CONFIDENTIAL

Maximizing Shareholder Value

FannieMae

Board presentation

July 18, 2005

MAXIMIZING FM SHAREHOLDER VALUE – EXECUTIVE SUMMARY

- **Market forces are challenging the viability of FM's business model and earnings trajectory**
  - Fannie Mae has historically had a successful business model and financial performance
  - Structural market forces, e.g., consolidation, disintermediation, consumer demand, the global supply and demand for investments, etc. are shifting the opportunity away from FM's traditional "sweet spot"
  - Cyclical factors may affect the timing of market evolution, but the longer-term direction and implications for FM's business model and future earnings trajectory are clear
  - In addition, recent and expected changes in the legislative and regulatory environment will put further downward pressure on the net benefits derived from GSE status

- **Full "privatization" is not recommended at this time**
  - Significant earnings and returns to capital will be derived from the charter for the foreseeable future
  - To significantly grow beyond its core, FM must build upon its proprietary assets, distinctive skills, and privileged relationships, all of which are based upon its advantaged position in the current businesses
  - Under most scenarios, privatization implies shifting rather than avoiding regulatory oversight
  - Privatization should be re-considered in the future, after FM has had the chance to build significant non-core businesses and at the point when (if) the guaranty businesses fail to return their cost of capital

- **Optimizing existing businesses will, by itself, be insufficient to maximize shareholder value**
  - In the guaranty markets in which FM is now focused (i.e., 15-yr, 30-yr FRM), growth over the next 10 years will be slower than the last 5 years; share gains are unlikely given aggressive competitors such as Freddie, Countrywide, and Lehman
  - The portfolio business will remain a market-timing driven/opportunistic business and will also be characterized by increasing competition from Wall Street banks, hedge funds and overseas investors
  - The positive impact from optimization will largely be captured over the next 2 years, with limited potential as a platform for sustaining longer-term earnings growth
  - Top talent will be harder to attract and retain with a reduced growth ambition and outlook
  - Once management has re-established its credibility for delivering on performance promises, additional shareholder value creation will significantly depend upon the investment community's longer-term earnings growth expectations for FM

MAXIMIZING FM SHAREHOLDER VALUE – EXECUTIVE SUMMARY

- **FM has significant opportunities to grow beyond its existing core businesses**
  - FM currently has only ~10% share of the estimated $60 billion US mortgage market pre-tax profit pool and no presence outside the US; most of the mortgage profit pools in the US and beyond have favorable growth prospects
  - FM has the potential to build upon its proprietary assets (e.g., scale, information), privileged relationships (e.g., with medium-sized lenders) and distinctive skills (e.g., credit and interest rate risk management) to succeed in capturing a number of alternative business opportunities

- **To maximize shareholder value, FM needs to reshape its performance culture to become more focused on innovation and strengthen its ability to develop significant new earnings streams**
  - The Board and management team need to get aligned on and committed to the specific growth vision and themes, definition of what success will look like, and what it will take to get there
  - A compelling proposition needs to be urgently communicated and then delivered to re-energize employees about FM's future prospects and how they will benefit, starting with the top 250
  - A broader program should be implemented to reshape ~5,000 employees' mindsets and behaviors to enable them to succeed in the new FM environment
  - Processes should be redesigned to support rigorous management of initiatives and investments that will create growth engines beyond current year budget requirements

- **A first-cut effort identified five broad types of new business opportunities representing an estimated range of $1-3 billion in potential annual pre-tax profits for FM in 3-5 years**
  - Categories of available growth opportunities include: adjacent guaranty areas, asset management/ alternative investments, 'home value management' (i.e., helping Americans capture the full value of home ownership beyond the point of purchase or refinance), service businesses, and international
  - Capturing these opportunities will require FM to overcome explicit and implicit constraints, including exploring new structures such as establishing a holding company, negotiating strategic alliances, etc.

MARKET FORCES ARE CHALLENGING THE VIABILITY OF FANNIE MAE'S BUSINESS MODEL AND EARNINGS TRAJECTORY

	Potential threat	Illustration/example
Single family	• Increasing concentration in deliveries by large lenders leading to pricing pressure • Broad shift in consumer demand from standardized products to customized products • Growing investor acceptance driving rapid private label securities issuance • Increasing importance of second liens/ home equity	• Share of deliveries from Fannie Mae's top 10 customers increased from 28% in 1994 to 68% in 2004 • Guarantee fee under pressure approximately 8 bps better gap (i.e., charged fee – modelled fee) for small vs. large lenders
Multi family	• Large influx of capital and expertise into market from large lenders and capital markets • Increasingly integrated commercial and MF markets exerting pressure on Fannie Mae's MF-only business	• DUS guarantee fee down from 46 bps in 01/02 to 36 bps in 03/05
Portfolio	• Elimination of arbitrage between MBS and agency debt securities • Influx of new investors (e.g., Asian Central Banks) • Active participation of total return investors • Accounting standards for hedging and market gains challenging returns	• Fannie Mae current coupon yield MBS OAS spread to 7-year agency debt tightened from 34 bps in 2/99 to -15 bps in 05/05

Source: Interviews; McKinsey analysis

MARKET FORCES ARE SHIFTING THE OPPORTUNITY AWAY FROM FANNIE MAE'S TRADITIONAL "SWEET SPOT"

Macroeconomic drivers

- **Strong home price appreciation**, low credit default rates, historically **low interest rates**
- Unlocking of capital from international markets
- Changing US demographics – **aging population** facing significant retirement, healthcare challenges, growing immigration

Consolidation and disintermediation

- **Primary mortgage markets consolidating**
  - Technology and operations cost advantage in servicing
  - Driven in part by overall industry M&A
  - Arbitrage opportunity open to aggregators
- Accelerating **vertical integration** from both primary and secondary ends of market **fueling private label issuance**

- Shift in **product mix away from Fannie Mae's traditional "sweet spot"** (i.e., 15- and 30-year FRM)
- **Reduced market power in guarantee business**
  - Pressure on credit guaranty fees from large lenders
  - Large lenders acting to potentially substitute GSEs by aggregating loans from smaller lenders
- **Challenges to portfolio business** earning historical average returns with traditional business model

Changing consumer demand and product mix

- **Increased risk based pricing** and **changing demographics** driving rapid growth in sub-prime and Alt-A originations
- Current rate environment, consumer sophistication and home price appreciation **driving high demand for ARMs and IOs**
- Consumers increasingly using homes as **active financing vehicles**
  - Rapid home equity growth
  - Proliferation of more complex, bundled products

Challenging investing environment

- **Greater investor comfort** with mortgage securities through better understanding of risk, indexing
- **Excess capital chasing yield** and putting downward pressure on agency MBS spreads
- **Alternative investment vehicles** (e.g., REITS, hedge funds) and investor appetite for lower credit collateral driving non-agency MBS liquidity
- Depositories **holding of mortgage assets rising in search of yield – Basel II to reinforce this trend**

FANNIE MAE'S RELATIVE SIZE AND MARKET POWER HAS DIMINISHED SIGNIFICANTLY OVER THE LAST 15 YEARS

Top 10 financial institutions*, 1990	Market capitalization $ billion
American Express	10
JPMorgan	8
Nat West	8
BankAmerica	6
Bank One	4
SLM Corporation	4
Citicorp	4
Bankers Trust	4
Wells Fargo	3
Wachovia	3
Fannie Mae	9
Freddie Mac	3

Top 10 financial institutions*, 2005	Market capitalization $ billion
Citigroup	242
BankofAmerica	182
JPMorganChase	122
Wells Fargo	103
Wachovia Corp	79
American Express	67
Morgan Stanley	58
US Bancorp	54
Merrill Lynch	53
Goldman Sachs	51
Fannie Mae	57
Freddie Mac	46

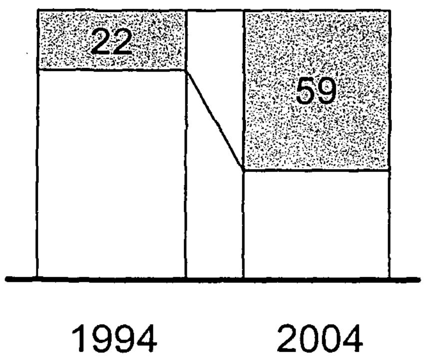
* Excluding insurance companies

Source: McKinsey Corporate Performance Database

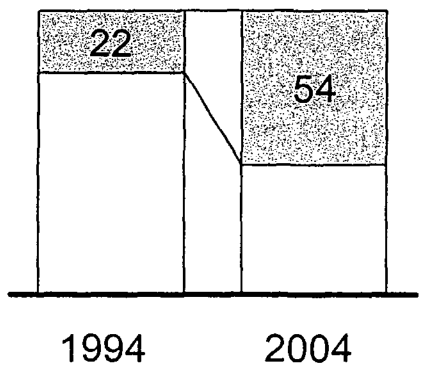
CONTINUED CONSOLIDATION IN ORIGINATION AND SERVICING CONSISTENT WITH OTHER CONSUMER CREDIT INDUSTRIES

Top 10 market share

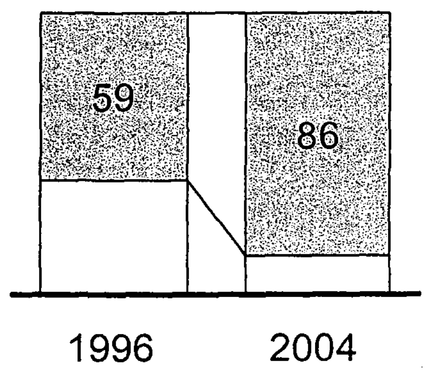
Mortgage origination share
Percent



Mortgage servicing share
Percent



Credit card outstandings
Percent



Source: Mortgage Market Statistical Annual, "Inside Mortgage Finance"; Big Wheels; Nilson; McKinsey analysis

ACCELERATING VERTICAL INTEGRATION ESPECIALLY IN SUBPRIME

Sub-prime market share across value chain
Percent

Top 3 rank
Top 10 rank

- Revenues from origination and servicing down to 67% from 95% in 1995
- Fannie Mae share of deliveries down to 35% from 90% in 1995

	Origination	Servicing	MBS Issuance	Underwriting
Countrywide	6.0	5.6	5.8	6.8
AMERIQUEST® MORTGAGE COMPANY	11.7	7.0	15.1	
citifinancial	6.5	7.2		7.5
JPMorganChase		4.0	3.6	4.5

* Subprime servicing balances
Source: IMF-PUBS Top Subprime Mortgage Market Players, McKinsey analysis

PROPRIETARY AND CONFIDENTIAL – CONFIDENTIAL TREATMENT REQUESTED BY FANNIE MAE

EVOLUTION OF MORE DISTINCT CONSUMER SEGMENTS REQUIRING CUSTOMIZATION OF PRODUCTS

- Users of non-standard products
- Potential size of customer base (Percent of households)

1. Affluent relationship-oriented, conservative home owner

- Predominantly use mortgage company
- Finances in good order
- Value long-term relationships and quality (potentially at the expense of lowest costs)
- Unlikely to try new financial services
- 62% identified as Boomers
- 33% identified as generation X
- 54% with incomes between $50-100K

16% of HHs

2. Affluent, well-informed, low-loyalty value shopper

- Finances in good order
- Prefer machines to face-to-face interactions
- Very confident about financial decisions
- Primarily work through banks
- Will shop for best value
- Low loyalty to financial institutions
- Very willing to try new services
- Affluent consumer segment
  - 46% income between $75-100K
  - 25% above $100K

18% of HHs

3. Lower income skeptic

- High use of banks
- Like to spend money rather than save
- Not happy with current financial situation
- Distrust of financial system
- Not confident with decisions and feel need for help in managing finances
- Prefer single contact for various financial services
- High ethnic proportion

22% of HHs

4. Lower-income worried consumers

- Low home equity
- Highly price sensitive with regards to financial services
- High use of mortgage companies
- Very organized with financial affairs *but worried* about finances
- Do not value long-term relationships
- Lowest income segment (70% under $50K)
- High ethnic proportion

11% of HHs

5. Face-to-face relationship valuing retiree

- Experienced with mortgages
- Highest proportion of home equity
- Highest use of banks
- Finances in good order
- Value long-term relationships
- Prefer to do business in person and like to chat with financial advisors
- 92% identified as Retirees or WWII generation (Oldest non-retired age segment)

17% of HHs

6. Young spender

- First mortgage predominantly use mortgage companies (70%) but prefer convenience of single contact where possible
- Highest use of mortgage companies
- Spenders rather than savers
- Not disciplined with finances and tend to dislike managing finances
- Not satisfied with current financial situation and distrustful of institutions
- Large proportion of first mortgage
- Likely to try new things
- Will shop for value

16% of HHs

Source: McKinsey cluster analysis

HEALTHCARE AND RETIREMENT COSTS WILL REQUIRE TAPPING INTO THE VALUE OF THE U.S. HOUSING STOCK

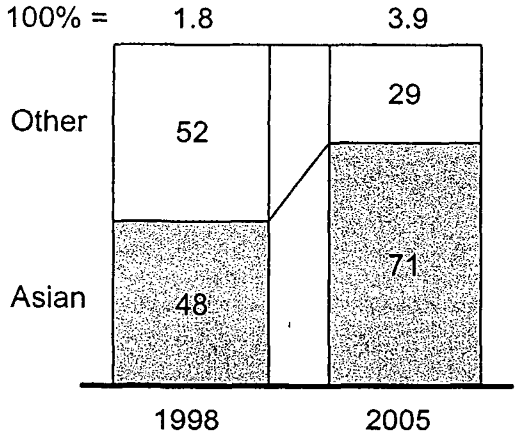
What was it like to retire in 1985	What it will be like to retire in future
• Almost 65% of retirement income came from social security	• Social security already provides less than 40% of retirement income
• Defined benefit plans from high quality employers covered 53% of households	• Defined benefit pension plans cover only 35% of households • Shortfall of $450 billion in pension plans (up 27% from 2003) and rising • PBGC paid out $3 billion in 2004, having to take over ~190 pension plans
• Healthcare expenses were largely covered by *employee* retirement health plans	• Healthcare expenses of $ 1.9 trillion in 2005, growing at 10-15% per year, and expected to reach 17% of GDP by 2010 • Retirees likely to spend ~40% of income on healthcare by 2020; the last few years of life tend to require significantly higher healthcare expenditures (i.e., 10x of the previous 10-year average)

Estimated equity in U.S. residential property of $ 8 - 10 trillion will need to be tapped to offset increasing healthcare and retirement costs

Source: Analyst reports; literature search; Fed Flow of Funds; McKinsey analysis

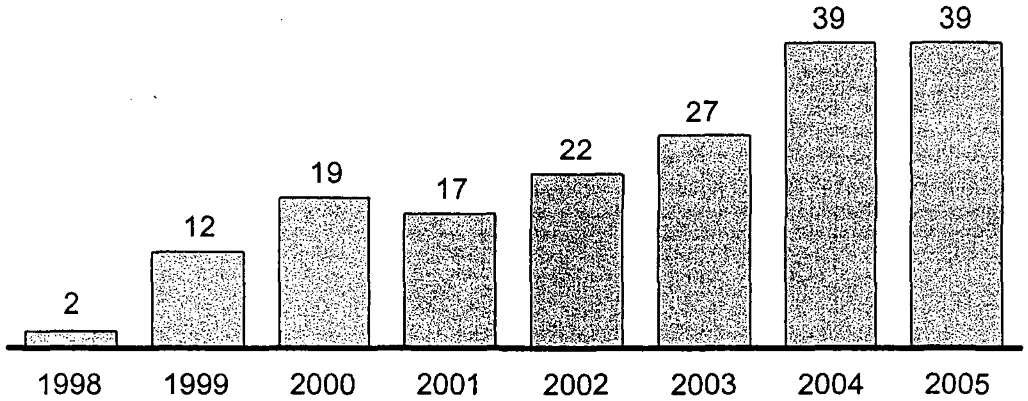
INCREASING DEMAND FOR MBS FROM ASIAN CENTRAL BANKS

Central Bank FX reserves
$ Trillion, percent



65% of FX reserves invested in U.S. dollar assets

Central Banks with MBS/ABS as approved asset classes
Percent of banks surveyed, UBS Central Bank Survey



"Foreign assets should be invested in…Agency bonds, supranational bonds and securitized bonds which offer high liquidity and certainty of redemption"

– Ministry of Finance, Japan

"We have sufficient reserves to secure our sovereign credibility… We now need to take more consideration of profitability…manage our reserves in a more useful way"

– Governor Park Seung, Bank of Korea

Source: UBS Mortgage Strategist

MANY OF THE SHIFTS OBSERVED IN THE MORTGAGE INDUSTRY APPEAR STRUCTURAL

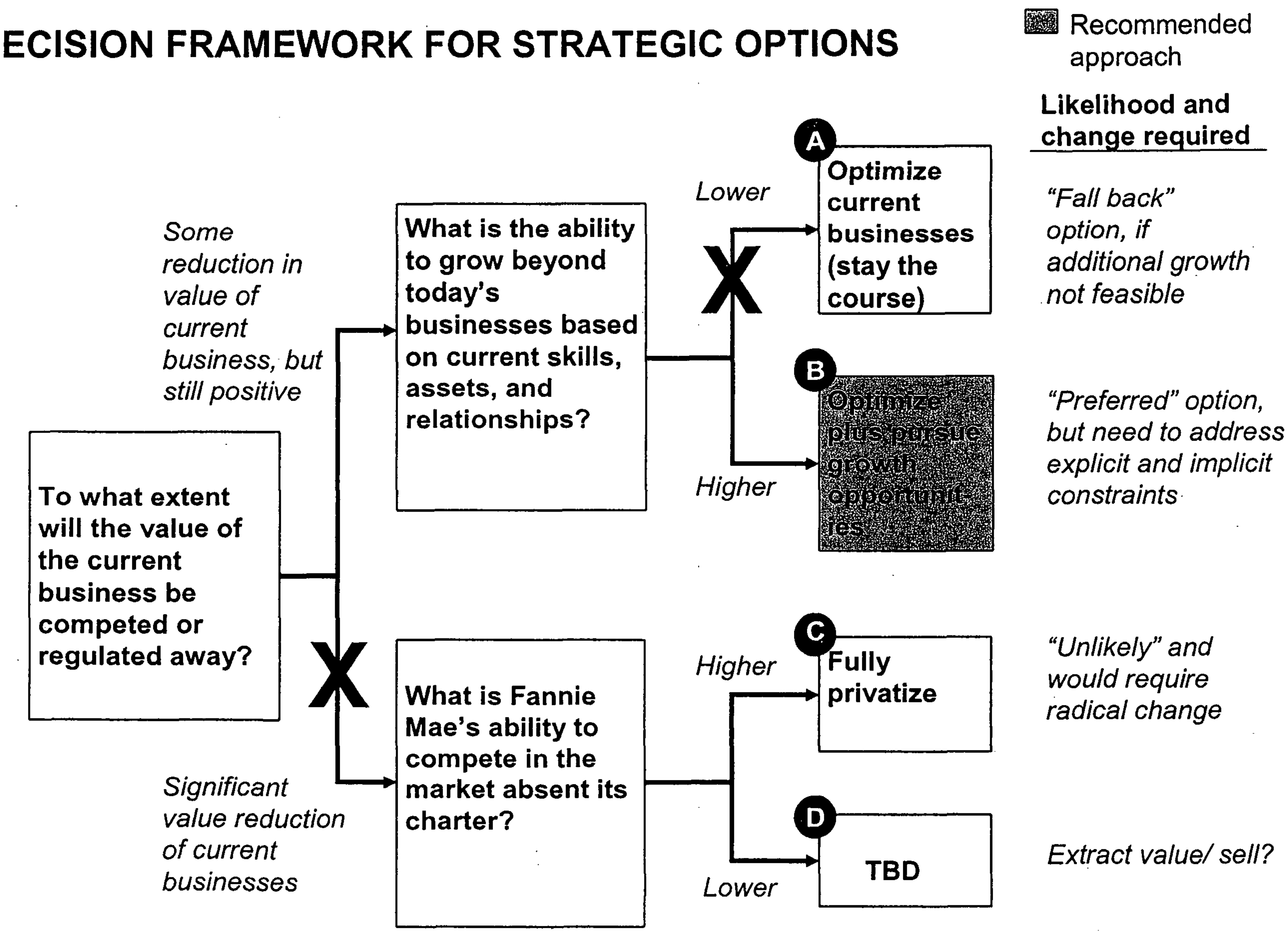
Structural

Major trend	Nature of trend	Rationale
• **Primary market consolidation**	Structural	• Scale benefits in technology, operations and retail access
• **Depository mortgage assets**	Structural	• Search for yield structural – likely to be reinforced by Basel II
• **Vertical integration**	Structural	• Build up of skills; ability to "cherry-pick" best assets
• **Global capital markets deepening**	Structural	• Improving efficiency in global markets
• **Home equity growth**	Mostly structural	• Shift in consumer behavior toward using homes as active financing vehicles
• **Narrowing of portfolio OAS**	Mostly structural	• Structural deepening of global capital markets; increased investor comfort in substituting agency debt with MBS
• **Sub-prime, Alt-A growth**	Both structural and cyclical	• Expansion of product availability through risk based pricing structural; low credit defaults cyclical
• **Private label issuance**	Both structural and cyclical	• Increased investor appetite for subordinate bonds
• **ARMs and IOs demand**	Mostly cyclical	• Fueled by current rate environment and home price appreciation, hybrid ARMs structural
• **Home price appreciation**	Cyclical	• Benefiting from long economic "bull run"

Cyclical

Source: McKinsey Analysis

DECISION FRAMEWORK FOR STRATEGIC OPTIONS



WHY "PRIVATIZATION" IS *NOT* RECOMMENDED AT THIS TIME

1. **Significant earnings and returns to capital will be derived from the charter for the foreseeable future**
   - *Credit guaranty:* Scale and liquidity benefits derived from the implied guarantee and TBA privilege
   - *Portfolio:* Funding advantage of ~15-20 bps as unsecured debt trades at AAA levels compared to most banks' AA-/A unsecured debt
   - Capital advantage of 2-3% relative to banks, although this may be eliminated through future legislation

2. **Fannie Mae's strengths, from which to grow beyond its core, are based upon its advantaged position, particularly in the guaranty business, e.g.**
   - *Scale:* Over $500 billion of MBS issuance in 2004
   - *Ready access to capital* for specified purposes, making rapid expansion possible
   - *Proprietary information:* Loan performance data on over 54 million loans dating back 25 years; 500 million transaction records supporting valuation of ~70 million properties

3. **Privatization implies shifting, rather than avoiding regulatory oversight** (e.g., SEC, other bank regulators)

4. **Privatization should be re-considered in the future, after Fannie Mae has had the chance to build significant non-core businesses and at the point when (if) the guaranty businesses fail to return their cost of capital**

COMPARISON OF SALLIE MAE IN 1994 AND FANNIE MAE IN 2005

	Sallie Mae - 1994	Fannie Mae - 2005	
Market conditions	• $80 billion student loans outstanding, poised for rapid growth in originations • Small role in overall economy • Exploding secondary market with creation of ABS in 1991- 65% CAGR from 1993-97	• $9 trillion mortgage debt outstanding • Moderate origination growth expected in the medium term • Critical to overall economy • Mature secondary market - 7% CAGR projected for MBS through 2010	Significant differences in size, scope, nature of guarantee and business importance to economy
Size and market power	• Market capitalization of $ 2.4 billion • Net income of $400 million • $14 billion of ABS outstanding (1997) • ~55% of student loan ABS origination	• Market capitalization of ~$56 billion • Net income of ~$8 billion (2004) • $1.3 trillion of MBS outstanding • ~28% of MBS origination (2004)	
Business presence	• Credit guaranty • Portfolio • Servicing • Operations and IT services/ consulting	• Credit guaranty • Portfolio	
Nature of guarantee	• Student loans had guarantee on underlying asset - consumers continue to benefit from subsidy even with privatization of GSE	• Implicit guarantee on agency debt benefits conforming borrowers - GSE privatization would eliminate this consumer benefit	
Rationale for privatization	• Federal government entering student lending directly - legislation allowing up to 60% of originations to be direct lending • 30 bps user fee on all loans acquired after 8/1993 - estimated 33% reduction in profit margins over 5 years • ABS funding model proven to be successful alternative to holding whole loans on balance sheet	• Market trends driving shift away from charter-linked businesses • Affordable housing fund: 5% of profits; estimated impact of ~$400 million reduction on 2003 NI of $7.9 billion • No alternative funding model beyond MBS	Sallie Mae business model more fundamentally threatened by proposed legislative changes

Source: Literature search; McKinsey analysis

WHY OPTIMIZATION BY ITSELF *WILL NOT BE SUFFICIENT* TO MAXIMIZE SHAREHOLDER VALUE

- **In the guaranty markets in which Fannie Mae has traditionally focused (i.e., 15-yr, 30-yr FRM), growth over the next 10 years will be slower than the last 5 years, share gains are unlikely given aggressive competitors such as Freddie, Countrywide, and Lehman**
  - Origination CAGR of 16.5% over last 5 years vs. long term average of 7-8%
  - Home price appreciation CAGR of 8% over last 5 years vs. the long term average of 4-5%
  - Portfolio spreads likely to be tighter in future (down from 98 bps MBS OAS over 6-month treasury in 2000 to 39 bps over treasury in 2005)
- **The portfolio business will remain a market-timing driven/opportunistic business and will also be characterized by increasing competition from Wall Street banks, hedge funds and overseas investors**
- **The positive impact from optimization will largely be captured over the next 2 years, with limited potential as a platform for sustaining longer-term earnings growth**
- **Top talent will be harder to attract and retain with a reduced growth outlook**
- **Creating additional shareholder value will significantly depend upon the investment community's longer-term earnings growth expectations for Fannie Mae**
  - Average terminal value for top 20 North American financial institutions = 22%
  - Terminal value for Freddie Mac = 8%
  - Terminal value for Fannie Mae = -8% (for current market capitalization)

- **Optimization *by itself*, could improve market capitalization by ~$1 billion over 2-3 years**
- **Optimization *by itself*, would likely result in:**
  - Limited investment in business, given lower underlying growth
  - Focus on cost containment/ reduction
  - Increased return of capital to shareholders
  - Increased challenges in attracting and retaining talent
- **By comparison, however, a 2-3% increase in the long-term earnings growth rate from new growth opportunities will have a $7-10 billion impact on shareholder value**

OPTIMIZING EXISTING BUSINESSES CAN PROVIDE SIGNIFICANT NEAR-TERM EARNINGS LIFT

Critical business needs

- Grow beyond traditional 30-year and 15-year FRMs focus and capture value from emerging segments (e.g., expand further in ARMs)
- Develop flexibility in technology and operations to support multiple, customized products
- Adapt to changing needs of consumers and offer competitive products and services
- Optimize capital to invest in growth initiatives

Illustrative optimization levers

- Risk based micro-pricing across customer segments
- Technology re-architecting and productivity improvement
- Lean manufacturing approach to streamline operations and achieve best-in-class cost, quality and productivity
- Rebalancing customer and product groups and applying key account management to strategically important accounts
- Optimize capital across different businesses and growth opportunities

Potential opportunity to improve earnings in the range of $100-200 million over the next 2-3 years

HOWEVER, MARKET SHARE GAINS WILL BE DIFFICULT GIVEN INTENSE COMPETITION

Freddie Mac

- Aggressive pricing targeted at switching lenders (e.g., Wamu) from Fannie Mae; stated goal of achieving 50% MBS issuance market share
- Aggressively targeting IOs, recently exceeded Fannie Mae in loan purchases (since April, 2005)
- Developed new customer-centric strategy and leadership team within single-family business with head of national lending to cover large accounts
- Growing portfolio business by 6-7% post re-statement

- $46 billion market capitalization
  - #2 agency MBS issuer

Countrywide Financial

- Leveraging synergies from shared institutional relationships, production flows through the value chain, mortgage analytics, shared technology and distribution infrastructure
- Developed Capital Markets BU – directing less than 1/3 of deliveries to Fannie Mae – rest to private label
- Growing portfolio capability – directed $15 billion of loans in Q2, 2005 to the bank vs. $8 billion in Q1, 2005
- 20% of revenues from new businesses (e.g., credit risk management, MBS structuring and issuance, commercial real estate, CDO lending through C-BASS JV)

- Nearly $3 billion in mortgage-related revenues and $22 billion market capitalization
  - #1 mortgage originator & servicer
  - #1 issuer of Alt A
  - # 2 issuer of non-Agency MBS

LEHMAN BROTHERS

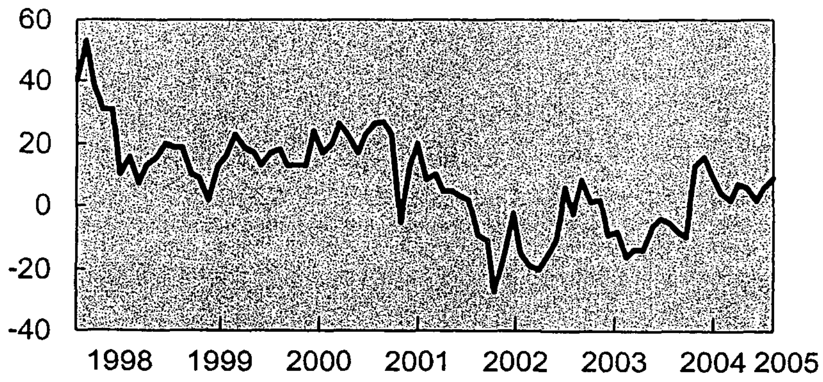
- Purchased Finance America, Aurora Loan Services, and several other small subprime originators
- Sourced more that 55% of the residential securitization product from own origination platform in 2004
- Has rapidly grown its SASCO conduit through warehouse lending
- Geographic and product diversification by
  - Developing origination capability in other markets e.g. Netherlands, UK
  - Looking to diversify product offering rather than focusing on specific asset class e.g. Alt A, Sub-prime, reverse, conventional

- Over $2 billion in mortgage-related revenues
  - #1 underwriter of non-agency MBS
  - #4 issuer of non-agency MBS
  - #6 underwriter of Agency-backed REMICs

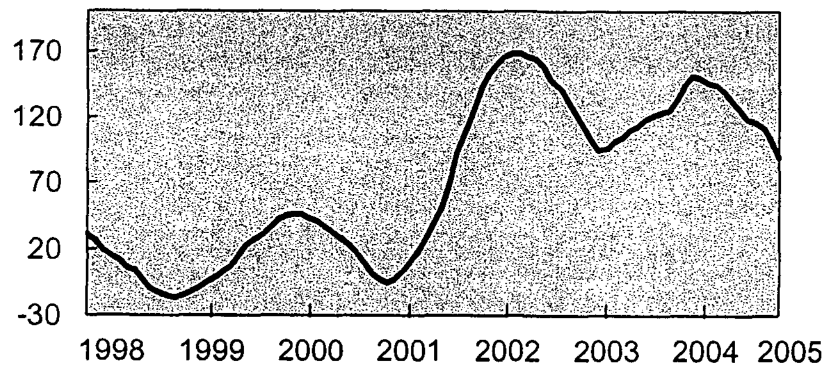
Source: IMF-PUBS; Company reports; Literature Reviews, Interviews

THE PORTFOLIO BUSINESS WILL REMAIN AN OPPORTUNISTIC BUSINESS AND NOT A DRIVER OF LONG TERM GROWTH

Aggregate OAS for MBS (all maturities) with LIBOR
Bps



1Y moving average of 3Y agency cost of debt versus 1Y moving average of 6M LIBOR
Bps



- Portfolio buy-and-hold earnings dependent on option-adjusted spread of MBS to agency debt
  - Cyclical, and linked to supply and demand of MBS and agency debt
  - Negative today for 15-year and 30-year FRMs
- Significant earnings volatility expected from use of interest rate derivatives under GAAP accounting
- Dramatic growth in retained portfolio compared to competition likely to draw negative attention from Government and industry

"The method of GSE financing most consistent with the GSE's missions is to securitize assets and hold in their portfolios only those that are very difficult or unduly expensive to securitize"

– Alan Greenspan

"Under the new regulatory regime we envision, Fannie and Freddie's retained portfolios will generate returns on equity of 10-12%...we expect the portfolios to remain flat, neither growing nor shrinking, as Fannie and Freddie focus on preserving their margins."

– Morgan Stanley Equity Research

Source: Deutsche Bank U.S. Mortgage TBA Index

FANNIE MAE HAS ONLY ~10 % OF THE $ 60 BILLION U.S. MORTGAGE PRE-TAX PROFIT POOL

$ Billion, 2005 Estimate

Fannie Mae primary focus

Growth expectation

Origination	Servicing	Insurance	Credit Risk Mgmt	Portfolio	Trading
Jumbo ~2.5 (M)	Jumbo ~1 (M)	Mortgage insurance ~2 (L)	Agency ~5 (L)	Agency ~6 (L)	Agency debt ~1 (L)
Sub-prime, Alt-A ~9.5 (H)	Sub-prime, Alt-A ~1 (H)	Title insurance ~2 (L)	Conduit/ private label* ~3 (H)	Banks & Others ~11 (M)	Agency MBS, CMOs ~1 (M)
Prime ~2.5 (L)	Prime ~3 (L)		Whole loans* ~4 (M)	Asset mgmt ~2 (M)	Non-Agency MBS ~0.5 (H)
Home equity ~2 (H)	Home equity ~0.5 (H)				
Total pre-tax profit					
~16.5	~5.5	~4	~12	~19	~2.5

Does not include international mortgage profit pool, estimated at $50 billion, and growing more rapidly in select countries

* Pre-tax profit pool for Jumbo credit risk management = $2 bn

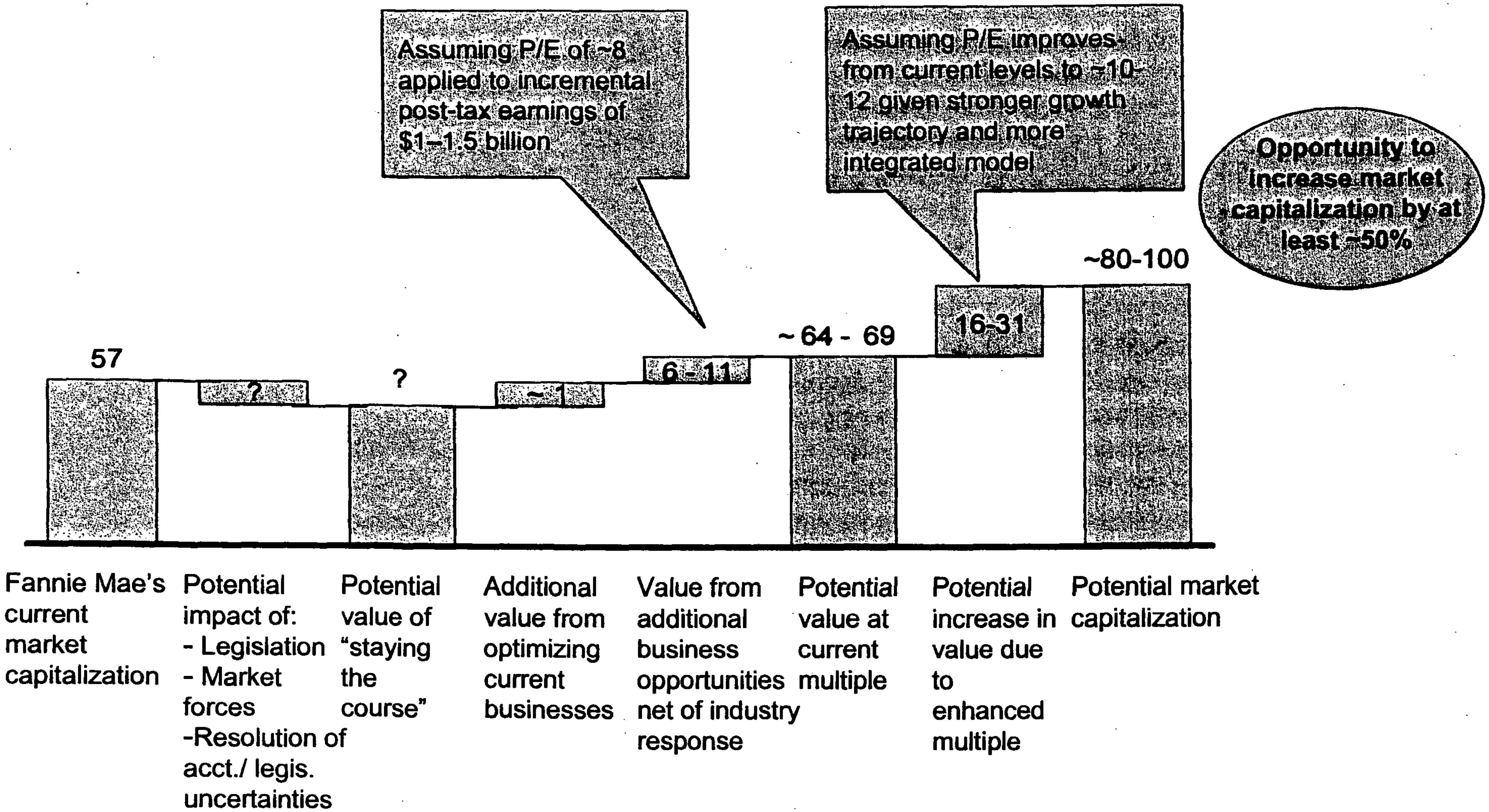
Source: McKinsey Analysis

STRENGTHS ON WHICH FANNIE MAE CAN BUILD PROFITABLE GROWTH

	Fannie Mae strength	Description
Proprietary assets	• Ready access to low-cost capital (for specific purposes)	• Charter benefits give lower cost of capital and unrivalled access to capital markets
	• Scale	• Large scale provides leverage across the mortgage value chain and a unique ability to set standards
	• Brand	• Positive brand recognition in the mortgage and housing industry among consumers and investors
	• Technology	• Mortgage models and software are market standard (i.e. Desktop Underwriter 40% share) *- facilitates cross sell and locks in customers*
	• Information	• Strong loan performance and property valuation data – 54 million loans dating back over 25 years – 500 million transaction records supporting valuation of ~70 million properties
Privileged Relationships	• Small and medium-sized lenders	• Small lenders prefer selling to Fannie Mae due to neutrality and trust-based relationships – this could erode over time under competition from large lenders
	• Investor base	• Broad base of investors and counterparties familiar and comfortable with Fannie Mae products and processes
Distinctive skills	• Credit risk management and analytics	• Extensive experience in data analytics, modelling and managing credit and pre-payment risk
	• Hedging and interest rate risk management	• Top tier pricing capability arising from superior interest rate risk management (especially for pass-throughs)
	• REO, loss mitigation	• Top tier loss mitigation and REO capability

CAPTURING NEW GROWTH OPPORTUNITIES COMBINED WITH OPTIMIZING CURRENT BUSINESSES, COULD RESULT IN AT LEAST A 50% INCREASE IN MARKET CAPITALIZATION

ILLUSTRATIVE



Source: McKinsey analysis

RESHAPING PERFORMANCE CULTURE INVOLVES OVERCOMING BARRIERS TO CHANGE REPRESENTED BY DEEPLY INGRAINED EMPLOYEE MINDSETS AND BEHAVIORS

Example actions

- Take symbolic leadership actions
- Provide leadership opportunities
- Foster more explicit coaching/mentoring

1 Role modeling

"I see leaders and other key influencers consistently behaving in the new ways"

2 Ensuring understanding and conviction

"I know what is expected of me, I agree with it, and it is motivating to me"

Example actions

- Codify and cascade integrated change story
- Gain top team alignment and commitment to making changes happen
- Meaningfully engage employees on underlying hopes, fears, and values

"I have the support, skills and access to opportunities to succeed in the new environment"

3 Enabling people to succeed via skills and confidence

- Invest in developing knowledge, skills, and external awareness
- Expand leadership capacity and skills to drive day-to-day change
- Upgrade talent at each level of the organization

"The structures, processes and systems that reinforce the changes in behavior I am being asked to make"

4 Reinforcing with consistent formal mechanisms

- Restructure the organization
- Revise key performance metrics and target setting methodology
- Redesign management processes
- Align financial incentives and recognition
- Ensure sufficient, timely MIS

Source: McKinsey Organization Practice

APPROACH TO IDENTIFY AND PRIORITIZE GROWTH OPPORTUNITIES FOR FANNIE MAE *ABSENT CONSTRAINTS*

Step 1 – Opportunity identification → **Step 2 – Attractiveness screening** → **Step 3 – Prioritization**

Market based themes
- Macro
- Consumer
- Consolidation
- Investing environment

Fannie Mae capabilities/ competitive advantages
- Assets
- Relationships
- Skills

→ **20 opportunities** → **14 opportunities**

Nature and magnitude of earnings
- **Size**
- **Source of earnings**
- **Volatility**

1. What is the comprehensive list of growth opportunities Fannie Mae can consider?

2. What are the attractive opportunities in the mortgage (and related) industry?
   – Materially significant (pre-tax earnings potential >$200 m in 3-5 years)
   – High growth/ value creation potential
   – Strategic fit with current business

3. How should Fannie Mae prioritize these opportunities, given their nature and magnitude?

WITHOUT TAKING CONSTRAINTS INTO ACCOUNT, FANNIE MAE HAS FIVE BROAD TYPES OF NEW GROWTH OPPORTUNITIES

● High
◔ Low

Materially significant growth opportunities		Pre-tax profit pool, $ billion	Growth	Attractiveness	Potential Fannie Mae pre-tax earnings $ million
1 Expand into adjacent spaces	1. Credit guaranty: extend core business to subprime, home equity, Jumbo, and expansion in ARMs	$ 3 bn	H		300
	2. Servicing - financial management: manage prepayment risk	3.5	M		350
	3. Mortgage insurance	2	L		200
	4. Title insurance	2	L		400
2 Enter asset management and alternative investing businesses	5. Asset management: invest third party funds in MBS	2	H		300
	6. Commercial/ multifamily investing: significantly expand current presence to invest own/third party capital in real estate	5	H		400
	7. Credit risk investing (own/third party capital)	1.5	H		300
	8. Distressed assets investing (in distressed financial and physical assets)	1.5	H		400
	9. Infrastructure bonds: invest in development infrastructure	3	H		500
	10. Construction finance (for multifamily/ commercial assets)	6	M		300
3 Create home-value management industry	11. Customer benefits of home ownership beyond purchase (including transferable stock, reverse mortgages, home value insurance)	~5	H		500 (over longer time frame)
4 Build service businesses	12. Servicing: create processing utility for industry	2	M		350
	13. Analytics/ data-driven appraisals	3.5	M		200
5 Move internationally	14. Create MBS markets and invest in 9 major countries (UK, Canada, Netherlands, France, Germany, Japan, Brazil, China, India)	50	H		1000 (across 9 countries)

Others de-prioritized due to low size/ growth, lower strategic fit

- Technology outsourcing
- Deposit taking
- Consulting
- Mortgage origination
- Market making in MBS (dealer)
- Home-equity origination

CAPTURING ANY OF THESE OPPORTUNITIES REQUIRES ADDRESSING CURRENT CONSTRAINTS

Growth opportunity	Explicit constraint (Charter limitation)	"Implicit" regulatory/ constituent constraint	Strong negative competitive/ customer response	Internal capability gap
1. Credit guaranty expansion (subprime, ARM, jumbo)	✓ (Jumbo)	✓	✓	✓
2. Servicing – financial management			✓	
3. Mortgage insurance	✓ (> 80 LTV)		✓	
4. Title insurance	✓ (Jumbo?)		✓	✓
5. Asset management		✓		✓
6. Commercial/ multi-family investing	✓ (Non-multifamily)		✓	
7. Credit risk investing	✓ (Non-multifamily)	✓		✓
8. Distressed assets investing	✓ (SF > 80 LTV)	✓		✓
9. Infrastructure bonds				✓
10. Construction finance				✓
11. Home value management			✓	✓
12. Servicing – processing			✓	✓
13. Analytics/ data-driven appraisals		✓		
14. International	✓			✓

Constraints could be addressed by exploring a range of alternative structures – e.g., bank holding company, alliances/JV, out-licensing

SUGGESTED ACTIONS FOR THE NEXT 90-120 DAYS

1. Determine specific 2005/2006 earnings improvement opportunities from optimization of existing businesses, and launch key initiatives

2. Gain alignment on aspirations for growth and valuation over the next 3-5 years

3. Drive efforts to reshape performance culture with particular emphasis on galvanizing top 250

4. Analyze in more detail highest priority growth opportunities

5. Work through implicit and explicit constraints and what it will take to capture priority growth opportunities

6. Develop detailed business cases for the short list of feasible, highest impact ideas