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Action Plan for the Housing Goals Rewrite

- Size the goals market
- Assess potential goals performance of our business
- Evaluate alternative goals approaches
- Identify key policy issues and build our positions

Detailed Analysis and Appendix

Revised January 22, 2003

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Building the Strategy: Key Issues

- Political and Policy Context
  - Politics will mostly press for higher goals
  - MBA and others will push for new structures or increased targeting
  - Realtors and multifamily lenders potential allies against higher goals
- Market Context
  - 2002 was a very challenging year for meeting current goals
  - HUD will estimate a future goals market larger than current goals
- Business Context
  - We can meet current goals under projected market conditions -- if HUD retains current bonuses and business climate is favorable
  - Current goals mean continued possibility of diminished margins and increased credit risks in years with large SF refinance volumes
- Successful Outcomes
  - Retaining current goals is the preferred business outcome
  - Alternative goals structure may help manage future market risks
  - Strategic questions -- tone, timing, enrollment -- are critical

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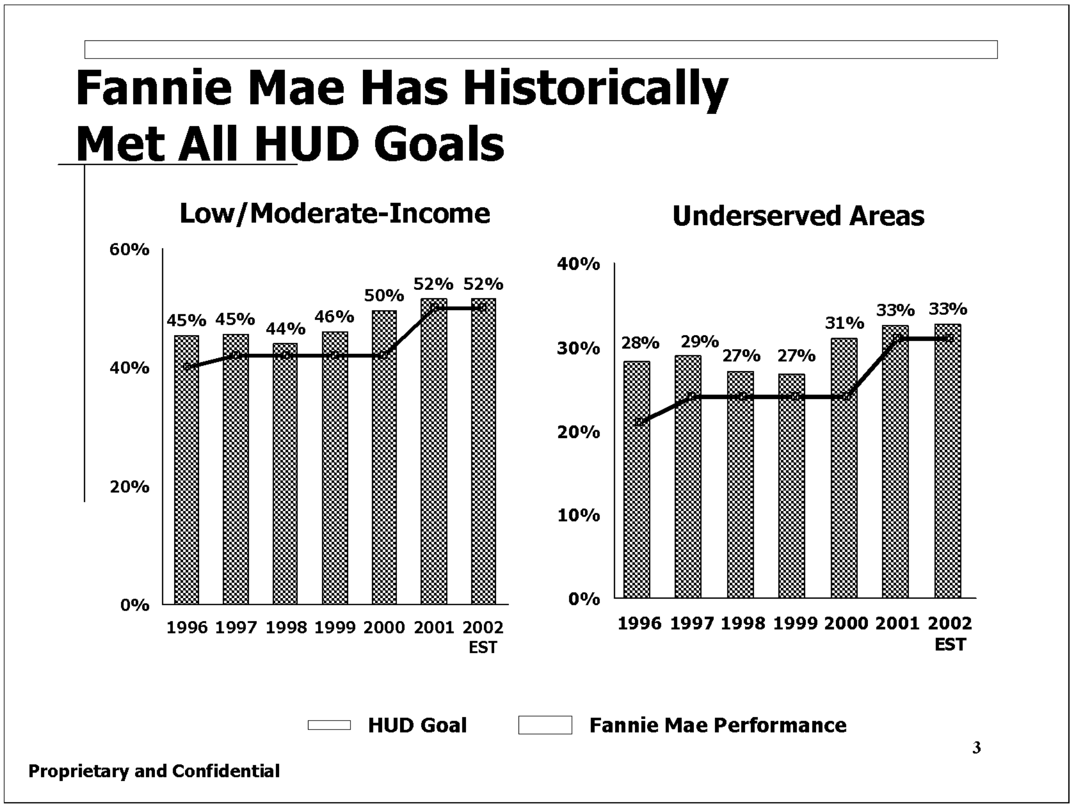

Fannie Mae Has Historically Met All HUD Goals
Low/Moderate-Income
60%
40%
20%
0%
45% 45% 44% 46% 50% 52% 52%
1996 1997 1998 1999 2000 2001 2002 EST
Underserved Areas
40%
30%
20%
10%
0%
28% 29% 27% 27% 31% 33% 33%
1996 1997 1998 1999 2000 2001 2002 EST
HUD Goal
Fannie Mae Performance
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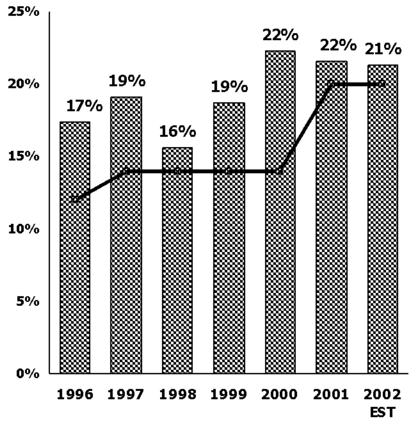
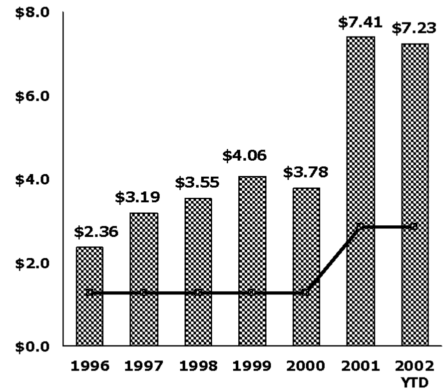
Fannie Mae Has Historically Met All HUD Goals

Special Affordable



Special Affordable MF Subgoal ($ billions)



HUD Goal   Fannie Mae Performance

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Political and Policy Context: Competing Pressures Expected

Political Environment

- Administration
  - Statements suggest predisposition toward higher goals and a focus on minority first-time homebuyers
- Freddie Mac
  - Exploring changes to current goals
  - Will pursue renewal of MF adjustment factor
- Congress
  - Deferred to HUD in last cycle
- Industry and Other Groups
  - Some pressures for increases from advocates
  - MBA has called for separate SF and MF goals and for income targeting like CRA
  - Realtors oppose allocation of credit away from middle-income buyers
- Multifamily Industry
  - Concerns that goals push for low-income homeownership is hurting rental housing
  - Concerns that goals create an incentive for "irrational" multifamily market participation

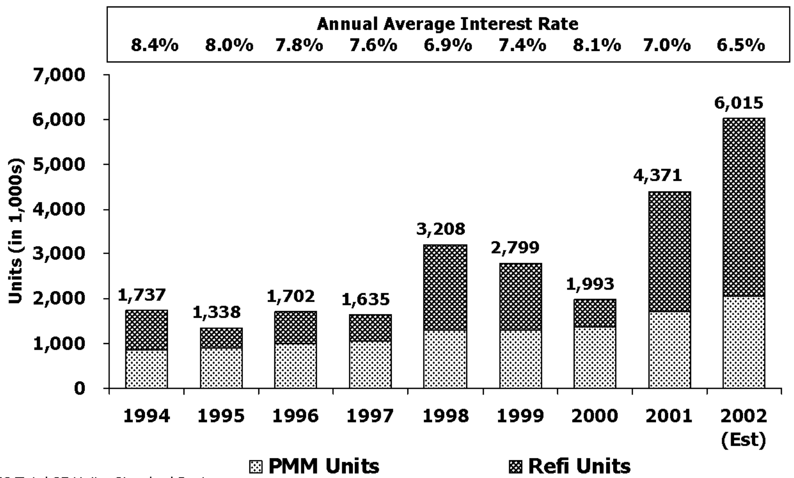
Policy Risks

- Possible Loss of Bonuses
  - Current bonuses expire after 2003: extension requires action this year
  - Freddie Mac adjustment factor
- Possibility of New Subgoals
  - Rural or manufactured
  - PMMs or minority first-time homebuyers
- Potential for New Requirements
  - Tighter targeting on underserved areas
  - Increased data disclosure
  - Additional restrictions on predatory lending
  - Expanded new program approval authority
  - Fair lending enforcement
  - Scoring tied to credit risk

2002 Business Context:

Soaring SF Refinance Volumes Made for Difficult Goals Year

Fannie Mae Single-Family Business (units)



Source: FMIS Total SF Units, Standard Business.

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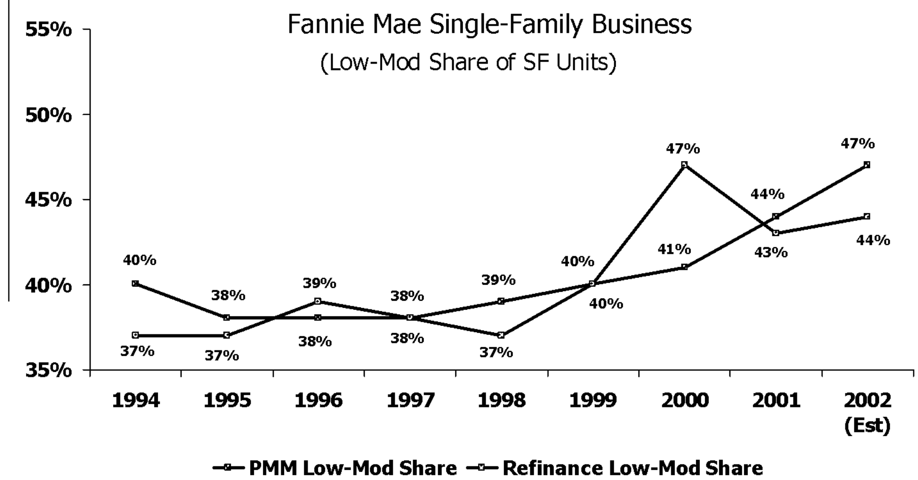
2002 Business Context:

Though SF has Become More Goals Rich, Refinances Depressed Performance



Source: FMIS Total SF Units, Standard Business. Treats all missing data as not affordable and excludes bonus.

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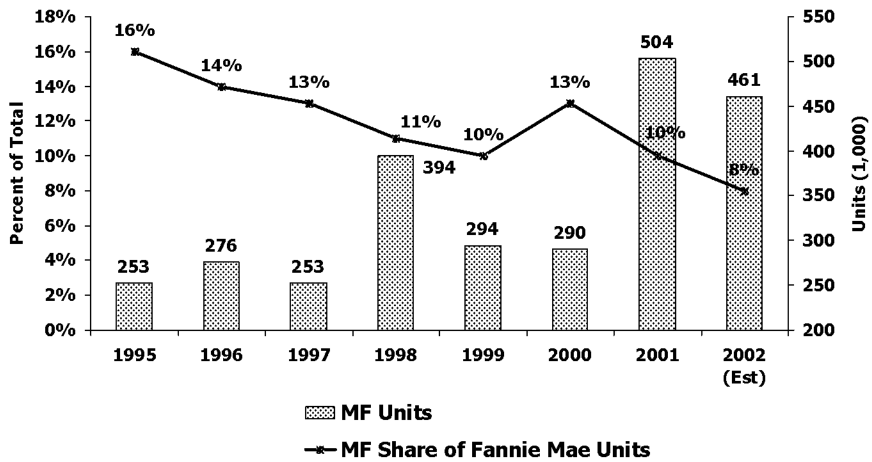
2002 Business Context:

SF Business Volumes Drove MF Share of Units to Historic Lows

Multifamily share of business is a major driver of goals performance.



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Looking Forward: Market Size Projections

- Size the goals market and potential variability
- Highlight differences between HUD and Fannie Mae's market projections
- Identify the drivers of the housing goals market

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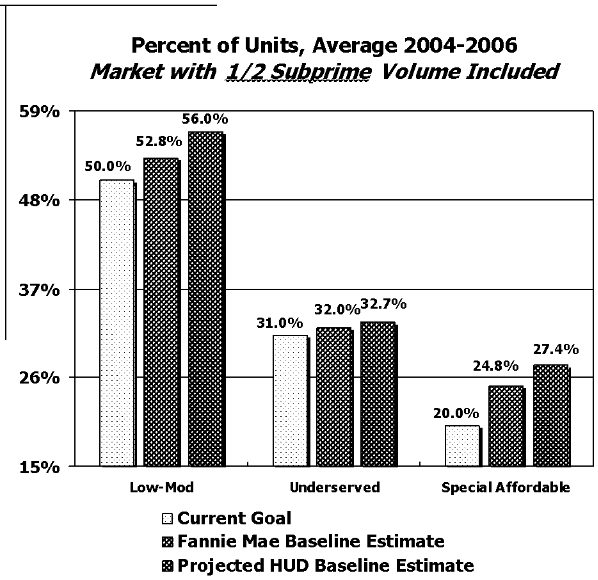
Size of the Market:

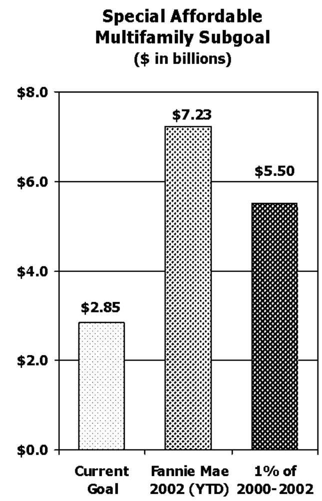
HUD and Fannie Mae Will Likely Differ on Market Sizing Assumptions

- Fannie Mae and HUD estimate different market originations volumes
  - Fannie Mae starts with internal projections of the SF and MF markets
  - Estimate of multifamily market size will most likely differ due to lack of a single reliable source of data for industry
  - HUD traditionally has assumed a larger multifamily market and a smaller single-family market than Fannie Mae
- Size of SF rental market is uncertain and subject to debate
  - HUD uses higher estimate of this market based on decade-old study
  - Fannie Mae uses observed values from HMDA
- Fannie Mae and HUD differ on SF goals richness
  - HUD likely to project that higher participation of low-mod households in the market will continue
  - Fannie Mae uses lower longer-term average to account for potential future variations

Size of the Market:

HUD Will Likely Cite Larger Affordable Markets than Current Goals





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Size of the Market:

Lower SF Refinances and Increasing Subprime Drive Projected Market Profile

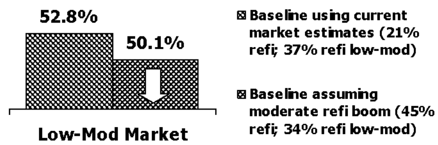
- SF volume drops while MF grows slowly
  - Refinance share of SF drops back to historical average as interest rates rise above 7%
  - MF market projected to increase slowly but steadily after drop in 2002
- Subprime share of SF market projected to increase
  - Increase from 11% in 2001 to 20% in 2006

Market Drivers	1997-2000	2001-2003	2004-2006
Unemployment Rate	4.4%	5.4%	5.2%
FRM Interest Rate	7.5%	6.6%	7.0%
Home Price Appreciation	6.0%	5.9%	4.6%
Refi Share of SF Units	35.0%	56.0%	23.8%
Subprime Share of SF Units	16.2%	11.5%	19.7%
Rental Share of SF Units	13.1%	12.5%	12.8%
Single-Family Low-Mod Richness	48.6%	46.7%	48.7%
Multifamily Share of Total Units	11.9%	6.6%	9.0%
Multifamily Low-Mod Richness	90.0%	87.5%	87.5%
Low-Mod Market Size (with ½ subprime)	**53.8%**	**49.7%**	**52.8%**

Goals Strategy Needs to Consider Potential Variability in Market Profile

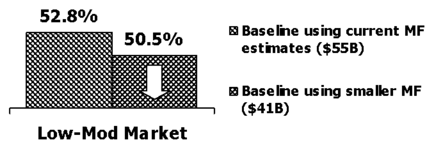
Single-Family Refinance Boom

- A moderate refinance boom during 2004-2006 could lead to a low-mod market size as low as 50%



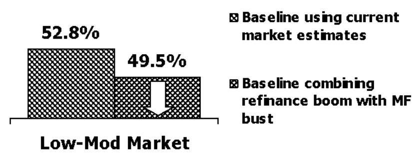
Multifamily Bust

- A 20% drop in the projected MF market would result in low-mod market size close to 50%



SF Refinance Boom *and* MF Bust

- The combination of these two scenarios could result in a market size below 50%



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Looking Forward: Business Projections

- Project the goals potential for Fannie Mae's business
- Identify the drivers of future Fannie Mae performance

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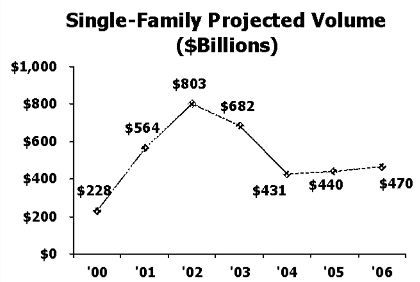
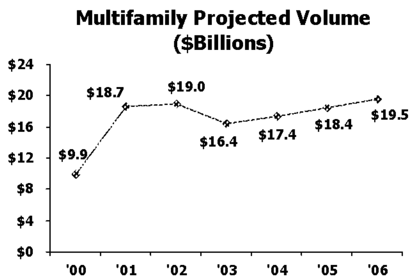
FNM Business Projections:

Projections of Performance Begin with Projections of MF and SF Volumes





Single-Family

- 2003 expected to produce second largest volume ever
- In 2004-2006, single-family business projected to return to annual volumes of $400-500 billion.

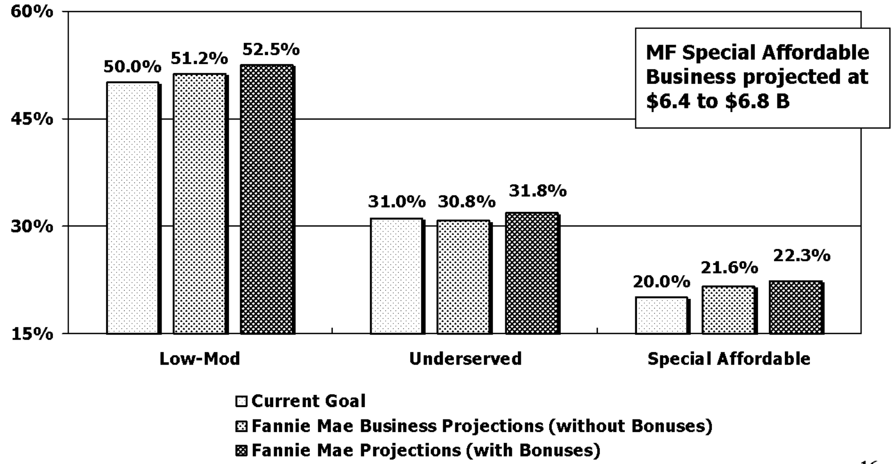
Multifamily

- 2003 volumes of $17-19 billion projected
- Based on these projections, MF shares of total units will average 12.6% of units over the 2004-2006 period

FNM Business Projections:

Projections Suggest We Can Continue to Meet Current Goals – With Bonuses

Percent of Units, Average 2004-2006
Based on SF and MF Business Volume Projections
Assuming No Repeat of Refinance Boom



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FNM Business Projections:

Subprime and SF Rental Drive Projected Increase in Goals Performance

- Subprime and SF rental have driven increases in current score.
- Subprime products to continue to increase through 2004-06.
- End of high refinance shares projected to increase multifamily share back to levels achieved during the late 1990s

Business Drivers	1997-2000	2001-2003	2004-2006
Refi Share of SF Units	45.0%	64.1%	27.1%
Subprime Share of SF Units	0.0%	3.2%	9.5%
Rental Share of SF Units	6.5%	9.3%	9.3%
SF Low-Mod Richness	39.5%	44.1%	46.0%
MF Share of Total Units	12.0%	8.6%	12.6%
MF Low-Mod Richness	92.5%	91.3%	90.0%
Bonus Points	none	2.0%	1.3%
Low-Mod Performance	**46.2%**	**50.7%**	**52.9%**

Projected Performance Depends on Key Assumptions Going Forward

- Market Conditions
  - Goals richness of SF and MF markets stays at recent levels
  - Interest rates climb above 7% by 2005
  - No repeat of SF refinance boom as experienced in 2001-2002
- Business Practices
  - Appetite for higher SF credit risk products continues
  - Continued penetration of SF rental markets
  - Historical balance between MF and SF is restored
    - **SF volumes below $500 Billion**
    - **MF volumes at $17-19 Billion**
- Goals Structures
  - Bonuses and proxies are retained
  - Freddie retains Temporary Adjustment Factor

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Exploring Alternative Approaches to Housing Goals

- Are there options for reducing effects of market volatility?
- What options could respond to pressures to do more?
- Are there alternative goals structures that are more manageable?

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Development of Strategy Examined Four Possible Approaches to Goals

- Option 1: Maintain Current Goals Structure
  - Within current structure there are possibilities for more favorable scoring conventions and other adjustments.
- Option 2: Align Goals with CRA
  - Lending industry participants have advocated aligning Fannie Mae goals with CRA income and geographic targeting at 80% AMI.
- Option 3: Separate SF and MF Goals
  - In 2000 process, MBA proposed setting separate SF and MF goals.
  - MBA proposed low-mod goals of 44% for SF and 95% for MF.
- Option 4: Add Structures to Address Market Volatility
  - Counting rules could change to protect against effects of high levels of SF refinances or could adjust annual goals to market opportunities.

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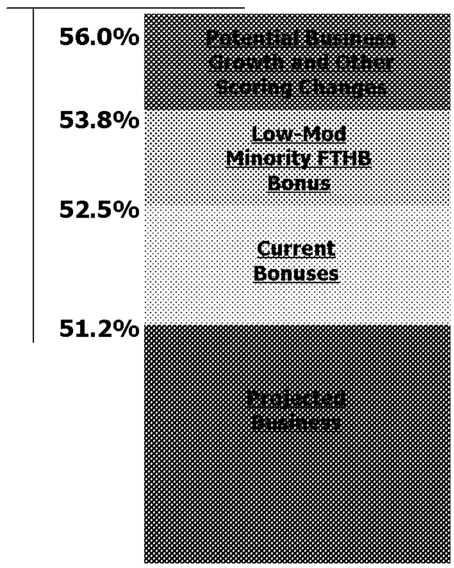
Option One:

Vary Existing Goals Structure

Category	Menu of Options
Goals Levels	• Propose no change based on 2002 experience • Adopt increases ***only*** with favorable changes to scoring conventions or with new bonuses
Scoring Conventions	• Make no changes to current scoring • Expand missing data treatment and/or proxies for MF and SF rental units • Allow goals credit for MRB units
Bonuses and Subgoals	• Retain existing bonuses • Retain Freddie Mac's Multifamily Temporary Adjustment Factor • Add new bonuses to align with planned initiatives
Related Initiatives	• Offer no new initiatives • Offer new initiatives (e.g. additional minority goals or a SF rural effort) in return for maintaining goal level
Timeframe	• 2004-2006 • Align with *American Dream Commitment* timetable • Phased in new goals over multiple years

Option One:

Options for Bringing Housing Goals Scores Closer to HUD's Market Estimate



Potential Business Growth
- Manufactured housing
- Increase SF rental above 9.3% of total (2001-03)
- Increase small MF business with bonuses
- Goals credit for FHA SF risk-sharing units

New Scoring Conventions and Bonuses
- Bonus for LMI minority first-time homebuyers
- Proxy for SF rental missing data (now excluded)
- Increased SF OO missing data exclusion to 2%
- Expand ability to proxy MF units
- Credit for MRB units

Current Scoring Conventions and Bonuses
- Exclude 1% of SF units in LMI tracts missing data
- Apply proxy data for rents on MF units up to 5%
- Bonuses for OO 2-4 Units and MF 5-50 Units

Option One:

Assessment of Current Structure:

Familiar, but Lacks of Flexibility for Wide Market Fluctuations

Advantages

- Company is familiar with goals; avoids the risks and uncertainty of change
- Administratively easier and less expensive to retain existing systems and infrastructure
- Allows flexibility to pursue goals through various products, business lines, and channels
- Does not require charter changes
- Produces quantitative measures of Company's public benefits

Disadvantages

- Structure brings continued pressures to increase percentage of business dedicated to goals
- Once goals have increased they are difficult to bring back down
- SF refinance booms have forced significant year-end costs and risks to purchase additional units
- Percent of business goals create pressures to allocate credit in difficult years
- No built-in scoring flexibility for dealing with wide fluctuations in market
- New initiatives are difficult to manage alongside multiple existing goals

Option Two:

Align Goals with CRA?

- Community Reinvestment Act (CRA) requires depositories to reinvest in the communities from which they take deposits
- MBA and others have advocated that housing goals targeting should mirror CRA requirements
  - Industry focus is on applying CRA targeting to Fannie Mae and Freddie Mac: Income targets at 80 percent of area median incomes and geographic targeting to census tracts of with 80 percent AMI
  - Under existing housing goals statutes, HUD could adopt CRA geographic targeting, but not income targeting
- CRA has other features with potential applicability to housing goals and alignment with industry
  - Lenders assessed in three areas: lending, investments, and services.
  - Examiners assign ratings --"Outstanding," "Satisfactory," "Needs to improve," or "Substantial noncompliance" -- based on performance against peer institutions in identified markets
  - Regulations set by Federal Financial Institutions Examinations Council (FFIEC) and enforced by each institutions principal regulator

Option Two:
HUD Could Achieve Some CRA-Like Alignments Under Existing Law

Full Alignment Would Require Complicated Statutory and Administrative Changes

	Menu of Options Shaded cells require legislation
Level of Alignment	• Align underserved definition only • Adopt CRA subjective ratings system
	• Alignment with CRA ratings, targeting, and enforcement provisions
Goals Structure	• Assign a "satisfactory" to current goals and an "outstanding" for reaching goals above current levels • Create unenforceable ratings based on investment and services
	• Goals based on lending, investments, and services • Performance assessed relative to peer institutions • All LIHTC and MRB investments count for the goals
Targeting	• Change underserved areas to 80 percent of AMI tracts
	• Change definition of low-mod to 80 percent AMI • Use CRA test of either 80% AMI or 80% of AMI tracts • Adopt concept of assessment areas to Fannie Mae business
Examination Model	• Retain current HUD oversight model
	• Change affordable housing regulator

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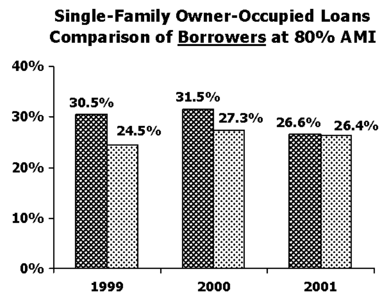
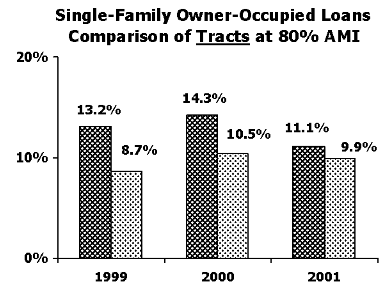
Option Two:

CRA-Like Targeting has Been Challenging, But Gap With Market Has Narrowed

- Fannie Mae's performance has traditionally trailed the broader market for SF borrowers and tracts below 80% AMI
- Picture changes in 2001 as Fannie Mae performance in SF lending essentially matched this broader market for lower-income borrowers and moved closer in lower-income tracts





HMDA 0-80% AMI　Fannie Mae 0-80% AMI

* SF Owner-Occupied loans from HMDA including manufactured housing and subprime lenders.

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Option Two:

Assessment of CRA Options

MBA Goal of Aligning Income Targeting Requires Legislation

Advantages

- Aligns affordable business and policy with our customers
- Aligns HUD's definition of our mission and market to our expanded focus on community development
- Allows more recognition of market-leading investment activities (e.g. LIHTC)
- Fannie Mae would score well using $ volumes and # of loans analysis against a peer group rather than a percent of business measure

Disadvantages

- Would require legislation for some changes, opening up the Charter to disadvantageous changes
- Could invite the imposition of new rules and restrictions without shedding others imposed by HUD
- Creates management challenge of subjective goals
- Places us in a more complex regulatory environment which could include banking regulators under some options
- Increases competition with customers for investments
- Goals for 80% AMI targeting are potentially more difficult to meet than current goals if set at market

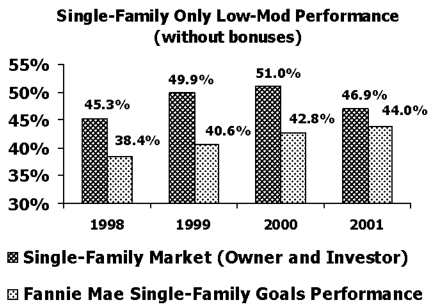
Option Three:

MBA Has Proposed Separate SF and MF Goals

View of Separate Goals Depends on Levels Chosen for Each Goal

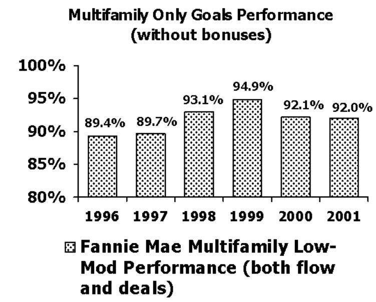
Single-Family

- MBA proposed 44% SF low-mod goal
- Fannie Mae SF performance has improved relative to the estimated market
- 2004-2006 projections assume 46% goals richness for SF business



Multifamily

- MBA proposed 95% MF goal for LMI
- Fannie Mae has consistently scored at or about 90% LMI for MF, but percentage has dropped this year
- Business projections assume continued scoring at 90% LMI



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Option Three:

Assessment of Separate SF and MF Goals

Advantages	Disadvantages
• Removes challenge of balancing SF and MF volumes in high refinance year • Properly-sized multifamily goal (and/or continuation of Temporary Adjustment Factor) could reduce irrational Freddie Mac behavior in that market • Allows better calibration of goals levels and predictability in strategies for meeting annual goals	• Removes flexibility to meet the goals using combined MF and SF strategies • Expands possibility that competitors constrain our markets by forcing increased targeting of our businesses • Requires statutory changes, extreme interpretations of existing authorities, or the imposition of unenforceable subgoals • Diminishes homeownership "brand" by disaggregating single-family and multifamily and reducing single-family goal below 50%

Lessened flexibility and needed charter changes diminish any potential benefits from this option

Option Four:

Add Alternative Structures to Current Goals to Address Market Volatility

Years in which high SF volumes depress the multifamily share of units make it difficult to reach goals. Scorekeeping changes that limit these impacts are possible within HUD's current authorities.

Menu of Options

- Cap on SF Refinance Units
  - Do not count refinance loans above a preset percent of SF units
  - Cap would increase housing goals scores by reducing relative size of SF volume in high refinance years
- Exempt/Underweight SF Refinance Loans
  - Exempt all SF refinance loans from goals
  - Change scoring to weight SF refinances as ½ loan
- Determine Goals Each Year Based on Market Conditions
  - Goals would change each year based on predetermined index of key market drivers (e.g. goals raised or lowered based on projected MF share of units)

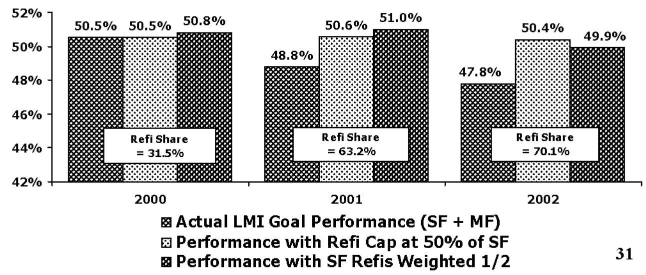
Option Four:

Changed Scoring for SF Refinance Loans Could Reduce Downside Risks

- Various options exist to depress the negative effects of SF refinance loans on overall goals performance.
  - ✓Do not count SF refinance units toward goals when percentage of refinances reach a preset value (e.g. 50%). Apply goals performance of entire refinance business for the year to the reduced number of refinance units used when calculating goals.
  - ✓Apply scorekeeping changes that weight units in SF refinance loans less than units in purchase money mortgage loans.
  - ✓Application of same treatment to multifamily business would have deleterious effects on goals performance.

Refinance caps/ scorekeeping changes imply higher potential goals by reducing the relative size of SF units to MF units

Revised Low-Mod Performance
Using Alternative Refi Scoring Methods



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Option Four:

Determine Goals Annually Based on Actual Annual Market Opportunities

- Goals would be indexed to annual market opportunities based on projections of key variables such as MF share of market and/or refinance share of SF market.
- Levels set at beginning of year based on projected index values and recalibrated at the end of the year should actual market conditions vary considerably from projected values.
- Has the advantage of avoiding problem of meeting multi-year, fixed goals based on one set of assumptions when market conditions change contrary to those assumptions.
- High levels of uncertainty with respect to key variables (e.g. size of the multifamily market) implies difficult and constant negotiations with HUD on annual goals.

Example of Index Approach to Setting Annual Low-Mod Goal

Projected Refinance Share of SF Market	Projected Multifamily Share of the Market (MF Richness = 90%)			
	8%	10%	12%	14%
20% (SF average low-mod = 48.8%)	52.4%	53.3%	54.2%	55.1%
40% (SF average low-mod = 48.0%)	51.7%	52.6%	53.5%	54.4%
60% (SF average low-mod = 47.2%)	51.0%	51.9%	52.8%	53.7%

Option Four:

Assessment of Alternative Approaches for Addressing Market Volatility

Advantages	Disadvantages
• **Protects Fannie Mae from having to take extraordinary measures to meet goals in high refinance years**	• **Retroactive application of caps would show increased goals performance and allow HUD to push for higher goals**
• **Reduces need to balance MF and SF in refinance boom years**	• **Policy arguments for limiting role of SF refinances in the goals may apply to multifamily loans also**
• **Allows Fannie Mae to provide full liquidity to lenders in a refinance market without concern for goals impact**	• **Option to adjust goals annually for changing market conditions relies on potentially disputed market data**
• **Better aligns annual goals with variations in market opportunities**	• **Options that inflate Fannie Mae performance or depress goals may pose public relations problems**

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Constructing a Strategy for Moving Forward

- Set Objectives for Housing Goals Rewrite
- Frame the Issues for Negotiation with HUD
- Decide a Strategic Approach to Next Steps

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Objectives for the Housing Goals Rewrite

- Successful outcomes are those that:
  - Are consistent with our business strategies
  - Serve to demonstrate our commitment to our mission
  - Provide flexibility in changing market conditions
  - Increase certainty and decrease volatility
  - Do not force inappropriate, uneconomic allocations of credit
  - Do not result in irrational financial decisions or impact
- Fannie Mae should strongly oppose:
  - Goals increases and new subgoals
  - A minority lending goal or rural multifamily goal
  - Expansion of HUD program approval authorities
  - Limits on flexibility to reach goals
  - Increased administrative burden or waste
  - Fair lending enforcement responsibilities
  - Proposals to open up the Charter to make goals changes

Shaping the Strategy

- Tone of the Engagement?
  - Measured discussion of options and analytics?
  - Presentation of win-win package that addresses HUD's perceived needs?
  - Resist?
  - Let Freddie lead?
- Timing of the Engagement?
  - Late HUD start could mean one-year delay
  - Retention of bonuses requires affirmative HUD action before end of 2003
  - Delays mean others have opportunity to shape HUD thinking
- Enrolling Other Players in Advance?
  - Freddie Mac
  - Housing and Banking Trades
  - Advocacy Community
  - Capitol Hill

Required Milestones for 2004 Effective Date

February 2003
HUD begins discussions with Fannie Mae and others

March-June 2003
HUD drafts proposed rule

June 2003
HUD publishes proposed rule

July-September 2003
90-day comment period

December 2003
HUD publishes final rule

Timetable is aggressive: Discussions around October 2000 rule began in May 1999. HUD took 5 months to review public comments and issue final rule.

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Appendices

Supplementary Materials and Reference Documents

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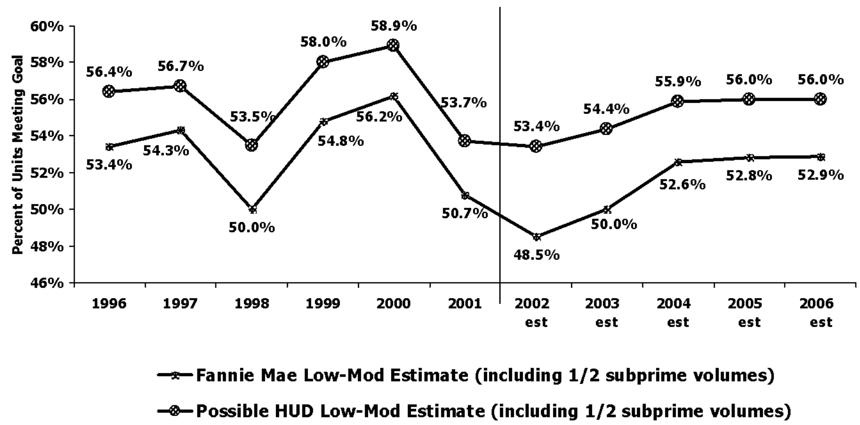
Market Size Estimates Show Considerable Variation in Recent Years

While projections show little variation, HUD should anticipate that actual future market size could fluctuate from year to year.



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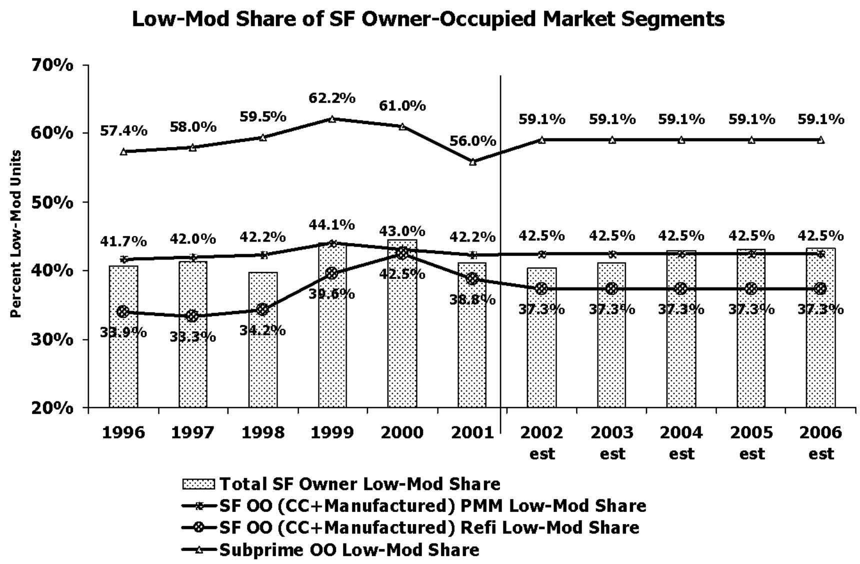
* Due to changes in balance between SF and MF, the total market size has declined significantly in recent years.

FNM Projections Assume Stable Low-Mod Richness for SF Owner-Occupied Units



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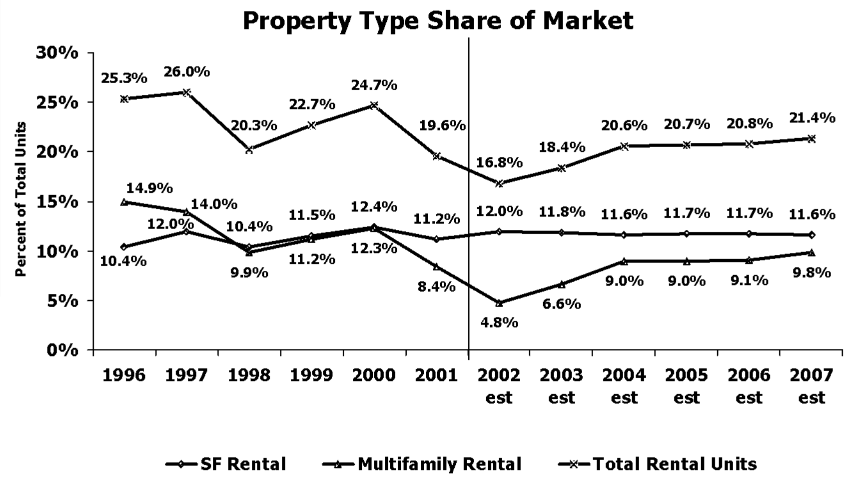
* Due to changes in balance between SF and MF, the total market size has declined significantly in recent years.

FNM Projections Assume Rental Share of Market Climbs Back to 21% in 2004-2006



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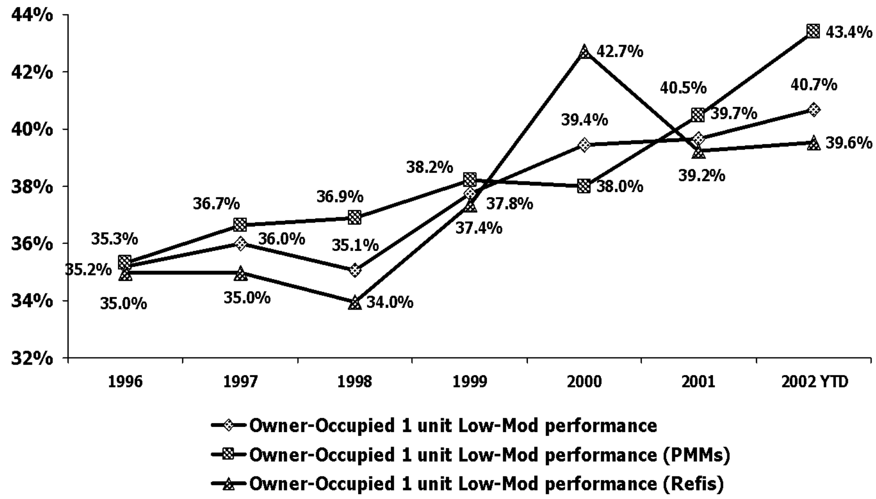
Fannie Mae's Owner-Occupied 1 unit Low-Mod Performance Has Consistently Improved



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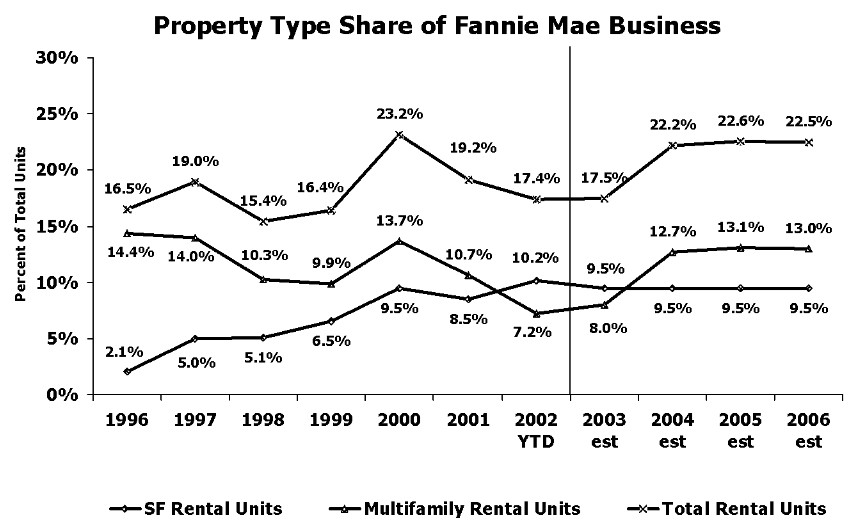
Fannie Mae Rental Units Projected to Reach to Levels Comparable to Market



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Fannie Mae Goals and CRA Rules Differ in Many Key Aspects

	Housing Goals	CRA Rules
Regulator	HUD (w/OMB interagency review)	FFIEC (Fed, OCC, OTS, NCUA, and FDIC)
Ratings System	3 separate, quantitative percent-of-business goals measured in units: Low-mod = 50% Underserved = 31% Special affordable = 20%	Subjective ratings for large institutions based on blend of lending, investments, and services tests relative to peer institutions and market: "Outstanding," "Satisfactory," "Needs to improve," or "Substantial noncompliance"
Targeting	Low-mod = 100% AMI; Underserved = 90% AMI and 120% AMI with 30% minority; National market	Low-income borrowers at 80% AMI ***or*** low-income areas at 80% AMI in lender-identified assessment areas
Lending Activities	SF and MF (no FHA) mortgage purchases	Residential (SF and MF), small business, farm lending, and community development lending
Investment Activities	None: No credit for ACF, LIHTC, MRBs, CDFI, and other market rate equity investments	Deposits, shares, or grants with community development purpose
Services	None	Availability and effectiveness of retail services, innovation in community development services
Examination Model	Quarterly data transmissions Annual report, Occasional oversight/audit	Full CRA examinations every two years for large institutions