MGIC INVESTMENT CORP
Form 10-K
March 02, 2009

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FORM 10-K
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2008

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

Commission file number 1-10816

MGIC INVESTMENT CORPORATION

(Exact name of registrant as specified in its charter)

WISCONSIN	**39-1486475**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
MGIC PLAZA, 250 EAST KILBOURN AVENUE, MILWAUKEE, WISCONSIN	**53202**
(Address of principal executive offices)	(Zip Code)

(414) 347-6480

(Registrant s telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class:	Common Stock, Par Value $1 Per Share Common Share Purchase Rights
Name of Each Exchange on Which Registered:	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:

Title of Class:	None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ Noo

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). o Yes þ No
State the aggregate market value of the voting stock held by non-affiliates of the Registrant as of June 30, 2008: Approximately $756 million*
* Solely for purposes of computing such value and without thereby admitting that such persons are affiliates of the Registrant, shares held by directors and executive officers of the Registrant are deemed to be held by affiliates of the Registrant. Shares held are those shares beneficially owned for purposes of Rule 13d-3 under the Securities Exchange Act of 1934 but excluding shares subject to stock options.
Indicate the number of shares outstanding of each of the Registrant s classes of common stock as of February 25, 2009: 124,951,497
The following documents have been incorporated by reference in this Form 10-K, as indicated:

Document	Part and Item Number of Form 10-K Into Which Incorporated*
Proxy Statement for the 2009 Annual Meeting of Shareholders	Items 10 through 14 of Part III

* In each case, to the extent provided in the Items listed

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PART I

Item 1. Business.

A. General

We are a holding company, and through our wholly owned subsidiary Mortgage Guaranty Insurance Corporation (MGIC) we are the leading provider of private mortgage insurance in the United States. In 2008, our net premiums written exceeded $1.4 billion and our new insurance written was $48.2 billion. As of December 31, 2008, our insurance in force was $227.0 billion and our risk in force was $59.0 billion. For further information about our results of operations, see our consolidated financial statements in Item 8. MGIC is licensed in all 50 states of the United States, the District of Columbia, Puerto Rico and Guam. In addition to mortgage insurance on first liens, we, through our subsidiaries, provide lenders with various underwriting and other services and products related to home mortgage lending.

Overview of the Private Mortgage Insurance Industry

The private mortgage insurance industry was established in 1957 to provide a private market alternative to federal government insurance programs. Private mortgage insurance covers losses from homeowner defaults on residential first mortgage loans, reducing and, in some instances, eliminating the loss to the insured institution if the homeowner defaults. Private mortgage insurance plays an important role in the housing finance system by expanding home ownership opportunities through helping people purchase homes with less than 20% down payments, especially first time homebuyers. In this annual report, we refer to loans with less than 20% down payments as low down payment mortgages or loans. During 2007 and 2008 more than $550 billion of mortgages were insured by private mortgage insurance companies, allowing approximately 4 million borrowers to access low down payment loans. Private mortgage insurance facilitates the sale of low down payment mortgages in the secondary mortgage market to the Federal National Mortgage Association, commonly known as Fannie Mae, and the Federal Home Loan Mortgage Corporation, commonly known as Freddie Mac. In this annual report, we refer to Fannie Mae and Freddie Mac collectively as the GSEs. The GSEs purchase residential mortgages from mortgage lenders and investors as part of their governmental mandate to provide liquidity in the secondary mortgage market and we believe that the GSEs purchased over 50% of the mortgages underlying our flow new insurance written during the last five years. As a result, the private mortgage insurance industry in the U.S. is defined in part by the requirements and practices of the GSEs. These requirements and practices, as well as those of the federal regulators that oversee the GSEs and lenders, impact the operating results and financial performance of companies in the mortgage insurance industry. Private mortgage insurance also reduces the regulatory capital that depository institutions are required to hold against low down payment mortgages.

The U.S. single-family residential mortgage market has historically experienced long-term growth, including an increase in mortgage debt outstanding every year between 1985, when our company began operations, and 2007. The rate of growth in U.S. residential mortgage debt was particularly strong from 2001 through 2006. In 2007, this growth rate began slowing and we believe that U.S. residential mortgage debt outstanding decreased in 2008. During the last several years of this period of increased growth and continuing through 2007, the mortgage lending industry increasingly made home loans at higher loan-to-value ratios, to individuals with higher risk credit profiles and based on less documentation and verification of information provided by the borrower. Beginning in 2007, job creation slowed and the housing markets began slowing in certain areas, with declines in certain other areas. In 2008, payroll employment in the U.S. decreased substantially and almost all areas experienced home price declines. Together, these conditions resulted in significant adverse developments for us and our industry. After earning an average of approximately $580 million annually from 2004 through 2006 and earnings of $169 million in the first half of 2007, we had net losses of $1.670 billion for full-year 2007 and $518.9 million for 2008. During 2008, the insurer financial strength rating of MGIC was downgraded a number of times by all three rating agencies. See the risk factor titled Our financial strength rating has been downgraded below Aa3/AA-, which could reduce the volume of our new business writings in Item 1A. Beginning in late 2007 and continuing through 2008, we made significant underwriting changes that limited the types of loans that we will insure in an effort to improve the risk profile of our new business.

Due to the changing environment described above and the credit crisis that began in the third quarter of 2008, at this time we are facing two particularly significant challenges, which we believe are shared by the other participants in our industry:

- Whether we will have access to sufficient capital to continue to write new business. For additional information about this challenge, see Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Capital in Item 7.

- Whether private mortgage insurance will remain a significant credit enhancement alternative for low down payment single-family mortgages. For additional information about this challenge, see Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Future of the Domestic Residential Housing Finance System in Item 7.

General Information About Our Company

We are a Wisconsin corporation. Our principal office is located at MGIC Plaza, 250 East Kilbourn Avenue, Milwaukee, Wisconsin 53202 (telephone number (414) 347-6480).

Historically, our investments in joint ventures and related loss or income from joint ventures principally consisted of our investment and related earnings in two less than majority owned joint ventures, Credit-Based Asset Servicing and Securitization LLC, C-BASS, and Sherman Financial Group LLC, Sherman. In 2007, joint venture losses included an impairment charge equal to our entire equity interest in C-BASS, as well as equity losses incurred by C-BASS in the fourth quarter that reduced the carrying value of our $50 million note from C-BASS to zero. As a result, beginning in 2008, our joint venture income principally consisted of income from Sherman. In August of 2008, we sold our entire interest in Sherman to Sherman. Beginning in the fourth quarter of 2008, our results of operations are no longer affected by any joint venture results.

As used in this annual report, we, us and our refer to MGIC Investment Corporation s consolidated operations. Sherman, C-BASS and our other less than majority-owned joint ventures and investments are not consolidated with us for financial reporting purposes, are not our subsidiaries and are not included in the terms we, us and our. The description of our business in this document generally does not apply to our Australian operations, which are immaterial. For information about our Australian operations, see Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Australia in Item 7.

Our revenues and losses may be materially affected by the risk factors applicable to us that are included in Item 1A of this annual report. These risk factors are an integral part of this annual report. These factors may also cause actual results to differ materially from the results contemplated by forward looking statements that we may make. We are not undertaking any obligation to update any forward looking statements or other statements we may make even though these statements may be affected by events or circumstances occurring after the forward looking statements or other statements were made. No investor should rely on the fact that such statements are current at any time other than the time at which this annual report was filed with the Securities and Exchange Commission.

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B. The MGIC Book

In our industry, a book is a group of loans that a mortgage insurer insures in a particular period, normally a calendar year. We refer to the insurance that has been written by MGIC as the MGIC Book.

Types of Product

In general, there are two principal types of private mortgage insurance: primary and pool. We are currently not issuing new commitments for pool insurance and expect that the volume of any future pool business will be insignificant to us.

Primary Insurance. Primary insurance provides mortgage default protection on individual loans and covers unpaid loan principal, delinquent interest and certain expenses associated with the default and subsequent foreclosure (collectively, the claim amount). For the effect of bankruptcy cramdowns on the claim amount, see Exposure to Catastrophic Loss; Defaults; Claims; Loss Mitigation Claims below. In addition to the loan principal, the claim amount is affected by the mortgage note rate and the time necessary to complete the foreclosure process. The insurer generally pays the coverage percentage of the claim amount specified in the primary policy, but has the option to pay 100% of the claim amount and acquire title to the property. Primary insurance is generally written on first mortgage loans secured by owner occupied single-family homes, which are one-to-four family homes and condominiums. Primary insurance is also written on first liens secured by non-owner occupied single-family homes, which are referred to in the home mortgage lending industry as investor loans, and on vacation or second homes. Primary coverage can be used on any type of residential mortgage loan instrument approved by the mortgage insurer.

References in this document to amounts of insurance written or in force, risk written or in force and other historical data related to our insurance refer only to direct (before giving effect to reinsurance) primary insurance, unless otherwise indicated. References in this document to primary insurance include insurance written in bulk transactions that is supplemental to mortgage insurance written in connection with the origination of the loan or that reduces a lender s credit risk to less than 51% of the value of the property. For more than the past five years, reports by private mortgage insurers to the trade association for the private mortgage insurance industry have classified mortgage insurance that is supplemental to other mortgage insurance or that reduces a lender s credit risk to less than 51% of the value of the property as pool insurance. The trade association classification is used by members of the private mortgage insurance industry in reports to Inside Mortgage Finance, a mortgage industry publication that computes and publishes primary market share information.

Primary insurance may be written on a flow basis, in which loans are insured in individual, loan-by-loan transactions, or may be written on a bulk basis, in which each loan in a portfolio of loans is individually insured in a single, bulk transaction. New insurance written on a flow basis was $46.6 billion in 2008 compared to $69.0 billion in 2007 and $39.3 billion in 2006. New insurance written for bulk transactions was $1.6 billion for 2008 compared to $7.8 billion in 2007 and $18.9 billion for 2006. As noted in - Bulk Transactions below, in the fourth quarter of 2007, we decided to stop writing the portion of our bulk business that insures mortgage loans included in home equity (or private label) securitizations, which are the terms the market uses to refer to securitizations sponsored by firms besides the GSEs or Ginnie Mae, such as Wall Street investment banks. We refer to portfolios of loans we insured through the bulk channel that we knew would serve as collateral in a home equity securitization as Wall Street bulk transactions. While we will continue to insure loans on a bulk basis when we believe that the loans will be sold to a GSE or retained by the lender, we expect the volume of any future business written through the bulk channel will be insignificant to us.

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The following table shows, on a direct basis, primary insurance in force (the unpaid principal balance of insured loans as reflected in our records) and primary risk in force (the coverage percentage applied to the unpaid principal balance) for the MGIC Book as of the dates indicated:

Primary Insurance and Risk In Force

	December 31,				
	2008	2007	2006	2005	2004
			(In millions)		
Direct Primary Insurance In Force	$226,955	$211,745	$176,531	$170,029	$177,091
Direct Primary Risk In Force	$ 58,981	$ 55,794	$ 47,079	$ 44,860	$ 45,981

For loans sold to Fannie Mae or Freddie Mac, the coverage percentage must comply with the requirements established by the particular GSE to which the loan is delivered. For other loans, the lender determines the coverage percentage we provide, from the coverage percentages that we offer.

We charge higher premium rates for higher coverage percentages. Higher coverage percentages generally result in increased severity, which is the amount paid on a claim, and lower coverage percentages generally result in decreased severity. In accordance with GAAP for the mortgage insurance industry, reserves for losses are only established for loans in default. Because, historically, relatively few defaults typically occur in the early years of a book of business, the higher premium revenue from deeper coverage has historically been generally recognized before any significant higher losses resulting from that deeper coverage may be incurred. See - Exposure to Catastrophic Loss; Defaults; Claims; Loss Mitigation - Claims. Our premium pricing methodology generally targets substantially similar returns on capital regardless of the depth of coverage. However, there can be no assurance that changes in the level of premium rates adequately reflect the risks associated with changes in the depth of coverage.

In recent years the GSEs, with mortgage insurers, have offered programs under which, on delivery of an insured loan to a GSE, the primary coverage was restructured to an initial shallow tier of coverage followed by a second tier that was subject to an overall loss limit, and compensation may have been paid to the GSE reflecting services or other benefits realized by the mortgage insurer from the coverage conversion. Lenders receive guaranty fee relief from the GSEs on mortgages delivered with these restructured coverage percentages. We believe that the GSEs ceased offering these programs in 2008, though we continue to insure loans subject to these programs.

In general, mortgage insurance coverage cannot be terminated by the insurer. However, a mortgage insurer may terminate or rescind coverage for, among other reasons, non-payment of premium and in the case of certain material misrepresentations made in connection with the issuance of the insurance policy. See Exposure to Catastrophic Loss; Defaults; Claims; Loss Mitigation Loss Mitigation. Mortgage insurance coverage is renewable at the option of the insured lender, at the renewal rate fixed when the loan was initially insured. Lenders may cancel insurance written on a flow basis at any time at their option or because of mortgage repayment, which may be accelerated because of the refinancing of mortgages. In the case of a loan purchased by Freddie Mac or Fannie Mae, a borrower meeting certain conditions may require the mortgage servicer to cancel insurance upon the borrower s request when the principal balance of the loan is 80% or less of the home s current value.

Under the federal Homeowners Protection Act, or HPA, a borrower has the right to stop paying premiums for private mortgage insurance on loans closed after July 28, 1999 secured by a property comprised of one dwelling unit that is the borrower s primary residence when certain loan-to-value ratio thresholds determined by the value of the home at loan origination and other requirements are met. Generally, the loan-to-value ratios used in this annual report represent the ratio, expressed as a percentage, of the dollar amount of the first mortgage loan to the value of the property at the time the loan became insured and do not reflect subsequent housing price appreciation or depreciation. In general, under the HPA a borrower may stop making mortgage insurance payments when the loan-to-value ratio is scheduled to reach 80% (based on the loan s amortization schedule) or actually reaches 80% if the borrower so requests and if certain requirements relating to the borrower s payment history, the absence of junior liens and a decline in the property s value since origination are satisfied. In addition, a borrower s obligation to make payments for private mortgage insurance generally terminates regardless of whether a borrower so requests when the loan-to-value ratio (based on the loan s amortization schedule) reaches 78% of the unpaid principal balance of the mortgage and the borrower is or later becomes current in his mortgage payments. A borrower s right to stop paying for private mortgage insurance applies only to borrower paid mortgage insurance. The HPA requires that lenders give borrowers certain notices with regard to the cancellation of private mortgage insurance.

In addition, some states require that mortgage servicers periodically notify borrowers of the circumstances in which they may request a mortgage servicer to cancel private mortgage insurance and some states allow the borrower to require the mortgage servicer to cancel private mortgage insurance under certain circumstances or require the mortgage servicer to cancel private mortgage insurance automatically in certain circumstances.

Coverage tends to continue in areas experiencing economic contraction and housing price depreciation. The persistency of coverage in these areas coupled with cancellation of coverage in areas experiencing economic expansion and housing price appreciation can increase the percentage of an insurer s portfolio comprised of loans in economically weak areas. This development can also occur during periods of heavy mortgage refinancing because refinanced loans in areas of economic expansion experiencing property value appreciation are less likely to require mortgage insurance at the time of refinancing, while refinanced loans in economically weak areas not experiencing property value appreciation are more likely to require mortgage insurance at the time of refinancing or not qualify for refinancing at all and, thus, remain subject to the mortgage insurance coverage.

The percentage of primary risk written with respect to loans representing refinances was 21.9% in 2008 compared to 23.2% in 2007 and 32.0% in 2006. When a borrower refinances a mortgage loan insured by us by paying it off in full with the proceeds of a new mortgage that is also insured by us, the insurance on that existing mortgage is cancelled, and insurance on the new mortgage is considered to be new primary insurance written. Therefore, continuation of our coverage from a refinanced loan to a new loan results in both a cancellation of insurance and new insurance written. When a lender and borrower modify a loan rather than replace it with a new one, or enters into a new loan pursuant to a loan modification program, our insurance continues without being cancelled, assuming that we consent to the modification or new loan.

In addition to varying with the coverage percentage, our premium rates for insurance vary depending upon the perceived risk of a claim on the insured loan and, thus, take into account, among other things, the loan-to-value ratio, whether the loan is a fixed payment loan or a non-fixed payment loan (a non-fixed payment loan is referred to in the home mortgage lending industry as an adjustable rate mortgage or ARM), the mortgage term, whether the loan finances a home in a market we categorize as higher risk, whether the property is the borrower s primary residence and, for A-, subprime loans and certain other loans, the location of the borrower s credit score within a range of credit scores. In general, in this annual report we classify as A- loans that have FICO credit scores between 575 and 619 and we classify as subprime loans that have FICO credit scores of less than 575. However, in this annual report we classify loans without complete documentation as reduced documentation loans regardless of FICO credit score rather than as prime, A- or subprime loans, although as discussed in footnote 3 to the table titled Default Statistics for the MGIC Book in Exposure to Catastrophic Loss; Defaults; Claims; Loss Mitigation Defaults below, certain doc waiver GSE loans are included as full doc loans by us.

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A FICO credit score is a score based on a borrower s credit history generated by a model developed by Fair Isaac and Company.

Premium rates cannot be changed after the issuance of coverage. Because we believe that over the long term each region of the United States is subject to similar factors affecting risk of loss on insurance written, we generally utilize a nationally based, rather than a regional or local, premium rate policy for insurance written through the flow channel. However, beginning in 2008, changes in our underwriting guidelines implemented more restrictive standards in markets and for loan characteristics that we categorize as higher risk.

The borrower s mortgage loan instrument may require the borrower to pay the mortgage insurance premium. Our industry refers to loans having this requirement as borrower paid. If the borrower is not required to pay the premium, then the premium is paid by the lender, who may recover the premium through an increase in the note rate on the mortgage or higher origination fees. Our industry refers to loans in which the premium is paid by the lender as lender paid. Most of our primary insurance in force and new insurance written, other than through bulk transactions, is borrower paid mortgage insurance. New insurance written through bulk transactions is generally paid by the securitization vehicles or investors that hold the mortgages, and the mortgage note rate generally does not reflect the premium for the mortgage insurance. In February 2008, Freddie Mac and Fannie Mae informed us and the rest of our industry that they were reviewing the appropriateness of all mortgage insurers lender-paid insurance premium rates. We have not received subsequent updates regarding the status of these reviews.

Under the monthly premium plan, the borrower or lender pays us a monthly premium payment to provide only one month of coverage, rather than one year of coverage provided by the annual premium plan. Under the annual premium plan, the initial premium is paid to us in advance, and we earn and recognize the premium over the next twelve months of coverage, with annual renewal premiums paid in advance thereafter and earned over the subsequent twelve months of coverage. The annual premiums can be paid with either a higher premium rate for the initial year of coverage and lower premium rates for the renewal years, or with premium rates which are equal for the initial year and subsequent renewal years. Under the single premium plan, the borrower or lender pays us a single payment covering a specified term exceeding twelve months.

During each of the last three years, the monthly premium plan represented more than 85% of our new insurance written. The annual and single premium plans represented the remaining new insurance written.

Pool Insurance. Pool insurance is generally used as an additional credit enhancement for certain secondary market mortgage transactions. Pool insurance generally covers the loss on a defaulted mortgage loan which exceeds the claim payment under the primary coverage, if primary insurance is required on that mortgage loan, as well as the total loss on a defaulted mortgage loan which did not require primary insurance. Pool insurance usually has a stated aggregate loss limit and may also have a deductible under which no losses are paid by the insurer until losses exceed the deductible.

We are currently not issuing new commitments for pool insurance and expect that the volume of any future pool business will be insignificant to us. New pool risk written was $145 million in 2008 compared to $211 million in 2007 and $240 million in 2006. New pool risk written during 2006 and 2007 was primarily comprised of risk associated with loans delivered to the GSEs (agency pool insurance), loans insured through private label securitizations, loans delivered to the Federal Home Loan Banks under their mortgage purchase programs and loans made under state housing finance programs. New pool risk written during 2008 was primarily comprised of risk associated with agency pool insurance and loans made under state housing finance programs. Direct pool risk in force at December

31, 2008 was $1.9 billion compared to $2.8 billion and $3.1 billion at December 31, 2007 and 2006, respectively. The risk amounts referred to above represent pools of loans with contractual aggregate loss limits and in some cases those without these limits. For pools of loans without these limits, risk is estimated based on the amount that would credit enhance these loans to a AA level based on a rating agency model. Under this model, at December 31, 2008, 2007 and 2006 for $2.5 billion, $4.1 billion, and $4.4 billion, respectively, of risk without these limits, risk in force is calculated at $150 million, $475 million, and $473 million, respectively. New risk written, under this model, for the years ended December 31, 2008, 2007 and 2006 was $1 million, $2 million and $4 million, respectively.

The settlement of a nationwide class action alleging that MGIC violated the Real Estate Settlement Procedures Act, or RESPA, by providing agency pool insurance and entering into other transactions with lenders that were not properly priced became final in October 2003. In a February 1, 1999 circular addressed to all mortgage guaranty insurers licensed in New York, the New York Department of Insurance advised that significantly underpriced agency pool insurance would violate the provisions of New York insurance law that prohibit mortgage guaranty insurers from providing lenders with inducements to obtain mortgage guaranty business. In a January 31, 2000 letter addressed to all mortgage guaranty insurers licensed in Illinois, the Illinois Department of Insurance advised that providing pool insurance at a discounted or below market premium in return for the referral of primary mortgage insurance would violate Illinois law.

In February 2008, Freddie Mac and Fannie Mae informed us and the rest of our industry that they were reviewing the appropriateness of all mortgage insurers criteria and underwriting requirements for pool insurance on mortgages to the extent that they do not meet such insurer s published underwriting guidelines. We have not received subsequent updates regarding the status of these reviews.

Risk Sharing Arrangements. We have participated in risk sharing arrangements with the GSEs and captive reinsurance arrangements with subsidiaries of certain mortgage lenders that reinsure a portion of the risk on loans originated or serviced by the lenders which have MGIC primary insurance.

In a February 1, 1999 circular addressed to all mortgage insurers licensed in New York, the New York Department of Insurance said that it was in the process of developing guidelines that would articulate the parameters under which captive mortgage reinsurance is permissible under New York insurance law. These guidelines, which were to ensure that the reinsurance constituted a legitimate transfer of risk and were fair and equitable to the parties, have not been issued. As discussed under We are subject to the risk of private litigation and regulatory proceedings in Item 1A, we provided information regarding captive mortgage reinsurance arrangements to the New York Department of Insurance and the Minnesota Department of Commerce. The complaint in the RESPA litigation described in - Pool Insurance alleged that MGIC pays inflated captive reinsurance premiums in violation of RESPA. Since December 2006, class action litigation was separately brought against a number of large lenders alleging that their captive mortgage reinsurance arrangements violated RESPA. We are not a defendant in any of these cases and we believe no other mortgage insurer is a defendant.

In addition, we participate in risk sharing arrangements with persons unrelated to our customers. When we reinsure a portion of our risk through such a reinsurer, we make an upfront payment or cede a portion of our premiums in return for a reinsurer agreeing to indemnify us for its share of losses incurred. Although reinsuring against possible loan losses does not discharge us from liability to a policyholder, it can reduce the amount of capital we are required to retain against potential future losses for rating agency and insurance regulatory purposes.

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For further information about risk sharing arrangements, see Management s Discussion and Analysis Results of Consolidated Operations Risk Sharing Arrangements in Item 7 and Note 9 to our consolidated financial statements in Item 8.

Bulk Transactions. In bulk transactions, the individual loans in the insured portfolio are generally insured to specified levels of coverage. The premium in a bulk transaction, which is negotiated with the securitizer or other owner of the loans, is based on the mortgage insurer s evaluation of the overall risk of the insured loans included in the transaction and is often a composite rate applied to all of the loans in the transaction.

In the fourth quarter of 2007, we decided to stop writing the portion of our bulk business insuring loans included in Wall Street bulk transactions. These securitizations represented approximately 41% and 66% of our new insurance written for bulk transactions during 2007 and 2006, respectively, and 10% of our risk in force, or 74% of our bulk risk in force, at December 31, 2008. New insurance written for bulk transactions was $1.6 billion during 2008, all of which were eligible for delivery to the GSEs, compared to $7.8 billion for 2007 and $18.9 billion for 2006. We wrote no new business through the bulk channel during the second half of 2008. We expect the volume of any future business written through the bulk channel will be insignificant to us. In general, the loans insured by us in Wall Street bulk transactions consisted of loans with reduced underwriting documentation; cash out refinances that exceed the standard underwriting requirements of the GSEs; A- loans; subprime loans; and jumbo loans. A jumbo loan has an unpaid principal balance that exceeds the conforming loan limit. The conforming loan limit is the maximum unpaid principal amount of a mortgage loan that can be purchased by the GSEs. The conforming loan limit is subject to annual adjustment, and for mortgages covering a home with one dwelling unit was $417,000 for 2006, 2007 and early 2008; this amount was temporarily increased to up to $729,500 in the most costly communities in early 2008. For additional information about new insurance written through the bulk channel, see Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Consolidated Operations Bulk Transactions in Item 7.

Customers

Originators of residential mortgage loans such as savings institutions, commercial banks, mortgage brokers, credit unions, mortgage bankers and other lenders have historically determined the placement of mortgage insurance written on a flow basis and as a result are our customers. To obtain primary insurance from us written on a flow basis, a mortgage lender must first apply for and receive a mortgage guaranty master policy from us. In 2008, we issued coverage on mortgage loans for more than 3,300 of our master policyholders. Our top 10 customers, none of whom represented more than 10% of our consolidated revenues, generated 40.3% of our new insurance written on a flow basis in 2008, compared to 43.0% in 2007 and 34.2% in 2006.

When writing insurance for Wall Street bulk transactions, we historically dealt primarily with securitizers of the loans or other owners of the loans, who considered whether credit enhancement provided through the structure of the securitization would eliminate or reduce the need for mortgage insurance.

Sales and Marketing and Competition

Sales and Marketing. We sell our insurance products through our own employees, located throughout all regions of the United States, Puerto Rico and Guam.

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Competition. Our competition includes other mortgage insurers, governmental agencies and products designed to eliminate the need to purchase private mortgage insurance. For flow business, we and other private mortgage insurers compete directly with federal and state governmental and quasi-governmental agencies, principally the FHA and, to a lesser degree, the Veterans Administration. These agencies sponsor government-backed mortgage insurance programs, which during 2008 accounted for approximately 60.3%, of the total low down payment residential mortgages which were subject to governmental or private mortgage insurance, a substantial increase from approximately 22.7% in both 2007 and 2006, according to statistics reported by Inside Mortgage Finance. We believe the FHA, which in recent years was not viewed by us as a significant competitor, accounted for the overwhelming majority of this increase in 2008.

Loans insured by the FHA cannot exceed maximum principal amounts which are determined by a percentage of the conforming loan limit. For loans originated in the first half of 2007, the maximum FHA loan amount for homes with one dwelling unit in high cost areas was as high as $362,790; this amount was temporarily increased to up to $729,750 in the most costly areas for loans originated in the second half of 2007 or during 2008. For loans originated in 2009, this limit was lowered to $721,050 in Alaska and Hawaii and $625,500 in other states. Loans insured by the Veteran s Administration do not have mandated maximum principal amounts but have maximum limits on the amount of the guaranty provided by the Veteran s Administration to the lender. For loans closed on or after December 10, 2004, the maximum Veteran s Administration guaranty is $156,375 in Alaska and Hawaii and $104,250 in other states.

In addition to competition from the FHA and the Veteran s Administration, we and other private mortgage insurers face competition from state-supported mortgage insurance funds in several states, including California and New York. From time to time, other state legislatures and agencies consider expanding the authority of their state governments to insure residential mortgages.

Private mortgage insurers are also subject to competition from the GSEs to the extent that they are compensated for assuming default risk that would otherwise be insured by the private mortgage insurance industry. See Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Future of the Domestic Residential Housing Finance System for a discussion about the risk that private mortgage insurance will not remain a significant credit enhancement for low down payment single-family mortgages and Changes in the business practices of Fannie Mae and Freddie Mac could reduce our revenues or increase our losses in Item 1A for a discussion of how potential changes in the GSEs business practices could affect us.

The capital markets and their participants have historically competed with mortgage insurers by offering alternative products and services and may further develop as competitors to private mortgage insurers in ways we cannot predict. Competition from such alternative products and services was substantial prior to 2007 but declined materially in late 2007 and their presence was insignificant in 2008.

Prior to 2008, we and other mortgage insurers also competed with transactions structured to avoid mortgage insurance on low down payment mortgage loans. These transactions include self-insuring, and 80-10-10 and similar loans (generally referred to as piggyback loans), which are loans comprised of both a first and a second mortgage (for example, an 80% loan-to-value ratio first mortgage and a 10% loan-to-value ratio second mortgage), with the loan-to-value ratio of the first mortgage below what investors require for mortgage insurance, compared to a loan in which the first mortgage covers the entire borrowed amount (which in the preceding example would be a 90% loan-to-value ratio mortgage). Competition from piggyback structures was substantial prior to 2007 but declined materially later in 2007 and declined further in 2008.

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The U.S. private mortgage insurance industry currently consists of seven active mortgage insurers and their affiliates; one of the seven is a joint venture in which another mortgage insurer participates and another is, according to filings with the Securities and Exchange Commission as of February 20, 2009, our largest shareholder. The names of these mortgage insurers are listed under Competition or changes in our relationships with our customers could reduce our revenues or increase our losses in Item 1A. In 2008, a mortgage insurer ceased writing new insurance and placed its existing book of business in run-off. According to Inside Mortgage Finance, which obtains its data from reports provided by us and other mortgage insurers that are to be prepared on the same basis as the reports by insurers to the trade association for the private mortgage insurance industry, for more than ten years, we have been the largest private mortgage insurer based on new primary insurance written, with a market share of 24.5% in 2008, 21.3% in 2007, 21.6% in 2006, 22.9% in 2005 and 23.5% in 2004, and at December 31, 2008, we also had the largest book of direct primary insurance in force. For more than five years, these reports do not include as primary mortgage insurance insurance on certain loans classified by us as primary insurance, such as loans insured through bulk transactions that already had mortgage insurance placed on the loans at origination.

The private mortgage insurance industry is highly competitive. We believe that we currently compete with other private mortgage insurers based on customer relationships, name recognition, reputation, the ancillary products and services provided to lenders (including contract underwriting services), the strength of management teams and field organizations, the depths of databases covering insured loans and the effective use of technology and innovation in the delivery and servicing of insurance products. Several private mortgage insurers compete based on the types of captive mortgage reinsurance that they offer. Historically, the industry has competed for business written through the flow channel principally on the basis of programs involving captive mortgage reinsurance, agency pool insurance, and other similar structures involving lenders; the provision of contract underwriting and related fee-based services to lenders; financial strength as it is perceived by persons making or influencing the selection of a mortgage insurer; the provision of other products and services that meet lender needs for risk management, affordable housing, loss mitigation, capital markets and training support; and the effective use of technology and innovation in the delivery and servicing of insurance products. We believe competition for Wall Street bulk business was based principally on the premium rate and the portion of loans submitted for insurance that the insurers were willing to insure.

The complaint in the RESPA litigation described in - Pool Insurance alleged, among other things, that captive mortgage reinsurance, agency pool insurance, and contract underwriting we provided violated RESPA.

Certain private mortgage insurers compete for flow business by offering lower premium rates than other companies, including us, either in general or with respect to particular customers or classes of business. On a case-by-case basis, we will adjust premium rates, generally depending on the risk characteristics, loss performance or class of business of the loans to be insured, or the costs associated with doing such business.

The mortgage insurance industry historically viewed a financial strength rating of Aa3/AA- as critical to writing new business. At the time that this annual report was finalized, the financial strength of MGIC, our principal mortgage insurance subsidiary, was rated Ba2 by Moody s Investors Service and the outlook for this rating was considered, by Moody s, to be developing; Standard & Poor s Rating Services insurer financial strength rating of MGIC was A- with a negative outlook; and the financial strength of MGIC was rated A- by Fitch Ratings with a negative outlook. MGIC could be further downgraded by one or more of these rating agencies.

For further information about the importance of our ratings, see the risk factor titled Our financial strength rating has been downgraded below Aa3/AA-, which could reduce the volume of our new business writings in Item 1A. In assigning financial strength ratings, in addition to considering the adequacy of the mortgage insurer s capital to withstand very high claim scenarios under assumptions determined by the rating agency, we believe rating agencies review a mortgage insurer s historical and projected operating performance, franchise risk, business outlook, competitive position, management, corporate strategy, and other factors. The rating agency issuing the financial strength rating can withdraw or change its rating at any time.

Contract Underwriting and Related Services

We perform contract underwriting services for lenders in which we judge whether the data relating to the borrower and the loan contained in the lender s mortgage loan application file comply with the lender s loan underwriting guidelines. We also provide an interface to submit data to the automated underwriting systems of the GSEs, which independently judge the data. These services are provided for loans that require private mortgage insurance as well as for loans that do not require private mortgage insurance. A material portion of our new insurance written through the flow channel in recent years involved loans for which we provided contract underwriting services. The complaint in the RESPA litigation described in - Pool Insurance alleged, among other things, that the pricing of contract underwriting provided by us violated RESPA.

Under our contract underwriting agreements, we may be required to provide certain remedies to our customers if certain standards relating to the quality of our underwriting work are not met. The cost of remedies provided by us to customers for failing to meet these standards has not been material to our financial position or results of operations for the years ended December 31, 2008, 2007 and 2006. However, a generally positive economic environment for residential real estate that continued through a portion of 2007 may have mitigated the effect of some of these costs, the claims for which may lag, by as much as several years, deterioration in the economic environment for residential real estate. There can be no assurance that contract underwriting remedies will not be material in the future.

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In February 2008, Freddie Mac and Fannie Mae informed us and the rest of our industry that they were reviewing all mortgage insurers business justifications for activities, such as contract underwriting services, that have the potential for creating non-insurance related contingent liabilities. We have not received subsequent updates regarding the status of these reviews.

Risk Management

We believe that mortgage credit risk is materially affected by:

- the borrower s credit strength, including the borrower s credit history, debt-to-income ratios, and cash reserves and the willingness of a borrower with sufficient resources to make mortgage payments to do so when the mortgage balance exceeds the value of the home;
- the loan product, which encompasses the loan-to-value ratio, the type of loan instrument, including whether the instrument provides for fixed or variable payments and the amortization schedule, the type of property and the purpose of the loan;
- origination practices of lenders and the percentage of coverage on insured loans;
- the size of loans insured; and
- the condition of the economy, including housing values and employment, in the area in which the property is located.

We believe that, excluding other factors, claim incidence increases:

- for loans with lower FICO credit scores compared to loans with higher FICO credit scores;
- for loans with less than full underwriting documentation compared to loans with full underwriting documentation;
- during periods of economic contraction and housing price depreciation, including when these conditions may not be nationwide, compared to periods of economic expansion and housing price appreciation;
- for loans with higher loan-to-value ratios compared to loans with lower loan-to-value ratios;
- for ARMs when the reset interest rate significantly exceeds the interest rate at loan origination;
- for loans that permit the deferral of principal amortization compared to loans that require principal amortization with each monthly payment;
- for loans in which the original loan amount exceeds the conforming loan limit compared to loans below that limit; and
- for cash out refinance loans compared to rate and term refinance loans.

Other types of loan characteristics relating to the individual loan or borrower may also affect the risk potential for a loan. The presence of a number of higher-risk characteristics in a loan materially increases the likelihood of a claim on such a loan unless there are other characteristics to lower the risk.

We charge higher premium rates to reflect the increased risk of claim incidence that we perceive is associated with a loan, although not all higher risk characteristics are reflected in the premium rate. There can be no assurance that our premium rates adequately reflect the increased risk, particularly in a period of economic recession, slowing home price appreciation or housing price declines. For additional information, see our risk factors in Item 1A, including the one titled The premiums we charge may not be adequate to compensate us for our liabilities for losses and as a result any inadequacy could materially affect our financial condition and results of operations.

In 2008, we made significant underwriting changes that limited the types of loans that we will insure. For information about these changes, see Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Consolidated Operations New insurance written in Item 7.

Delegated Underwriting and GSE Automated Underwriting Approvals. Delegated underwriting is a program under which approved lenders are allowed to commit us to insure loans originated through the flow channel. Until January 2007, lenders were able to commit us to insure loans utilizing only their own underwriting guidelines and underwriting evaluation. In addition, from 2000 through January 2007, loans approved by the automated underwriting services of the GSEs were automatically approved for MGIC mortgage insurance. As a result, during this period, a substantial majority of the loans insured by us through the flow channel were approved as a result of loan approvals by the automated underwriting services of the GSEs or through delegated underwriting programs, including those utilizing lenders proprietary underwriting services. Beginning in 2007, loans that did not meet our underwriting guidelines would not automatically be insured by us even though the loans were approved by the underwriting services described above. As a result, our delegated underwriting program began requiring lenders to commit us to insure only loans that complied with our underwriting guidelines.

Exposure to Catastrophic Loss; Defaults; Claims; Loss Mitigation

Exposure to Catastrophic Loss. The private mortgage insurance industry has from time to time experienced catastrophic loss similar to the losses currently being experienced. Prior to the current cycle of such losses, the last time that private mortgage insurers experienced substantial losses was in the mid-to-late 1980s. From the 1970s until 1981, rising home prices in the United States generally led to profitable insurance underwriting results for the industry and caused private mortgage insurers to emphasize market share. To maximize market share, until the mid-1980s, private mortgage insurers employed liberal underwriting practices, and charged premium rates which, in retrospect, generally did not adequately reflect the risk assumed, particularly on pool insurance. These industry practices compounded the losses which resulted from changing economic and market conditions which occurred during the early and mid-1980s, including (1) severe regional recessions and attendant declines in property values in the nation s energy producing states; (2) the lenders development of new mortgage products to defer the impact on home buyers of double digit mortgage interest rates; and (3) changes in federal income tax incentives which initially encouraged the growth of investment in non-owner occupied properties.

Defaults. The claim cycle on private mortgage insurance begins with the insurer s receipt of notification of a default on an insured loan from the lender. We define a default as an insured loan with a mortgage payment that is 45 days or more past due. Lenders are required to notify us of defaults within 130 days after the initial default, although most lenders do so earlier. The incidence of default is affected by a variety of factors, including the level of borrower income growth, unemployment, divorce and illness, the level of interest rates, rates of housing price appreciation or depreciation and general borrower creditworthiness. Defaults that are not cured result in a claim to us. See - Claims. Defaults may be cured by the borrower bringing current the delinquent loan payments or by a sale of the property and the satisfaction of all amounts due under the mortgage.

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The following table shows the number of primary and pool loans insured in the MGIC Book, including loans insured in bulk transactions and A- and subprime loans, the related number of loans in default and the percentage of loans in default, or default rate, as of December 31, 2004-2008:

Default Statistics for the MGIC Book

	December 31, 2008	2007	2006	2005	2004
PRIMARY INSURANCE					
Insured loans in force	1,472,757	1,437,432	1,283,174	1,303,084	1,413,678
Loans in default	182,188	107,120	78,628	85,788	85,487
Default rate all loans	12.37%	7.45%	6.13%	6.58%	6.05%
Flow loans in default	122,693	61,352	42,438	47,051	44,925
Default rate flow loans	9.51%	4.99%	4.08%	4.52%	3.99%
Bulk loans in force[(1)]	182,268	208,903	243,395	263,225	288,587
Bulk loans in default[(1)]	59,495	45,768	36,190	38,737	40,562
Default rate bulk loans	32.64%	21.91%	14.87%	14.72%	14.06%
Prime loans in default[(2)]	95,672	49,333	36,727	41,395	39,988
Default rate prime loans	7.90%	4.33%	3.71%	4.11%	3.66%
A-minus loans in default[(2)]	31,907	22,863	18,182	20,358	20,734
Default rate A-minus loans	30.19%	19.20%	16.81%	17.21%	15.00%
Subprime loans in default[(2)]	13,300	12,915	12,227	13,762	14,150
Default rate subprime loans	43.30%	34.08%	26.79%	25.20%	22.78%
Reduced documentation loans delinquent[(3)]	41,309	22,009	11,492	10,273	10,615
Default rate reduced doc loans	32.88%	15.48%	8.19%	8.39%	8.89%
POOL INSURANCE					
Insured loans in force	603,332	757,114	766,453	767,920	790,935
Loans in default	33,884	25,224	20,458	23,772	25,500
Percentage of loans in default (default rate)	5.62%	3.33%	2.67%	3.10%	3.22%

(1) At December 31, 2008, 118,000 bulk loans in force and 45,482 bulk loans in default related to Wall Street bulk transactions. Among other things, the default rate for bulk loans is influenced by our decision to stop writing the

portion of our bulk business that we refer to as Wall Street bulk transactions. This decision increases the default rate because it results in a greater percentage of the bulk business consisting of vintages that traditionally have higher default rates.

(2) We define prime loans as those having FICO credit scores of 620 or greater, A-minus loans as those having FICO credit scores of 575-619, and subprime credit loans as those having FICO credit scores of less than 575, all as reported to MGIC at the time a commitment to insure is issued. Most A-minus and subprime credit loans were written through the bulk channel.

(3) In accordance with industry

practice, loans approved by GSE and other automated underwriting (AU) systems under doc waiver programs that do not require verification of borrower income are classified by us as full documentation. Based in part on information provided by the GSEs, we estimate full documentation loans of this type were approximately 4% of 2007 new insurance written. Information for other periods is not available. We understand these AU systems grant such doc waivers for loans they judge to have higher credit quality. We also understand that the GSEs terminated their doc waiver programs in the second half of 2008.

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Different areas of the United States may experience different default rates due to varying localized economic conditions from year to year. The following table shows the percentage of loans we insured that were in default as of December 31, 2008, 2007 and 2006 for the 15 states for which we paid the most losses during 2008:

State Default Rates

	December 31,		
	2008	2007	2006
California	25.17%	13.60%	6.31%
Florida	29.46	12.30	4.62
Michigan	13.61	9.78	9.07
Arizona	21.54	7.48	3.13
Ohio	9.93	8.01	8.03
Illinois	13.28	7.73	6.36
Georgia	14.36	8.79	8.07
Texas	8.68	6.27	6.45
Nevada	25.10	8.73	4.12
Minnesota	13.17	9.07	7.71
Colorado	9.02	6.27	6.97
Virginia	11.99	6.62	4.27
Massachusetts	10.86	7.42	5.68
Indiana	10.07	6.77	6.80
New York	10.52	7.49	5.84
Other states	9.03	5.85	5.54

The default inventory for the 15 states for which we paid the most losses during 2008, at the dates indicated, appears in the table below.

Default Inventory by State

	December 31,		
	2008	2007	2006
California	14,960	6,925	3,000
Florida	29,384	12,548	4,526
Michigan	9,853	7,304	6,522
Arizona	6,338	2,169	800
Ohio	8,555	6,901	6,395
Illinois	9,130	5,435	4,092
Georgia	7,622	4,623	3,492
Texas	10,540	7,103	6,490
Nevada	3,916	1,337	530
Minnesota	3,642	2,478	1,820
Colorado	2,328	1,534	1,354
Virginia	3,360	1,761	981
Massachusetts	2,634	1,596	1,027
Indiana	5,497	3,763	3,392
New York	4,493	3,153	2,458
Other states	59,936	38,490	31,749
	182,188	107,120	78,628

Claims. Claims result from defaults which are not cured. Whether a claim results from an uncured default depends, in large part, on the borrower s equity in the home at the time of default, the borrower s or the lender s ability to sell the home for an amount sufficient to satisfy all amounts due under the mortgage and the willingness and ability of the borrower and lender to enter into a loan modification that provides for a cure of the default. Various factors affect the frequency and amount of claims, including local housing prices and employment levels, and interest rates.

Under the terms of our master policy, the lender is required to file a claim for primary insurance with us within 60 days after it has acquired title to the underlying property (typically through foreclosure). Depending on the applicable state foreclosure law, generally at least twelve months pass from the date of default to payment of a claim on an uncured default. The rate at which claims are received and paid has slowed recently due to various state and lender foreclosure moratoriums, servicing delays including as a result of attempts to modify loans, fraud investigations by us, our pursuit of mitigation opportunities and a lack of capacity in the court systems.

Within 60 days after a claim has been filed and all documents required to be submitted to us have been delivered, we have the option of either (1) paying the coverage percentage specified for that loan, with the insured retaining title to the underlying property and receiving all proceeds from the eventual sale of the property, or (2) paying 100% of the claim amount in exchange for the lender s conveyance of good and marketable title to the property to us. After we receive title to properties, we sell them for our own account.

Claim activity is not evenly spread throughout the coverage period of a book of primary business. For prime loans, relatively few claims are typically received during the first two years following issuance of coverage on a loan. This is typically followed by a period of rising claims which, based on industry experience, has historically reached its highest level in the third and fourth years after the year of loan origination. Thereafter, the number of claims typically received has historically declined at a gradual rate, although the rate of decline can be affected by conditions in the economy, including slowing home price appreciation or housing price depreciation. Due in part to the subprime component of loans insured in Wall Street bulk transactions (which were the majority of our bulk transactions prior to 2007), the peak claim period for bulk loans has generally occurred earlier than for prime loans. Moreover, when a loan is refinanced, because the new loan replaces, and is a continuation of, an earlier loan, the pattern of claims frequency for that new loan may be different from the historical pattern of other loans. As of December 31, 2008, 66% of the MGIC Book of primary insurance in force had been written on or after January 1, 2006, although a portion of that insurance arose from the refinancing of earlier originations. See - Insurance In Force by Policy Year.

Another important factor affecting MGIC Book losses is the amount of the average claim paid, which is generally referred to as claim severity. The main determinants of claim severity are the amount of the mortgage loan, the coverage percentage on the loan and local market conditions. The average claim severity on the MGIC Book of primary insurance was $52,239 for 2008, compared to $37,165 for 2007, and $28,228 in 2006. The continued increase in average claim severity in 2008 was primarily the result of the default inventory containing higher loan exposures with expected higher average claim payments as well as our inability to mitigate losses through the sale of properties due to slowing home price appreciation or home price declines in some areas.