



2016 Dodd-Frank Act Stress Test (DFAST) Disclosure



October 24, 2016

This presentation contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, as amended, including projections of the Company's financial results and condition under a hypothetical scenario that incorporates a set of assumed economic and financial conditions prescribed by its regulators. The projections are not intended to be a forecast of expected future economic or financial conditions or a forecast of the Company's expected future financial results or condition, but rather reflect possible results under the prescribed hypothetical scenario. Forward-looking statements may be identified by words such as believe, expect, anticipate, intend, plan, estimate, may increase, may fluctuate, and similar expressions or future or conditional verbs such as will, should, would and could. The Company's future financial results and condition will be influenced by actual economic and financial conditions and various other factors as described in its reports filed with the Securities and Exchange Commission and available at www.sec.gov.

Any forward-looking statements made by or on behalf of us speak only as to the date they are made, and we do not undertake to update forward-looking statements to reflect the impact of circumstances or events that arise after the date the forward-looking statements were made, except as required under United States securities laws.

INTRODUCTION

Flagstar Bancorp, Inc. (NYSE: FBC, “Flagstar” or the “Company”) is a \$14.3 billion savings and loan holding company headquartered in Troy, Michigan. Flagstar Bank, FSB, (the “Bank”) provides commercial, small business, and consumer banking services through 99 branches in the state of Michigan. It also provides home loans through a wholesale network of brokers and correspondents in all 50 states, as well as through 31 retail locations in 21 states. Flagstar is a leading national originator and servicer of mortgage loans, handling payments and record keeping for nearly \$76 billion of home loans for nearly 370,000 borrowers. For more information, please visit flagstar.com.

Per regulatory guidance, the 2016 DFAST exercise does not consider the capital transactions approved in June 2016 and executed in July 2016 that redeemed the Fixed Rate Cumulative Perpetual Preferred Stock (formerly “TARP”).

Flagstar’s 2016 Dodd-Frank Act Stress Test (DFAST) results, given the hypothetical Severely Adverse scenario provided by the regulatory agencies, suggest that Flagstar would maintain sufficient capital to remain well capitalized throughout the nine-quarter DFAST time horizon.

DFAST

Flagstar Bank, FSB, is required to conduct annual company run stress tests pursuant to the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The disclosure requirements of the Act are defined by a number of regulatory pronouncements including “Supervisory Guidance on Implementing Dodd-Frank Act Company-Run Stress Tests for Banking Organizations with Total Consolidated Assets of More than \$10 Billion but less than \$50 Billion.”

The annual DFAST is a forward looking exercise under which the Company and Bank estimate the impact two hypothetical adverse economic scenarios would have on a company’s capital ratios over a nine-quarter time horizon from January 1, 2016 through March 31, 2018. The Supervisory Adverse and Supervisory Severely Adverse Scenarios are released by the Office of the Comptroller of the Currency. The 2016 Supervisory Severely Adverse scenario is characterized by a severe global recession, accompanied by a period of heightened corporate financial stress and negative yields for short-term U.S. Treasury securities. In this scenario, the level of U.S. real GDP begins to decline in the first quarter of 2016 and reaches a trough in the first quarter of 2017 that is 6 ¼ percent below the pre-recession peak. Unemployment increases by 5 percentage points, to 10 percent, by the middle of 2017. Asset prices drop sharply in the scenario with house prices dropping 25 percent through the third quarter of 2018 and commercial real estate prices falling 30 percent through the second quarter of 2018.

It is important to note that this is a hypothetical scenario designed to assess the strength of banking organizations and their resilience to unfavorable economic conditions. This scenario does not represent a forecast of the Federal Reserve, the Office of the Comptroller of the Currency, or the Company.

RISKS INCLUDED IN THE STRESS TEST

In order to conduct its business, Flagstar assumes certain risks. Management has identified risks, as further described below, that are inherent in Flagstar's business:

Credit Risk:

Credit risk is the risk of loss to us arising from an obligor's inability or failure to meet contractual payment or performance terms. Like other financial services institutions, we make loans, extend credit, purchase securities, and enter into financial derivative contracts, all of which have related credit risk. The majority of our credit risk is associated with lending activities, as the acceptance and management of credit risk is central to profitable lending.

Interest Rate Risk:

Interest rate risk is the risk to income as a result of changes in market interest rates, and results from timing differences in the repricing of our assets and liabilities, changes in the relationships between rate indices, and the potential exercise of explicit or embedded options. Due to the nature of Flagstar's operations, the volume of new mortgage originations each period is a significant driver of revenue and impacts several revenue streams. This volume is highly sensitive to macroeconomic conditions, including market interest rates.

Market Risk:

Market risk is the risk of reduced earnings and/or declines in the net market value of the balance sheet primarily due to changes in interest rates, currency exchange rates, or equity prices. We do not have any material foreign currency exchange risk or equity price risk. The primary market risk is interest rate risk.

Operational Risk:

Operational risk is the risk of loss due to human error; inadequate or failed internal systems and controls; violations of, or noncompliance with, laws, rules and regulations, prescribed practices, or ethical standards; and external influences such as market conditions, fraudulent activities, disasters, and security risks. We continuously strive to strengthen our system of internal controls to ensure compliance with laws, rules and regulations, and to improve the oversight of our operational risk. We evaluate internal systems, processes, and controls to mitigate loss

from cyber-attacks and, to date, have not experienced any material losses. The goal of this framework is to implement effective operational risk techniques and strategies, minimize operational and fraud losses, and enhance our overall performance.

Liquidity Risk:

Liquidity risk is the risk that we will not have sufficient funds to meet current and future cash flow needs as they become due. The liquidity of a financial institution reflects its ability to meet loan requests, to accommodate possible outflows in deposits and to take advantage of interest rate and market opportunities. The ability of a financial institution to meet current financial obligations is a function of the balance sheet structure, the ability to liquidate assets, and access to various sources of funds.

METHODOLOGIES USED IN THE STRESS TEST

Stress testing methodologies focus on empirically defining the relationship between macroeconomic variables and production volumes, revenues, credit losses, and expenses in order to estimate outcomes for the hypothetical Severely Adverse Scenario. The Company utilizes a series of statistical and financial models, paired with management judgment, to project pre-provision net revenues (PPNR), provisions for loan losses (provision), income tax expenses, balance sheet, and capital ratios. The models utilized undergo a robust series of model risk management procedures, a third party validation, and an internal audit.

To manage the stress testing and capital adequacy assessment processes, the Company has developed a stress testing framework. The framework specifies roles and responsibilities of the Board of Directors, management, and various committees which aid in the development, oversight and review of the Company's stress testing process. Each committee is comprised of senior management across multiple lines of business to provide for the effective challenge of assumptions, methodology and results. The overall goal of the framework is to help management and the Board of Directors better understand the integrated sensitivity of various risk exposures through quantifying the potential financial and capital impacts of hypothetical stress events and scenarios.

RESULTS

The stress testing results provided in this disclosure should not be interpreted as expected or likely outcomes, but rather as a possible result under hypothetical, severely adverse economic conditions.

Table 1 below displays nine quarter cumulative results under the Supervisory Severely Adverse Scenario for the Company and the Bank over the nine-quarter time horizon.

Table 1 - Supervisory Severely Adverse Scenario Cumulative Nine Quarter Revenue, Expense and Income (\$ In mms)		
Measurement	Bank	Bancorp
Pre-provision net revenue	\$175.2	\$158.8
Provision expense	275.5	275.5
Income tax expense	<u>(34.1)</u>	<u>(39.7)</u>
Net loss	<u>(\$66.2)</u>	<u>(\$77.1)</u>

Table 2 below displays nine quarter cumulative credit losses under the Supervisory Severely Adverse Scenario for the Bank's held-for-investment loan portfolios. There is no difference in credit losses at the Bank compared to the Company.

Table 2 - Supervisory Severely Adverse Scenario Cumulative Nine Quarter Credit Losses (\$ In mms)		
Loan portfolio	Nine quarter cumulative credit losses	Cumulative portfolio loss rate (1)
1st lien residential mortgages	\$98.6	3.8%
Commercial real estate	66.8	6.9%
Commercial and industrial	34.7	4.4%
All other loans	<u>38.2</u>	2.3%
Total	<u>\$238.3</u>	4.0%

(1) Calculated on a cumulative basis by dividing the nine quarter cumulative net losses by the average portfolio balance over the same period.

Capital estimates (pro forma regulatory capital ratios) were developed utilizing quarterly pro forma financial statements produced by the stress testing process. Changes to equity reflect

the net income estimate for the quarter. The equity is then adjusted for certain regulatory deductions as defined by Regulatory Capital Rules. In each quarter, the Basel III rules in place for that quarter were utilized for projecting pro forma regulatory capital. The pro forma balance sheet was utilized to project risk-weighted assets, based on changes in the overall balance sheet size and asset mix.

Tables 3 and 4, below, display the pro forma regulatory capital ratios in the hypothetical Supervisory Severely Adverse Scenario over the nine quarter projection period for the Company and the Bank. The pro forma ratios reflect certain assumptions related to capital actions, as prescribed by the Dodd-Frank Act. No common dividends, share repurchases, or other capital transactions are assumed to occur during the nine quarter projection period. Per regulatory guidance, the DFAST exercise does not consider the capital transactions approved in June 2016 and executed in July 2016 that redeemed the Fixed Rate Cumulative Perpetual Preferred Stock (formerly "TARP").

Table 3 - Pro Forma Regulatory Capital Ratios, Bancorp

Supervisory severely adverse scenario	Actual 12/31/15	Stressed ratios		"Well Capitalized" Regulatory Minimum (1)
		3/31/18	Minimum	
Common equity Tier-1	14.1%	11.8%	11.8%	6.5%
Tier 1 capital	19.0%	18.6%	18.2%	8.0%
Total risk-based capital	20.3%	19.9%	19.5%	10.0%
Tier 1 leverage	11.5%	11.6%	11.2%	5.0%

(1) As defined under the Prompt Corrective Action regulatory requirements.

Table 4 - Pro Forma Regulatory Capital Ratios, Bank

Supervisory severely adverse scenario	Actual 12/31/15	Stressed ratios		"Well Capitalized" Regulatory Minimum (1)
		3/31/18	Minimum	
Common equity Tier-1	19.4%	19.7%	19.4%	6.5%
Tier 1 capital	19.4%	19.7%	19.4%	8.0%
Total risk-based capital	20.7%	21.0%	20.6%	10.0%
Tier 1 leverage	11.8%	12.3%	11.6%	5.0%

(1) As defined under the Prompt Corrective Action regulatory requirements.

Tables 5 and 6, below, display the key drivers of changes to the regulatory capital ratios in the hypothetical Supervisory Severely Adverse Scenario over the nine quarter projection period for the Company and the Bank, respectively.

Table 5 - Key Drivers of Changes In Regulatory Capital Ratios, Bancorp

Supervisory severely adverse scenario	CET-1 Ratio	Tier-1 Capital	Total RBC	Tier 1 Leverage
Beginning ratio	14.1%	19.0%	20.3%	11.5%
Pre-provision net revenue	2.1%	2.1%	2.1%	1.3%
Provision expense	-3.6%	-3.6%	-3.6%	-2.2%
All other (1)	-0.8%	1.1%	1.1%	1.0%
Ending ratio	<u>11.8%</u>	<u>18.6%</u>	<u>19.9%</u>	<u>11.6%</u>

- (1) "All Other" incorporates changes in risk-weighted assets, income taxes, and all other adjustments, including regulatory capital adjustments related to mortgage servicing assets and deferred tax assets.

Table 6 - Key Drivers of Changes In Regulatory Capital Ratios, Bank

Supervisory severely adverse scenario	CET-1 Ratio	Tier-1 Capital	Total RBC	Tier 1 Leverage
Beginning ratio	19.4%	19.4%	20.7%	11.8%
Pre-provision net revenue	2.3%	2.3%	2.3%	1.4%
Provision expense	-3.6%	-3.6%	-3.6%	-2.2%
All Other (1)	1.6%	1.6%	1.6%	1.3%
Ending ratio	<u>19.7%</u>	<u>19.7%</u>	<u>21.0%</u>	<u>12.3%</u>

- (1) "All Other" incorporates changes in risk-weighted assets, income taxes, and all other adjustments, including regulatory capital adjustments related to mortgage servicing assets and deferred tax assets.