Annual Report 2005

Bringing Wall Street to Main Street

Ginnie Mae

Ginnie Mae's Mission

To expand affordable housing in America by linking global capital markets to the nation's housing markets

Ginnie Mae's Vision

Ginnie Mae is the world's leading financial institution committed to solving America's affordable housing needs.

Secretary's Message

Since its inception in 1968 Ginnie Mae has made affordable housing a reality for more than 32 million low- and moderate-income American households by channeling global capital into the nation's housing markets. Ginnie Mae has accomplished this through its innovation and guarantee of mortgage-backed securities (MBS). To date the corporation has guaranteed more than $2.4 trillion in MBS. Ginnie Mae's guarantee, the only one of its kind to carry the backing of the full faith and credit of the United States Government, sustains affordable housing by minimizing mortgage interest rates paid by home buyers and rents paid by lessees.

Ginnie Mae securities remain a beacon of stability, providing reliable performance for their investors and issuers. Likewise, Ginnie Mae's operations have continued to support the Department of Housing and Urban Development's housing goals. For example, during fiscal year 2005, Ginnie Mae, through its guarantee program, facilitated the financing of approximately 790,000 units of low- and moderate-income housing. Remarkably, it has accomplished this while generating consistently positive net revenues in a responsible manner, thus minimizing risk to the federal government.

We are proud of Ginnie Mae's stellar performance and continued important role in supporting affordable housing in the United States.

Alphonso Jackson
Secretary

The Honorable Alphonso Jackson
Secretary
U.S. Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410

Dear Mr. Secretary:

I am pleased to present to you the Fiscal Year (FY) 2005 Annual Report and the audited financial statements of the Government National Mortgage Association (Ginnie Mae). HUD's Office of Inspector General (OIG) delivered an unqualified opinion of Ginnie Mae's financial statements and found no material weaknesses or reportable conditions.

Congress formed Ginnie Mae in 1968 to help expand the supply of affordable housing in the United States, which includes single-family dwellings, apartments, nursing homes, and assisted living facilities. Ginnie Mae does this by providing an attractive and efficient government-guaranteed investment vehicle—mortgage-backed securities (MBS)—to link global capital markets to the nation's housing markets. Ginnie Mae's focus is on the federal affordable housing market, which includes single and multifamily dwellings with owner mortgages insured or guaranteed by four federal programs. Two are part of HUD: the Federal Housing Administration (FHA) and the Office of Public and Indian Housing (PIH). The other two are the Department of Veterans Affairs' (VA) home loan program for veterans and the Rural Housing Service (RHS) of the Department of Agriculture.

During its 37 years of existence, Ginnie Mae has helped to provide over 32 million low- and moderate-income Americans with affordable shelter by guaranteeing over $2.4 trillion of MBS. During FY 2005, Ginnie Mae:

- Provided the capital to finance the purchase or refinance of homes, or provided rental housing, for approximately 790,000 units for low- and moderate-income American families;
- Guaranteed securities that represented 92.7 percent of all eligible FHA and VA home loans;
- Earned net revenues of $705.2 million. Revenues were $786.5 million, of which $327.5 million was in fees, $458.8 million was in interest income from U.S. Treasury securities, and $0.2 million was in net other income; and operating expenses were $71.3 million;
- Made product and disclosure enhancements that demonstrated responsiveness to investors in the ever-changing capital markets; and
- Continued to implement program changes that reduced time and expense for its issuers, ultimately decreasing friction in the market and reducing costs for borrowers.

FY 2005 saw a 10 percent decline in the number of single-family homes and a 19 percent decrease in the number of multifamily dwellings supported by Ginnie Mae. The decline in these units is due to a decrease in the number of homes financed by government agencies that are eligible for Ginnie Mae's MBS program over the past year. Many families who bought their first homes with federally insured or guaranteed loans have built equity in their homes to the point where they qualified for conventional financing.

Ginnie Mae's continued success depends on its ability to channel mortgage capital into low- and moderate-income housing. Before 1968, mortgage capital markets tended to be local or regional. Today, Ginnie Mae operates in a global market that attracts capital and excess savings from around the world into American neighborhoods. This is because Ginnie Mae securities are among the world's most secure investments. Ginnie Mae's MBS carry the full faith and credit guaranty of the United States Government, which means that even in uncertain times, Ginnie Mae investors are guaranteed timely payment of principal and interest. Ginnie Mae is also proactive and aggressive in seeking the input of MBS issuers and investors on how to make Ginnie Mae programs better, and Ginnie Mae invests in information technology that improves those programs' efficiency. And, Ginnie Mae has been a driving force in advancing the secondary market and the multiplying effect of mortgage capital.

As evidenced by the constant stream of foreign officials who visit Ginnie Mae, the U.S. secondary mortgage market is envied throughout the world. Homeownership enables low- and moderate-income families to accumulate equity as the value of their homes grows. That equity is their capital, which is available for savings and investment. Today, Americans who previously lacked access to capital have the opportunity to create wealth for themselves and for the national economy with assistance from Ginnie Mae.

Sincerely,

Michael J. Frenz
Executive Vice President

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I. Overview

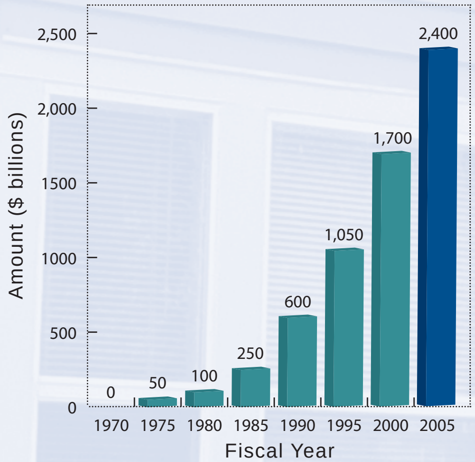
Ginnie Mae plays a critical role in expanding affordable housing and homeownership in America. Formed by Congress in 1968 as the Government National Mortgage Association, Ginnie Mae links global capital markets to the nation's housing markets by providing an attractive and efficient government-guaranteed investment vehicle–mortgage-backed securities (MBS). The Ginnie Mae MBS program enhances liquidity, expands capital access, and creates a multiplier effect in the housing finance market by allowing mortgage lenders to pool, securitize, and sell loans in the secondary market and use the proceeds to make new loans. During its 37 years of existence, Ginnie Mae has guaranteed over $2.4 trillion in MBS (see Figure 1), thereby providing access to affordable housing for over 32 million low- and moderate-income Americans and creating first-time homebuyer opportunities in every state.

Ginnie Mae is a wholly owned government corporation within the U.S. Department of Housing and Urban Development (HUD) and is administered jointly by the Secretary of HUD and the President of Ginnie Mae. Ginnie Mae significantly helps HUD meet its affordable housing mission by increasing mortgage capital for federally insured or guaranteed loans.

Despite the recent decline in the number of government guaranteed and insured loans, Ginnie Mae has continued to exceed its securitization goals, decrease its expenses, attract additional sources of capital, develop new securities, and improve security disclosures.

This report highlights Ginnie Mae's achievements and financial and operating performance during Fiscal Year (FY) 2005 and provides an overview of its history, organization, and critical role in America's housing markets.

Figure 1: Cumulative Amount of Ginnie Mae Mortgage-Backed Securities (1970 – 2005)



The Need for Affordable Housing Capital

Housing is a vital segment of the U.S. economy. According to the Bureau of Economic Analysis, housing represents almost 10 percent of gross domestic product (GDP) and plays a key role in driving the growth of the overall economy, particularly in recent years.

To a large degree, the strength of the housing markets today depends on a housing finance system that traces its roots to the Great Depression. In the early 1930s, the housing market was essentially broken. Soaring unemployment produced large-scale defaults and foreclosures that lead to an oversupply of property and caused real estate prices to plunge. Congress responded to this crisis by passing the National Housing Act of 1934, which established the Federal Housing Administration (FHA). One of the principal objectives of the FHA was to increase the flow of capital to the housing markets by insuring private lenders against the risk of mortgage default. FHA also was tasked with chartering and regulating a national mortgage association that would buy and sell FHA-insured mortgages. In 1938, Congress amended the act to create the Federal National Mortgage Association (FNMA, now known as Fannie Mae), which established a secondary market for FHA loans.

Until the development of the secondary market, housing finance was a fragmented, inefficient, and highly illiquid market largely dominated by the nation's thrifts. Mortgage rates varied from region to region, reflecting underlying differences in the local demand and supply of funds. Since there was no ready outlet for their loans, lenders were forced to hold mortgages on their books until the loans paid off, which reduced the number of new mortgages that could be originated.

The creation of Fannie Mae helped to address many of these issues, but it did not solve the problem. Lending continued to be localized and dependent upon funds available from depositories. These inherent weaknesses in the system came to a head in the late 1960s when high rates of inflation caused market interest rates to soar. One particular issue was Regulation Q, established by the Banking Act of 1935, which allowed the Federal Reserve to set a ceiling on the rates that could be offered on both checking and savings accounts. Depositors withdrew their funds from banks and thrifts and invested them in other financial institutions where higher rates were available. As a result, the funds available for mortgage lending decreased dramatically.

In 1968, responding to the need to broaden the capital base available for mortgages, Congress partitioned Fannie Mae into two entities, Fannie Mae and the Government National Mortgage Association, commonly known as Ginnie Mae.

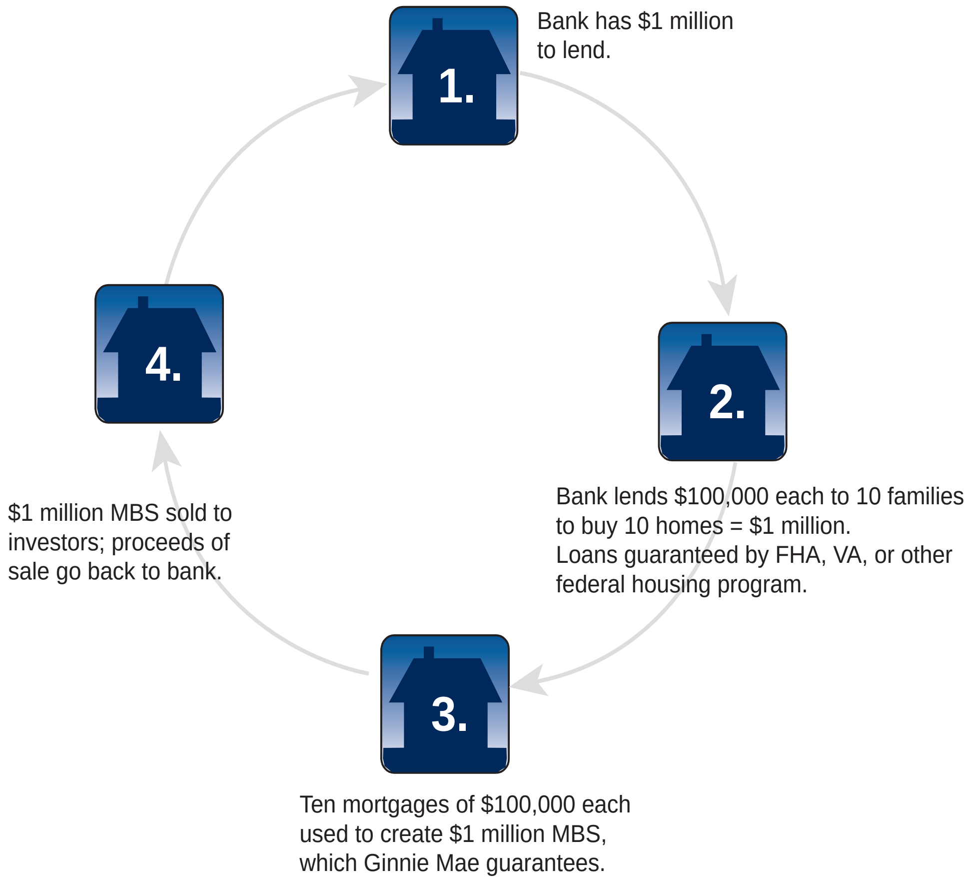
Ginnie Mae's role was set forth to guarantee the timely payment of principal and interest to investors on MBS backed by loans that are insured or guaranteed by two HUD programs: the FHA and the Office of Public and Indian Housing (PIH). In addition, Ginnie Mae guarantees the pass-through of monthly principal and interest on loans insured by the Department of Veterans Affairs' (VA) home loan program for veterans and the Rural Housing Service (RHS) of the U.S. Department of Agriculture (USDA). FHA, RHS, and PIH operate in the primary mortgage market in cooperation with lending institutions that make loans to low- and moderate-income homebuyers. The FHA, RHS, and PIH loan programs provide government-supported mortgage insurance, while VA home loans carry a partial government guarantee of payment. By reducing the risk of investing in these government-backed mortgages, Ginnie Mae expands access to capital markets, and in the process, helps to reduce the cost and increase the availability of mortgage credit for veterans and low- and moderate-income families who might otherwise be unable to buy a home.

Development of the Mortgage-Backed Securities Market

In 1970, shortly after it was created, Ginnie Mae developed and pioneered the MBS, the most important financial vehicle in the new secondary mortgage market at that time.

An MBS passes the principal and interest payments on mortgages from lenders to investors in the form of shares in a pool of mortgages. Figure 2 shows the process of using a Ginnie Mae MBS to replenish continually the supply of capital for the housing market. In Step 1, a bank has, for example, $1 million to lend for home mortgages. In Step 2, the bank lends $100,000 each to ten families that qualify for FHA, VA, or other federal loan guarantees. In Step 3, these ten mortgages are combined into an MBS, which has its principal and interest payments guaranteed by Ginnie Mae. In Step 4, the Ginnie Mae MBS is sold to investors, who receive a pro-rata share of the resulting cash flows (net of servicing and guaranty fees), and the proceeds of the sale are returned to the lending bank. This makes another

Figure 2: The Ginnie Mae Process

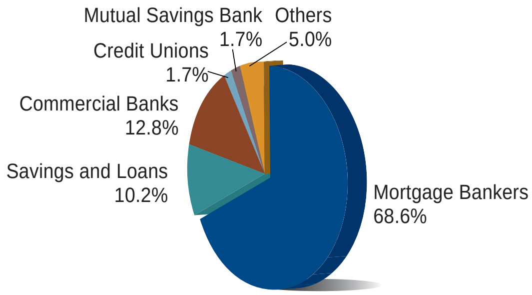


$1 million available for the bank to lend, and the cycle is repeated.

Ginnie Mae MBS allow lenders to sell their loans quickly to other investors in order to obtain funds to make more loans. Likewise, issuers want to sell MBS quickly for a fair price in order to acquire more mortgages to pool for more MBS. Ginnie Mae promotes this recycling by guaranteeing that, if approved MBS issuers are delinquent or default on payments to investors, the federal government will make the payments. This guarantee reduces the risk to investors. *Ginnie Mae MBS are the only MBS that carry the full faith and credit of the U.S. Government.* In fact, today, the secondary mortgage market has expanded into the international capital market as foreign investors value Ginnie Mae MBS and their U.S. Government guarantee. The market liquidity provided by Ginnie Mae's guarantee expands the amount of capital available for mortgages, which helps keep interest rates and down payments low. The result is increased affordable housing opportunities available to low- to moderate-income Americans.

Figure 3 shows institution types that issue Ginnie Mae MBS.

Figure 3: Breakout of Ginnie Mae Issuers by Institution Type: Number of Issuers (Data as of FY 2005)



Ginnie Mae Securities

Ginnie Mae has developed a variety of securities tailored to investors with diverse needs in constantly changing housing and capital markets. Ginnie Mae's most significant innovations are new financial products that are derivations of the basic MBS. Ginnie Mae executives and staff work continually to improve the corporation's offerings and keep up with secondary and homebuyer market demands.

Primary MBS Programs

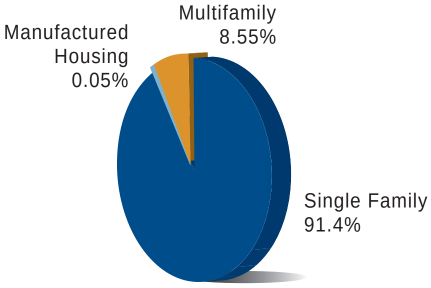
Ginnie Mae offers two primary types of MBS products, known as Ginnie Mae I and Ginnie Mae II:

Ginnie Mae I MBS require all mortgages in a pool to be the same type (e.g., single-family). Ninety percent of the pooled mortgages backing 30-year pass-throughs must have original maturities of 20 years or more. The servicing and guarantee fee equal 50 basis points[1] for each pool. In addition, the mortgage interest rates must be the same and the mortgages must be issued by the same lender. The minimum pool size is $1 million; payment on a Ginnie Mae I MBS is made on the 15th day of each month.

Ginnie Mae II MBS allow multiple-issuer pools to be assembled, which in turn allows for larger and more geographically dispersed pools, as well as the securitization of smaller portfolios. A wider range of interest rates is permitted in a Ginnie Mae II MBS pool, and issuers are given greater flexibility on the range of fees–from 25 to 75 basis points for pools issued after July 1, 2003 and 50 to 150 basis points for pools issued earlier. The minimum pool size is $250,000 for multi-lender pools and $1 million for single-lender pools. Payment for a Ginnie Mae II MBS is made on the 20th day of each month. To date, the remaining principal balance (RPB) of Ginnie Mae II MBS is approximately 42 percent of the total amount of outstanding Ginnie Mae MBS. This percentage has increased steadily over the past two years, up from just one-third in FY 2003, due to modifications to the program in 2003 and the recent increase in adjustable rate mortgage (ARM) activity.

Single-family pools comprise the majority of MBS pools, based on RPB, as of the end of FY 2005 (see Figure 4). The number and RPB of both single-family and multifamily loans have increased by approximately 1.5 percent over FY 2004.

Figure 4: Types of Loans in Ginnie Mae Issuer Pools Based on RPB, FY 2005



Multiclass Securities Program

The Multiclass Securities Program was developed to meet specific investor requirements not met by Ginnie Mae I

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[1] *Each basis point is 1/100 of 1 percent*

MBS or Ginnie Mae II MBS pass-through programs. Multiclass securities allow capital markets participants (i.e., sponsors and investors) to combine and restructure cash flows from Ginnie Mae MBS into securities that meet unique investor requirements in connection with yield, maturity, and call-option protection. The goal of the Multiclass Securities Program is to increase liquidity in the secondary mortgage market and to attract new sources of capital for federally insured or guaranteed residential loans. Ginnie Mae guarantees the timely payment of principal and interest on multiclass securities.

Real Estate Mortgage Investment Conduits (REMICs) are multiclass securities that direct principal and interest payments from underlying MBS to classes with different principal balances, interest rates, average lives, prepayment characteristics, and final maturities. Unlike traditional pass-throughs, the principal and interest payments in REMICs are not passed through to investors pro rata; instead, they are divided into varying payment streams to create classes with different expected maturities, different levels of seniority or subordination, or other differing characteristics.

REMICs allow approved sponsors to create securities with short, intermediate, and long-term maturities, thereby providing sponsors with flexibility to meet the needs of a variety of investors.

Since the inception of the REMIC program in 1994, Ginnie Mae has guaranteed more than $340 billion of such securities.

Ginnie Mae Platinum Securities provide investors with greater operating efficiency, allowing holders of multiple MBS to combine them into a single platinum certificate. Platinum Securities lower costs for internal processing and accounting by reducing the number of pools that have balances and monthly payments to be monitored. Ginnie Mae Platinum Securities are interchangeable with Ginnie Mae I and II MBS as eligible collateral for TBA[2] trades, and can be used in structured finance transactions or repurchased transactions, as well as in general trading.

Stripped Mortgage-Backed Securities (SMBS) allow approved sponsors to transfer and assign to a grantor trust (an "SMBS Trust") all of their rights, title and interest in certain securities previously guaranteed by Ginnie Mae, in exchange for two or more classes of Ginnie Mae Guaranteed SMBS. SMBS represent entitlements to all of the interest or principal collections or partial principal and interest collections received on the pool of assets underlying the related SMBS Trust. In addition, the holders of specified portions of SMBS may exchange the SMBS for equivalent combinations of other SMBS and, under certain circumstances, may exchange the SMBS for the assets underlying the SMBS Trust. Currently, only Ginnie Mae Platinum Securities can be assets for an SMBS Trust.

Risk Management

The principal risks the federal government faces in the Ginnie Mae MBS program are fraud and issuer defaults. In its role as security guarantor, Ginnie Mae also acts to protect MBS investors. To mitigate the risk of fraud, Ginnie Mae continuously monitors its program participants' portfolios, including the loan origination and pooling process to detect any deception committed by program participants. In addition, Ginnie Mae closely monitors counterparties' financial conditions, collections from borrowers, and records of pass-throughs of principal and interest payments to investors.

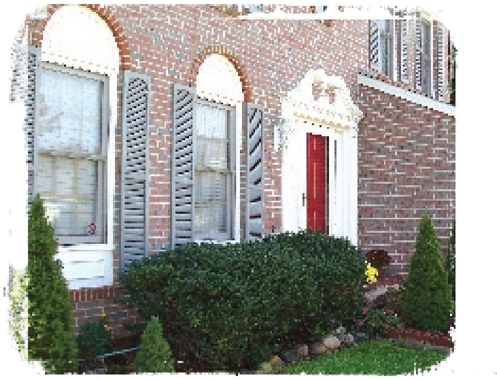
[2] *TBA (To Be Announced) trades refer to contracts for the purchase or sale of MBS to be delivered at an agreed-upon future date but do not include specified pool numbers and number of pools or precise amount to be delivered.*

Ginnie Mae also tracks trends in delinquency and default rates for mortgages that are the collateral for mortgage-backed securities. Should Ginnie Mae determine that a servicer is subjecting Ginnie Mae to unacceptable risk, Ginnie Mae can take over the administration of all of that servicer's MBS portfolio.

In the fourth quarter of FY 2005, 93.3 percent of the RPB in Ginnie Mae's securities was serviced by 50 servicers.[3] Among these, 33 servicers or their parent entities, which service 82 percent of the RPB in Ginnie Mae pools, were rated A (or its equivalent) or higher by a nationally recognized statistical rating organization (NRSRO) or had a NRSRO servicer rating of strong or stable. In addition, 39 of the 50 largest servicers, collectively servicing 71 percent of the RPB, are federally insured depository institutions or are subsidiaries of such institutions. In sum, 89 percent of the RPB is administered by 50 servicers meeting at least one of the following criteria:

- Has a NRSRO Credit Rating of A (or equivalent) or better (or is a subsidiary to a parent with such a rating),
- Has a servicer rating of Strong or Stable, and/or
- Is a federally insured depository institution (or a subsidiary of such an institution).

This concentrated group of high quality servicers reduces the systematic risk to the federal government and investors from servicer default, fraud, or malfeasance.



Benefits to Homeowners, the Economy, and the Federal Government

The U.S. housing capital market is envied throughout the world. Ginnie Mae has been a driving force in advancing the secondary market, the multiplying effect of mortgage capital, and the ability of lenders to provide FHA and VA financing. The secondary mortgage market has created homeownership opportunities that previously did not exist for millions of low- and moderate-income families. It also has enabled families of all income levels to build personal wealth from the equity in their homes as the values increase. This wealth provides opportunities for these families to save and invest, which, at a macro level, stimulates and improves the national economy.

In addition to benefiting homeowners and the economy, Ginnie Mae does not depend on the federal government to pay for its operations. Instead, Ginnie Mae operations are funded by revenues generated from guaranty fees and on its securities, and it has ended each fiscal year with positive net revenues. Furthermore, Ginnie Mae has worked with HUD over the years to be a leader in the housing and capital markets and has made a powerful contribution to HUD's affordable housing mission.

Significant Highlights and Achievements in FY 2005

Ginnie Mae's significant results and achievements in FY 2005 are highlighted below. Details of these and other events are presented in Sections III, IV, and V herein.

Security Issuance

During FY 2005, Ginnie Mae:

- Through issuance of MBS, provided the capital to finance the purchase or refinance of 660,550 single-family homes and provision of rental housing for 129,500 multifamily rental units throughout America.

[3] Inside Mortgage Finance, *August 12, 2005.*

- Guaranteed securities that represented over 92 percent of eligible FHA or VA single-family mortgages, exceeding its goal of 85 percent for the third consecutive year.
- Guaranteed securities that represented over 91 percent of FHA multifamily mortgages, exceeding 90 percent for the third consecutive year.
- Guaranteed MBS for the first-ever rural multifamily property secured by a USDA RHS Section 538 multifamily loan.
- Enhanced its existing five-year hybrid ARM security.

Financial Results

For FY 2005, Ginnie Mae:

- Had operating revenues of $787 million and expenses of $71 million.
- Had balance sheet assets totaling $12.1 billion as of September 30, 2005.
- Received an unqualified audit opinion on its financial statements.

Other Significant Achievements and Highlights

Also during FY 2005, Ginnie Mae:

- Expanded its Business Improvement Initiative (BII), which was designed to streamline Ginnie Mae's business operations and reduce paperwork, by considering more than 70 important suggestions generated by MBS market participants.
- Made significant improvements in security disclosure, which further aligned Ginnie Mae with industry best practices.
- Expanded its Targeted Lending Initiative (TLI) to include 40 new Renewal Communities and eight new Urban Enterprise Zones designated by HUD.

- Continued the implementation of a Business Process Improvement (BPI) project and an Enterprise Architecture migration plan, which will result in a more cost-effective and streamlined operating environment during FY 2006 and beyond.
- Increased its small business contracting obligations substantially. Approximately 31 percent of Ginnie Mae's FY 2005 contract obligations went to small businesses, a significant increase over FY 2004 results (14 percent). The 31 percent level is a record for Ginnie Mae and demonstrates Ginnie Mae's commitment to small business.

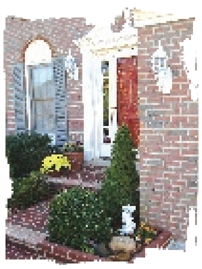
II. Organization and Infrastructure

Structure and Staffing

The U.S. Congress anticipated Ginnie Mae's need for speed and agility when it structured Ginnie Mae as a wholly owned corporation housed within HUD. Throughout its history, Ginnie Mae has been able to operate as a lean and efficient organization. Almost all transactional and support work (over 80 percent) is now outsourced to contractors. Despite its relatively small staff of 65 employees, Ginnie Mae supported the issuance of $90.3 billion in new securities in FY 2005. This was possible as most employees of Ginnie Mae are engaged in core business processes, including monitoring issuers and capital markets, managing contractors, and working with customers and stakeholders to develop responses to changing market conditions.

Ginnie Mae strongly supports HUD's commitment to increase contracting and subcontracting opportunities for Small, Small Disadvantaged, 8(a), Women-Owned, Veteran-Owned, Service Disabled Veteran-Owned, and HUBZone small businesses. The institution increased its small business contract obligations from 14 percent as of September 30, 2004, to 31 percent as of September 30, 2005. Ginnie Mae's procurement opportunities are included in HUD's Forecast of Contracting Opportunities, which can be viewed at http://www.hud.gov/offices/osdbu/4cast.cfm.

Technology



Ginnie Mae has made significant investments in information technology (IT) that provide issuers and investors with comprehensive information and reliable service in an increasingly internet-based environment. Its technology initiatives have been responsive to a dynamic secondary market, in which immediate access to information is paramount to success. Ginnie Mae's approach to business reflects the President's Management Agenda Initiative for Competitive Sourcing and Expanded Electronic Government.

In FY 2005, Ginnie Mae continued to enhance its IT infrastructure by integrating state-of-the-art solutions into its operational infrastructure and streamlining its business processes, reducing processing time and costs for both Ginnie Mae and its customers. It also worked with the lending community to establish a well-defined vision to enhance the operational infrastructure. Finally, it tightened its control measures by establishing stronger information security policies based upon the federal government's preeminent producer of such guidelines, the National Institute of Standards and Technology (NIST).

Specific technology initiatives are described as follows:

Modernization of Operating Environment

Ginnie Mae initiated the implementation of its BPI study and the Enterprise Architecture migration plan. The implementation will result in a more cost-effective and streamlined operating environment. The development of a service-oriented architecture (SOA) will permit Ginnie Mae to respond rapidly to changes within the marketplace, enhance its ability to leverage opportunities in the secondary market, and reduce operating costs for Ginnie Mae partners and the corporation itself.

The Reporting and Feedback System (RFS) is the first phase of the BPI that will be implemented. This business application, to be initiated in FY 2006, will capture all reporting information and provide streamlined reporting and enhanced data management of information submitted by Ginnie Mae issuers. The Enterprise-Wide Operational Data Store (EWODS) initiative will greatly improve data disclosures, improve risk management, and provide issuers with direct access to Ginnie Mae information concerning their own accounts. Ginnie Mae made several enhancements during FY 2005 to its flagship application GinnieNET, which it uses to conduct business with customers. The enhanced technical architecture will improve Ginnie Mae's ability to provide cost-effective services to the financial services community. All of these program initiatives will strengthen Ginnie Mae's ability to adapt quickly to changing market conditions and respond to investors' needs.

Continuity of Operations and Disaster Recovery

During FY 2005, Ginnie Mae remained vigilant in its awareness and readiness to thwart potential threats to its operations and financial systems, and hence to protect its vital role in America's economy. Ginnie Mae is committed to ensuring compliance with all Department of Homeland Security guidelines in support of the federal government's requirement to establish, maintain, and support sustained operations in the event of a crisis. Ginnie Mae routinely updates and exercises its Continuity of Operations Plan

(COOP) and Disaster Recovery programs with internal Ginnie Mae enterprise-wide COOP tests, training, and exercises. These tests, training, and exercises assess the readiness of Ginnie Mae's COOP Emergency Relocation Group (CERG) Team, essential business partners, telecommunications tools, technology, and staff.

IT Legislative Analysis

The Ginnie Mae IT legislative analysis team, established by the Office of the Chief Information Officer (CIO), has been tasked with analyzing and assessing federal IT legislation and providing its findings to the CIO to assist the CIO in making prudent IT decisions that impact the enterprise at large. This in-depth legislative analysis ensured that Ginnie Mae's critical infrastructure remained in compliance with applicable rules and guidelines, and allowed Ginnie Mae to stay abreast of ever-changing state-of-the-art technological solutions.

e-Commerce

Ginnie Mae and its business partners continue to benefit from internet technologies. During FY 2005, Ginnie Mae reengineered the method by which stakeholders access information and migrated from hard copy mailings to electronic dissemination of monthly pool accounting and pool origination information. A notable enhancement has been the creation of the electronic Issuer Feedback Report that allows issuers to compare their portfolio statistics with Ginnie Mae averages on the internet. This is one of the many new innovations in process to assist investors and issuers in performing analytics on Ginnie Mae securities.

III. Highlights and Recent Initiatives

Ginnie Mae Security Issuance in FY 2005

Ginnie Mae guaranteed $90.3 billion in MBS in FY 2005 (see Figure 5), which supported capital for an additional 790,000 units of housing for low- and moderate-income American families (see Figure 6). The recent trend of lower MBS issuance reflects the overall decrease in the number of FHA and VA loans originated over the past several years.[4] Nevertheless, the cumulative amount of both single-family and multifamily Ginnie Mae securities that have been issued since Ginnie Mae's securitization program began in 1970 is $2.4 trillion, demonstrating the dramatic impact Ginnie Mae has had on providing financing for affordable housing and expanding homeownership opportunities.

Figure 5: Value of Ginnie Mae MBS, FY 2001-2005

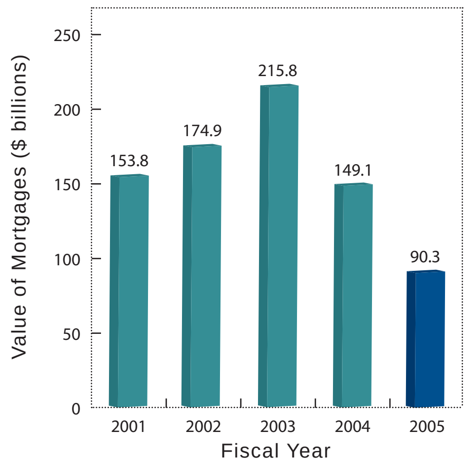
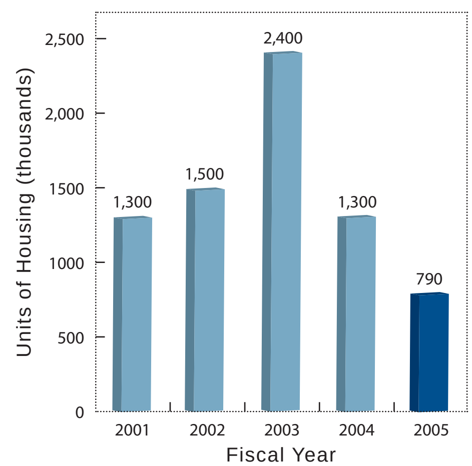


Figure 6: Ginnie Mae Supported Units of Housing, FY 2001-2005



In FY 2005, FHA and VA programs represented the bulk of mortgage originations that collateralized Ginnie Mae securities (67.6 percent and 29.4 percent in dollar terms, respectively), with the remaining loans coming from the PIH and RHS programs.

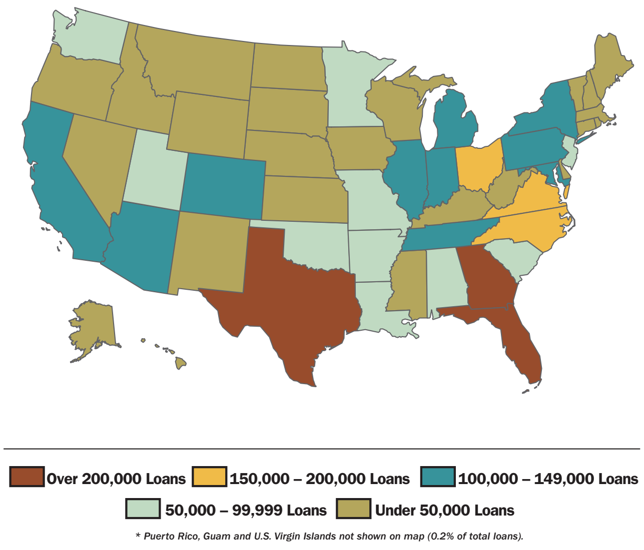
Single-Family Security Issuance in FY 2005

Ginnie Mae exceeded its goal–to guarantee at least 85 percent of eligible FHA and VA single-family loans–for a third consecutive year. Approximately 92 percent of all VA and FHA loans were placed into Ginnie Mae securities, an increase of five percentage points over FY 2004.

The amount of outstanding single-family securities at the end of FY 2005 was $376.5 billion, compared to $420.4 billion at the end of the previous year. This decline was primarily due to mortgage repayments exceeding new issuance. A key factor has been the appreciation of home prices, which increases equity and enables existing FHA and VA-financed homeowners to qualify for conventional financing when they refinance their mortgages or finance a move to a new home. FHA and VA borrowers

[4] Ginnie Mae's market share is constrained by the limited dollar amount of FHA and VA loans. FHA loans have maximum loan amounts that vary by county and cannot exceed the lesser of 95 percent of the median house price in the area and 87 percent of the conforming loan limit, which changes annually. There is no statutory VA loan limit analogous to the FHA limit; however, lenders generally will not lend in excess of four times the amount of the veteran's "entitlement," an amount that can be as little as $36,000. Because many residential markets in the U.S. have experienced significant home appreciation, many residential markets have been priced out of FHA and VA loans.

Figure 7: Geographic Distribution of Single Family Properties Securing Ginnie Mae Securities



State	Loans	Percent of Total Loans	RPB (in millions)
Texas	578,398	14.3%	$47,384
Florida	273,095	6.8%	$23,869
Georgia	204,010	5.1%	$20,970
Virginia	160,469	4.0%	$16,740
Ohio	156,284	3.9%	$14,547
North Carolina	156,018	3.9%	$15,277
California	137,424	3.4%	$13,723
Illinois	130,057	3.2%	$13,686
New York	126,653	3.1%	$11,373
Tennessee	120,218	3.0%	$10,625

typically refinance into conventional mortgages (or use conventional mortgages to purchase new homes) during or after a period of strong home-price appreciation, which creates borrower wealth through home equity.

Ginnie Mae has created homeownership opportunities in every state in the country. The map in Figure 7 shows areas with the highest concentrations of single-family loans in Ginnie Mae securities at the end of FY 2005, and the RPB of such loans.

Thirty-year fixed-rate mortgages dominate single-family Ginnie Mae MBS. In FY 2005, 15-year mortgages accounted for 5.5 percent of loans in MBS pools.

Multifamily Security Issuance in FY 2005

Over 91 percent of eligible FHA multifamily mortgages were placed into Ginnie Mae securities during FY 2005, exceeding Ginnie Mae's goal of 80 percent by 11 percentage points. Ginnie Mae has continued to streamline the multifamily program by enhancing its efficiency as a securitization vehicle, which has made the program more attractive to investors. In FY 2005, however, market competition resulted in the contraction of FHA multifamily originations. As a result, Ginnie Mae's multifamily issuances fell by 19 percent, from $10.5 billion in FY 2004, to $8.5 billion in FY 2005. Despite the decline in new issuances, the multifamily program's RPB still increased by 8 percent, from $32.7 billion to $35.3 billion by the end of FY 2005. The increase in the multifamily RPB reflects the appeal of multifamily government-guaranteed loans to investors due to their attractive yield maintenance features. Ginnie Mae securities provide investors with a longer term guarantee of income streams compared with other MBS that do not actively manage prepayment curtailment through penalty fees.

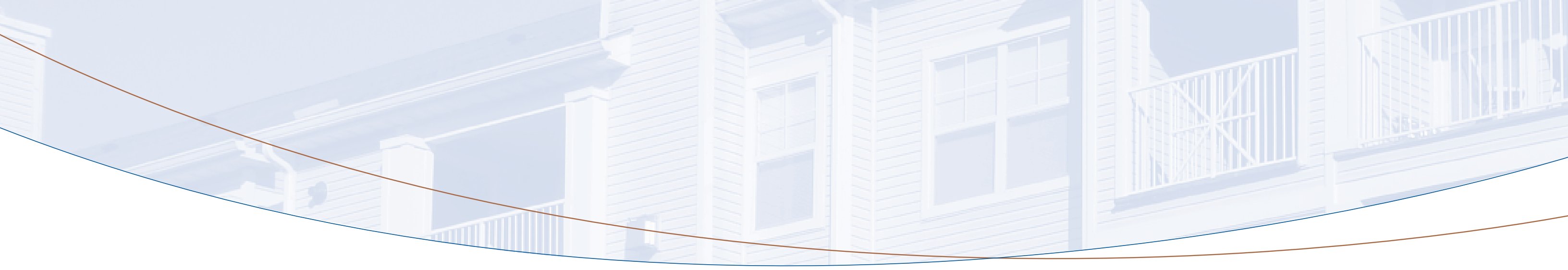
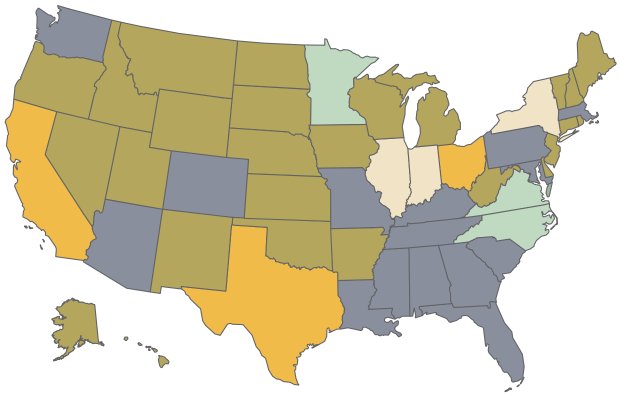


Figure 8: Geographic Distribution of Multifamily Properties Securing Ginnie Mae Securities



State	Total Loans	Percent of Total Loans	RPB (in millions)
Texas	537	8.0%	$3,416
California	505	7.5%	$2,549
New York	322	4.8%	$2,218
Illinois	343	5.1%	$2,215
Ohio	442	6.6%	$1,755
Virginia	230	3.4%	$1,584
Maryland	199	3.0%	$1,580
Minnesota	237	3.5%	$1,405
Florida	187	2.8%	$1,309
Indiana	315	4.7%	$1,143

Ginnie Mae has helped to create affordable rental housing for low- to moderate-income families in every state in the country. The map in Figure 8 shows areas with the highest concentrations of multifamily loans in securities guaranteed by Ginnie Mae at the end of FY 2005 and the RPB of such loans.

Security Innovations

ARM Securities

Ginnie Mae enhanced its existing five-year hybrid ARM security by changing its existing annual interest rate change cap amount from 1 percent to 2 percent and the maximum lifetime interest rate cap from 5 percent to 6 percent. These enhancements were made to improve the security's marketability, which has helped to increase demand in the capital markets and stimulate mortgage origination for these types of mortgages. Ultimately, this reduces, and will continue to reduce, the cost of homeownership to low- and moderate-income borrowers.

Changes to the ARM program, along with an overall expansion of ARM product demand by borrowers, have helped to increase ARMs as a percentage of Ginnie Mae single-family issuance. Prior to these changes, and due to historically low long-term interest rates, ARM share had been somewhat stagnant, hovering around 5 percent (with a brief spike in mid-2002). ARMs now account for 10 to 20 percent of all single-family issuance during the past two years.

Platinum Securities

In FY 2005, Ginnie Mae further simplified and reduced fees on newly issued Platinum securities. The reduced fees increased their marketability as evidenced by the significant increase in the number of pools produced since the first fee modification in July 2004. Again, increased marketability and liquidity for Ginnie Mae securities has resulted in lower costs to American homeowners.

Rural Multifamily Securities

The RHS Department of the USDA approached Ginnie Mae's management to ask it to create a new security that would provide affordable multifamily housing in rural communities. The rural multifamily market has long been a neglected segment of the housing market. The lack of a robust rural multifamily secondary market increases the costs of these loans to borrowers and reduces the supply of rental units in these markets. During FY 2004, Ginnie Mae worked with Congress to enact legislation to authorize securitization of multifamily Rural Housing Section 538 loans. In February 2005, Ginnie Mae guaranteed the first ever rural multifamily property security, Whispering Pines in Coldwater, Michigan. This 112-unit apartment property was secured by a USDA Rural Housing Section 538 multifamily loan.

Ginnie Mae's new multifamily security will expand the supply of multifamily housing for low- and moderate-income families in rural areas throughout America. To date, 11 securitizations totaling $17 million, and representing 11 properties with a total of 606 affordable housing units, have been done under this new program.

Enhanced Securities Disclosures

In FY 2005, Ginnie Mae continued to focus on improving its security disclosures as part of its commitment to transparency, efficiency, and organizational improvement. In response to investor requests, Ginnie Mae increased the frequency of its data disclosure cycle, moving from a quarterly to a monthly basis, and added new information that will enable investors to make more informed decisions. During the last quarter of FY 2005, it announced several new operational enhancements that will be implemented in early FY 2006. In October 2005, Ginnie Mae began releasing monthly disclosure information on the second business day of the month instead of the seventh, and began disclosing the volume of mortgages backing its MBS that are insured or guaranteed by the RHS and PIH.

Beginning in December 2005, Ginnie Mae's monthly disclosure file will provide data on unscheduled principal paydowns on loans collateralizing Ginnie Mae MBS, including the unpaid principal balance of loans that are (1) paid off in full by borrowers, (2) repurchased by issuers due to delinquency, and (3) liquidated from the pool upon receipt of insurance funds after foreclosure. This new disclosure will also identify loans that are 30, 60, and 90 or more days delinquent as well as the number of buydown loans insured or guaranteed by the FHA and the VA. Capital market participants believe that improving disclosures will increase liquidity, resulting in better pricing on Ginnie Mae MBS, which in turn leads to lower interest rates for low- and moderate-income borrowers.

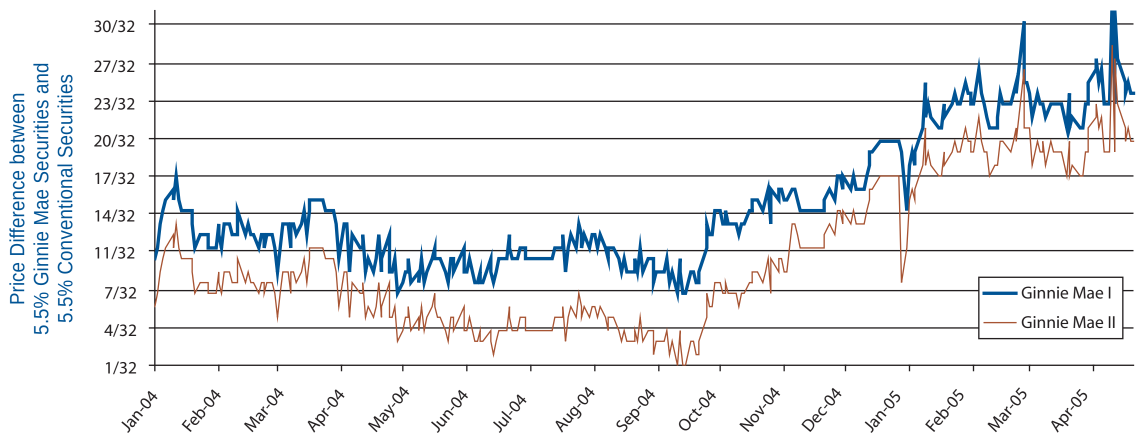
Upcoming Securities Initiatives

In furthering its statutory mission to expand affordable housing in America by linking global capital markets to the nation's housing markets, Ginnie Mae, operating under its current legal authority, is planning to implement an Excess Yield Securities Program (XMBS) during FY 2006. Through this program, Ginnie Mae will provide its guarantee to interest-only securities backed by a portion of the servicing fee that is paid out of the monthly cash-flows from government-insured or -guaranteed mortgage loans previously issued into Ginnie Mae MBS.

The Excess Yield Securities Program will allow qualifying Ginnie Mae issuers to reduce the amount of mortgage servicing rights on their balance sheets, which will in turn reduce the amount of capital they are required to hold against that asset. By increasing the liquidity of mortgage servicing rights for Ginnie Mae issuers, the Excess Yield Securities Program should lower the costs of, and encourage the origination of, government-insured and-guaranteed loans that back Ginnie Mae MBS. This should directly benefit low- and moderate-income borrowers.

Ginnie Mae posted a Notice of Proposed Rule Making in FY 2005 to develop and implement the program during FY 2006. The proposed rule clarified the authority of

Figure 9: Historical Spread of Ginnie Mae I and II Securities over Conventional Securities



Ginnie Mae to guarantee this new product and provided Ginnie Mae the opportunity to consider public comment before implementing the program.

Security Performance

MBS Performance

Over the past 18 months, Ginnie Mae MBS have outperformed their conventional counterparts in market trading. This is evidenced by the spread, or differential, in market prices between Ginnie Mae MBS and its conventional benchmark, which is Fannie Mae MBS. The graph in Figure 9 shows for the current coupon, 5.5 percent, a substantial increase in spread for both the Ginnie Mae I MBS and the Ginnie Mae II MBS over the Fannie Mae 5.5 percent MBS. At the end of FY 2005, Ginnie Mae prices were near a historical high relative to conventional securities.

The performance of Ginnie Mae securities is driven by both supply and demand. Although the decline in FHA and VA mortgage originations has limited new supply (resulting in net paydowns), investor demand has been strong, especially among total return money managers, banks, Ginnie Mae funds, and foreign investors. Central banks have a strong preference for Ginnie Mae securities because they represent the full faith and credit guarantee of the U.S. Government, which is often part of their regulatory requirements. Therefore, market demand is expected to remain high. Strong performance for Ginnie Mae securities not only enhances Ginnie Mae's market share, but demonstrates the value that Ginnie Mae brings supporting homeownership for low- and moderate-income Americans.

In addition, Ginnie Mae has seen an increase in the demand for and performance of its Ginnie Mae II securities. Ginnie Mae II securities have historically traded at a lower price than Ginnie Mae I securities, primarily due to the payment delay. The spread of Ginnie Mae II versus Ginnie Mae I pricing (as shown above in Figure 9), however, has been narrowing as Ginnie Mae II securities have increased in popularity. This is due to greater pooling flexibility for originators and issuers, as well as a more predictable expected prepayment experience.

REMIC Activity and Performance

Dealer participation in the Ginnie Mae REMIC program remained active during FY 2005. Fourteen securities dealers sponsored transactions, with most doing at least three.

Ginnie Mae's REMIC activity, as measured by issuance volume, is influenced by both MBS issuance and the price of MBS collateral. Although the dollar volume of REMICs issued in FY 2005 has declined relative to Ginnie Mae's past high years in FY 2002 and FY 2003, the number of deals issued has remained fairly constant as shown in Figure 10. Securities dealers have an incentive to provide structured Ginnie Mae product to their investors, even if this requires sponsoring smaller deal sizes than what has typically been executed in the marketplace. In addition, dealers increasingly use existing Ginnie Mae REMIC classes as collateral for new REMIC securities. In FY 2005, $5.8 billion (16 percent) of the dollar volume of REMICs was comprised of such collateral. A Ginnie Mae re-REMIC is a REMIC or security whose related trust assets include a previously issued REMIC or MX security[5], directly or indirectly backed by Ginnie Mae MBS certificates.

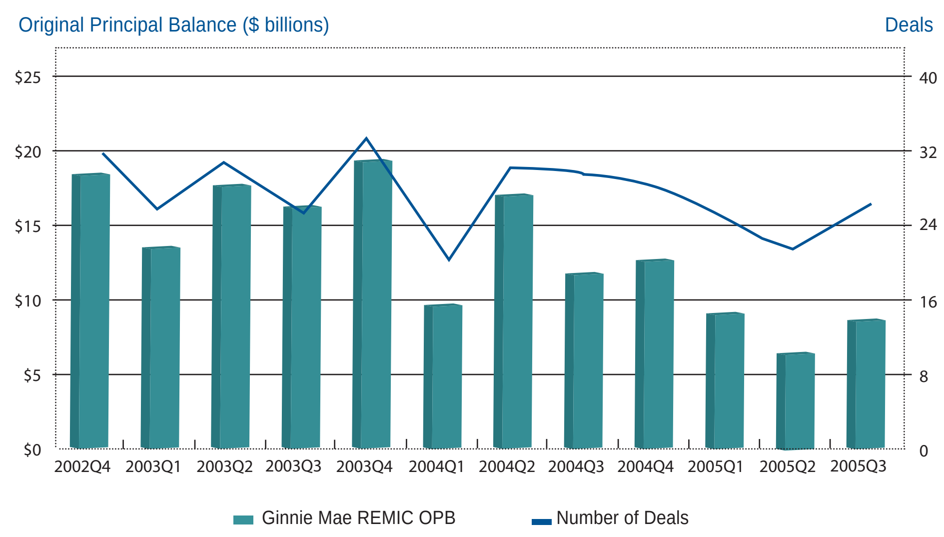
The strong pricing of MBS has also impacted the amount of collateral supporting REMIC securities, and hence, total REMIC volume. REMICs enable dealers to create additional value from underlying MBS, creating new types of securities that broaden the investor base, which increases demand. At a certain point, however, the spread of MBS can become so wide (relative to its benchmark securities) that the opportunity to create additional value may diminish. At this point, the costs (e.g., participant fees) associated with creating a REMIC may outweigh the benefits.

During FY 2005 Ginnie Mae II MBS was the predominant collateral, due to its cheaper price, used in Ginnie Mae REMICs (supporting 68 percent of the dollar volume of new issuance). Ginnie Mae I collateral and multifamily collateral supported 19 percent and 13 percent, respectively.

Business Improvement

During FY 2005, Ginnie Mae's management demonstrated its desire to increase its attentiveness and responsiveness to its investors, issuers, broker/dealers, and other business partners by soliciting recommendations for changes concerning business processes and procedures. It

Figure 10: Ginnie Mae REMIC Activity



[5] *A MX security is a type of security class within a multiclass security created by combining one or more other classes from the same REMIC.*

sought these recommendations as part of a BII, which is designed to enhance Ginnie Mae's business operations. To date, more than 70 ideas have been submitted from various market participants, with the majority of suggestions focused on streamlining Ginnie Mae's operations and reducing paperwork. Subsequent to the end of FY 2005, Ginnie Mae responded to these suggestions on its website. During FY 2006, it plans to implement the most promising of these ideas.

The technology-related ideas captured through this initiative will be integrated into the vision and plans Ginnie Mae established through the BPI Action Steps and Enterprise Architecture Migration Plans as described in Section II above.

Focusing Capital Markets on Economically Depressed Areas

The Targeted Lending Initiative (TLI) program offers discounts ranging from 1 to 3 basis points on Ginnie Mae's 6 basis point guaranty fee, depending on the percentage of TLI-eligible loans within the security. Eligible loans are those contained within underserved areas, which include urban and rural areas designated by HUD as Empowerment Zones, Enterprise Communities, and Renewal Communities.

Ginnie Mae expanded the TLI in FY 2005 to include the colonias (poor rural communities, almost always unincorporated, that lie in a 150-mile-wide strip along the U.S.-Mexico border between Texas and California) as well as 40 new Renewal Communities and eight new Urban Enterprise Zones designated by HUD. The result of including these new areas in the TLI program was a 59 percent increase in TLI-eligible census tracts. In FY 2005, 4,083 TLI pools were issued, which is the highest number in any fiscal year since the program began and a 33 percent increase from FY 2004. Under the TLI program, Ginnie Mae provides a reduction in its MBS guaranty fee by as much as 50 percent for approved lenders that purchase or originate loans in eligible areas. The reduced guaranty fee gives lenders an incentive to originate loans in TLI areas.

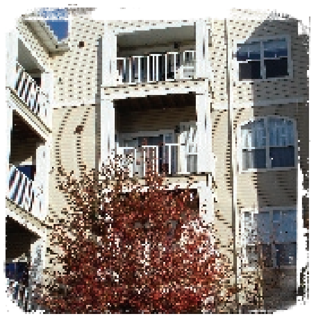
The use of TLI can be a powerful tool for expansion of lending activities in underserved areas. For example, since the colonias were incorporated in the TLI program in June 2004, 6,757 loans, totaling $718 million, have been made to families in these areas. This action has helped these families dramatically improve their financial position, since they now own their homes and have the ability to benefit from any appreciation in value.

Responding to Natural Disasters

In response to the devastation caused to parts of the states of Louisiana, Mississippi, Alabama, and Florida by Hurricane Katrina in August 2005, Ginnie Mae offered various forms of forbearance to issuers of Ginnie Mae MBS with greater than five percent of their Ginnie Mae loan portfolios in declared disaster areas. Ginnie Mae disaster forbearance includes assistance in making payment to MBS investors where homeowners are unable to make payment. In addition, Ginnie Mae is not including delinquent loans in affected areas as part of its delinquency statistics used in risk monitoring. Ginnie Mae also extended its TLI for new MBS to areas designated as disaster areas.

Outlook

Through enhanced and effective best-practices business management, including better uses of technology, more advanced investor and financial reporting capabilities, offering products and programs which meet changing investor needs, and the ability to generate and provide better performance metrics on its portfolio, Ginnie Mae will continue to excel by fostering its credibility and reliability within the capital markets. Ginnie Mae has a superior track record of cultivating and retaining investor confidence. This credibility and confidence translates into strong market demand for Ginnie Mae securities, which enables Ginnie Mae to sustain and expand affordable housing in the United States. And with this reputation for quality and reliability, Ginnie Mae looks forward to a successful future.



To maintain its credibility, Ginnie Mae is dependent upon the federal government's counterparty lender mortgage insurance programs, which, by its legislative charter, Ginnie Mae supports with its guarantor programs. To maintain its reliability, Ginnie Mae must continue to advance and enhance the value of its underlying programs within the marketplace. A variety of market-driven and other factors have led government insurance program originations to decline precipitously over the past five years. At some point, these declines may have a significant impact on the liquidity of Ginnie Mae securities, despite continued programmatic innovation and enhancement to securities performance initiated by Ginnie Mae. Ginnie Mae will continue to work hard to advance and enhance the value of its programs so that its mission to expand affordable housing in America will endure and prevail.

IV. Management's Discussion and Analysis of Results of Operations and Financial Position

Financial Highlights of 2005

FY 2005 was marked by modest declines in revenue, operating expenses, and excess revenue (i.e., revenue less operating expenses), combined with an increase in total assets. FY 2005 revenues decreased by 3.5 percent, to $787 million, down from $815.5 million in FY 2004. Excess revenues decreased by 4.4 percent in FY 2005, to $705.2 million, down from $737.7 in FY 2004. Total assets increased by 6.3 percent to $12.1 billion in FY 2005, up from $11.4 billion in FY 2004.

Refinancing runoff and reduced MBS issuance led to a decline in the size of outstanding MBS portfolio, which decreased the revenues generated by guarantee fees. Revenues related to the MBS programs declined to $327.5 million in FY 2005, down from $372.8 million in FY 2004. Total expenses as a percentage of total revenues decreased from 9.5 percent in FY 2004 to 9.1 percent in FY 2005.

Ginnie Mae issued $112.5 billion in commitment authority in FY 2005, a 23 percent decrease from FY 2004. FY 2005 MBS issuance declined by 39 percent, to $90.3 billion. Since repayments exceeded new issuances, the outstanding MBS balance at the end of FY 2005 dropped to $412.3 billion, down from $453.4 billion in the previous year.

Ginnie Mae's financial performance remained stable during FY 2005, with excess revenue over expenses invested in U.S. government securities, which is a requirement imposed on Ginnie Mae by the Department of the Treasury. To date, Ginnie Mae's earnings have provided the capital to finance its operations, and, as a result, Ginnie Mae has not needed to obtain funds through federal appropriations.

To assist readers in understanding Ginnie Mae's recent financial history, Table 1 provides three-year financial highlights of the corporation.

Table 1: Ginnie Mae Financial Highlights

September 30	2005	2004	2003
(Dollars in thousands)			
Balance Sheets Highlights and Liquidity Analysis			
Funds with U.S. Treasury	$ 3,711,400	$ 3,355,100	$ 2,931,800
U.S. Government Securities	$ 7,921,000	$ 7,539,800	$ 7,215,800
Total Assets	$ 12,134,600	$ 11,411,300	$ 10,353,900
Total Liabilities	$ 1,041,700	$ 1,023,600	$ 703,900
Investment of U.S. Government	$ 11,092,900	$ 10,387,700	$ 9,650,000
Total RPB Outstanding (1)	$ 412,303,791	$ 453,421,816	$ 473,907,979
LLR (2) and Investment of U.S. Government	$ 11,631,400	$ 10,906,400	$ 10,169,300
Investment of U.S. Government as a Percentage of Average Total Assets	94.22%	95.45%	96.94%
LLR and Investment of U.S. Government as a Percentage of RPB	2.82%	2.41%	2.15%
Capital Adequacy Ratio (3)	2.74%	2.35%	2.10%
Highlights From Statements of Revenues and Expenses & Profitability Ratios Years Ended September 30			
MBS Program Income	$ 327,500	$ 372,800	$ 406,100
Interest Income	$ 458,800	$ 442,700	$ 389,300
Total Revenues	$ 786,500	$ 815,500	$ 799,600
MBS Program Expenses	$ 58,300	$ 63,300	$ 55,400
Administrative Expenses	$ 10,600	$ 10,600	$ 10,300
Provision for Loss	$ 10,000	$ –	$ –
Total Expenses	$ 71,300	$ 77,800	$ 68,100
Excess of Revenues Over Expenses	$ 705,200	$ 737,700	$ 731,500
Total Expense as a Percentage of Average RPB	0.0165%	0.0168%	0.0131%
Provision for Loss as a Percentage of Average RPB	0.0023%	–	–

(1) Remaining Principal Balance (RPB) of Ginnie Mae MBS, and, in addition, $81.7 million of Ginnie Mae Guaranteed Bonds

(2) Loan Loss Reserve (LLR)

(3) LLR and Investment of U.S. Government divided by the sum of Total Assets and Remaining Principal Balance

Results of Operations

Ginnie Mae believes that the following discussion will provide the reader with information that is relevant to understanding the results of its operations and its current financial condition. The discussion should be read in conjunction with the financial statements and notes thereto. Ginnie Mae's operating results are subject to fluctuation each year, depending on the frequency and severity of losses resulting from general economic conditions, mortgage market conditions, and the number of terminating issuers.

Revenues

Ginnie Mae's operations are self-financed through a variety of fees. It receives no appropriations from general tax revenues. For FY 2005, Ginnie Mae generated total revenue of $786.5 million. Revenue consisted of $327.5 million in program income and $458.8 million in interest income from U.S. Treasury securities.

Figure 11 shows Ginnie Mae's total annual revenues for the last five years.

MBS Program Income

MBS program income consists primarily of guaranty fees, commitment fees, and multiclass fees. For FY 2005, MBS program income was concentrated in guaranty fees of $285.5 million followed by commitment fees of $19.4 million. Combined guaranty fees and commitment fees composed 93 percent of total MBS program revenues for FY 2005. Other lesser income sources were new issuer fees, handling fees, and transfer of servicing fees. MBS program income decreased in FY 2005 due to the decline in the MBS portfolio and MBS issuance.

Guaranty Fees

Guaranty fees are income streams earned for providing Ginnie Mae's guaranty of the full faith and credit of the U.S. Government to investors. These fees are recognized over the life of the outstanding securities.

Guaranty fees are collected on the aggregate principal balance of the guaranteed securities outstanding in the non-defaulted issuer portfolio. MBS guaranty fees decreased 6.9 percent to $285.5 million in FY 2005 from $306.8 million in FY 2004. The lower guaranty fees reflect the decline in the MBS portfolio. The outstanding MBS balance at the end of FY 2005, was $412.3 billion, compared with $453.4 billion the previous year, as repayments exceeded new issuances (see Figure 12).

Figure 11: Ginnie Mae Revenues FY 2001-2005

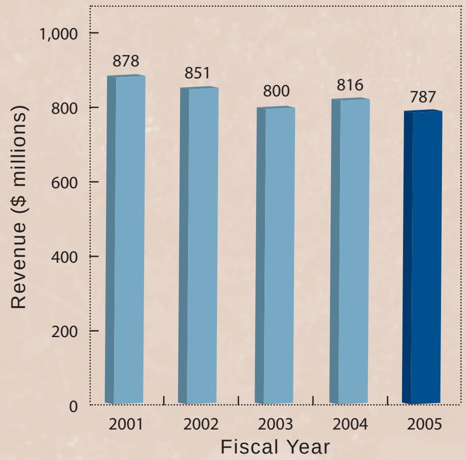
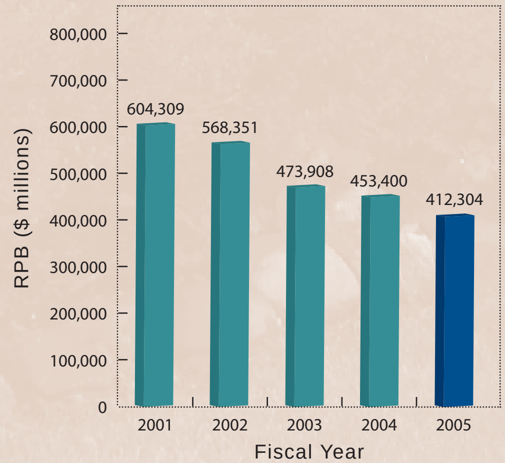


Figure 12: Remaining Principal Balance (RPB) Outstanding in the MBS Portfolio



program fees. In FY 2005, Ginnie Mae issued $57.1 billion in its multiclass securities program. In FY 2005, Ginnie Mae issued approximately $20.1 billion in Platinum products. Total cash fees for Platinum securities amounted to $6.4 million, representing a 33 percent decrease in fee income from the previous year, a result of lower Platinum product issuance. Guaranty fees from REMIC securities amounted to $14.5 million on $36.5 billion in issuance for those products. Ginnie Mae recognizes a portion of the REMIC, Callable Trust, and Platinum program fees in the period they are received, with the balance deferred and amortized over the remaining life of the financial investment.

The estimated outstanding balance of multiclass securities included in the total MBS balance on September 30, 2005, was $187.6 billion. This was a one percent decrease from the outstanding balance in FY 2004 of $189.1 billion.

Commitment Fees

Commitment fees are income that Ginnie Mae earns for providing approved issuers with authority to pool mortgages into Ginnie Mae MBS. The authority Ginnie Mae provides expires 12 months from issuance for single-family issuers and 24 months from issuance for multifamily issuers. Ginnie Mae receives commitment fees as issuers request commitment authority, and recognizes fees as earned when issuers use their commitment authority, with the balance deferred until earned or expired, whichever occurs first. Fees from expired commitment authority are not returned to issuers. As of September 30, 2005, total commitment fees deferred totaled $9.4 million.

Commitment fees realized decreased to $19.4 million in FY 2005 from $29.3 million in FY 2004 because of diminished MBS issuance. Ginnie Mae issued $90.3 billion in commitment authority in FY 2005, a 38.2 percent decrease from FY 2004.

Multiclass Revenue

Multiclass revenue is part of the MBS program revenues, and is composed of REMIC, SMBS, and Platinum

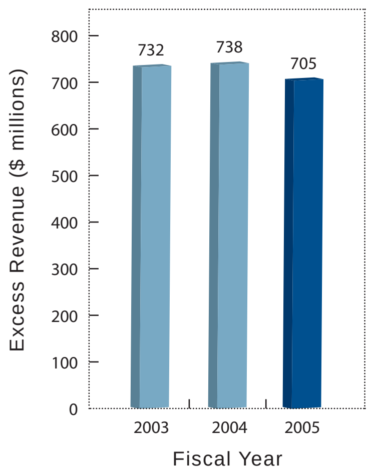
Interest Income

Ginnie Mae invests all of its accumulated revenues over expenses in U.S. Government securities. As Ginnie Mae issuance has decreased over the past two years, interest income has steadily increased as a percentage of revenue. For FY 2005, interest income increased by four percent to $458.8 million from $442.7 million in FY 2004. This increase resulted from higher interest rates in FY 2005 relative to FY 2004 and an increased average amount of treasuries held during FY 2005 compared to FY 2004.

Expenses

Management exercised prudent expense control during FY 2005. Operating expenses decreased by 8.4 percent to $71.3 million from $77.8 million in the prior year. Total expenses were 9.1 percent of total revenues in FY 2005, which was down slightly from 9.5 percent of total revenues in FY 2004. Due to the decline in securities issuance and related income, the decrease in operating expenses was not sufficient to offset the decrease in revenues. This resulted in slightly lower excess revenues over expenses of $705.2 million for FY 2005 versus $737.7 million for FY 2004 (see Figure 13).

Figure 13: Excess of Revenues over Expenses



To support U.S. military personnel called into action, Ginnie Mae reimburses interest to soldiers and sailors who have FHA or VA mortgages in excess of 6 percent. This reimbursement expense was approximately $4.1 million in FY 2005, which represented a substantial decline over FY 2004 related expenses of $11.8 million.

Credit-Related Expenses

Credit-related expenses include Ginnie Mae's Provision for Loss and defaulted issuer portfolio costs. Provision for Loss is charged against income in an amount considered appropriate to maintain reserves for losses at levels that management determines are adequate to absorb potential losses from defaulted issuer portfolios and programs. Based on management's assessment of reserve adequacy, a provision of $10 million was made to the reserve for losses on the single-family MBS program in 2005 due to expected losses from Hurricane Katrina.

Financial Models

Ginnie Mae's Policy and Financial Analysis Model (PFAM) is a comprehensive model that allows Ginnie Mae to evaluate its financial condition in terms of cash flow, capital adequacy, and budget projections. The model does this under an array of economic and financial scenarios modified by policy or programmatic decisions. PFAM incorporates Ginnie Mae's inherent operating risks with modeling that employs economic, financial, and policy variables to generate output that assesses risks and overall performance.

PFAM information provides support to Ginnie Mae management for key financial decisions, such as allocating reserves against future losses. The model also helps Ginnie Mae prepare its budget by estimating the credit subsidy rate for each Ginnie Mae program.

PFAM includes a well-designed, self-documenting database that supports the model and streamlines the process of updating data while reducing turnaround time. Its relational database is a vital feature because it enables expanded reporting capabilities, such as drill-down graphs and charts, and it gives the user meaningful access to the wealth of data available in the model.

In FY 2005, PFAM was used to estimate Ginnie Mae's credit subsidy rate based on historical loan performance data, economic measures, and program and policy assumptions. Changing interest rates, housing values and the preferences of issuers to hold FHA and VA mortgages were accommodated through the ability to adjust assumptions in the "major drivers" feature of PFAM. The cash flow output from PFAM was used to estimate the Net Present Value of Ginnie Mae's future cash flows from the outstanding guaranty portfolio at the end of FY 2005. Additionally, mid-year re-forecasts of cash flows were accomplished to understand the effects of observed changes in new origination volume. The ability to leverage the flexibility of PFAM will be a key driver of future analytics.

Every year Ginnie Mae works with FHA and VA to obtain the most current and comprehensive loan-level data. The data support detailed segmentation of loans according to key risk indicators–including loan type, loan size, loan-to-value ratio, and region–and enable Ginnie Mae to map the current risk profile of the collateral supporting its guaranteed MBS.

Liquidity

Ginnie Mae's primary sources of cash are MBS and Multiclass Guaranty Fee Income, Commitment Fee Income, and Interest Income. After accounting for expenses and other factors, as of September 30, 2005, Ginnie Mae reported Funds with the U.S. Treasury of $3.7 billion, compared with $3.4 billion on September 30, 2004.

In addition to the Funds with the U.S. Treasury, Ginnie Mae's investment in U.S. Government securities was $7.9 billion as of September 30, 2005. Of this amount, $1.3 billion was held in overnight certificates on September 30, 2005. The balance of the portfolio's maturities is spread over time to ensure that Ginnie Mae has a ready source of funds to meet various liquidity needs. Emergency liquidity needs are met through short-term maturities.

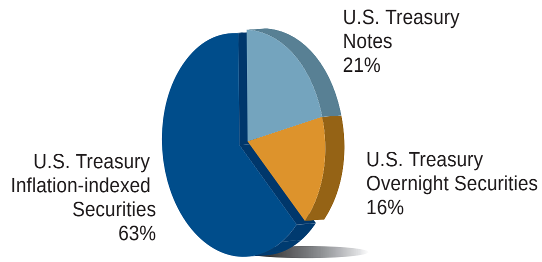
Table 2 describes the fair value composition and maturity of Ginnie Mae's Treasury securities as of September 30, 2004 and September 30, 2005.

Table 2: Composition of Treasury Securities as of September 30 (Percentage of Total)

Maturity	2005	2004
Due within 1 year	25%	27%
Due in 1–5 years	18%	16%
Due in 5–10 years	57%	57%

Figure 14 illustrates the components of Ginnie Mae's investments in U.S. Government securities as of September 30, 2005.

Figure 14: Components of Investment in U.S. Government Securities, Septeber 30, 2005

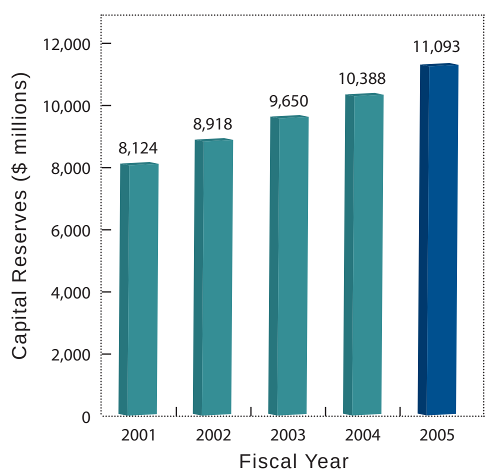


Capital Adequacy

Ginnie Mae's activities involving the guaranty of MBS have historically operated at a profit. Management believes the corporation maintains adequate capital reserves to withstand downturns in the housing market that could cause issuer defaults to increase.

As of September 30, 2005, the Investment of U.S. Government was $11.1 billion after establishing reserves for losses on credit activities, compared with $10.4 billion as of September 30, 2004. Over the past three years, Ginnie Mae has increased its capital adequacy ratio (investment in U.S. Government securities, plus loan loss reserve as a percentage of total assets and RPB) from 1.64 percent to 2.74 percent. To assess the strength of its capital position, Ginnie Mae uses a "stress test" methodology that measures its ability to withstand severe economic conditions. Figure 15 shows Ginnie Mae's capital reserves (Investment of U.S. Government securities) as of September 30, 2005, for the last five years.

Figure 15: Capital Reserves (Investment of U.S. Government Securities)



Risk Management

Ginnie Mae continues to enhance its automated systems and business processes to increase the efficiency of its operations and to reduce its business risk. During FY 2005, Ginnie Mae continued periodic reviews of all master subservicers and major contractors to ensure compliance with the terms and conditions of their contracts with Ginnie Mae. In addition, the audits and reviews enable Ginnie Mae to strengthen its internal controls and minimize risks. Furthermore, as described in Section I above, Ginnie Mae actively monitors its issuers to minimize fraud and default risk, which would negatively impact financial and operating results.

Management Comments on Systems of Internal Controls

Ginnie Mae management maintains and depends on a system of internal administrative and accounting controls that, in the corporation's opinion, provides reasonable assurance that transactions are properly authorized and recorded, permits preparation of financial statements in conformity with generally accepted accounting principles, and ensures that Ginnie Mae's assets are safeguarded. The system of internal and accounting controls includes policies and procedures for the execution, documentation, and recording of transactions, and an organizational structure that provides for effective segregation of duties and responsibilities. Ginnie Mae management believes that this internal assessment meets the intent of the U.S. Office of Management and Budget (OMB) internal control review requirements outlined in OMB Circular A-123, Management Accountability and Control, and OMB Circular A-127, Financial Management Systems. In addition, management believes that Ginnie Mae complies with the reasonable assurance standards of Sections 2 and 4 of the Federal Managers' Financial Integrity Act of 1982.