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Fannie Mae Board of Directors CEO Report 10-18-2005

Federal National Mortgage Association (Fannie Mae)

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Fannie Mae Board of Directors CEO Report

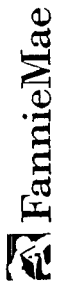
October 18, 2005

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BY FANNIE MAE

Confidential Treatment
Requested By Fannie Mae

FMSE 534693

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Executive Summary

- **Business:** Both Credit Guaranty businesses on solid footing; Portfolio remains constrained by market conditions and Capital Restoration Plan
- **Housing and Minority Lending Goals:** All-out effort underway; prospects to achieve PMM sub-goals weak
- **Katrina/Rita:** 8-K filed estimating after-tax losses expected to be in a range of \$250 to \$550 million
- **Competition:** Remains intense
- **Foundation:** Disaster relief aid and Help the Homeless top priorities; minor 2002 and 2003 restatement required
- **Legislative:** Compromise reached in the House, which may clear the way for a full House vote during the week of October 24; Senate remains in "wait" mode
- **HR:** New organization to best align all functions
- **Other Matters:** Early read on impact of outreach to media, business, and policy advocates positive

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Business Update: Guaranty Business

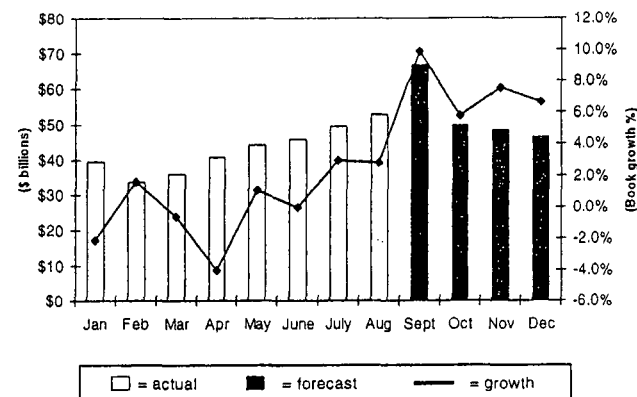
Single-Family

- Volume through August at \$340.7B, \$7.2B above plan
- Volume outlook for the year at \$553.6B, \$54.4B above plan
- Full-year book growth forecasted at 2.6%, compared to target of 1.75% (original plan of 4.2%)
- Net charged fee through August at 24.4 bps, 1.6 bps under plan
- Borrowers are beginning to switch from ARMs to fixed rate mortgages, our signature product
- Successfully launched new customer-focused organization
- Continuing to focus on:
 - Business retention
 - Competitive pressures (private label and subprime)
 - Regulatory and minority lending goals

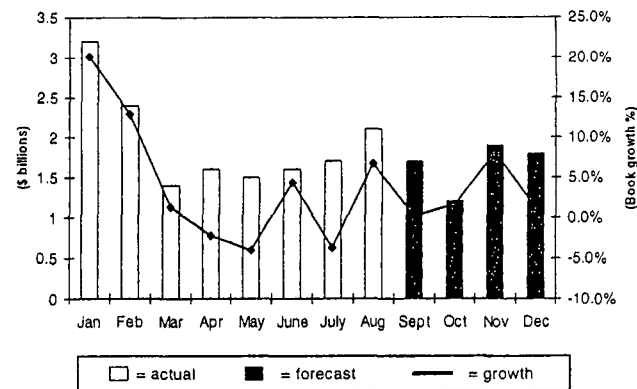
Multifamily

- Volume through August at \$14.9B, \$3.0B above plan
- Charged guaranty fee through August at 26.0 bps, 3.2 bps above plan; higher fees due to favorable product mix
- Book growth is significantly below plan (2.8% vs. 7.3%), resulting from higher than expected liquidations
- Credit losses through August were \$23.8 million, significantly favorable to plan of \$65.6 million
- Continuing to implement New DUS; increased authority for Business Heads to make underwriting decisions; circulating streamlined Loan Narrative for comment; approved movement of Quality Control to Standard Flow Loan Channel group

Single-Family Volume and Book Growth



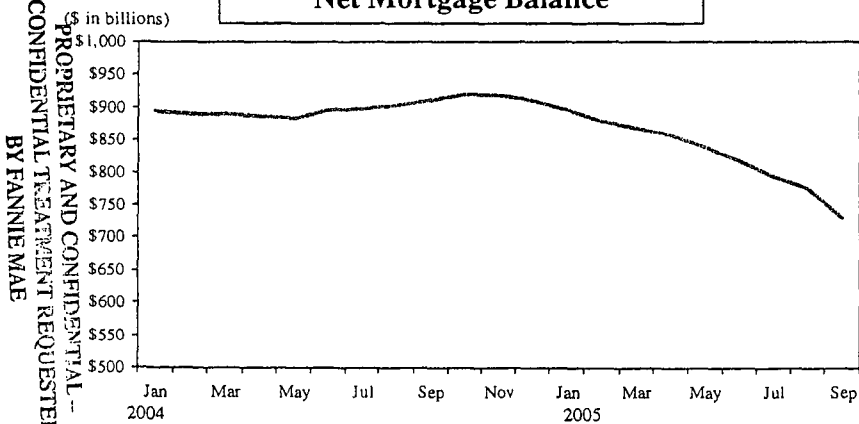
Multifamily Debt & Equity Volume and Debt Book Growth



Business Update: Portfolio Business

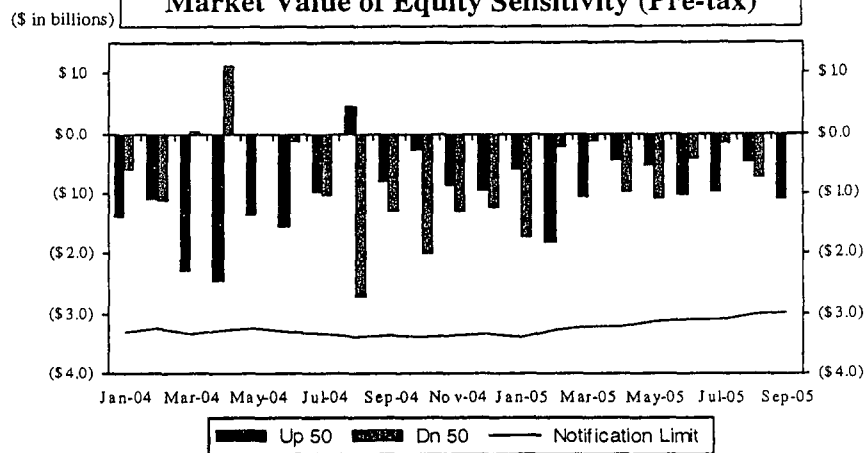
- Short-term interest rates have steadily increased over the year in line with Fed Funds rate hikes
- Debt to swap spreads have improved due to decreased issuance
- Mortgage option-adjusted spreads have remained very tight
- Market value risk of the portfolio managed actively, with sensitivity for +/- 50bp change in rates under \$2B (pre-tax) throughout 2005
- Monthly portfolio duration gap reported at +/- 1 month or less through September
- Mortgage balance growth through September is -25% annualized, driven by tight MBS spreads and the Capital Restoration Plan

Net Mortgage Balance



The Net Mortgage Balance includes a mark-to-market adjustment for all securities available for sale

Market Value of Equity Sensitivity (Pre-tax)



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Business Update: Corporate Objectives – August Report

	Current Month	Past Month
Priority 1: Become a first-rate regulated company		
1 Foster productive relationship with OFHEO	●	●
2 Fulfill OFHEO Agreement	●	●
3 Achieve significant progress in restating earnings and completing audit	▽	▽
4 Achieve capital restoration target levels	●	●
5 Work with Congress and the Administration on regulatory reform	▽	●
Priority 2: Meet the tremendous business challenges		
<u>Single Family, including eBusiness</u>		
6 Maintain leadership and retain or grow our key accounts	▽	▽
7 Address key competitive issues and maintain 30% MDO share	▽	▽
8 Implement products and exceed target book growth of 1.75%	▽	●
9 Increase participation in subprime	●	●
10 Use technology tools for process improvement and delivery preference	●	●
<u>Multifamily/HCD</u>		
11 Set up mezzanine financing and address borrower concentration	▽	●
12 Develop alternatives to the current DUS program	▽	▽
13 Refine and implement new ACF strategy	▽	▽
<u>Portfolio</u>		
14 Enhance business model	●	●
15 Develop new tools to buy and sell assets more actively	●	●
16 Manage debt issuance to maximize port. value and improve executions	●	●
<u>Corporate</u>		
17 Cut non-priority areas and re-allocate resources to priority initiatives	●	●
18 Maintain MBS as the most liquid security	●	●

	Current Month	Past Month
Priority 3: Be true leaders in affordable housing		
19 Achieve the HUD Goals	●	▽
20 Lead the market in minority lending and achieve targets	●	●
21 Achieve the ADC 3.0 targets	▽	▽
Priority 4: Instill operational discipline		
22 Implement SF Core	●	●
23 Implement HCD Core	▽	▽
24 Implement systems for Portfolio biz model and ops requirements	●	▽
25 Optimize MBS organization, practices, and controls	▽	▽
26 Implement Finance transactions, accounting and control systems	▽	●
27 Implement operational risk oversight framework and controls	▽	▽
28 Create and implement Chief Risk Officer function	●	●
Priority 5: Care for our people and culture		
29 Implement compensation recommendations	●	●
30 Develop culture that supports business and mission	▽	▽
31 Implement a "One Fannie Mae" customer relationship strategy	▽	▽

Key	
⊗	Achieved
●	On-track to meet Corporate Objective
▽	Meeting Corporate Objective uncertain
●	Off-track to meet Corporate Objective
⊗	Will not achieve this year

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Key	
⊗	Achieved
●	On-track to meet Corporate Objective
▽	Meeting Corporate Objective uncertain
●	Off-track to meet Corporate Objective
⊗	Will not achieve this year

Housing and Minority Lending Goals Update

STATUTORY HOUSING GOALS

	FY05 Plan	8/05 YTD Actual
Low Mod (Affordable)	52.00%	54.15%
Special Affordable	22.00%	25.66%
Underserved	37.00%	40.35%

PMM SUB-GOALS

	FY05 SF PMM Sub-Goal Plan	8/05 YTD Actual
Low Mod (Affordable)	45.00%	42.32%
Special Affordable	17.00%	15.16%
Underserved	32.00%	30.76%

MINORITY LENDING GOALS

	FY05 Target	8/05 YTD Actual
African American	5.40%	5.24%
Hispanic	11.60%	11.17%
Total Minority	24.70%	23.66%

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Issue

- Although we remain above target on our three base regulatory goals, August scores deteriorated; Multifamily's strong performance continues to bring corporate scores above goal
- HUD denied our request to include reverse mortgages in the regulatory PMM sub goals; as a result, sub goal performance fell significantly below target for all three goals
- Tension exists between strategies to meet PMM sub goals and minority lending targets (deals may support one goal and negatively affect another)

Next Steps

- We are aggressively pursuing all opportunities with a focus on the enforceable regulatory goals:
 - CitiFinancial Portfolio
 - B of A Whole Loan Strategy
 - CitiMortgage/Self Help
 - Other Subprime Portfolios
 - Acquire Manufactured Housing Loans
- Direct acquisition of subprime whole loans
- MCM Enhancements
- Continue to brief HUD and OFHEO on efforts and expectations of success

Other Options

- Defer \$13.5-\$17.4 billion of projected 4Q non-goals loans
- Direct acquisition of subprime whole loans
- Manufactured housing chattel

Katrina/Rita Update

Allowance Impact Summary as of 10/7/05

(\$ in millions)	Low End Estimate	High End Estimate
Single Family Loans	\$320	\$700
Multifamily Loans	75	150
Total Pre-tax Impact	395	850
Total After-tax Impact (35%)	257	553
Range Disclosed in 8K Filing on Oct. 7, 2005	\$250	\$550

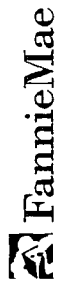
(additional Katrina/Rita impact information will be provided at the Board Meeting)

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Competitive Update: Primary Market

Mortgage Origination

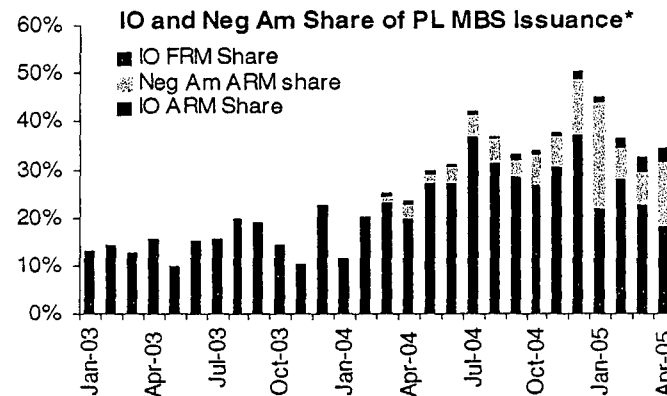
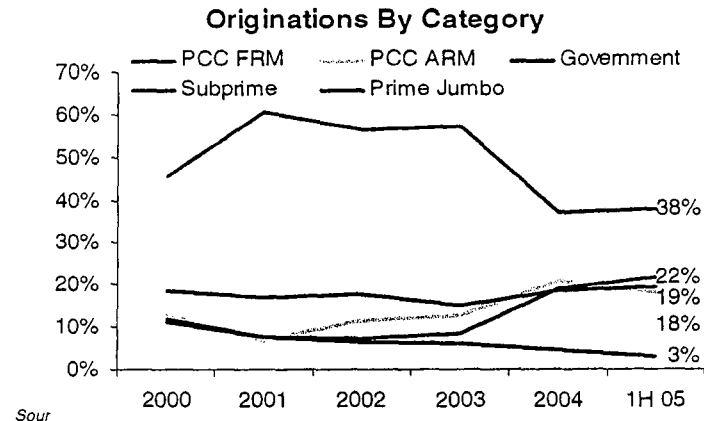
- Prime conventional conforming (PCC) FRM share has stabilized
- PCC ARM share is down from its 2004 peak, but remains high
- Subprime share of originations up slightly from 19% in 2004 to 22% in 1H 05, but margin compression is forcing lenders to raise rates
- Alt A share of originations up from 6% in Q1 04 to 12% in Q2 05

“Exotic” Products

- Combined share of IO and negative amortization (neg am) products down from peak, but neg am share growing

Consolidation

- Top-5 lenders’ share of originations moved from 44% in 2002 to 45% in 1H 05
- Countrywide is the only top-5 lender growing faster than market
- Other top-5 (Wells Fargo, Washington Mutual, JP Morgan Chase, BofA) shares are flat or down since 2004



*PL MBS data is used as a proxy for Neg Am and IO shares of originations not delivered to the agencies
 Source: Fannie Mae Economics & Mortgage Market Analysis, Inside MBS & ABS; based on Loan Performance data for loans backing Alt A, Jumbo, and Subprime MBS

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Competitive Update: Primary Market

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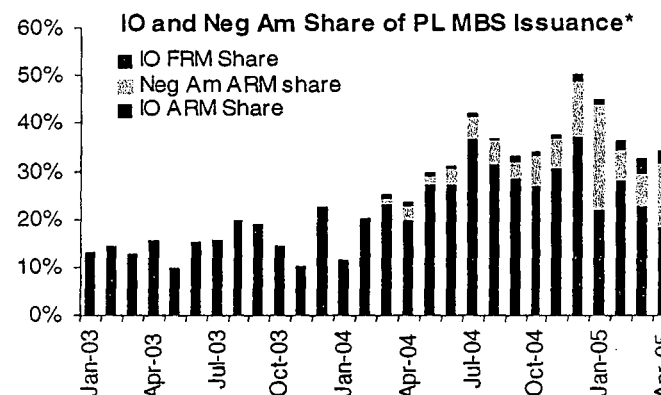
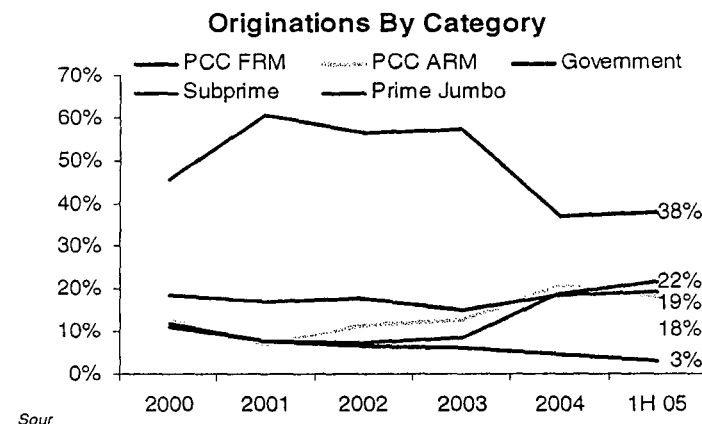
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Competitive Update: Secondary Market

Private Label MBS Issuance

- Share has leveled off, but remains more than combined agency share
- Credit enhancement concerns forcing lenders to tighten underwriting

Freddie Mac

- Freddie Mac closing in on our book of business and portfolio size; our share of credit risk remains higher
- Rapid growth in private label MBS held in their portfolio
- Expanding PC disclosures
- Expanding structured securities issuance capabilities

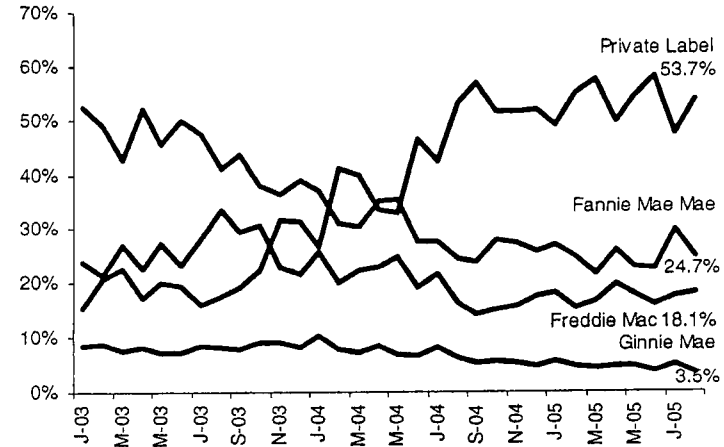
Ginnie Mae and FHLB

- Share remains low
- HUD attempting to make FHA more competitive

Bank mortgage holdings

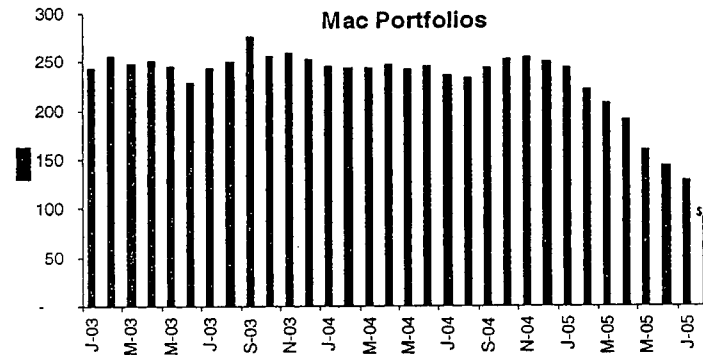
- Growing on par with MDO
- BofA and Countrywide growing faster than the market

Share of New MBS Issuance



Source: Inside MBS & ABS, Corporate Development

Difference in Size of Fannie Mae and Freddie Mac Portfolios



Source: Inside MBS & ABS, Corporate Development, company reports

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Foundation Update

18th Annual Help the Homeless Campaign

- Marlon Byrd of the Washington Nationals will serve as Honorary Chair of the Walkathon Saturday, November 19 and appear at the HTH Auction on Friday, November 18 at Fannie Mae
- 166 campaign sponsors recruited thus far to help support 178 local service providers
- The Foundation will donate an additional dollar for hurricane relief for every Help the Homeless walker

Disaster Relief

- Eligibility for the special double match announced in September expanded to any contribution to the American Red Cross for U.S. disaster relief, including recovery from Hurricane Rita
- As of October 4, 773 employees have requested matches for contributions of \$202,293; with \$404,586 in matches from the Foundation, plus the initial \$500,000 Foundation contribution, the current total donated to the Red Cross is \$1,106,879
- A Foundation task force will soon make recommendations for how best to invest the additional \$500,000 committed to mid- and long-term rebuilding efforts

Foundation Gifts Program Revisions

- Retirees will become ineligible for the Matching Gifts and Dollars for Doers programs as of 1/1/06
- Effective 1/1/07, the annual Matching Gift limit will be reduced to \$5,000 (from \$10,000) and the 2:1 match (for up to \$500) will be eliminated

Restatement of Foundation Financials

- The Foundation will restate its 2002 and 2003 audited financial statements as a result of Fannie Mae's conclusion that it did not have sufficient documentation to support its 2002 financial statements' recording of an unconditional promise to donate \$25 million to the Foundation (per FAS 116 – Accounting for contributions received and contributions made)
- The Foundation will likely amend its prior year federal tax information returns as well

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Legislative Update

FALL CONGRESSIONAL PRIORITIES

- Judiciary – Supreme Court Nominee
- Federal Spending
- Hurricane/Disaster Relief

GSE LEGISLATION IN THE HOUSE

- House Financial Services Committee approved GSE legislation on May 25th, by a 65-5 vote
- Retained portfolio language gives the regulator authority to address safety and soundness issues
- House Financial Services Committee Chairman Oxley reached a compromise with House conservatives in their disagreement over eligible uses of the Affordable Housing Funds (AHF), which may clear the way for a full House vote on the legislation during the week of October 24; the compromise includes:
 - Previous agreement to give priority consideration in the AHF to building affordable housing in the Gulf Coast Communities hit by Hurricane Katrina
 - New language also makes it clear that groups who engage in Federal election activity could not receive any AHF funds

GSE LEGISLATION IN THE SENATE

- On July 28th, the Senate Banking Committee passed, in an 11 to 9 party-line vote, Senator Shelby's GSE bill; both Democrats and Republicans, on and off the Senate Banking Committee, have expressed concern over the portfolio provision in the Senate bill

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HR Update

- Launched new HR organization based on Mercer Consulting work to best align all of the functions of the Human Resources team, in support of the company's focus on the recognition and development of our people
- **Kristy Williams** will lead the “People and Culture” component of our work:
 - Remake our corporate culture to emphasize SEAM
 - Drive our overall “People Strategy,” including diversity, human capital, workforce and leadership development, and succession planning
- **Betty Thompson** will lead HR Management and Operations, ensuring we'll take a consistent and rigorous approach to this function:
 - Staffing and recruiting
 - Compensation and benefits
 - Account management
 - HR systems and operations for the company

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Other Matters

MEDIA

- 9/28: Dow Jones September wire story
 - Original focus shifted in response to facts provided and inquiries to reporter by OFHEO and Senator Rudman
 - Following the story, OFHEO affirmed company's "adequately capitalized" classification and said "it anticipates Fannie Mae will meet the capital target for September 30, 2005."
- 9/29: Wall Street Journal – broad and productive discussion in New York with 11 editors and reporters including
 - Alan Murray, assistant managing editor
 - Bob Hagerty, real estate reporter
 - Leslie Scism, Money & Investing news editor
 - Connie Mitchell-Ford Mitchell, economics editor
- New York Times, Wall Street Journal, and The Washington Post have expressed interest in doing pieces; working with the reporters to see what we can provide during the quiet period

OUTREACH

- 9/21: Business Roundtable - CEO roundtable discussion with the Republican House Leadership
- 9/29: John Thain, NYSE and CEO roundtable discussion with Commerce Secretary Gutierrez
- 9/30: Peter Wallison, AEI
- 10/4: Zoe Cruz, Acting President, Morgan Stanley
- 10/13: Bert Ely