I'm extremely optimistic, concerning the entire insurance segment, which is Balboa Life and Casualty, Balboa Re, and the agency. They really demonstrated a turnaround in the – in the fourth quarter, particularly Balboa Life and Casualty, irrespective of the fact that we had the fires here and had approximately \$10 million – \$10 million in reserves we had to put aside for the fire and smoke damage. The – we've spent all of 2003 restructuring Balboa Life and Casualty. We had in that entity an excellent team of very motivated, experienced, and time-tested managers, and a foundation has been established, in my opinion, for this entity to really have an impact on the overall company in 2004, both in terms of its base business that it's in now, and some new businesses that it's entertaining getting into. And we have a gentleman I mentioned in my presentation, Robert James out of CNA, 25 years in the business, just came with us as the new CEO of Balboa Life and Casualty. We're very impressed with him. We have a team above him in the parent who now is experienced in that area. So I'm very pleased where we are, in the insurance operation. I'll just include that in global. I just got back from London, and our global operation is shaping up beautifully as we restructured – again, spent the entire 2003 restructuring our global operations. So both of those entities, insurance and global, I expect some great performance in 2004. As to the split off of the costs, Keith, you want to go through that with him? And did we have it in there at one time and it's not in there now, is that what you're saying?

<A>: It's been in there historically and up through the third quarter you broke out direct pricing costs and loan origination fees and it's not in the fourth quarter release.

<A>: What's on the website?

<A>: What we did was we conformed the presentation on the website to be consistent with the external presentation. If you remember, about a year ago, we combined loan origination income and gain on sale together on the external reporting because in our mind they're fairly interchangeable.

<Q - Robert Hottensen>: Uh huh.

<A>: And we – in this current quarter, we conformed the production website to be consistent with that. And as you'll notice, we restated all of the prior periods, so that they would be comparable.

<Q - Robert Hottensen>: Okay. So you won't be – you won't be releasing that anymore in the segment breakdown?

<A>: Right.

<Q - Robert Hottensen>: Okay.

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<A>: Hold on a second. Hold on a second. Let me just check.

<A>: That's correct.

<A>: Well, but if you want to get at the MSR's that were capitalized during the period, you can do that by referring to the footnotes, which flow

<Q - Robert Hottensen>: Right. The – the value of servicing booked?

<A>: Uh huh.

<Q - Robert Hottensen>: I've got that. I just – I didn't know the direct pricing costs. I usually look at that relative to – to primary and secondary spreads in rates and sort of look at the correlation there, to get an idea of what pricing costs may be. That's why – you know, traditionally I've broken that out in the model but ...

<A>: Keith, you want to respond to that?

<A>: Well, yeah. I think you can essentially still perform that analysis, once you know the MSR's and other retained interests that we've capitalized as part of the gain on sale.

<Q - Robert Hottensen>: Yeah. Well, and, too, if I knew the breakout of the origination fees, too, from the gain on sale. That's the other change in disclosure.

<A>: Right. Well, the announcements can still be done – I think you'd have to recast it essentially, given the numbers that have been restated for the historical periods.

<Q - Robert Hottensen>: Okay. I just – I just bring it up because you guys have great disclosure relative to any other mortgage bank out there, so, you know, keep up the good work. But that's just one suggestion I'd have. I like having the – the expanded disclosure, but ...

<A>: Okay. We're going to – we're going to take note of that.

<Q - Robert Hottensen>: Okay.

<A>: And address it internally here.

<Q - Robert Hottensen>: Thanks, Angelo.

<A>: You're very welcome.

Operator

There is a question from the line of Vincent Daniel with KBW.

<Q - Vincent Daniel>: Thanks and good afternoon, almost. Two questions. One, CFC seems to be a taxpayer on a consistent basis. Should we see that continue going forward? And any initial thoughts on the new auditor on board?

<A>: I would expect that Countrywide will be a consistent taxpayer going forward. Any thoughts on the new auditor? We went through a very arduous, diligent process, in – in making the – what we believe is the best choice for the shareholders of the company in terms of a firm that had depth and – and a structure that could accommodate all of the needs of Countrywide, which is now, you know, relatively complex in terms of all the businesses that we have. We'll have the – you know, the intellectual strength and the geographic diversification to provide, you know, what we need and so all of us in management are very pleased with the choice and pleased so far with the interaction that we've had with KPMG.

<Q - Vincent Daniel>: Will they be auditing '03 results or is it an '04 event?

<A>: '04.

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Current Quarter: 1329.667
Current Year: 5816.200

<Q - Vincent Daniel>: Thanks, guys.

Operator

And the next question is from the line of Ed Groshans with Moors and Cabot.

<Q - Ed Groshans>: Good afternoon. How are you all doing?

<A>: Good.

<Q - Ed Groshans>: I have a couple of quick questions. Branch openings, you say you're going to have 60 by year-end. I was just wondering if you could elaborate on the regions that you're targeting there, or MSAs.

<A>: Yeah. You know, I can't. But I think it's a good question. I'd have to sit down with Jim Furash [Senior Managing Director, Countrywide Financial Corporation; President and CEO, Countrywide Bank], unless you know the area – we don't know the geographic areas that we're opening. We're trying to get diversified. You know, we opened up California first. Obviously, it was the home base and we wanted to test this model. It worked well. We then moved into Florida, and into Texas. Again, we find that the model works wherever we place it. I think we just opened up in Illinois, Chicago area. But I'll get – what I'll do is I'll put out in the operations release in March the business plan for the balance of the year for the opening of the branches.

<Q - Ed Groshans>: Also, with the capital markets, you talked about one, not being a primary deal growing the salesforce, going international. Would you be looking for the volumes to maybe be stable from this year, or was this year just so outsized that volume is going to come down next year?

<A>: Are you talking about the – when I talked about \$2.9 trillion in capital markets?

<Q - Ed Groshans>: I didn't hear that. I'm sorry.

<A>: Is that the number you're talking about.

<Q - Ed Groshans>: Yeah. I didn't hear the 2.9 trillion.

<A>: 2.9 trillion. That was 2003. That's the number you're talking about, will that increase or decrease going forward?

<Q - Ed Groshans>: Yes, yes.

<A>: It's hard to tell right now. I mean obviously being a primary dealer is going to help us. Not only, you know, in the trading activity of treasuries, but it brings to us, one, prestige, but it also brings to us other customers that will buy other product from us. And even though the mortgage bank, as you know, you've seen the activities slow down because of the increasing rates and lower refinance activity, we have not seen that yet in capital markets. So the capital markets continues to expand its market share. I wouldn't hazard a guess as to what their volume is going to be but they certainly are not following the pattern of the mortgage bank.

<Q - Ed Groshans>: Excellent. Thank you very much.

<A>: Yeah.

<A>: Yeah. Just to – you know, we have some first quarter branch openings so I can kind of give you where the next eight

<Q - Ed Groshans>: Oh, good.

<A>: – bank branches are. We have five of the branches will be in the Texas area--- Houston, Fort Myers area. Then the remaining branches are targeted for between Los Angeles, Orange County, and San Francisco.

<Q - Ed Groshans>: And then, you know, just on that, you said – you mentioned you have 3.5 billion in retail deposits so far.

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<A>: Yes.

<Q - Ed Groshans>: Which seems like a pretty good growth rate. Is your pricing on the CD product, is it like a little bit above market, toward the top end of the market, in the middle?

<A>: I'd say it's the top end of the range, but you have to take into consideration that our operating costs are over a hundred basis points less than the average – about 125 basis points less than the average commercial branch, so we got a lot of room to play with to – you know, in terms of being aggressive in pursuing the – the CD market in the communities in which we serve.

<Q>: Excellent. Thank you very much.

Operator

Joel Houck, Wachovia Securities.

<Q - Joel Houck>: Thanks. Good afternoon. On the issue of disclosure, you know, I would vote for continuing to break out origination fees with gain on sale. And while we're on that issue, given the projected growth in bank assets, obviously interest income is going to continue to grow and be an important part of the total revenue mix. It would be helpful if the company could provide the components used to analyze and project the margin, like average earning assets, yield, average interest liabilities, cost of funds, so more of a comment than anything else.

<A>: Okay. All right. Would you make note of that, Lori.

<A>: Uh huh.

<A>: Okay. We're making note of all of these. Our – you know, what we'd like to do is provide you with as much information as you need in order to make, you know, your analysis of the company, so this is helpful to us. By letting us know what you need.

<Q - Joel Houck>: All right. Thanks, Angelo.

<A>: Okay.

Operator

Lawrence Kam, Sonic Capital.

<Q - Lawrence Kam>: Hi. Congratulations. I think nobody's actually congratulated you on a fantastic

<A>: And I appreciate that I thought I was speaking to my mother all morning. (Laughter)

<Q - Lawrence Kam>: And congratulations to Stan and the rest of the team that have gotten promotions recently.

<A>: Thank you.

<Q - Lawrence Kam>: I would like to throw my hat in and say – agree that certainly the origination fee disclosure is helpful because you're one of the few banks that actually provides a clean gain on sale number, as opposed to a number that is more close to the production margins and that's – you know, the breakdown is helpful. A few odds and ends. For the lines that are now

<A>: I've got – I've got Keith McLaughlin wrestled to the floor but he hasn't given in yet.

<Q - Lawrence Kam>: Okay.

(Laughter)

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<Q - Lawrence Kam>: For the lines that are now convertible, how much of that liability is still in the balance sheet and how much do you think that's going to be going into the next year?

<A>: 500 million. 500 million. You've got – you know, that has a convert feature on it which has been triggered, obviously, with the pricing stock, but it's an issue that we're addressing as to how that best can be managed. But it's 500 million.

<Q - Lawrence Kam>: Right. Because right now, it's being double counted in the share count and the liabilities, right?

<A>: Yeah, we're kind of in the worst world right now where we've got a liability on the balance sheet but we've got the full effect of the dilution in our earnings

<Q - Lawrence Kam>: Right, right.

<A>: Yes. So we're working on strategies to address that and resolve it and it's going to be okay.

<Q - Lawrence Kam>: Okay. Keith, with respect to the fair value versus the lower of cost of market for the MSR, what is the fair value for the MSR right now?

<A>: It's at – it's as stated on the balance sheet. About 6.9 billion.

<Q - Lawrence Kam>: Well, didn't Stan say earlier that you hit some strata levels so that you couldn't write it up above the – the cost?

<A>: Yeah. That's – yeah. There's a modest amount there of about 50 million, I'd say.

<Q - Lawrence Kam>: Oh, okay. So it's not a significant issue yet?

<A>: Not yet.

<Q - Lawrence Kam>: Okay. And finally, I noticed that, you know, there's very significant excess capital on the balance sheet, and I really think you guys should be driving towards 30 plus percent return on equity, as opposed to 20 plus and I think that, you know, a billion or two in a tender offer for the stock would be a helpful way to do that, because I don't think that the acquisition opportunities, you know, with the price of the market out there, I don't think that that's attractive. Can you have some comments on that, please?

<A>: Yeah. Our comments are that we've been pretty effective managers over 35 years now, and a pretty efficient user of capital, and I think we know how to run this business, and to date, we have not found giving back capital to be an effective way of growing this business to where we want it to be over the next – over the balance of this decade and into the next one. There's lots of opportunities out there, despite how you may feel about it. We want to assure that we have – we hold our powder to take advantage of those opportunities.

<Q - Lawrence Kam>: Well, you certainly have a lot more powder today than you did, say, a year ago.

<A>: Yeah.

<Q - Lawrence Kam>: Would you agree with that?

<A>: Powder is good.

<Q - Lawrence Kam>: Powder is good. Thank you very much.

Operator

Mike Seltzer with Barclays.

<Q>: Yes. Hi, Angelo. I have a question on the balance sheet in general, with the – with the forecast for 2008 or the goals for 2008 for bank assets and servicing portfolio. Can you walk us through the funding requirements, the capital

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requirements, for both servicing and bank assets and where they'll be coming from?

<A>: I think – well, we go from one – it's interesting. We go from one guy who wants to give out the capital to the other guy that says where the hell are you going to get the capital. That just shows you that's why we have to keep our head steady and focused on what we do each and every day and sort of crowd out the noise. We believe, at least at this time, that this can be done organically. All the growth plans that you see through 2008, the 30% market share, the 1 1/2 trillion, the support of that asset of the MSR asset, the growth of the bank, can be done generating – you know, with capital that we're generating. We're now a big capital generator and a cash generator, that we can do this internally. It's not a guarantee, you know, we'll have to assess this as time goes on, to see what the most effective way of funding this – these growth plans. But – but I believe that we currently believe that we can do this internally. We have no – nothing on the horizon, unless a unique opportunity came along as was the LYONs at the time we did it, to do anything other than continue to – to generate capital and use our own organic capital to do what we're doing. Stan, do you have any comment on that?

<A>: Yeah. No, I think it's absolutely correct. Our – you know, our modeling demonstrates that we can, in combination with our capital that we have today and the earnings that we'll retain from our operations, support the plans out to 2008.

<Q>: What's the leverage ratio that you're targeting for the bank side?

<A>: We're presently at a – I think the regulatory is 5%. Is that – is that – 5%

<A>: Yeah.

<A>: – capital? Yeah. We're still in the de novo stage. That stage is over in May. And I think we currently, what, eight or nine?

<A>: 8%.

<A>: 8%. We would expect again, you know, the ones who dictate this are our partners, the regulators, but we would expect at the end of our de novo period that we'd have a lower leverage requirement, and – and so we anticipate that we'll be at around a 5% in the bank.

<Q>: Okay. And most of the funding is going to be from deposits? Is it escrow deposits or just...?

<A>: Escrow deposits – yeah, escrow deposits, Federal Home Loan Bank borrowings, which is very significant for us. We're the largest borrower from the Atlanta Fed today, and the consumer deposits.

<Q>: Okay. I mean the 120 billion is a pretty big balance sheet

<A>: Excuse me?

<Q>: 120 billion is a pretty big balance sheet. I'm wondering, you know, are there enough deposits out there?

<A>: This is a big country.

<Q>: Yeah.

<A>: And a great one.

<A>: Yeah. We actually went through those studies in terms of money market accounts and CD accounts and where they're projected to be and the type of share growth that we would have. It's very reasonable.

<A>: Yeah. And you know, you got to remember this, too, just to give you an example. You know, you got to remember the growth of wealth in the United States is – continues to accelerate, so the numbers, you know – you make a mistake if you use the numbers today as a static number to project that forward. To give you an example, today there's about 6 1/2 billion – close to 7 billion – trillion, rather – trillion in mortgage outstanding in the United States. By the end of this decade, there will be 12 trillion mortgages outstanding. So the whole basis of everything that's being done in the country, whether it be the deposit base, CD base, mortgage base, all of that is increasing at a very rapid

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pace so you can't look at what's existing today in terms of the CD market, for example, versus where it's going to be in 2007, '08, '09, and '10.

<Q>: Okay. And the asset side will be primarily – it's primarily going to be ARMs, HELOCs?

<A>: Yeah, it will be ARM-related. You know, hybrids.

<Q>: Okay.

<A>: Hybrids, ARMs. You know, there may be some other type of product. We're looking at some other activities at the moment that may fit the criteria for the bank. Again, the bank has to meet several criteria. One, it has to meet our – our thresholds, management's thresholds, it has to meet the regulatory thresholds, and it has to meet the economic thresholds within the bank as to, you know, its return on investment.

<Q>: Okay. And then interest rate risk management is – basically if you're holding less fixed rate product or less product that's refinaneable that's going to allow you to manage your risk on that.

<A>: That's right. It gives us a lot of flexibility and has to date. Plus, the quality has been, you know, we're now 2 1/2, almost 3 years into this. We enjoy very, very low delinquency ratio, extremely low, virtually no repossessions that I'm aware of to date, and so it's the quality of the assets in the bank are very, very high.

<Q>: Okay. Thanks very much, gentlemen.

Operator

There's a question from the line of Matthew Lindenbaum with Basswood Partners.

<Q - Matthew Lindenbaum>: Hi. Thanks a lot. My first question is on the page where you go through your target for '08, you have 1 1/2 trillion, is that period end or the average because I'm having trouble getting to the number and then the same for bank assets, is that the period end or average for '08.

<A>: Period end.

<Q>: And the 1 1/2 trillion servicing?

<A>: 1 1/2 trillion?

<A>: Yeah. It's average. Actually – yeah, it's

<Q>: That looks like an average to me.

<A>: Yeah, it is for that year.

<Q>: Right. And the bank assets is period end?

<A>: Yes.

<Q>: Okay. And the – what was the other question? The – in terms of disclosure, I just want – and I've asked this in the past and I guess now that the bank is going to become an even bigger part, I wanted to just ask again, and just to elaborate on what someone else mentioned. In terms of disclosure, I think it would also be helpful, obviously, to have all the disclosure that was talked about earlier for the bank, but also interest rate risk disclosure, because, you know, I think we want to just get our hands around – I know what you said about it and I understand that. I just want to be able to confirm with some disclosure what – what the gap is, the maybe duration mismatch, anything like that, so we can get our hands around what kind of interest rate risk is being taken in the bank.

<A>: Okay.

<Q>: Okay?

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<A>: We have it. We've made note of that. Appreciate it.

<Q>: Thank you.

Operator

There's a question from Hai Vu with Jeffries & Company.

<Q - Hai Vu>: Good morning, guys. Your pre-tax production margin of 90 basis points, given that we're done with about a month of this quarter, is that still a sustainable run-rate for this quarter?

<A>: Margins are very much in line with – with what we saw in the fourth quarter.

<Q - Hai Vu>: Okay. And just a couple other follow-ups. Your servicing strip, is the spread there still around 34 basis points as it was last quarter? And also, do you have – do you track your cash earnings for this – this quarter and the last? Thanks.

<A>: Servicing is

<A>: The net servicing fee is down to about 33 basis points.

<A>: 33, so some excess. So it's about 33.

<Q - Hai Vu>: Okay.

<A>: Okay. And what – what was the question on the – what was the second part of that?

<Q - Hai Vu>: Cash earnings. Do you track cash earnings? What was it this quarter and what was it last quarter?

<A>: Yeah, I don't have those numbers off the top of my head. But you can get there – you can get there by referring to the sector P&L that's on the web.

<Q - Hai Vu>: Okay. I'll do that. Thanks.

Operator

And the next question is from Don Meader, Bear Stearns.

<Q>: I'd like to add congratulations on a great year. It was exciting to see the year unfold Angelo and Stan.

<A>: Thank you, Don.

<Q>: Nice to see that you're recognized as a primary dealer. I would – you've hired some talent and some names that we are familiar with.

<A>: I know. You should be very familiar with them.

<Q>: That's right. And it's good. It's good for Countrywide. I assume that the headquarters of that division will be in Calabasas, but how large do you expect your presence to be in New York City and perhaps Chicago?

<A>: Right now, it will be in Calabasas. Probably, you know, we don't have anybody in Chicago and New York now but it's very possible that we'll have one person in New York. I'm not sure about Chicago. And it's possible to have one person in London.

<Q>: So there's no – no expectation of a large presence in New York, a lot of traders and what have you?

<A>: No, no. We want to – you know, Don, for you

<Q>: It's for your own – go ahead.

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<A>: You know how Greenberg feels about it. We have to be -- we want the traders-- we want to be close to the traders right at their hip.

<Q>: That's right. Make sure they're hedged, right Angelo?

<A>: Yeah.

<Q>: I notice that your sales count is now 7500, you've mentioned a couple times. I think last quarter it was 6,000.

<A>: Right

<Q>: In that 7500, does that include, for instance, all the personnel in your -- your bank now or your mortgage offices or your people, for instance, in treasuries? It's

<A>: No.

<Q>: -- consolidated mortgage selling?

<A>: No. It just relates to the mortgage banking operation, which is in each of our channels of the mortgage operation, which would be correspondent, wholesale, and the consumer markets division. And that -- along those lines, since you mentioned that, what we're finding now, you know, is that we are clearly the lender of choice

<Q>: Yeah.

<A>: -- in the United States where salesmen want to come to, salespeople want to come to, and so, you know, initially several years ago, we had to go out and aggressively pursue these salespeople. They're calling us and that's a good position to be in.

<Q>: Those are bonus -- I mean salary and bonus jobs or strictly salary?

<A>: No. Commission only.

<Q>: I'm sorry. I meant commission only. Commission only

<A>: Right.

<Q>: I also wanted to add congratulations to Stan and Dave on their promotions and look forward to the next quarter, Angelo. Thanks.

<A>: Thanks very much, Don.

Operator

Bob Napoli, Piper Jaffray.

<A>: No. You recycled. Ma'am, you recycled. That was the first one that asked questions.

Operator

And we have Thomas Denslow, Hamilton Investment Management. Mr. Denslow, your line is open.

<A>: Not there.

Operator

Next we have Sanford Park, Chatta Capital.

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<Q>: Hey, guys. Thanks for taking my question. In your presentation, you mentioned that your production pre-tax margins were 12 1/2%. Given your expansion plans and the rising rate environment and how that reduces revenues in ARMs, do you think that these margins are sustainable past '04?

<A>: Where is that 12 1/2% coming from.

<A>: Yeah. I don't know.

<A>: Where did you get that 12 1/2% from?

<Q>: 12 1/2%. It's on Page 11 of your presentation. It's your overall production margin.

<A>: Market share.

<A>: Estimated market share.

<A>: Yeah.

<A>: Yeah. That's market share.

<Q>: That's your market share.

<A>: Yeah.

<Q>: Okay. Well, given – given the rising rate environment, do you think your margin is going to be sustainable past '04?

<A>: Past '04?

<Q>: Correct.

<A>: Well, we're just addressing '04 and our feeling – I think Stan expressed, you know, our feeling at the moment. I mean this is not axiomatic but that our feeling is that – and it's been at least sustained up to this point in time that the players that are left in the industry are acting very responsibly, on average, and we believe that – that we will enjoy very solid margins throughout this year, irrespective of the movement of interest rates. That's our expectation, and certainly as Stan alluded to in the first quarter so far, we've seen that – we've seen that – the conduct of our – of our competitors to be, you know, very rational.

<Q>: Okay. Thanks.

Operator

That does conclude our questions and answers for today. Mr. Mozilo.

Angelo Mozilo, Chairman and CEO

Okay. Thank you very much. Okay. Thank you. Appreciate it. Talk to you next quarter.

Operator

And ladies and gentlemen, this conference will be available for replay after 3:00 p.m. today until February 15th at midnight. You may access the replay service by dialing 1 800 475 6701 and entering the access code 715497. International participants may dial 1 320 365 3844 and entering the same access code, 715497. That does conclude your teleconference for today. Thank you for your participation. You may now disconnect.

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