MGIC INVESTMENT CORP
Form 10-K
March 01, 2007

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

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

For the fiscal year ended December 31, 2006

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 þ No o

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 No o

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. þ

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ
State the aggregate market value of the voting stock held by non-affiliates of the Registrant as of June 30, 2006: $5.5 billion *

* 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 15, 2007: 83,038,993
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 2007 Annual Meeting of Shareholders	Items 10 through 14 of Part III

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

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 to the home mortgage lending industry. We have ownership interests in less than majority-owned joint ventures, principally Credit-Based Asset Servicing and Securitization LLC (C-BASS) and Sherman Financial Group LLC (Sherman). As used in this Annual Report on Form 10-K, we, us and our refer to MGIC Investment Corporation s consolidated operations. C-BASS and Sherman are not consolidated with us for financial reporting purposes, are not our subsidiaries and are not included in the terms we, us and our.

Private mortgage insurance covers residential first mortgage loans and expands home ownership opportunities by enabling people to purchase homes with less than 20% down payments. If the homeowner defaults, private mortgage insurance reduces and, in some instances, eliminates the loss to the insured institution. Private mortgage insurance also facilitates the sale of low down payment and other mortgage loans in the secondary mortgage market, including to the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (Fannie Mae and Freddie Mac are collectively referred to as the GSEs). 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.

MGIC is licensed in all 50 states of the United States, the District of Columbia, Puerto Rico and Guam. 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).

As noted above, we also have ownership interests in C-BASS and Sherman. C-BASS is principally engaged in the business of investing in the credit risk of credit sensitive single-family residential mortgages. Sherman is principally engaged in purchasing and collecting for its own account delinquent consumer receivables, which are primarily unsecured, and in originating and servicing subprime credit card receivables.

We and our business may be materially affected by the risk factors applicable to us that are included in Item 1A of this Annual Report on Form 10-K. C-BASS and Sherman and their respective businesses may be materially affected by the risk factors applicable to them included in Item 1A. These factors may also cause actual results to differ materially from the results contemplated by forward looking statements that we may make.

Recent Developments. On February 6, 2007, we entered into a definitive agreement under which Radian Group Inc. (Radian), one of our mortgage insurance competitors, would merge into us (the Merger). In the Merger, 0.9658 share of our common stock will be exchanged for each share of Radian common stock. Radian has publicly reported that at October 27, 2006 it had 80.6 million shares of common stock outstanding. The Merger has been unanimously approved by each company s board of directors and is expected to be completed in the fourth quarter of 2007, subject to regulatory and shareholder approvals. For additional information about the Merger, see our Current Report on Form 8-K filed on February 12, 2007 (the Merger 8-K).

B. The MGIC Book

Types of Product

In general, there are two principal types of private mortgage insurance: primary and pool.

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). 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 generally applies to owner occupied, first mortgage loans on one-to-four family homes, including condominiums. 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 (see Bulk Transactions below) 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. Effective with the third quarter of 2001, in reports by private mortgage insurers to the trade association for the private mortgage insurance industry, 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 is classified as pool insurance. The trade association classification is used by members of the private mortgage insurance industry in reports to 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 $39.3 billion in 2006 compared to $40.1 billion in 2005 and $47.1 billion in 2004. New insurance written for bulk transactions was $18.9 billion during 2006 compared to $21.4 billion for 2005 and $15.8 billion for 2004.

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 insurance that has been written by MGIC (the MGIC Book) as of the dates indicated:

Primary Insurance and Risk In Force

	2006	2005	December 31, 2004 (In millions)	2003	2002
Direct Primary Insurance In Force	$176,531	$170,029	$177,091	$189,632	$196,988
Direct Primary Risk In Force	$ 47,079	$ 44,860	$ 45,981	$ 48,658	$ 49,231

The coverage percentage provided by us is determined by the lender. For loans sold by lenders 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.

We charge higher premium rates for higher coverages. We believe depth of coverage requirements have no significant impact on frequency of default. 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 industry accounting practice, reserves for losses are only established for loans in default. Because relatively few defaults occur in the early years of a book of business (see Exposure to Catastrophic Loss; Defaults; and Claims Claims below), the higher premium revenue from deeper coverage is recognized before any higher losses resulting from that deeper coverage may be incurred. 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 partnership with mortgage insurers, the GSEs are also offering programs under which, on delivery of an insured loan to a GSE, the primary coverage is restructured to an initial shallow tier of coverage followed by a second tier that is subject to an overall loss limit and compensation may be 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 coverages.

Mortgage insurance coverage cannot be terminated by the insurer, except for non-payment of premium, and remains renewable at the option of the insured lender, generally 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 (the 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 (LTV ratio) thresholds determined by the value of the home at loan origination and other requirements are met. In general, a borrower may stop making mortgage insurance payments when the LTV 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 LTV ratio (based on the loan s amortization schedule) reaches 78% of the unpaid principal balance of the mortgage and the borrower is (or thereafter 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 such insurance automatically in certain circumstances.

Coverage tends to continue in areas experiencing economic contraction and housing price depreciation. The persistency of coverage in such 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 32.0% in 2006 compared to 39.5% in 2005 and 37.4% in 2004. 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.

In addition to varying with the coverage percentage, our premium rates vary depending upon the perceived risk of a claim on the insured loan and, thus, take into account the LTV, the loan type (fixed payment versus non-fixed payment) and mortgage term and, for A- and subprime loans and certain other loans, the location of the borrower s credit score within a range of credit scores. In general, A- loans have FICO scores between 575 and 619 and subprime loans have FICO credit scores of less than 575. A FICO 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.

The borrower s mortgage loan instrument may require the borrower to pay the mortgage insurance premium (borrower paid mortgage insurance) or there may be no such requirement imposed on the borrower, in which case 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 (lender paid mortgage insurance). 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 that hold the mortgages; the mortgage note rate generally does not reflect the premium for the mortgage insurance.

Under the monthly premium plan, a monthly premium payment is made to us 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 earned 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 (level) for the initial year and subsequent renewal years. Under the single premium plan, a single payment is made to us, covering a specified term exceeding twelve months.

During each of the last three years, the monthly premium plan represented more than 90% 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 may have 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.

New pool risk written was $240 million in 2006 and $358 million in 2005. New pool risk written during these years was primarily comprised of risk associated with loans delivered to Freddie Mac and Fannie Mae (agency pool insurance), loans insured through the bulk channel, loans delivered to the Federal Home Loan Banks under their mortgage purchase programs and loans made under state housing finance programs. Direct pool risk in force at December 31, 2006 was $3.1 billion compared to $2.9 billion and $3.0 billion at December 31, 2005 and 2004, respectively. The risk amounts referred to above represent pools of loans with contractual aggregate loss limits and those without such limits. For pools of loans without such 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, 2006, 2005 and 2004 for $4.4 billion, $5.0 billion, and $4.9 billion, respectively, of risk without such limits, risk in force is calculated at $473 million, $469 million, and $418 million, respectively. New risk written, under this model, for the years ended December 31, 2006 and 2005 was $4 million and $51 million, respectively.

The settlement of a nationwide class action alleging that MGIC violated the Real Estate Settlement Procedures Act (RESPA) by providing agency pool insurance and entering into other transactions with lenders that were not properly priced (the RESPA Litigation) 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 (NYID) 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.

Risk Sharing Arrangements. We participate 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 purchased by the lender which have MGIC primary insurance. During the nine months ended September 30, 2006 and the year ended December 31, 2005, about 46% and 48%, respectively, of our new insurance written on a flow basis was subject to risk sharing arrangements. (New insurance written through the bulk channel is not subject to such arrangements.) The percentage of new insurance written during a quarter covered by such arrangements normally increases after the end of the quarter because, among other reasons, the transfer of a loan in the secondary market can result in a mortgage insured during a quarter becoming part of such an arrangement in a subsequent quarter. Therefore, the percentage of new insurance written for 2006 covered by such arrangements is shown only for the nine months ended September 30, 2006.

In a February 1, 1999 circular addressed to all mortgage insurers licensed in New York, the NYID 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. Such guidelines, which were to ensure that the reinsurance constituted a legitimate transfer of risk and were fair and equitable to the parties, have not yet been issued. As discussed under The mortgage insurance industry is subject to the risk of private litigation and regulatory proceedings in Item 1A, we provided information regarding captive mortgage reinsurance arrangements to the NYID and the Minnesota Department of Commerce. The complaint in the RESPA Litigation alleged that MGIC pays inflated captive reinsurance premiums in violation of RESPA. In December 2006, class action litigation was separately brought against three large lenders alleging that their captive mortgage reinsurance arrangements violated RESPA. We are not a defendant in any of these cases. During the three years ended December 31, 2004, 2005 and 2006, MGIC ceded $101.7 million, $105.2 million and $117.4 million of written premium in captive reinsurance arrangements.

External Reinsurance. At December 31, 2006, disregarding reinsurance under captive structures, less than 2% of our insurance in force was externally reinsured. Reinsuring against possible loan losses does not discharge us from liability to a policyholder; however, the reinsurer agrees to indemnify us for the reinsurer s share of losses incurred. During 2006 and 2005, we entered into three reinsurance arrangements with separate unaffiliated special purpose reinsurance companies. See Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Consolidated Operations Risk Sharing Arrangements in Item 7.

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 general, the loans insured by us in bulk transactions consist of A- loans; subprime loans; cash out refinances that exceed the standard underwriting requirements of the GSEs; jumbo loans; and loans with reduced underwriting documentation. A- loans have FICO scores between 575 and 619 and subprime loans have FICO credit scores of less than 575. 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 is $417,000 for 2007 and was $417,000 in 2006 and $359,650 in 2005.

Approximately 65% of our bulk loan risk in force at December 31, 2006 had FICO credit scores of at least 620, compared to 60% at December 31, 2005. Approximately 22% of our bulk loan risk in force at December 31, 2006 had A- FICO credit scores compared to 25% at December 31, 2005, and approximately 13% had subprime credit scores at December 31, 2006 compared to 15% at December 31, 2005. Most of the subprime loans insured by us in 2006 were insured in bulk transactions. More than 30% of our bulk loan risk in force at December 31, 2006 and 2005 had LTV ratios of 80% and below.

New insurance written for bulk transactions was $18.9 billion during 2006 compared to $21.4 billion for 2005 and $15.8 billion for 2004. For a discussion of factors that affect 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 mortgage bankers, savings institutions, commercial banks, mortgage brokers, credit unions and other lenders have historically determined the placement of mortgage insurance written on flow basis and as a result are our customers. To obtain primary insurance from us written on flow basis, a mortgage lender must first apply for and receive a mortgage guaranty master policy (Master Policy) from us. We had approximately 13,900 master policyholders at December 31, 2006 (not including policies issued to branches and affiliates of large lenders). In 2006, we issued coverage on mortgage loans for approximately 3,600 of our master policyholders. Our top 10 customers generated 34.2% of our new insurance written on a flow basis in 2006, compared to 30.5% in 2005 and 31.9% in 2004.

In insurance written through the bulk channel, we deal with securitizers of the loans, who consider whether credit enhancement provided through the structure of the securitization may 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.

Competition. 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 (VA). These agencies sponsor government-backed mortgage insurance programs, which during 2006 and 2005 accounted for approximately 22.7% and 23.6%, respectively, of the total low down payment residential mortgages which were subject to governmental or private mortgage insurance. Loans insured by the FHA cannot exceed maximum principal amounts which are determined by a percentage of the conforming loan limit. For 2006 and 2007, the maximum FHA loan amount for homes with one dwelling unit in high cost areas is as high $362,790. Loans insured by the VA do not have mandated maximum principal amounts but have maximum limits on the amount of the guaranty provided by the VA to the lender. For loans closed on or after December 10, 2004, the maximum VA guarantee is $156,375 in Alaska and Hawaii and $104,250 in other states.

In addition to competition from the FHA and the VA, 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 expansions of the authority of their state governments to insure residential mortgages.

Private mortgage insurers are also subject to competition from Fannie Mae and Freddie Mac to the extent the GSEs are compensated for assuming default risk that would otherwise be insured by the private mortgage insurance industry. Fannie Mae and Freddie Mac each have programs under which an up-front delivery fee can be paid to the GSE and primary mortgage insurance coverage is substantially reduced compared to the coverage requirements that would apply in the absence of the program. In October 1998, Freddie Mac s charter was amended (and the amendment immediately repealed) to give Freddie Mac flexibility to use protection against default in addition to private mortgage insurance and the two other types of credit enhancement required by the charter for low down payment mortgages purchased by Freddie Mac. In addition, to the extent up-front delivery fees are not retained by the GSEs to compensate for their assumption of default risk, and are used instead to purchase supplemental coverage from mortgage insurers, the resulting concentration of purchasing power in the hands of the GSEs could increase competition among insurers to provide such coverage.

The capital markets and their participants also compete with mortgage insurers by offering alternative products and services and may further develop as competitors to private mortgage insurers in ways we cannot predict. During 1998, a newly-organized off-shore company funded by the sale of notes to institutional investors provided reinsurance to Freddie Mac against default on a specified pool of mortgages owned by Freddie Mac. We have also engaged in similar reinsurance transactions. See Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Consolidated Operations Risk Sharing Arrangements in Item 7. In addition, the appetite for residential mortgage risk by capital markets participants, such as investment banks, hedge funds, and managers of collateralized debt obligations (CDOs), and by writers of credit default swaps (CDS) may reduce or eliminate the mortgage insurance in bulk transactions. See Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Consolidated Operations Bulk Transactions in Item 7. Similarly, with respect to pool insurance, not only does MGIC compete with the other mortgage insurers, and the GSEs who through the amount of guarantee fees in effect provide pool coverage or self-insure, but we compete with other forms of credit enhancement.

We and other mortgage insurers also compete with transactions structured to avoid mortgage insurance on low down payment mortgage loans. Such 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% LTV first mortgage and a 10% LTV second mortgage), with the LTV 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% LTV mortgage). Captive mortgage reinsurance and similar transactions also result in mortgage originators receiving a portion of the premium and the risk.

The private mortgage insurance industry currently consists of eight active mortgage insurers and their affiliates; one of the eight is a joint venture in which another mortgage insurer is one of the joint venturers. 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 of this Annual Report on Form 10-K. According to Inside Mortgage Finance, a mortgage industry publication, which obtains its data from reports to it 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 1995 and subsequent years, we have been the largest private mortgage insurer based on new primary insurance written (with a market share of 21.6% in 2006, 22.9% in 2005, 23.5% in 2004 and 21.9% in 2003) and at December 31, 2006, we also had the largest book of direct primary insurance in force. Effective with the third quarter of 2001, 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 we compete with other private mortgage insurers 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; the provision of other products and services that meet lender needs for risk management, affordable housing, loss mitigation, capital markets and training support; the strength of our management team and field organization; and the effective use of technology and innovation in the delivery and servicing of our insurance products. We believe our additional competitive strengths, compared to other private insurers, are our customer relationships, name recognition, reputation and the depth of our database covering loans we have insured. We believe we compete for bulk business principally on the basis of the premium rate and the portion of loans submitted for insurance that we are willing to insure. Most bulk business is competitively bid. In addition, as discussed above, capital markets participants and CDS writers may provide competition for mortgage insurers in bulk transactions.

The complaint in the RESPA Litigation alleged, among other things, that captive mortgage reinsurance, agency pool insurance, and contract underwriting as provided by us 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 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.

In the third quarter of 2001, the Office of Federal Housing Enterprise Oversight (OFHEO) adopted a risk-based capital stress test for the GSEs, which was amended in February 2002. One of the elements of the stress test is that future claim payments made by a private mortgage insurer on GSE loans are reduced below the amount provided by the mortgage insurance policy to reflect the risk that the insurer will fail to pay. Claim payments from an insurer whose claims-paying ability rating (which in this document is also referred to as a financial strength rating) is AAA are subject to a 3.5% reduction over the 10-year period of the stress test, while claim payments from a AA rated insurer, such as MGIC, are subject to a 8.75% reduction. The effect of the differentiation among insurers is to require the GSEs to have additional capital for coverage on loans provided by a private mortgage insurer whose claims-paying rating is less than AAA. As a result, there is an incentive for the GSEs to use private mortgage insurance provided by a AAA rated insurer.

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 such 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 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, 2006, 2005 and 2004. There can be no assurance that contract underwriting remedies will not be material in the future.

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 loan product, which encompasses the LTV 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.

We believe that mortgage credit risk is also affected by the origination practices of the lender and the condition of the housing market 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; for loans with higher LTV ratios compared to loans with lower LTV ratios; for ARMs during a prolonged period of rising interest rates compared to fixed rate loans in such a rate environment; 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 such limit; and for cash out refinance loans compared to rate and term refinance loans.

There are also other types of loan characteristics relating to the individual loan or borrower which 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.

Delegated Underwriting and GSE Automated Underwriting Approvals. Delegated underwriting is a program under which approved lenders are allowed to commit MGIC to insure loans originated through the flow channel utilizing their own underwriting guidelines and underwriting evaluation. Some major lenders having delegated underwriting authority use their own proprietary automated underwriting services to apply their underwriting guidelines to loans. In addition, from 2000 through the end of 2006, loans approved by the automated underwriting services of the GSEs have been automatically approved for MGIC mortgage insurance. Beginning in 2007, certain loans having a high risk of claim may not be insured by us even though such loans were approved by such underwriting services.

During the last three years, 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 though delegated underwriting programs, including those utilizing proprietary underwriting services. We expect the portion of our flow business that is approved in this manner to remain at this level. The loan approval criteria of automated underwriting services are within the risk management discretion and control of the GSEs or the lender operating the service. As a result of accepting the loan approval decisions of these services, we do not have the ability to control in advance the risk characteristics of such loans. Our risk management approach to such flow business has been to monitor periodically the credit quality of the loans we have recently insured in this manner. If as a result of such review we perceive certain loans insured in this manner have a high risk of claim, we can continue to insure loans with such characteristics that are thereafter submitted to us at A- rates. In addition, we can decline to continue to insure loans having such characteristics, although this course entails competitive risk.

Bulk Transactions Risk Management. The premium for loans insured in a bulk transaction is determined by our evaluation of the credit risk of the loans included in the transaction based on information about the loans represented to us by the securitizer. Individual loan files are generally not reviewed in advance of the issuance of an insurance commitment but are reviewed at the time a claim is made to confirm that the loan involved in the claim generally conforms to the representations that were previously made. We have the right to rescind coverage for loans that do not conform to such representations.

Exposure to Catastrophic Loss; Defaults; and Claims

The private mortgage insurance industry, which is exposed to the risk of catastrophic loss, experienced substantial losses 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 (i) severe regional recessions and attendant declines in property values in the nation s energy producing states; (ii) the development by lenders of new mortgage products to defer the impact on home buyers of double digit mortgage interest rates; and (iii) 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 and general borrower creditworthiness. Defaults that are not cured result in a claim to us. 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.

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 (default rate) as of December 31, 2002-2006:

Default Statistics for the MGIC Book

	December 31,				
	2006	2005	2004	2003	2002
PRIMARY INSURANCE					
Insured loans in force	1,283,174	1,303,084	1,413,678	1,551,331	1,655,887
Loans in default	78,628	85,788	85,487	86,372	73,648
Percentage of loans in default (default rate)	6.13%	6.58%	6.05%	5.57%	4.45%
Flow loans in default	42,438	47,051	44,925	45,259	43,196
Percentage of flow loans in default (default rate)	4.08%	4.52%	3.99%	3.76%	3.19%
Bulk loans in force	243,395	263,225	288,587	348,521	301,859
Bulk loans in default	36,190	38,737	40,562	41,113	30,452
Percentage of bulk loans in default (default rate)	14.87%	14.72%	14.06%	11.80%	10.09%
A-minus and subprime loans in force[(1)]	181,441	199,345	217,306	244,175	201,195
A-minus and subprime loans in default[(1)]	34,360	36,485	35,824	34,525	25,504
Percentage of A-minus and subprime loans in default (default rate)	18.94%	18.30%	16.49%	14.14%	12.68%
POOL INSURANCE					
Insured loans in force	766,453	767,920	790,935	1,035,696	1,208,157
Loans in default	20,458	23,772	25,500	28,135	26,676
Percentage of loans in default (default rate)	2.67%	3.10%	3.22%	2.72%	2.21%

(1) A portion of A-minus and subprime loans is included in the data for flow loans and the remainder is included in the data for bulk loans. Most A-minus and subprime credit loans are written through the bulk channel.

Regions 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 the MGIC Book s primary loans in default by MGIC region as of December 31, 2002-2006:

Default Rates for Primary Insurance By Region[(1)]

	December 31,				
	2006	2005	2004	2003	2002
MGIC REGION:					
New England	4.84%	3.98%	3.43%	3.43%	2.91%
Northeast	6.41	6.48	6.15	5.65	4.74
Mid-Atlantic.	4.83	4.89	4.81	4.53	4.05
Southeast	6.05	6.79	6.33	6.02	4.87
Great Lakes	8.07	8.60	8.19	6.99	5.17
North Central	5.96	6.01	5.78	5.38	4.22
South Central	6.07	7.94	6.35	5.94	4.65
Plains	4.17	4.51	4.51	4.03	3.41
Pacific	4.96	3.76	3.92	4.21	3.73
National	6.13%	6.58%	6.05%	5.57%	4.45%

(1) The default rate is affected by both the number of loans in default at any given date as well as the number of insured loans in force at such date.

Claims. Claims result from defaults which are not cured. Whether a claim results from an uncured default principally depends on the borrower s equity in the home at the time of default and the borrower s (or the lender s) ability to sell the home for an amount sufficient to satisfy all amounts due under the mortgage. Claims are affected by various factors, including local housing prices and employment levels, and interest rates.

Under the terms of the Master Policy, the lender is required to file a claim for primary insurance with us within 60 days after it has acquired good and marketable title to the underlying property through foreclosure. Depending on the applicable state foreclosure law, generally at least twelve months transpires from the date of default to payment of a claim on an uncured default.

Within 60 days after the claim has been filed, we have the option of either (i) 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 (ii) paying 100% of the claim amount in exchange for the lender s conveyance of good and marketable title to the property to us. We will then sell the property 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 received during the first two years following issuance of coverage on a loan. This is 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 received has historically declined at a gradual rate, although the rate of decline can be affected by conditions in the economy, including lower housing price appreciation. There can be no assurance that this historical pattern of claims will continue in the future and due in part to the subprime component of loans insured in bulk transactions, 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, 2006, 70% of the MGIC Book primary insurance in force had been written during 2004 2006, although a portion of such insurance arose from the refinancing of earlier originations.

In addition to the increasing level of claim activity arising from the maturing of the MGIC Book, 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 and the coverage percentage on the loan. The average claim severity on the MGIC Book primary insurance was $28,228 for 2006, compared to $26,361 in 2005 and $24,438 in 2004.

Loss Reserves

A significant period of time may elapse between the occurrence of the borrower s default on a mortgage payment (the event triggering a potential future claim payment by us), the reporting of such default to us and the eventual payment of the claim related to such uncured default. To recognize the liability for unpaid losses related to outstanding reported defaults (known as the default inventory), we, similar to other private mortgage insurers, establish loss reserves, representing the estimated percentage of defaults which will ultimately result in a claim (known as the claim rate), and the estimated severity of the claims which will arise from the defaults included in the default inventory. In accordance with industry accounting practices, we do not establish loss reserves for future claims on insured loans which are not currently in default.

We also establish reserves to provide for the estimated costs of settling claims, including legal and other fees, and general expenses of administering the claims settlement process (loss adjustment expenses), and for losses and loss adjustment expenses from defaults which have occurred, but which have not yet been reported to the insurer.

Our reserving process is based upon the assumption that past experience provides a reasonable basis for estimating future events. However, estimation of loss reserves is inherently judgmental. Conditions that have affected the development of the loss reserves in the past may not necessarily affect development patterns in the future, in either a similar manner or degree.

For further information about loss reserves, see Management s Discussion and Analysis Results of Operations Losses in Item 7 and Note 6 to our consolidated financial statements in Item 8.

Geographic Dispersion

The following table reflects the percentage of primary risk in force in the top 10 states and top 10 metropolitan statistical areas (MSAs) for the MGIC Book at December 31, 2006:

Dispersion of Primary Risk in Force

Top 10 States		
1.	Florida	9.5%
2.	California	7.8
3.	Texas	6.5
4.	Illinois	4.9
5.	Ohio	4.7
6.	Michigan	4.7
7.	Pennsylvania	4.1
8.	New York	3.7
9.	Georgia	3.3
10.	Indiana	2.7
Total		51.9%
Top 10 MSAs		
1.	Chicago	3.6%
2.	Atlanta	2.2
3.	Boston	2.0
4.	Washington, D.C.	2.0
5.	Detroit	1.9
6.	Los Angeles	1.9
7.	Riverside-San Bernardino	1.8
8.	Phoenix	1.8
9.	Philadelphia	1.7
10.	Houston	1.7
Total		20.6%

The percentages shown above for various MSAs can be affected by changes, from time to time, in the federal government s definition of an MSA.

Insurance In Force by Policy Year

The following table sets forth for the MGIC Book the dispersion of our primary insurance in force as of December 31, 2006, by year(s) of policy origination since we began operations in 1985:

Primary Insurance In Force by Policy Year

Policy Year	Primary Insurance in Force (In millions of dollars)	Percent of Total
1985 1999	$ 8,014	4.7%
2000	1,580	0.9
2001	6,073	3.4
2002	12,224	6.9
2003	25,397	14.4
2004	27,420	15.5
2005	43,496	24.6
2006	52,327	29.6
Total	$ 176,531	100.0%

Risk In Force and Product Characteristics of Risk in Force

At December 31, 2006 and 2005, 94% of our risk in force was primary insurance and the remaining risk in force was pool insurance. The following table sets forth for the MGIC Book the dispersion of our primary risk in force as of December 31, 2006, by year(s) of policy origination since we began operations in 1985:

Primary Risk In Force by Policy Year

Policy Year	Primary Risk in Force (In millions of dollars)	Percent of Total
1985 1999	$ 1,908	4.0%
2000	396	0.8
2001	1,563	3.3
2002	3,182	6.8
2003	6,569	14.0
2004	7,261	15.4
2005	11,859	25.2
2006	14,341	30.5
Total	$ 47,079	100.0%

The following table reflects at the dates indicated the (i) total dollar amount of primary risk in force for the MGIC Book and (ii) percentage of such primary risk in force (as determined on the basis of information available on the date of mortgage origination) by the categories indicated.

Characteristics of Primary Risk in Force

	December 31, 2006	December 31, 2005
Direct Risk in Force (In Millions):	$ 47,079	$ 44,860
LTV:(1)		
100s	21.1%	16.4%
95s	28.3	30.5
90s(2)	40.0	44.5
80s	10.6	8.6
Total	100.0%	100.0%
Loan Type:		
Fixed(3)	76.6%	74.5%
Adjustable rate mortgages (ARMs(4))	23.4	25.5
Total	100.0%	100.0%
Original Insured Loan Amount:(5)		
Conforming loan limit and below	93.2%	92.4%
Non-conforming	6.8	7.6
Total	100.0%	100.0%
Mortgage Term:		
15-years and under		