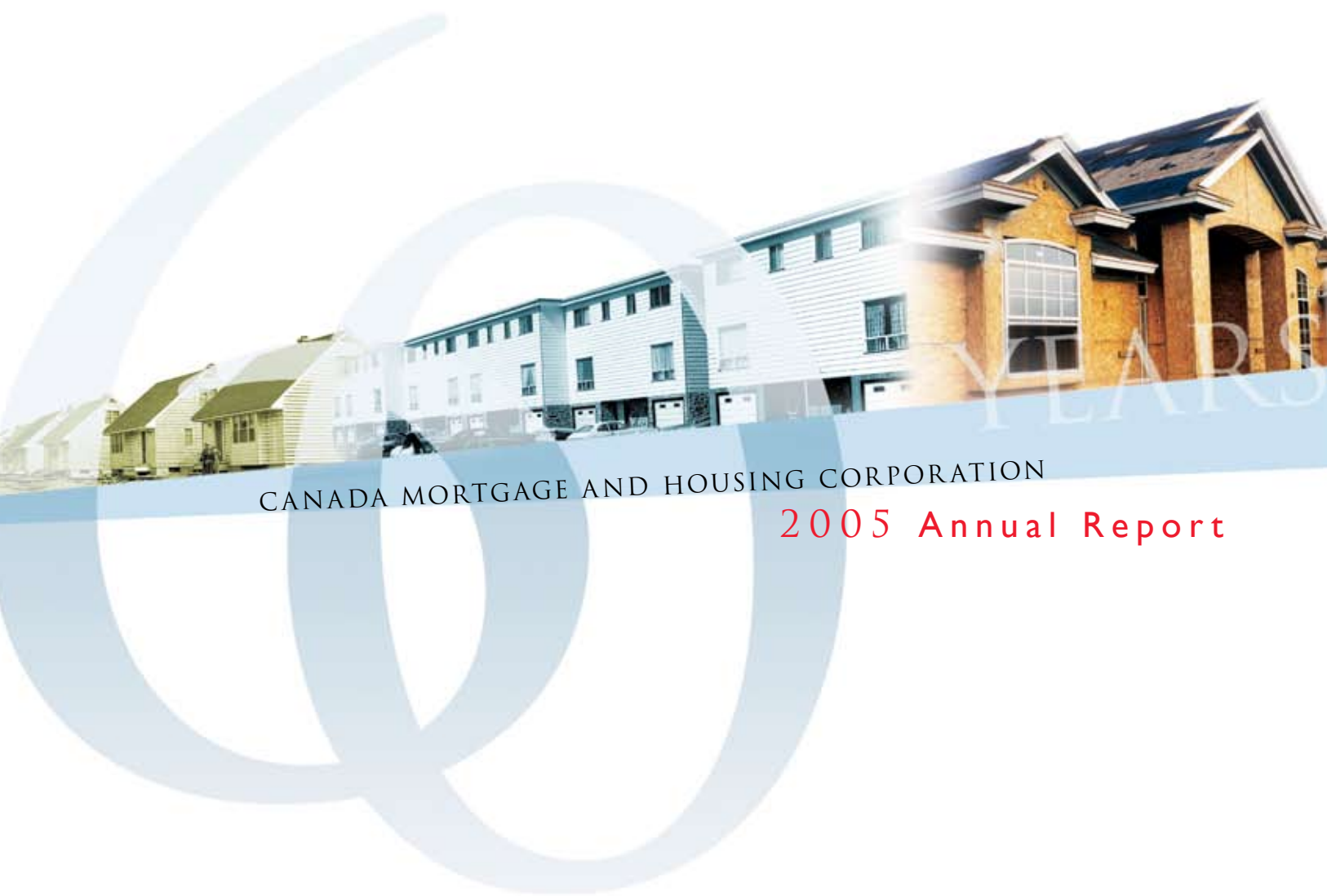


PROUD PAST
BRIGHT FUTURE



CANADA MORTGAGE AND HOUSING CORPORATION

2005 Annual Report

65043

Canada 

 **60** YEARS
ANS


CMHC SCHL
HOME TO CANADIANS

TABLE OF CONTENTS

Messages	3
Corporate Governance	9
Performance Against Objectives	19
Management's Discussion and Analysis	63
Financial Statements and Notes	85
Glossary and Corporate Listing	117

OUR MANDATE

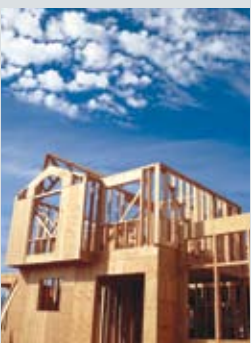
The promotion of:

- housing construction, repair and modernization;
- housing affordability and choice;
- improvements to overall living conditions;
- the availability of low-cost financing; and
- the national well-being of the housing sector.

FORWARD LOOKING STATEMENTS

CMHC's Annual Report contains forward-looking statements regarding objectives, strategies and expected financial results. There are risks and uncertainties beyond the control of CMHC that include, but are not limited to, economic and financial conditions globally, and regulatory conditions nationally and internationally.

These factors, among others, may cause actual results to differ substantially from the expectations stated or implied by forward-looking statements.



CMHC, A FEDERAL CROWN CORPORATION, IS CANADA'S NATIONAL HOUSING AGENCY.

In support of our three corporate objectives, we were engaged in a wide variety of activities in 2005 aimed at helping Canadians meet their housing needs.

Objective One WE HELP CANADIANS IN NEED

- ... by supporting the Affordable Housing Initiative with the provinces and territories to commit 25,000 units to date
- ... by investing \$1.7 billion to assist over 633,000 households who live in social housing
- ... by financially assisting 22,000 low-income households with housing renovation and repair
- ... by reducing or eliminating mortgage insurance premiums on affordable housing projects
- ... by committing new funds to reduce the current shortage of suitable housing on reserve
- ... by working closely with First Nations, Métis and Inuit people to build housing capacity

Objective Two WE FACILITATE ACCESS TO MORE AFFORDABLE, BETTER QUALITY HOUSING FOR ALL CANADIANS

- ... by facilitating access to low cost mortgages by approving 746,000 mortgage loan insurance applications
- ... by lowering mortgage insurance premiums by 15% for first-time homebuyers with a five per cent down-payment
- ... by continuing to introduce innovations like our new mortgage insurance product for energy-efficient homes
- ... by guaranteeing more than \$30 billion in mortgage-related securities to ensure a steady supply of low-cost funds for mortgage lending
- ... by providing objective and reliable information through housing related research and housing market conferences

Objective Three WE ENSURE THE CANADIAN HOUSING SYSTEM REMAINS ONE OF THE BEST IN THE WORLD

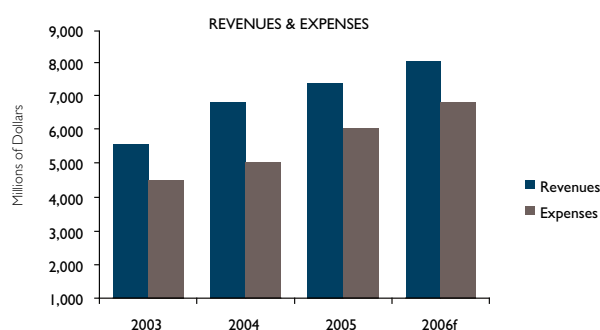
- ... by advising the Government of Canada on matters of housing policy
- ... by creating a vision for a healthy, sustainable future as promoted through initiatives such as the Net-Zero Energy Healthy Housing demonstration project
- ... by partnering with Canadian exporters in the housing industry and promoting Canadian solutions in markets around the world
- ... by ensuring CMHC remains a strong organization, able to fulfil our mandate

FINANCIAL PERFORMANCE	2003 ACTUAL	2004 ACTUAL	2005 ACTUAL	2005 PLAN
Total Assets (in millions of dollars)*	59,925	81,008	101,093	88,588
Total Liabilities (in millions of dollars)*	57,449	77,582	96,665	84,430
Total Equity (in millions of dollars)	2,476	3,426	4,428	4,158
Total Revenues (in millions of dollars)*	5,563	6,560	7,334	7,069
Total Expenses (in millions of dollars)	4,556	5,161	5,870	5,859
Net Income After Income Taxes (in millions of dollars)	667	950	1,002	817
Staff Years	1,799	1,814	1,804	1,902

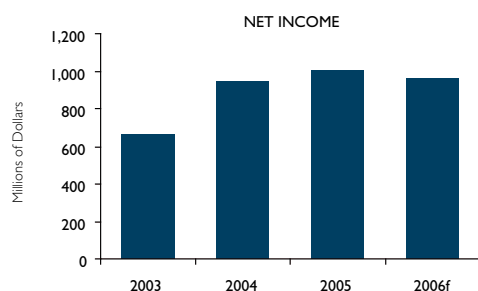
* Historical values and plans have been restated to show the consolidation of Canada Housing Trust which took effect on 1 January 2005.

We managed our business well, successfully extending the reach and benefit of our programs, while generating value for Canada and Canadians.

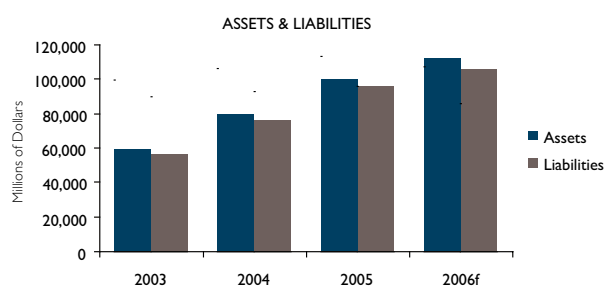
*We expanded our business, while **prudently managing our expenses.***



*Business excellence and favourable economic conditions helped **bolster net income.***



*As a result, Equity of Canada **increased by 29%.***





IN 2006, CANADA MORTGAGE AND HOUSING CORPORATION CELEBRATES 60 YEARS OF SERVICE TO CANADIANS.

Sixty years ago, CMHC opened its doors as Canada's national housing agency to welcome home the soldiers returning from World War II. Since that time, we have helped hundreds of thousands of Canadians to access decent, affordable housing through a host of programs, policies and initiatives.

The 1940s: A new beginning for housing in Canada

CMHC is established to house returning war veterans. Prime Minister Mackenzie King incorporates the Central Mortgage and Housing Corporation by Act of Parliament.

The 1950s: From home building to community building

CMHC evolves from home builder to community builder through new loan insurance and public housing projects.

The 1960s: The renaissance of Canada's cities

CMHC shifts its focus to municipal planning and development to help cities deal with rapid urban growth.

The 1970s: Focus on social housing

CMHC plays an important role in social housing; CMHC helps low-income people attain homeownership, helps maintain existing housing stock, preserves historic neighbourhoods, and addresses Aboriginal housing needs.

The 1980s: Laying a new foundation for quality and affordability

In response to dramatic shifts in Canada's economy, CMHC offers loan programs to make homeownership more accessible.

The 1990s: A new era for building science

CMHC helps develop and share information on new building technology to address indoor air quality, moisture and environmental sensitivity. CMHC fosters public/private cooperation in housing projects, introduces emili, an automated insurance underwriting system, and expands its activities internationally.

2000 and beyond: Leading the way home

CMHC remains committed to helping Canadians access a wide choice of safe, quality, affordable homes, and making vibrant and sustainable communities and cities a reality across the country. CMHC is truly home to Canadians.



MISSION

Promote housing quality, affordability and choice for Canadians

VALUES

Integrity at Work

We lead by example, we honour our obligations, and are committed to:

physical, and human resources entrusted to our care. We encourage learning, innovation and personal initiative to continuously improve the way we do business and achieve the best possible results for the Canadian public.

Serving the Public Interest

As stewards of the public trust we serve with fairness, impartiality and objectivity. All of our activities, including those that are commercial in nature, are carried out in support of our public policy objectives. Our actions are inspired by a respect for human dignity and the value of every person.

Building a Workplace Community

We practice mutual respect and honesty in our working relationships. We help each other to achieve the goals of the team and the organization, and to maintain a healthy balance between our CMHC work and the other parts of our lives.

Achieving Business Excellence

We exercise the highest standards of competence, trustworthiness and prudence in conducting our business relationships and in managing the financial,

We willingly explain our actions so that we may hold ourselves, and each other, accountable for living these values in the workplace.



MESSAGES

Message from the Chairman

Message from the President

MESSAGE FROM THE CHAIRMAN

Governance. Every annual report these days — and this one is no exception — features this word front and centre. Why is governance so important? Simply put, good governance means long-lived, well-managed corporations that create value for the people who have a stake in them.

At CMHC, we are celebrating 60 years of good management; of financial prudence; of care and respect for our employees, the environment and our communities; of strong corporate values that have guided us through good and through troubled times; and, most importantly, of making a significant and meaningful difference in the everyday lives of Canadians.

Since 1946, we have continuously served the public interest by helping hundreds of thousands of Canadians who look to us for housing solutions. Simultaneously we have long been recognized for our reliable, effective and prudent governance practices. I, the members of the Board of Directors, the executive of the Corporation and all current and past CMHC employees are proud of our 60-year history of serving Canadians to the very best of our abilities.

Underlying our ability to serve the public interest is our knowledge and credibility. We know housing. What better demonstration can there be of this than the fact that increasingly the rest of the world is looking to Canada and CMHC to help improve their housing systems. We also know Canada. Over our 60 year history, we have been in every community in this nation and dealt with Canadians from all walks of life. We understand the realities, the issues, the challenges as well as the successes of housing in Canada.

In 2005, we continued our tradition of listening to Canadians with our involvement in national consultations on the direction forward for housing policy. We also worked closely with our provincial and territorial partners to develop housing solutions that resulted in signed agreements with all 13 provinces and territories under the Affordable Housing Initiative. Through the active involvement of these partners, we will jointly deliver and cost share phase II of the initiative and will increase the supply of affordable housing across the country. We listened to our stakeholders and made mortgages for affordable housing projects easier and cheaper to obtain. We leveraged our relationships within government and industry to launch a partnership aimed at dramatically reducing the amount of energy new homes use.



All of these accomplishments were founded on **our commitment to business excellence**. Through innovation and sound financial management, CMHC has long been a pillar of housing finance in Canada. We are the leading mortgage insurer and mortgage securitizer. Because of us, Canadians looking to buy or sell a home know that a well-functioning mortgage financing system is there to support them. As a result, hundreds of thousands of Canadians have gained access to homeownership sooner and more economically because of CMHC.

At the core of all of our accomplishments, from January 1, 1946 to today, is **the strong workplace community we have built** at CMHC. We hold ourselves and each other accountable to get the job done in a manner that is consistent with our ethical values. In the pages that follow, you will find more detailed accounting of our 2005 objectives and targets, which stemmed directly from the priorities and accountabilities given to us by the Government of Canada. You will also find an analysis of our strengths, challenges and risks, as well as details on our stewardship of the public resources entrusted to us. We will tell you about the systems that we have in place to manage our business effectively and the priorities we have set going forward.

While we have achieved many successes and continue to play a key role in creating the high quality of housing in Canada, we also recognize that we have serious challenges to address. We need only consider the state of housing on reserve or the numbers of families without affordable housing or the incidence of homelessness to understand much more needs to be done before we can be assured that all Canadians enjoy the benefits of a well-housed nation.

Looking forward, I would like to welcome the Board members who joined us this year: Harold Calla, who brings financial management experience and direct involvement in Aboriginal governance to our Board; Gary Mooney, with significant experience both as a lawyer and in the insurance sector; and Alexander Werzberger with over 40 years experience as a builder and land developer. I would also like to thank the members who completed their terms in 2005 for their outstanding contribution to CMHC: Michel Bérubé and Grace Kwok.

Throughout our history, we have shown our ability to adapt to current realities, to influence others to contribute what they can and how they can to improving housing and living conditions in Canada. As we celebrate 60 years as Canada's national housing agency, I have every confidence that we will continue to display the many attributes that have made CMHC the strong organization that it is: creativity, commitment, dedication, an ability to stay the course when needed and the vision to set new directions when challenges warrant.



Dino Chiesa
Chairman of the Board

MESSAGE FROM THE PRESIDENT

OUR LEGACY — PROUD PAST

Sixty years ago, CMHC opened its doors as Canada's national housing agency to welcome home the soldiers returning from World War II. Since that time, we have helped hundreds of thousands of Canadians to access decent, affordable housing through a host of programs, policies and initiatives. As we celebrate our 60th anniversary, we take pride in knowing that we have helped create Canada's high standard of housing and a quality of life that is the envy of the world.

From its beginnings as Central Mortgage and Housing Corporation, CMHC's mission has been guided by a desire to improve the lives of Canadians through good quality housing. Through the decades, we have evolved and adapted to meet changing needs. But while our product and service offering changed through the years, we have never lost sight of our fundamental purpose — to promote housing quality, affordability and choice for Canadians.

Together with other housing stakeholders, we have been helping to ensure that Canada maintains one of the best housing systems in the world. The hallmarks that have made the Corporation a success — a sense of mission, a commitment to excellence, dedication to serve and pride in achievement — have been the driving force behind the accomplishments we are showcasing in this annual report.

OUR ACHIEVEMENTS

In 2005, CMHC achieved significant results in each of our three corporate objectives. The accomplishments we are presenting in this report build on our past successes, demonstrate our commitment to serving the people of Canada in a responsible, progressive and transparent manner, and lay the foundation for our future efforts as we take on the challenges that remain.

Helping Canadians in need

One of our most important objectives is to help Canadians who are unable to afford safe, adequate housing on their own. We continue to work with our provincial and territorial partners to develop more affordable housing options for low-income Canadians through our Affordable Housing Initiative, with about \$175 million expended in 2005, and through innovative uses of our programs. On behalf of the Government of Canada, we manage more than \$2 billion dollars in annual housing expenditures, including ongoing subsidies that assist over 633,000 households.

In 2005, we committed financial assistance to almost 22,000 low-income households to help with needed housing repairs. Through our knowledge of the financing and management of affordable housing, we contributed to the development of almost



2,400 affordable housing units with little or no federal subsidy. We use seed funding and proposal development funding to increase the capacity of the housing sector to create new affordable housing options in the future.

One area of particular note in 2005 was our collaborative work with National Aboriginal Organizations and other federal partners to address Aboriginal housing issues and create more and better housing opportunities for Aboriginal Canadians. I was pleased to see that a new level of consensus on the direction forward is emerging and the growing commitment to using measurable targets to evaluate progress.

CMHC has been a catalyst in the effort to create more private market-like housing conditions on reserve for those individuals who can financially support the cost of homeownership. In 2005, we signed the first on-reserve Homeownership Loan Insurance pilot agreement with the Nak'azdli Band Council of northern British Columbia. This is a ground breaking risk-sharing venture that strives to create homeownership opportunities for members of the Band. Aboriginal housing and capacity development will continue to be a key priority for CMHC in 2006 as we contribute, both in the short and long term, to improving housing and living conditions for Aboriginal Canadians.

Facilitating access to more affordable, better quality housing for all Canadians

Our housing finance business represents another significant area of achievement in continuing to serve Canadians well.

In 2005, we introduced a number of enhancements to mortgage loan insurance products, including lowering homeowner premiums for the second time in two years and waiving premiums for certain types of affordable rental housing, both of which help to improve access to housing. CMHC again achieved record volumes of insurance business. We are committed in 2006 to continuing our leadership and ensuring our mortgage insurance products and services meet the changing needs of Canadians. Our efforts to ensure an abundant supply of low-cost funds for residential lending through our Mortgage-Backed Securities and Canada Mortgage Bonds programs also met with great success.

As a result of our housing finance activities, we now have \$273.7 billion of insurance in force and total securitization guaranties in force of \$103.7 billion.

In accordance with new Canadian Institute of Chartered Accountants Accounting Guideline 15 (AcG-15), we are presenting the consolidated financial statements of CMHC and the Canada Housing Trust. Consolidation of the Canada Housing Trust, an independent trust that issues the Canada Mortgage Bonds which CMHC guarantees, results in an increase in consolidated assets and liabilities of \$72.8 billion, and an increase in revenues and expenses of \$2.6 billion.

Going forward, we are well aware that pivotal changes are underway for the financial services sector in Canada. As a key player in the housing finance industry, CMHC is actively preparing for anticipated regulatory and competitive changes that have the potential to significantly impact our business environment and the way we approach our business. We will continue to examine possible impacts and how best to position our mortgage insurance and securitization activities to ensure we are able to respond to the challenges and opportunities ahead.

Ensuring the Canadian housing system remains one of the best in the world

In 2005, we devoted a great deal of effort to consultations with a host of partners and players in the housing sector to gain a better understanding of the diversity of housing needs in Canada, with a view to developing a new national housing strategy. We followed up with research, analysis and policy development to explore possible options.

Canada's high standard of housing and our housing expertise — both financial and technical — are eagerly sought after by many countries. In 2005, we continued our tradition of working in the international arena to help improve housing conditions around the world. Our international efforts have provided significant help to the Canadian housing industry to access export markets and this activity has contributed to strengthening the domestic economy.

Our focus on sustainability issues builds on our long-standing commitment to foster the development of sustainable housing and communities. To support this focus, we introduced mortgage loan insurance premium refunds for Energy Efficient Homes, and we are also undertaking two insurance pilot projects to support brownfield redevelopments. We are also leading the Net Zero Energy Healthy Housing Initiative to facilitate the integration of net-zero energy home demonstrations into sustainable planned communities across Canada.

With regard to our internal environment, CMHC has long recognized that our greatest strength is our employees. We continue to update our human resources programs, policies and practices to ensure our employees have the tools and skills they need to accomplish their jobs and make their best contribution. In 2005, we focused on succession management as a means of building our bench strength. We also completed the roll-out of our ethics awareness initiative to ensure that every member of the Corporation has the same appreciation and knowledge of the values that guide our activities.

LOOKING FORWARD TO A BRIGHT FUTURE

CMHC employees have always been motivated by the desire to create lasting value for their fellow Canadians. That commitment is visible in the high standard of housing we now enjoy in Canada. As we celebrate 60 years of achievements in 2006, we are also looking keenly at the future and to the opportunities to make an even greater contribution to improving housing and living environments for Canadians.

A key focus in 2006 and beyond will be in finding new and better approaches to help Canadians in need, approaches that respond to Canadian values of fairness, while recognizing the diversity of need and the range of capacity to meet that need in Canada. Particular emphasis will continue to be placed on the unique challenges facing Aboriginal Canadians, where we will use all the tools at our disposal, including maximizing the impact of housing subsidies, transferring needed skills and expertise and developing market-like conditions where possible.

In the area of housing finance, we will be setting the longer term direction for our existing mortgage insurance and securitization tools in light of the changes in the financial services industry, while continuing to bring innovations to the market that continue to improve housing access and serve Canadians well. Market analysis and housing information will continue to be key tools in bringing housing solutions to Canadians and we will adapt our products in these areas, as we gain an even greater understanding of client needs.

CMHC will remain committed to promoting sustainable housing and communities domestically and to supporting and promoting Canada's world-class housing products, services and systems internationally. We have much to share with the world and much to learn from others and we look to the World Urban Forum and the 26th World Congress of the International Union for Housing Finance, both of which will be held in Vancouver this year, as excellent opportunities to do that.

Finally, we understand that we need to be a strong, effective organization in order to fulfill the accountabilitys entrusted in us by the Government of Canada. We continue to look to leading edge human resources practices, modern financial and risk management techniques, a strong technology platform and a sound governance framework to help us accomplish that.

We do not have all the answers, nor do we believe that we can solve critical housing issues alone. As we have done for six decades, in 2006 we will call upon the expertise of our many partners and stakeholders, and the commitment and dedication of our employees, to work toward our dream that every Canadian will have a safe, affordable place to call home.



Karen Kinsley
President and Chief Executive Officer



CORPORATE GOVERNANCE

Board of Directors

Corporate Governance Practices

Committees of the Board of Directors

Focus on Values and Ethics

CORPORATE GOVERNANCE

Good corporate governance is at the heart of all of CMHC's activities and successes. It has been a hallmark of our way of doing business since we first opened our doors in 1946. And it is the guiding principle that will stand us in good stead as we continue to build on our 60-year legacy of providing value to Canadians. This ongoing commitment to ensuring a strong and relevant governance framework means prudent and efficient management of corporate resources, and transparent disclosure and accountability to Canadians.

BOARD OF DIRECTORS

Board Mandate

CMHC is a Crown corporation, reporting to the Parliament of Canada through a Minister, and governed by a Board of Directors which is accountable for the overall corporate governance of CMHC. The Board of Directors manages the affairs of the Corporation and the conduct of its business in accordance with the *CMHC Act*, the *National Housing Act*, the *Financial Administration Act* and the governing by-laws of CMHC. As stewards of the Corporation, the Board of Directors sets the strategic direction of the Corporation, provides housing policy advice to the Minister, ensures the

integrity of corporate policies and business processes, identifies and manages the key corporate risks, and evaluates the Corporation's overall performance.

In order to continue to promote effective accountability, CMHC's Board is currently undertaking a review of its charter and committee terms of reference to ensure that they clearly define the roles and responsibilities of the Board and committees, meet the Government of Canada's expectations and are reflective of best practices in corporate governance. The Board Charter and committee terms of reference will be published on CMHC's website in 2006 in order to further promote accountability and transparency.



From left to right: Sophie Joncas, Louis Ranger, Alexander Werzberger, Gary Mooney, Dino Chiesa, Karen Kinsley, Roberta Hayes, Harold Calla, Catherine C. Cronin, and Hugh Heron.

Board Composition and Appointment Process

CMHC's Board of Directors is comprised of 10 Directors: the Chairman of the Board, the President and Chief Executive Officer, and eight other members. With the exception of the President and CEO, all CMHC Directors are independent of management. Appointments to CMHC's Board of Directors follow the Governor in Council appointment process and procedures, and are typically for a term of three years.

In 2004, in accordance with the Government of Canada's new selection process, a Nominating Committee was established to ensure active Board participation in the selection of the Chairperson and the Chief Executive Officer.

The Board's overall renewal process is designed to ensure that the composition of the Board reflects the types of clients CMHC serves, as well as a proper balance of key criteria, including previous experience and service on boards, gender, ethnicity, geographical representation, representation of Canada's urban and rural population and understanding of Aboriginal housing needs.

Orientation and Continuing Education

In 2005, all newly-appointed Board members attended a two-day orientation session with CMHC's senior management team. On an ongoing basis, the Board members are kept informed of the Corporation's operations at meetings of the Board and its committees, and through reports and analyses by, and discussions with, management. Board members are also encouraged to attend other training events that will enhance their skills, performance and contributions to the Board.

Each year, two of the regularly scheduled Board meetings are held in different locations across the country to provide the Board with the opportunity to meet directly with CMHC's employees, clients, partners and stakeholders, and to become better acquainted with regional issues. In 2005, the cities of Toronto and Edmonton-Fort McMurray hosted the Board, offering them an insider's look at the housing issues, challenges and successes of these vibrant communities. Various members of the Board have also participated in corporate events across the country, including regional Housing Outlook Conferences, project openings under the Affordable Housing Initiative, and consultations on a national housing strategy.

Assessment Process

The Board is currently reviewing its assessment process to ensure alignment with Government of Canada expectations and industry best practices. In the past, the Board of Directors has conducted a self-assessment of their performance as a whole. In 2006, the Board self-assessment tool will be refined and a new self-assessment tool will be introduced to enable directors to assess their own individual performance.

CORPORATE GOVERNANCE PRACTICES

Corporate governance is a shared responsibility, engaging the Board of Directors, senior management, and all employees in ensuring that our operations are carried out in a manner that reflects our corporate integrity and values. Our governance practices transcend all aspects of our operations and are designed to ultimately ensure that we are a responsible organization, effectively using our resources to bring the best possible value to Canadians.

Strategic Planning Process

Establishing the strategic direction for the Corporation is the foundation for fulfilling the Board's governance responsibilities. The key tool for direction setting is the annual corporate plan process. The Board of Directors provides guidance to the Corporation at the outset of the planning cycle. The Board's input into the process reflects the direction provided by the Minister in support of the Government of Canada's current priorities. Therefore, the Board of Directors guides our senior management team as we translate the federal government's public policy objectives into programs and services designed to enhance the quality of life of Canadians.

FOLLOW-UP ON THE 2004 SPECIAL EXAMINATION

During 2004, the Corporation's external auditors conducted a statutorily required Special Examination — a form of performance audit undertaken every five years. The joint examiners produced a balanced report that included positive findings about CMHC's systems and practices, as well as areas for improvement. Based on all of the findings, there were no significant deficiencies reported and CMHC was issued a "clean" opinion for the fourth time in as many Special Examinations. The report is available on CMHC's website, www.cmhc.ca.

The Special Examination noted three areas for improvement related to issues of corporate governance and performance measurement. Management has taken the following actions to address these:

- Completed an external review of Board committees' mandate, and began implementation of resulting recommendations.
- Completed the initiative that was underway to communicate CMHC's values and ethics statement throughout the Corporation.
- Enhanced reporting of CMHC's corporate performance framework to ensure balanced measurement and clear linkage between financial and non-financial information, and incorporated explicit outcome statements in relation to each corporate objective in the 2006–2010 corporate plan.

In 2005, the Board of Directors was involved in the recasting of CMHC's overarching corporate objectives. For several years, CMHC's priorities were structured around four corporate objectives which focused on housing choice and affordability, housing and living conditions, housing sector well-being, and organizational effectiveness. In 2005, based on the direction provided by the Minister and the Board, CMHC's corporate objectives and strategic priorities were recast as follows to better reflect ongoing business and key client groups and to facilitate enhanced alignment of CMHC's business and financial plans: 1) Help Canadians in Need; 2) Facilitate Access to More Affordable, Better Quality Housing For All Canadians; and 3) Ensure the Canadian Housing System Remains One of the Best in the World.

The Board of Directors remains involved throughout the planning process, reviewing the corporate plan on two occasions before recommending the plan to the Minister for approval by the Governor in Council. Following approval of the corporate plan, the Board is actively involved in verifying follow through on the plan. The Board receives quarterly reports from management on progress against key objectives in the corporate plan, enabling it to monitor the Corporation's progress and ensure that appropriate actions are taken to meet the corporate objectives.

Integrity of Internal Control and Management Information Systems

As part of its stewardship responsibilities, the Board of Directors, with the help of the Audit Committee, works with CMHC's internal auditors to ensure the integrity of the Corporation's internal control and management of information systems. The Board is committed to financial transparency and closely examines all current and potential implications of new and proposed accounting guidelines and industry practices to ensure continued fair presentation of CMHC's financial situation.

In 2005, CMHC's audit committee oversaw Management's review and analysis of the accounting guideline on entities not controlled through ownership. This guideline became effective for the first time in 2005 for CMHC and its application resulted in the accounting consolidation of the Canada Housing Trust, an independent trust that issues the Canada Mortgage Bonds (CMB) that are guaranteed by CMHC.

The consolidation of the Canada Housing Trust does not change the Canada Mortgage Bond Program, the nature of the timely payment guarantee provided by CMHC nor the manner in which the Securitization activity of CMHC is governed. Accordingly, the internal control and management information systems that fall under the stewardship of the Board of Directors is limited to the prudent management of the timely payment guarantee provided on Canada Mortgage Bonds. These systems have existed since the inception of the Canada Mortgage Bond Program in 2001.

Succession Planning for Critical Senior Positions

CMHC's Board of Directors underlined its commitment to effective succession management in 2005. The Board was involved in approving a succession management framework to identify vulnerable senior positions within the organization. The Board is informed of any changes in the executive ranks, and plays a role in approving senior appointments within the Corporation, ensuring that appointees possess the qualifications and experience needed to carry out their responsibilities to the Corporation.

COMMITTEES OF THE BOARD OF DIRECTORS

The Board has established four Committees to assist it in exercising its responsibilities: the Corporate Governance Committee, the Audit Committee, the Human Resources Committee and the Nominating Committee. Two members of the Board also serve as trustees of the employee pension fund.

Corporate Governance Committee

The Corporate Governance Committee is responsible for overseeing and advising the Board on all aspects of corporate stewardship. The committee supports the Board in a number of ways, including helping to set corporate strategic direction, ensuring the adequacy and integrity of CMHC's information systems and practices, periodically examining the continued relevance of the Corporation's public policy objectives and legislated mandate, and promoting effective communication with the Government of Canada, other stakeholders and the public. The committee also evaluates the President and CEO's performance, which is directly linked to the achievement of strategic directions set out at the beginning of the annual planning process, and makes recommendations to the Board regarding the President's compensation.

During the year, the committee monitored the Corporation's performance reporting through quarterly corporate performance reports to the Board, providing committee members with timely and balanced information on the achievement of CMHC's objectives and identifying any needed corrective action to assist in the achievement of objectives by year-end. In addition to these functions, the committee will continue to actively monitor the Treasury Board review of the governance framework of Crown corporations in 2006.

Audit Committee

The Audit Committee advises the Board of Directors on the soundness of the financial management of the Corporation, assisting the Board in overseeing internal control systems and financial reporting and audit processes. The Audit Committee provides an open avenue of communication between internal audit, the external auditors and the Board of Directors. The committee reviews the annual external audit plan with the external auditors and regularly meets with them in camera without the presence of management. The Audit Committee also ensures implementation and maintenance by management of appropriate systems of internal control, including management information systems security and controls.

Following a mandate review by PriceWaterhouseCoopers (PWC) in 2004, the Audit Committee assumed responsibility for conducting an annual review of CMHC's funding, investment and management policies to ensure effective measurement, monitoring, control and management of financial risks. Responsibility for the annual review of the enterprise risk management framework and risk landscape has also been transferred to the Audit Committee, effective in 2005.

CMHC and the Board are satisfied that members of the Audit Committee possess the necessary qualifications to fulfill their responsibility to CMHC and the Government of Canada. With the inclusion of a new committee member in 2005, all committee members are deemed to be financially literate: two members hold accounting designations and the third member possesses expertise in financial management. All members of the Audit Committee are independent of management.

Human Resources Committee

The Human Resources Committee oversees corporate policies and strategies related to human resources, and reviews and approves the principles governing recruitment, selection, training, compensation and evaluation. The committee is responsible for reviewing succession planning for the leadership of the Corporation and makes recommendations to the Board regarding the organizational plan, the compensation plan, and the integration of human resources policies and strategies into the corporate plan.

During the year, the committee received an overview of CMHC's demographic profile and reviewed the results of the Corporation's environmental scan. The committee also participated in the update of CMHC's succession management framework to ensure the implementation of effective succession management plans for all critical positions within the Corporation.

Nominating Committee

The Nominating Committee was created in 2004 pursuant to new governance guidelines issued by the federal government. The committee identifies, evaluates and recommends a shortlist of qualified candidates for the Chairman position and the CEO position to the Board for subsequent recommendation to the Minister for appointment by the Governor in Council. The Nominating Committee also advises the Board on matters relating to the composition of the Board and its committees, as well as the criteria for Board membership including experience, attributes and skills. The Committee reviews the existing Board composition on a yearly basis, anticipates openings, reviews skills profiles and advises the Board on recommended changes or procedures.

In 2005, the Committee successfully completed the selection process to fill the vacant Chair position. Following the new process for Governor in Council appointments to Crown corporations, the Committee presented a short-list of candidates to the Minister. The government subsequently announced their intent to appoint Mr. Chiesa to the Chair position. Based on new procedures, the appointment was referred to the Standing Committee on Government Operations and Estimates for review. Mr. Chiesa appeared before the committee prior to the finalization of his appointment in March 2005.

Pension Fund Trustees

The Pension Fund Trustees are responsible for the management and administration of the Pension Fund pursuant to the Trust Agreement. In this function, the Trustees are responsible for setting investment policies and objectives, selecting external investment managers, and monitoring the investment results of the Pension Fund. The Trustees report to the Board of Directors on the performance of the Pension Fund, submit the Pension Plan Annual Report for approval, and recommend changes to the overall investment philosophy of the Pension Fund.

In the past year, the Trustees approved strategies to diversify investments in US equities, and the selection of an external manager to manage a portion of these investments. The Trustees also reviewed the Pension Fund's performance through quarterly reports and appointed an actuary to conduct the actuarial valuation of the Pension Plan as at the end of 2005.

Table of Directors' total compensation and attendance at meetings of the Board, and of Board Committees in 2005

Board Member	Total compensation (fees and honorarium) (\$)	Board of Directors (6 meetings)	Audit Committee (4 meetings)	Governance Committee (2 meetings)	Human Resources Committee (3 meetings)	Nominating Committee (1 meeting)	Pension Fund Trustees (3 meetings)
Dino Chiesa ¹	64,250	6/6		2/2		1/1	
Karen Kinsley	n/a	6/6					3/3
Michel Bérubé ²	7,557	1/2			0/1		
Harold Calla ³	13,673	3/3		1/1			
Catherine Cronin	31,200	6/6	4/4				3/3
Roberta Hayes	31,700	6/6			3/3	1/1	
Hugh Heron ⁴	33,200	6/6	3/3				
Sophie Joncas	34,700	6/6	4/4		2/2		
Grace Kwok ⁵	6,600	2/3		0/1			
Gary Mooney ⁶	13,174	3/3	1/1				
Louis Ranger	n/a	2/6			1/3		
Alexander Werzberger ⁷	15,143	3/4		1/1			

n/a — not applicable as members from the public service are not paid for their service

¹ Chairperson, effective March 2005

² Term ended 13 April 2005

³ Appointed on 2 June 2005

⁴ Audit Committee membership ended fall 2005

⁵ Term ended 1 June 2005

⁶ Appointed on 2 June 2005

⁷ Appointed on 14 April 2005

Travel and hospitality expenses of senior executives are posted on CMHC's website, www.cmhc.ca.

FOCUS ON VALUES AND ETHICS

CMHC has a proud past of service to Canadian society, a longstanding tradition founded on the strong values that have guided our employees since we first opened our doors 60 years ago. We know that our values are one of the strengths of our Corporation. We also know that our future success will depend on our ability to ensure that our values continue to live and flourish. With this in mind, CMHC launched a values and ethics program through the fall of 2004 and spring of 2005.

Our values and ethics program is driven by two objectives: to create an environment where an honest, open dialogue on ethical issues is welcomed and encouraged; and, to help employees feel confident that the decisions they make everyday while fulfilling their responsibilities are consistent with the values of the Corporation and of Canadians.

Ultimately, our shared values, and how we engage employees in these values, are the means through which we ensure that our governance and accountability practices are transacted throughout the Corporation and reflected in all our activities.

OUR STATEMENT OF VALUES

First launched in 2004, the *Our Statement of Values* document was developed through extensive consultation with CMHC employees. Dialogue sessions were held in each region of the country, with individuals working in a wide range of capacities within each of the corporate functional areas. The statement of values was derived directly from the employee dialogue that took place during these sessions, and was confirmed by the senior management team and the Board of Directors. Thus, we are confident that the statement represents who we are — as individuals and as a corporate entity — and articulates what is and should be important in everything we do. The Board, senior management and employees signed the *Our Values in Action* document, committing to live the values in carrying out our various functions and responsibilities.



OUR VALUES IN ACTION

As a result of our long-standing commitment to ethical conduct, CMHC has developed, over time, numerous policies on a wide range of issues related to corporate values and ethical conduct. To assist our employees in understanding the full breadth of CMHC policies and guidelines, the *Our Values in Action* tool was developed as the primary corporate reference for information and assistance in guiding employee conduct. The document provides policy guidance by summarizing the intent of the various policies, and it elaborates on CMHC values through practical case studies that were designed to assist employees in defining acceptable behaviour in a public sector environment. *Our Values in Action* provides guidance on six key areas related to the three corporate values: serving the public interest; preserving the public trust — gifts, hospitality, and invitations; managing sensitive information; fraud and other illegal activities; managing people, workload and work life balance; and managing relationships with others.

INTERNAL DISCLOSURE OF WRONGDOING IN THE WORKPLACE

To complement our suite of ethics tools, we have put in place a policy on internal disclosure of wrongdoing in the workplace. The intent of the policy is to provide employees with an internal process to bring forward information concerning wrongdoing in the workplace, and to ensure that employees are treated fairly and are protected from reprisal when reporting in good faith. Procedures have been established to enable employees to disclose wrongdoing related to a violation of any law or regulation; a misuse of public funds or assets; gross mismanagement; as well as a substantial and specific danger to the life, health and safety of employees, the public or the environment.

ETHICS AWARENESS

To assist employees in living up to the commitments implied through *Our Statement of Values*, all employees were required to attend an ethics awareness session. In addition to introducing the corporate statement of values and the related *Our Values in Action* resource, the sessions were designed to engage employees in a dialogue, through the use of pertinent case studies, to help them understand the relationship between values, judgement and action. To date, 98% of CMHC employees have participated in an ethics awareness session.



In 2005, we introduced a number of initiatives to further integrate the principles of business ethics into programs and training tools. An ethics module that focuses on the role of leaders in fostering dialogue on ethics in the workplace was added to the Fundamentals of Effective Leadership program for first-line supervisors, aspiring supervisors and project leaders. In addition, employees now have access to ethics resources, including *Our Statement of Values*, and *Our Values in Action*, on the corporate intranet, thus ensuring continued awareness of business ethics among our employees.

NEXT STEPS

In 2006, CMHC will continue to encourage awareness of ethics in the workplace by introducing several new initiatives, including ethics awareness sessions for new employees, lunch and learn sessions, and new case studies. In addition, the launch of conflict resolution workshops for managers and employees in 2006 will provide tools to help us deal with conflict in a respectful, understanding and open manner.

BOARD OF DIRECTORS LISTING (as at 31 December 2005)

Dino Chiesa

Chairman of the Board

Mr. Chiesa is Vice-Chair of the Board of Trustees of CAP REIT, one of Canada's largest owners of multi-family rental communities. Prior to this, he was the President and CEO of RESREIT, Assistant Deputy Minister of Ontario's Ministry of Municipal Affairs and Housing, and CEO of the Ontario Housing Corporation and Ontario Mortgage Corporation, and a CMHC employee from 1975 to 1987. He has been a member of the Board since June 2001 and was appointed Chairman of the Board of Directors in March 2005.

Karen Kinsley, CA

President and Chief Executive Officer

Karen Kinsley joined CMHC in 1987, has held a variety of positions in senior management, and was appointed President and Chief Executive Officer in June 2003.

Harold Calla, CGA, CAFM

North Vancouver, British Columbia

Harold Calla holds a number of positions with the Squamish Nation, including Chair — Economic Development/Land Management, Treaty Committee member, and Chair of the Finance Sub-committee. He was appointed to the Board of Directors in June 2005.

Catherine C. Cronin, CA

Winnipeg, Manitoba

Catherine Cronin is a chartered accountant who is currently active in several community organizations in the Winnipeg area. She was appointed to the Board of Directors in September 2003.

Roberta Hayes

Moncton, New Brunswick

Roberta Hayes is co-owner and manager of HomeLife Hayes Realty. Ms. Hayes was formerly the President and a director of the Greater Moncton Real Estate Board, as well as a director of both the New Brunswick Real Estate Association and the Canadian Real Estate Association. Roberta Hayes was appointed to CMHC's Board of Directors in October 2003.

Hugh Heron

Schomberg, Ontario

Hugh Heron is Principal and Partner of the Heron Group of Companies and President of Heron Homes Corporation. He is a past president of both the Toronto Home Builders' Association and the Ontario Home Builders' Association. Mr. Heron was appointed to the Board of Directors in June 2001.

Sophie Joncas, CA

Saint-Hubert, Quebec

Sophie Joncas is an accounting practitioner and an Administrator with Production Quarters, a television production company, and is a professor of economics and finance at the Académie de l'entrepreneuriat québécois inc. Ms. Joncas has served on the Board of Directors since August 2001.

Gary Mooney

Mississauga, Ontario

Gary Mooney is President and Chief Operating Officer of Fidelity National Financial, and a senior partner with the law firm Anderson, Sinclair. He was appointed to the Board of Directors in June 2005.

Louis Ranger

Ottawa, Ontario

Louis Ranger is Deputy Minister of Transport, Infrastructure and Communities. He was appointed to the Board of Directors in September 2002.

Alexander Werzberger

Outremont, Quebec

Mr. Werzberger is currently the President of Traklin Groups. He has served on the Board of Directors of various organizations, including the Association provinciale des constructeurs d'habitations du Québec and the Association de la construction du Québec. Mr. Werzberger was appointed to the Board of Directors in April 2005.

PERFORMANCE AGAINST OBJECTIVES

Help Canadians in Need

Facilitate Access to More Affordable, Better
Quality Housing for All Canadians

Ensure the Canadian Housing System Remains
One of the Best in the World

Business Highlights and Outlook (10 Years)

PERFORMANCE AGAINST OBJECTIVES

The 2005 Annual Report represents the conclusion of CMHC's 2005 corporate planning cycle. The report ensures that progress on planned activities is tracked and that managers are accountable for performance results against plans in the 2005–2009 Corporate Plan — CMHC's key planning document. In 2005, CMHC's corporate objectives and strategic priorities, which represent our public policy purpose, were recast to better reflect ongoing business and key client groups and to facilitate enhanced alignment of CMHC's business and financial plans. The 2005 Annual Report presents the corporate results based on the enhanced planning framework presented below.

Objective One **HELP CANADIANS IN NEED**

- 1.1 Help Canadians in need to access safe, affordable housing
- 1.2 Improve living conditions for Aboriginal Canadians

Objective Two **FACILITATE ACCESS TO MORE AFFORDABLE, BETTER QUALITY HOUSING FOR ALL CANADIANS**

- 2.1 Ensure Canadians have access to mortgage insurance products and tools that meet their needs
- 2.2 Enhance the supply of low cost funds for mortgage lending by expanding the securitization program
- 2.3 Provide comprehensive, timely and relevant information to enable Canadian consumers and the housing sector to make informed decisions

Objective Three **ENSURE THE CANADIAN HOUSING SYSTEM REMAINS ONE OF THE BEST IN THE WORLD**

- 3.1. Ensure Canada's housing system remains one of the best in the world
- 3.2 Support and promote Canada's world-class housing products, services and system internationally
- 3.3 Ensure that CMHC remains a strong organization able to fulfill its mandate

Objective One

HELP CANADIANS IN NEED



For 60 years, we have been helping provide a place to call home to hundreds of thousands of low-income families across the country. We have also been striving to close the housing gap faced by Aboriginal Canadians. We are proud of our legacy of programs and policies that have helped Canadians access safe, affordable housing. And we will continue to support needy families through our programs and initiatives to help ensure that all Canadians share in the benefits of living in a safe, affordable home.

RESOURCES

\$56.2 million in operating expenses
387 Staff Years

I.1 Help Canadians in Need to Access Safe, Affordable Housing

■ WHAT WE DO

Together with our public and private partners, we help low or modest income Canadians access high quality, safe and affordable homes.

■ WHY IT MATTERS

By helping to provide access to affordable housing, our efforts help to improve the quality of life of hundreds of thousands of Canadians.

■ HOW WE GET IT DONE

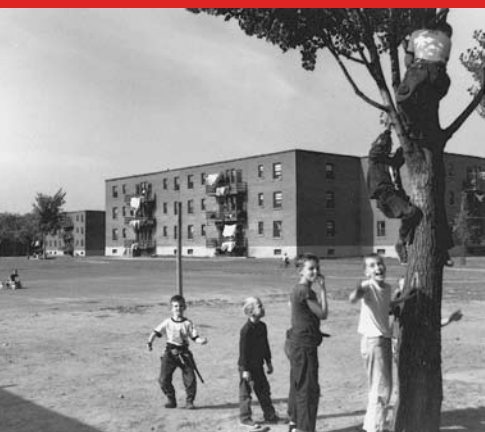
We provide funding to, and work with the provinces, territories and others to increase the supply of affordable housing.

We provide support and financial tools that help communities sponsor their own affordable housing projects.

We provide funding for renovations to preserve the supply of housing for low income households.

We subsidize existing social housing units.

We increase understanding of the distinct housing needs of at-risk population groups.



1946

CMHC builds Benny Farm in Montréal – one of the first subsidized housing developments in Canada and the largest at the time.

CMHC TOOLBOX

We draw on the following tools to achieve this strategic priority:

Affordable Housing Initiative

Flexible options for provinces and territories, including:

- New rental housing
- Home purchase
- Homeownership preservation
- Rental preservation
- Rent supplements

Renovation Programs

- Residential Rehabilitation Assistance Program
- Emergency Repair Program
- Home Adaptations for Seniors' Independence
- Shelter Enhancement Program

Public-Private Partnerships

- Seed funding
- Proposal development funding
- Advice and skills development
- Mortgage loan insurance flexibilities

Housing Subsidies Under Past Commitments

- Public housing
- Non-profit housing
- Rental supplement
- Co-operative housing

Direct Lending

For additional information on CMHC's programs and services, visit our website, www.cmhc.ca

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

1.5 Million Canadians are Currently in Need of Suitable or Affordable Housing

In 2001, 86% of Canadian households could afford to live in housing that was uncrowded and in a good state of repair.¹ However, there remained 1.5 million Canadian households, or about 14% of the population, who were in core housing need.² Recent immigrants, lone-parents, unattached individuals and Aboriginal people are more likely than other Canadians to be in core housing need.

Housing Need Has a Strong Income Dimension

For households in the lowest income bracket (\$10,000 and less), income completely determines their housing circumstances. The majority of these households (80%) were in core housing need. Most often, households in need cannot look to accumulated wealth to address their own housing needs because they do not have sufficient income to afford housing at market rents.

Governments Have Been Re-investing in Affordable Housing

The existing federally assisted social housing stock provides homes for some 633,000 families and individuals. Over the next 30 years, the operating agreements on these projects will be expiring and this could impact the supply of housing available to meet the needs of low-income Canadians and ultimately affect the number of households in need.

Recently, government investment in affordable housing has been on the rise. Since 2001, \$1 billion has been committed by the federal government under the Affordable Housing Initiative (AHI), a cost-sharing initiative with the provinces and territories. The initiative was announced in two phases: an initial investment of \$680 million in 2001 and an additional \$320 million in 2003. In total, the AHI is expected to make available 44,000 affordable housing units for those in need.

Funding Allocation Under the Affordable Housing Initiative

Province	Provincial Allocation (\$ millions)
Newfoundland	20.5
Prince Edward Island	4.2
New Brunswick	22.6
Nova Scotia	28.1
Quebec	236.5
Ontario	366.3
Manitoba	36.9
Saskatchewan	33.0
Alberta	98.6
Northwest Territories	7.9
British Columbia	130.4
Yukon	5.8
Nunavut	5.2
Administrative costs	4.0
Total	1,000.0

There is a Growing Recognition That Housing is Central to Health and Well-being

The importance of addressing housing need as a means of improving quality of life is reflected in the role of good housing as a basis for achieving other social policy objectives — health, strong communities, and secure environments for children.

While low income remains a large barrier to accessing adequate housing for most, differences in the housing and income circumstances of households in core housing need call for wide-ranging strategies. Moreover, some people, including recent immigrants and people living with disabilities, have special needs associated with their life circumstance that require more than just a housing response. Despite recent investment in affordable housing, many urban centres are continuing to report increases in homelessness. A holistic approach is therefore needed to ensure that housing is linked to necessary supports and services, and is tailored to reflect differing local needs.

1. Based on 2001 census estimates.

2. A household is in core housing need if its housing does not meet standards for affordability, adequacy or suitability and it would have to spend 30% or more of its income for housing that meets all three standards.

ANALYSIS OF OUR PERFORMANCE

We Helped Increase the Supply of Affordable Housing

To increase the supply of affordable housing, the Government of Canada is investing \$1 billion by the end of 2010–2011, through the Affordable Housing Initiative (AHI).

The development of new housing under the AHI has lagged behind target since the program's inception. As a result, CMHC undertook a series of discussions with our provincial and territorial partners in 2004 to identify challenges and find solutions that would enable more rapid progress in establishing agreements and developing housing. In late 2004 and early 2005, additional flexibilities were announced related to the AHI, including making rent supplement programs eligible for funding. This led to rapid progress in finalizing the Phase II AHI agreements, and stimulated the development of more affordable housing.

At the end of 2005, agreements with all 13 provincial and territorial jurisdictions have been signed and the production of affordable housing units is on track. Expenditures related to the AHI in 2005 were targeted at \$175 million and came in on plan.

To date, about 25,000 units were committed or announced under the initiative compared to an expected volume of just under 26,200 units, reflecting higher than planned production costs. Program activity levels have varied by jurisdiction reflecting the differing status of program roll-out across the country. CMHC will continue to work with its provincial and territorial partners to encourage timely take-up of funding and increased affordable housing supply.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Affordable Housing Initiative expenditures (\$ millions)	173	175	175*	159

* Target met or exceeded

* Target substantially met

† Target not met

OUR STRENGTHS

- Pre-eminent research program leading to an in-depth understanding of housing needs of a diverse population.
- Well established relationships with federal, provincial, municipal governments and housing stakeholders.
- History of effectively delivering diverse housing programs to Canadians.
- Ability to introduce new and enhanced programs that address the evolving needs of Canadians.

CHALLENGES AND RISKS

- Managing heightened expectations emanating from an increased focus on housing issues by the public, media and government.
- Developing and realizing housing solutions for Canadians in need.
- Continuing to effectively manage the varied and complex processes and systems controlling delivery and administration of housing programs.

NEXT STEPS

- Research the role of housing and communities in the successful integration of newcomers to Canadian society, and researching methods to improve access to housing options for homeless people.
- Maximize timely production of units under the Affordable Housing Initiative.
- Explore policy options to address the issues associated with the aging of the existing social housing stock and the planned expiration of the operating agreements.

We Helped Communities Sponsor Their Own Affordable Housing Projects

CMHC recognizes that no two communities are alike and that housing solutions are as varied as the housing challenges they address. That is why CMHC offers an innovative package of tools, with a range of customizable options, designed to facilitate the production of affordable housing through partnerships by meeting the specific needs of individual housing projects.

In 2005, partnerships led to the creation of 2,378 affordable housing units. This volume is 46% higher than planned largely due to accelerated project schedules, but significantly lower than 2004 results, reflecting a change in measurement practice by which CMHC more precisely measures its role in facilitating the units.

CMHC approved mortgage insurance applications for 1,640 public-private partnership units, which while significantly above target, reflects the overall greater volume through the Partnership Centre.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Public-Private Partnership units facilitated	n/a	1,625	2,378*	1,470
Mortgage insurance approvals of public-private partnership (units)	n/a	1,030	1,640*	1,250

* Target met or exceeded * Target substantially met † Target not met

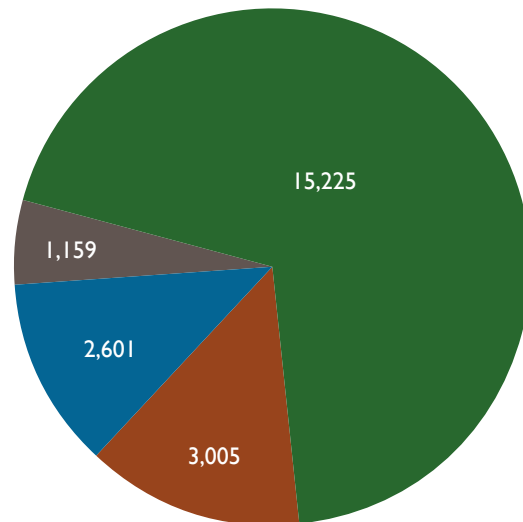
n/a not applicable due to new methodology adopted in 2005.

We Helped Maintain the Existing Supply of Housing For Low To Moderate Income Canadians

CMHC's renovation programs help low-income households, persons with disabilities and Aboriginal people bring their homes up to minimum health and safety standards, repair shelters for victims of family violence, and support home adaptations for low-income seniors so they can live independently for as long as possible. Over 750,000 households have benefited from CMHC's renovation and repair programs, since their inception more than 30 years ago.

In 2005, we provided funding assistance to almost 22,000 households, 2% behind our target of 22,509 housing units. This is slightly lower than 2004, which was an exceptionally strong year, since the timing of a program extension shifted a good deal of activity into the first quarter of 2004. In addition, higher costs for building materials and labour also contributed to a higher average cost per unit when compared to last year, affecting the level of production in 2005.

Our renovation programs helped almost 22,000 households in 2005



- Shelter Enhancement Program
- Emergency Repair Program
- Home Adaptations for Seniors' Independence
- Residential Rehabilitation Assistance Program

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Renovation Programs (units) ¹	25,539	22,509 (+/-5%)	21,990*	19,054 ²

* Target met or exceeded * Target substantially met † Target not met

¹ Renovation Programs include the Residential Rehabilitation Assistance Program, Home Adaptations for Seniors Independence, the Emergency Repair Program and the Shelter Enhancement Program.

² Revised following November 2005 announcement of one-year extension of the renovation programs.

A portion of CMHC's Residential Rehabilitation Assistance Program is dedicated to the renovation of affordable rental properties. In 2005, eligibility for this program was also expanded to include the creation of secondary suites and garden suites to accommodate seniors and disabled adults. This now provides an additional housing option, enabling this client group to remain in their communities and close to their family and social network.

The 2005 fourth quarter announcement of a one-year extension of \$128.1 million in funding for the renovation programs will permit more than 19,000 households to be assisted in 2006.

Through Our Investment in Social Housing, We Continued to Help Many Canadians in Need

As a result of many years of social housing program delivery through CMHC, Canada's existing stock of federally supported social housing assists over 633,000 lower-income Canadian families each year. We also supported social housing sponsors by providing low-cost funding to those sponsors seeking to refinance their existing social housing projects. These loans provide non-profit groups with funds at the best possible interest rates, thereby reducing costs they would otherwise have to carry.

We Facilitated the Start-up of The Agency for Co-operative Housing

In 2005, CMHC and The Agency for Co-operative Housing concluded an agreement for the agency to begin providing portfolio management services for federally administrated co-operative housing projects in BC, Ontario, Alberta and PEI in 2006. Under the Agreement, the Agency will provide services on a not-for-profit, fee-for-service basis. It will also offer a new risk-based, client-focused approach to service delivery which, over time, is expected to contribute to the viability and health of the co-operative housing portfolio. CMHC will continue to be responsible for program policy and for the administration of federal funds. In 2006, CMHC will continue to work closely with the Agency to ensure a smooth transition to the new arrangements.



In the early days, CMHC was heavily involved in the design and construction of public housing projects delivered by the provinces under joint funding arrangements to maximize resources and create more housing. The strong spirit of collaboration developed over six decades continues to bring success today as we celebrate the achievement of having completed the signing of all agreements with the provinces and territories under the Affordable Housing Initiative. Through 2006 and beyond, we will continue to work with our partners to develop the best possible options for effective, efficient delivery, looking at flexibilities and innovations, and bringing together the best mix of partners and expertise to deliver solid benefits to low-income Canadians.

I.2 Improve Living Conditions for Aboriginal Canadians

■ WHAT WE DO

We work with Aboriginal organizations to resolve Aboriginal housing issues.

■ WHY IT MATTERS

For the Aboriginal population, housing needs are urgent. We are working with Aboriginal groups to close the gap faced by Aboriginal Canadians in the area of housing.

We support the development of skills, markets and institutions that increasingly permit Aboriginal people to direct and control their own housing.

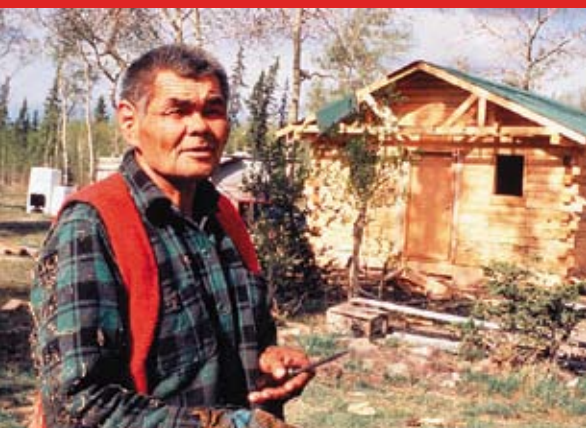
■ HOW WE GET IT DONE

We represent the Government of Canada in consultations and negotiations to improve Aboriginal housing conditions.

We provide funding and partner with First Nations, Indian and Northern Affairs Canada, and others on housing assistance programs, construction of new housing and renovations to existing housing.

We offer innovative financing techniques to stimulate market conditions on reserve.

We share our housing knowledge and expertise with Aboriginal home occupants and industry participants to increase Aboriginal housing capacity.



1978

Non profit Housing Program is delivered for the first time on-reserve.

CMHC TOOLBOX

We draw on the following tools to achieve this strategic priority:

Social Housing

- On-Reserve Non-Profit Rental Housing

Housing Subsidies Under Past Commitments

- Rural and Native Housing
- Urban Native Housing Program

Mortgage Loan Insurance On-Reserve

- Homeownership On-Reserve with Ministerial Guarantee
- Homeownership On-Reserve Without Ministerial Guarantee

Capacity Development

- Housing Internship for First Nations and Inuit Youth
- Inspector training
- Home occupant training
- Support for organizations such as the First Nations National Building Officers Association

Renovation Programs

- Residential Rehabilitation Assistance Program
- Home Adaptations for Seniors' Independence
- Shelter Enhancement Program

For additional information on CMHC's programs and services, visit our website, www.cmhc.ca

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

Aboriginal People Face Some of the Worst Housing Conditions in Canada

Aboriginal people living on- and off-reserve are much more likely than other Canadians to be in core housing need due to problems of overcrowding. According to the latest available Census data, 22.5% of on-reserve households live in inadequate housing and are unable to afford acceptable housing, while 10.3% live in crowded conditions.

The housing shortage faced by First Nations, Métis and Inuit people continues to grow despite efforts by CMHC and Indian and Northern Affairs Canada. The estimated shortage of housing on-reserve is between 20,000 and 35,000 units, where an additional 4,300 units are needed annually to meet the requirements of new households.³ This undersupply has resulted in severe overcrowding on reserve, which accelerates the deterioration of housing and related infrastructure, and affects the health and social well-being of occupants.

Problems are intensified in the North where subsidized rental housing comprises the majority of the housing stock. With high unemployment rates and high construction and operating costs, a large portion of the northern population relies on assisted housing. The accelerated deterioration of the housing stock due to overcrowding is made worse by the severe northern climate.



1971

CMHC introduces Winter Warmth, its first assistance program directed to Aboriginal people, to provide funds for making urgent repairs to housing in rural areas.

3. *Indian and Northern Affairs Canada*

The Challenges in Addressing Aboriginal Housing Need are Significant

Aboriginal households face tremendous challenges in accessing adequate housing. The challenges include low income and high unemployment, as well as regional characteristics such as remoteness and harsh climate conditions that contribute to high construction costs. Legal barriers to homeownership on reserves and the need to coordinate various federal, provincial and territorial players also undermine efficiency in the Aboriginal housing system. Further compounding the shortage of housing is the rapid growth of a young Aboriginal population, contributing to an increase in new household formations and a growing need for housing solutions. Rising building costs are further hampering efforts to alleviate housing need on reserve, particularly in the North. In 2005, builders faced shortfalls in skilled tradespeople and rising construction costs that were due to higher building material and energy costs.

Creating a New Vision for Aboriginal Housing

Our ability to address these challenges would be helped by increased Aboriginal control and management over housing, new approaches that encourage market solutions and homeownership, and enhanced partnerships including with other levels of government.

As a short-term measure to help address the backlog on reserve and stabilize the current housing conditions for First Nations, the 2005 federal budget provided \$295 million over five years. Long-term solutions for on- and off-reserve Aboriginal housing are being developed as part of the Aboriginal Peoples Roundtable follow-up process and the fall 2005 First Ministers' Meeting on Aboriginal Issues, where housing was one sector identified for further policy development. A key message heard throughout the Canada-Aboriginal Peoples Roundtable follow-up process and preparations for the First Ministers' Meeting was the need for increased Aboriginal capacity and empowerment in developing housing solutions as a means to strengthen Aboriginal self-reliance. There was also a general acknowledgment of the need to strengthen relationships among federal, provincial, territorial and Aboriginal partners to work collaboratively on Aboriginal housing solutions. Recent discussions have focused on a vision for increased Aboriginal control over housing and the need to work collaboratively on developing a new Aboriginal housing system.

ANALYSIS OF OUR PERFORMANCE

We Played a Lead Role in Shaping Policy for an Aboriginal Housing Strategy

In 2005, CMHC played a key role in shaping an Aboriginal housing strategy through immediate improvements to policy and programs and through longer-term policy proposals. We worked to build consensus within government and with national Aboriginal organizations on the direction forward for Aboriginal housing. The resulting Aboriginal housing directions gained widespread support and formed the basis of the agreement reached at the First Ministers' Meeting in November 2005.

CMHC worked closely with Aboriginal organizations and provinces and territories to identify sustainable approaches to addressing Aboriginal housing needs and develop the necessary indicators to measure success. These discussions strengthened relationships between federal, provincial and territorial governments, and Aboriginal leaders who committed to working together to improve Aboriginal housing conditions.

Further to the progress made at the First Ministers' Meeting, governments and Aboriginal organizations have expressed a willingness to continue to work together to achieve solutions for Aboriginal housing.

We are also continuing to support the development of indicators and data for assessing and tracking progress in Aboriginal housing. CMHC has signed memoranda of understanding with the First Nations Statistical Institute which will officially open its doors in April 2006, and the National Aboriginal Economic Development Board established in 1990 by Order-in-Council. CMHC will assist the First Nations Statistical Institute in mapping available housing information and will sit on a government advisory board to help the National Aboriginal Economic Development Board select and develop the indicators to be included in its National Aboriginal Benchmarking Report, to be published in 2006.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
On-reserve non-profit new commitment (units)	978	892	1,045*	4,007

* Target met or exceeded † Target substantially met ‡ Target not met

We Made an Immediate Investment in On-reserve Housing to Reduce or Eliminate the Growth in the Shortfall of Housing On Reserve

CMHC undertook the operational planning necessary to deliver on the additional funding announced through the February 2005 budget. A new allocation model based on need was developed and a delivery framework was put in place to ensure that increased government funding will be delivered within overall time frames.

This investment has the potential to triple the number of new units created on reserve over two fiscal years (2005/06 and 2006/07) and provide a 50% increase in the number of units renovated. In 2005, 1,045 new on-reserve housing commitments were made, exceeding our target by 17%. In order to narrow the gap in housing between Aboriginal people and other Canadians, the target for 2006 is set at 4,007 units. In addition to new construction, funding for the renovation and repair of 1,275 units on reserve was provided through the Residential Rehabilitation Assistance Program, exceeding our planned target of 884 on-reserve units by 44%.

We Supported the Establishment of Market Housing or Market-like Conditions On Reserve

CMHC worked to find ways to better use mortgage insurance products to facilitate access to private financing on reserve and to promote homeownership. A renewed focus was placed on promoting the new on-reserve homeownership loan insurance pilot product during 2005 and overcoming those barriers identified by First Nations as preventing them from taking advantage of the pilot. This renewed focus was successful. The historic first signing of an agreement under this pilot occurred with the Nak'azdli First Nation in BC, and there was significant movement towards future signings with other First Nations. The pilot will expand homeownership on reserve, fuel new home construction and renovations, as well as create employment and business opportunities on reserve. We will continue to work closely to implement the pilot with First Nations within all regions of the country in 2006.

Research into alternate land tenures on reserve, including the land designation process under the *Indian Act* and the *First Nations Land Management Act*, was also initiated. A second research project looking at homeownership on reserve and possible models that would promote best practices was initiated during the year and will be finalized in 2006.

We Shared Our Knowledge and Expertise and Helped Build Aboriginal Housing Capacity

CMHC is committed to developing a strong and effective Aboriginal housing system that will build Aboriginal capacity in areas such as land administration and housing and financial management. For Aboriginal home occupants, we work to raise the profile of indoor air quality and provide information on methods for improving housing and reducing the occurrence of mold to support the health and well-being of occupants.

In 2005, efforts to further assist the First Nations National Building Officers Association (FNNBOA) in developing the professional certification model that was implemented in 2005 have resulted in an increased profile for the organization. FNNBOA has formed formal partnerships with provincial government agencies such as the Alberta Safety Code Council and the Ministry of Municipal Affairs and Housing in Ontario. FNNBOA's profile was raised in 2005 when they were invited to do a presentation to the Senate Standing Committee on Aboriginal Economic Development.

Overall, the percentage of on-reserve programs and services delivered through First Nation or Aboriginal organizations exceeded its target by almost 12%. This is attributable to the successful recruitment of Aboriginal organizations for the delivery of RRAP in British Columbia as well as the recruitment and development of Aboriginal service providers for the delivery of training related to the Housing Quality Initiative for First Nations.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Delivery of on-reserve programs and services through First Nation or Aboriginal organizations (%)	89.2	80.0	89.3*	80.0

* Target met or exceeded * Target substantially met † Target not met

OUR STRENGTHS

- Extensive experience in delivering high quality, durable housing to First Nations communities.
- Efficiencies and enhancements in Aboriginal program administration and delivery resulting from the implementation of recommendations from the Auditor General's review in 2003.
- Awareness of Aboriginal housing needs developed through comprehensive research programs and first-hand experience in program delivery.
- A long history of skills transfer and capacity development.

CHALLENGES AND RISKS

- Assisting in the development of an efficient housing system on- and off-reserve, as well as in the North, given the system of collective land ownership on reserve, the lack of traditional mortgage security, and other social and economic challenges.
- Meeting the need to build increased capacity.
- Addressing the housing shortage on reserve, ensuring durable construction of new and existing housing, and reducing the incidence of mould in on-reserve housing.

NEXT STEPS

- Increase the understanding of Aboriginal trends and issues.
- Work with territories, provinces and Aboriginal groups to address distinct housing needs.
- Encourage adoption of market-based solutions where feasible and desired by the First Nations, including improving access to private sector financing, and homeownership on reserve.

We Made Organizational Changes to Better Address Severe Housing Need in the North

A wide range of barriers and impediments to meeting housing need and promoting sustainable development exist in the North, including extremely high cost of construction, limited technical capacity and fewer proven technologies for northern climates, as well as a range of social and economic issues.

In August 2005, in recognition of the level of need and the distinct issues faced in the North, CMHC created a new office within the Prairies and Territories region that has a distinct focus on northern housing. This new structure allows CMHC to better serve our partners, clients and stakeholders in the three northern territories. With extensive research and experience in dealing with northern housing issues, CMHC is well positioned to provide the support and advice required by northern stakeholders. CMHC's new northern housing office will manage the diverse and growing housing interests of the North and will focus on the unique challenges in bringing innovative housing solutions to this area. This focus better positions CMHC to help northern residents develop the plans necessary to increase housing supply. CMHC will also be in a better position to help northern communities take advantage of economic development opportunities, such as the Mackenzie Valley Pipeline, in addressing housing need.

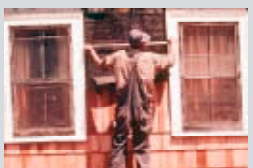


**PROUD PAST
BRIGHT FUTURE**

CMHC's contribution to improving the housing and living conditions of Aboriginal Canadians began in 1971 with the delivery of programs such as Winter Warmth Assistance and the Rural and Native Housing program, to fund urgent repairs to homes or to buy or build housing for low-income people in rural areas. Addressing the housing needs of Aboriginal Canadians continues to be a key focus for CMHC. We are starting to introduce innovative market tools to create more private market-like housing conditions on reserve. In 2005, we signed the first on-reserve Homeownership Loan Insurance pilot agreement with the Nak'Azdli Band council of northern British Columbia, and we are pursuing agreements with other interested bands across Canada. In 2006, we will continue to work with the Aboriginal community and a host of government and private partners to bring about the long-term transformational change needed to improve the living conditions of Aboriginal Canadians.

Objective Two

FACILITATE ACCESS TO MORE AFFORDABLE, BETTER QUALITY HOUSING FOR ALL CANADIANS



Thanks to the 60 year legacy of CMHC's programs, policies and initiatives, Canadians are among the best-housed people in the world. Since 1954, when we began our mortgage loan insurance program, CMHC has provided mortgage loan insurance on every one in three Canadian homes, helping make it possible for many Canadians to buy a home sooner or find affordable rental accommodation.

Today we continue that legacy by helping housing finance markets function effectively so that most Canadians are housed without direct government assistance. In order to maintain a well-functioning housing system, we facilitate access to affordable mortgage financing and ensure that an abundant supply of low-cost funds is available in the residential mortgage market. We also provide quality information to Canadian consumers and housing sector participants so that they can make well-informed housing choices.

RESOURCES

\$115.8 million in operating expenses

731 Staff Years

2.1 Ensure Canadians Have Access to Mortgage Insurance Products and Tools That Meet Their Needs

■ WHAT WE DO

We offer a wide range of mortgage insurance products to meet the needs of the financial services industry and consumers alike.

■ WHY IT MATTERS

Our mortgage insurance products lower the costs of homeownership for Canadians with less than a 25% down payment, allowing them to own a home sooner than would otherwise be possible.

Our mortgage insurance helps landlords and developers access low-cost financing, which benefits Canadians by ensuring that more accommodation is available for renters.

■ HOW WE GET IT DONE

We protect mortgage lenders from borrower default through our mortgage insurance products. This leads to interest rate reductions for homebuyers, even with a down payment as low as 5% of the value of the home.

We serve all parts of the country, including areas that the private sector is less inclined to serve.

We operate our mortgage insurance business in a commercial environment, on a fair and competitive basis, thereby helping to ensure fair pricing and innovative product development.



1954

Mortgage loan insurance is created to make homeownership more accessible to Canadians.

CMHC TOOLBOX

We draw on the following key mortgage insurance products to achieve this strategic priority:

Homeowner

- Purchase
- Refinance
- Flexible Down Payment
- Purchase Plus Improvements
- Lines of Credit
- Second Homes
- Mortgage Loan Insurance for Energy-Efficient Homes
- Homebuilder Progress Advance
- Mortgage Insurance products for purchase of mobile homes

Rental

- Rental Purchase
- Rental Refinance
- Mortgage Loan Insurance for Energy-Efficient Rental Units
- Floating Rate for CMHC Insured Rental Mortgages

For additional information on CMHC's programs and services, visit our website, www.cmhc.ca

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

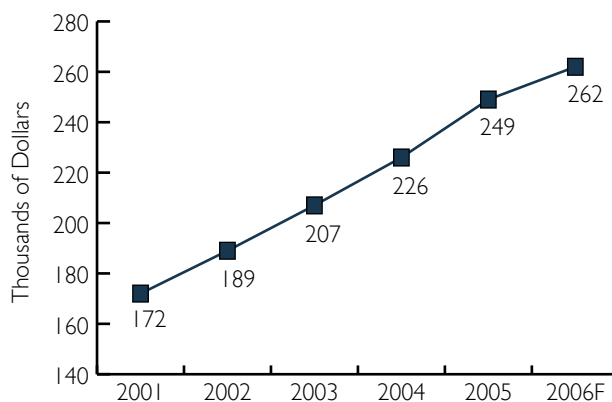
Economy and Housing Market Trends

Successive years of very strong housing markets have contributed to strong business volumes for the Corporation, with 2005 being no exception. The robust performance of the housing market in 2005 was based on underlying strength in the economy, such as employment growth and low interest rates. Housing markets will remain strong by historical standards in 2006, but will begin a gradual decline as the pent-up demand that helped drive the market over the past several years has largely been met. Rising mortgage carrying costs, due to recent home price increases and rising interest rates, will also temper demand for homeownership, particularly among first-time homebuyers.

Housing Finance Industry is Increasingly Focused on Gaining Competitive Advantage

New lenders, including subsidiaries of foreign institutions and non-regulated financial institutions focusing on niche markets, are expected to continue entering the Canadian marketplace. This and other industry conditions have maintained a highly competitive environment. There is an increased reliance on client segmentation strategies and greater emphasis on niche products. In an effort to meet their competitive objectives, lenders are increasingly relying on CMHC for market analysis, product innovation and staff training as they strive to ensure their customers are well served.

Average Residential Resale Price

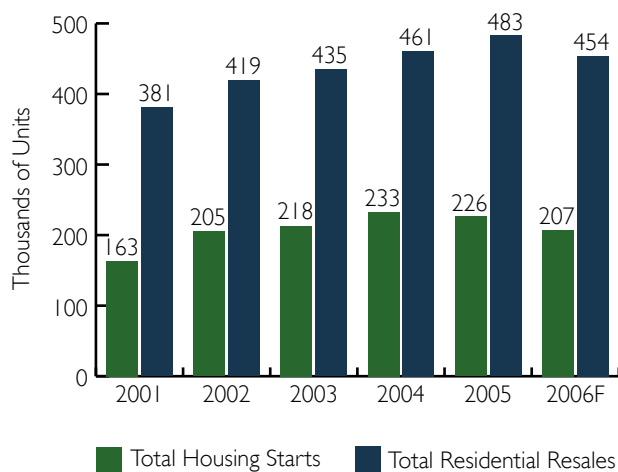


Sources: Canadian Real Estate Association and Real Estate Board of the Fredericton Area Inc., CMHC Forecast 2006.

Competition in Mortgage Insurance Sector is Growing

While CMHC remains the clear mortgage insurer of choice for the Canadian industry, the Corporation is facing increased competition in its high-ratio mortgage insurance business. Going forward, competitive pressures may increase further due to ownership changes

Total Housing Starts and Residential Resales



Housing Starts Source: CMHC Forecast 2005–2006 Residential Resales Sources: Canadian Real Estate Association and Real Estate Board of the Fredericton Area Inc., CMHC Forecast 2006.

**PROUD PAST
BRIGHT FUTURE**

From direct lending to mortgage loan insurance to a host of innovative products, services and options — with significant strides in automation and risk modelling along the way — CMHC has used its housing finance arm to encourage homebuilding, provide equal access to financing nation-wide, increase affordability and choice, and respond to a wide diversity of needs and lifestyles to help thousands of Canadians become homeowners. The housing finance expertise we've garnered over six decades is the cornerstone of our achievements today and the foundation that will secure future successes. We will continue to develop our product and service offering to keep pace of the evolving housing finance needs of Canadians.

at CMHC's mortgage insurance competitor, Genworth Financial Canada. In addition, AIG United Guaranty Corporation has received approval to incorporate a company for the purposes of providing mortgage insurance in Canada. United Guaranty is a wholly owned subsidiary of the leading international provider of insurance products and services, American International Group Inc., and is the fourth largest mortgage insurance provider in the United States.

Groundwork Laid for Transformational Change in the Housing Finance Sector

Basel II

A new framework for capital adequacy, established by the Bank of International Settlements' Basel Committee, is anticipated to be ready for implementation by late 2006 or early 2007. The proposed changes associated with Basel II will align capital requirements more closely to the risk of credit loss, thereby enabling more sophisticated financial institutions to hold less capital than other institutions for the same type of transaction. Under Basel II, the reserve requirement for lending institutions on mortgage-related debt will decline, possibly resulting in decreased demand for mortgage insurance as a risk mitigation tool.

Currently, Basel II would only impact demand for low-ratio mortgage insurance products (i.e., mortgages whose value is less than 75% of the value of the property) as there is a statutory requirement for mortgage insurance on high-ratio mortgage loans.

Financial Institutions Acts Review

As part of its periodic review of the Financial Institutions Acts, the Government of Canada sought industry input on a proposal to remove the statutory requirement under the *Bank Act of Canada* for mortgage loan insurance on high-ratio mortgage loans in order to provide greater flexibility to residential mortgage providers and homebuyers alike.

Under this scenario, the overall size of the mortgage insurance market could decline as some lenders may choose to self insure against risk of default by lower risk borrowers and adopt more risk-based pricing practices.



2000

CMHC negotiates an ambitious agreement to keep the former coal mining community of Tumbler Ridge, British Columbia alive.

ANALYSIS OF OUR PERFORMANCE

We Offered Made-in-Canada Mortgage Insurance Solutions to Help Canadians Access the Funds They Need to Buy a Home

Well-functioning housing finance markets benefit Canadians in every walk of life. One way CMHC is helping markets work better is through our mortgage insurance products that protect mortgage lenders against possible borrower default over the full term of a mortgage. This is particularly important in the housing finance industry where mortgages are often longer term loans, exposed to the highs and lows of a cyclical housing market. Because of our protection, lenders are able to offer mortgages to Canadians everywhere with as little as a 5% down-payment at interest rates that are similar to those for mortgages with a downpayment of 25% or more. This means more Canadians can own homes, sooner. It also means that affordable mortgage financing is available for rental housing.

OUR STRENGTHS

- Innovative products and services that meet the needs of Canadians from all across the country, including those in traditionally underserved areas.
- Strong and committed sales force, with locally-based and highly-knowledgeable underwriters, and predictable and reliable claims payment.
- Fully capitalized according to the Office of the Superintendent of Financial Institutions' guidelines.
- First-rate technology platform and risk models that facilitate fast and effective underwriting practices.

CHALLENGES AND RISKS

- Preparing for transformational change in the housing finance industry while increasing the value of mortgage insurance to lenders and consumers in the short-term.
- Maintaining competitive position in the context of the entry of a new competitor.
- Working with lenders and law enforcement to continue to fight mortgage fraud.

NEXT STEPS

- Continue to assess the effect of the changing regulatory environment on CMHC's programs and products and implement an appropriate directional strategy.
- Continue to explore and develop insurance products, services and policies to meet the needs of financial institutions, brokers and Canadians.
- Continue to emphasize and evolve effective customer relation strategies and supports, and enhance methods to measure success in this area.

In 2005, better than expected economic and financial conditions affecting housing markets, combined with ongoing enhancements to our product and service offerings, resulted in continued record high volumes of approvals in our mortgage insurance business. More than 746,000 units were approved, representing 132% of plan.

Net claims expense on insured mortgages remained low over the year, at approximately \$119 million, due to strong underlying market fundamentals, and effective risk modeling and quality assurance practices that helped to protect CMHC against unnecessary loss, including losses due to fraudulent activities.

The recent steep price increases, which pushed average home prices up by at least 10% in each of the past four years, have been particularly beneficial to individual homeowners, many of whom have realized significant increases in household equity. Homeowners that find themselves in financial difficulty are able to avoid defaulting on their mortgage commitments by selling their home, and moving to less costly homeownership options.

Healthy housing markets have also helped CMHC to achieve full capitalization of our mortgage insurance activity in 2005, according to the guidelines set by the Office of the Superintendent of Financial Institutions.

Looking ahead, while exceptionally low mortgage carrying costs have buoyed housing markets in recent years, elevated home prices combined with rising interest rates will gradually chip away at affordability. As a result, CMHC expects mortgage insurance volumes will begin to moderate in 2006, while claims will remain low.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Total mortgage insurance approved (units)	652,573	564,589	746,157*	574,633

* Target met or exceeded

* Target substantially met

† Target not met

We Created Access to Housing Finance for More Canadians and Introduced Product Innovations

Approximately 34% of the homes backed by CMHC mortgage insurance in 2005 were in markets where CMHC is the only mortgage insurer or where the private sector is relatively less active. Specifically, CMHC offered mortgage insurance products for loans on nursing and retirement homes, rental accommodations and mobile homes, as well as for loans in rural and northern areas, single-industry towns and on reserves. In addition, in 2005, we approved mortgage loan applications for 4,400 affordable housing units, helping to make it easier for low-income Canadians to access low-cost housing.

Our mortgage insurance products have continually evolved over the years to meet the changing needs of Canadians. This year was no exception. In 2005, we introduced a number of key enhancements to our mortgage insurance programs and policies to facilitate housing affordability and to promote the environmental sustainability of housing. Through an annual pricing review, we lowered mortgage insurance premiums by 15% for first time homebuyers with a 5% down-payment, passing along the benefits of enhanced risk analytics and gains in operational efficiencies to consumers. This is the second such reduction in as many years.

Other product enhancements include:

- introducing additional flexibilities to our 10% energy efficiency refund on mortgage insurance premiums, and extending program eligibility to include all types of condominiums;
- introducing a full waiver of premiums for new rental housing projects funded under the Affordable Housing Initiative; and
- lowering premiums on affordable rental housing developed through CMHC's Partnership Centre by 15%, as well as increasing underwriting flexibilities and waiving extended amortization surcharges for affordable housing.

In 2006, we will continue to introduce new homeowner insurance products to better serve borrowers and lenders alike. CMHC will be bringing forward new homeowner insurance products to better serve relatively underserved borrower populations and meet the needs of mortgage originators.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Total mortgage insurance units approved to address less served markets and/or support specific government priorities (%)	36.6	33.0	33.7*	33.0

* Target met or exceeded * Target substantially met † Target not met

2.2 Enhance the Supply of Low Cost Funds for Mortgage Lending by Expanding the Securitization Program

■ WHAT WE DO

We guarantee the timely payment of interest and principal on securities backed by residential mortgages.

■ WHY IT MATTERS

Our activities ensure a steady flow of low-cost funds for mortgages.

This helps keep mortgage rates as low as possible, thereby benefiting Canadian homebuyers.

■ HOW WE GET IT DONE

We develop and deliver securitization programs to provide CMHC's guarantee on mortgage-related securities issued by financial institutions and Canada Housing Trust that meet the needs of mortgage originators and the interests of investors.

Because mortgages are transferred from the lender's portfolio, additional funds are made available for mortgage lending to consumers.

We strive to increase investor participation in capital market issuances to create a liquid market for the mortgage-related securities.

CMHC TOOLBOX

We draw on the following programs to achieve this strategic priority:

- National Housing Act Mortgage-Backed Securities (NHA MBS) Program
- Canada Mortgage Bonds (CMB) Program



1986

Mortgage-Backed Securities are introduced to ensure the supply of low-cost mortgage funds.

For additional information on CMHC's programs and services, visit our website, www.cmhc.ca

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

Economy and Housing Markets

Continued strength in housing markets and bond markets in 2005 translated into strong demand by issuers and investors for new securitization product offerings. With consistently low mortgage rates over the last five years, variable-rate mortgages and adjustable-rate mortgages have gained considerable popularity with homebuyers. As a result, the demand for securitization products for variable-rate and adjustable-rate mortgages increased.

In Canada, we are also noticing rising competition for consumer lending, with new lenders and new mortgage products that are designed to enable higher consumer leverage.


Regulatory Environment

Many of the same issues and trends affecting CMHC's mortgage insurance business will also have an impact on its guarantee activities resulting from the *National Housing Act* Mortgage-Backed Securities (NHA MBS) and Canada Mortgage Bond programs. Overall, however, the demand for CMHC guaranteed mortgage securitization products is not expected to be negatively impacted by Basel II or the possible changes to the *Bank Act* as lenders will still require access to low-cost mortgage funding. However, since mortgage insurance is required for financial institutions to securitize mortgages via CMHC's securitization programs, changes to the legislative requirement for mortgage insurance on high-ratio loans may make CMHC's guaranteed mortgage securitization more expensive for financial institutions if they are not able to pass the insurance cost on to borrowers.

Nonetheless, it is expected that the Canadian housing finance system will continue to move from a deposit-based on-balance-sheet funding model to a model where securitization, likely with some form of sovereign guarantee, will dominate. The impact of changes in the operating environment is more likely to be greater pressures for increasing sophistication and the ability of CMHC to consider other credit enhancements, as opposed to the current approach which relies solely on mortgage insurance as the credit enhancer.

Review of Crown Corporation Borrowing Framework

The Department of Finance is in the process of conducting a review of the borrowing framework governing major Crown corporations who borrow from the capital markets, including CMHC, to determine whether the current framework is functioning effectively and to review alternative borrowing frameworks. As a result of this review, the Department of Finance is considering the centralization of Crown borrowing activities with the government's own borrowing program. The review includes the capital market activities of the Canada Housing Trust, which is an independent trust that issues Canada Mortgage Bonds.



**PROUD PAST
BRIGHT FUTURE**

In 1986, CMHC introduced *National Housing Act* Mortgage Backed Securities (NHA MBS) as an alternative to investing in individual mortgages. For the first time, NHA MBS offered private investors the opportunity to invest in a pool of insured residential mortgages issued by Canada's mortgage lenders, carrying guarantees of timely payment by CMHC. As a result, CMHC was able to help ensure a ready supply of low-cost funds for housing finance and help keep mortgage lending costs as low as possible for homeowners. Building on this success, in 2001, housing affordability received a boost when CMHC introduced Canada Mortgage Bonds, aimed at ensuring the supply of low-cost mortgage funding and keeping interest rates low.

CMHC continues to be a leader in secondary mortgage markets in Canada. This past year, we expanded our securitization program to better meet the needs of mortgage originators and investors, and we will continue to explore options and opportunities to help lower the cost of homeownership for Canadians.

While mortgage securitization will continue to grow in Canada, CMHC's role and activities, including the Canada Mortgage Bond Program, may be affected by this review. A centralized borrowing framework could impact CMHC's and Canada Housing Trust's borrowing and asset-liability management strategies. CMHC will continue to work closely with agencies involved in the review to improve federal borrower effectiveness and efficiency.

ANALYSIS OF OUR PERFORMANCE

We Helped to Ensure a Steady Flow of Low-cost Funds For Mortgage Lending

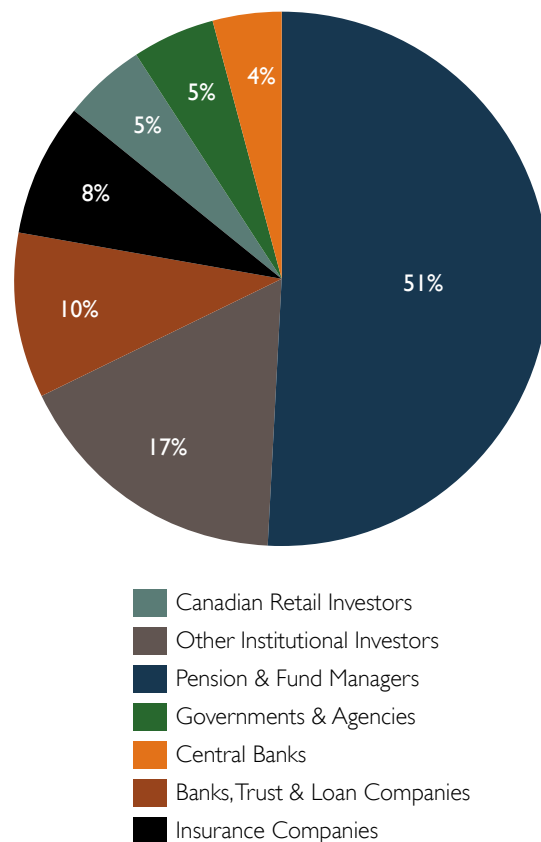
CMHC facilitates a steady flow of low-cost funds for mortgage lending through the guarantee of mortgage-related securities, including NHA MBS issued by Canadian financial institutions and Canada Mortgage Bonds issued by Canada Housing Trust. This helps to keep mortgage interest rates as low as possible. These securities also benefit investors by providing high quality, secure investments in Canadian residential mortgages.

In 2005, CMHC guaranteed timely payment of interest and principal on a total gross issuance of \$12.3 billion in NHA MBS. NHA MBS are created when a CMHC approved seller brings together a pool of eligible mortgages for the purpose of transforming the mortgages into securities that can be sold to investors.

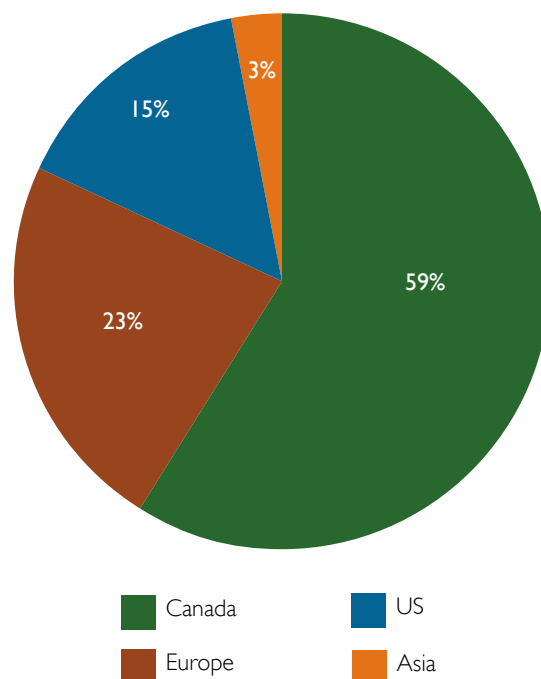
In 2005, CMHC also guaranteed timely payment on the seven Canada Mortgage Bond issuances by Canada Housing Trust, totalling \$18.1 billion.

Canada Housing Trust sells Canada Mortgage Bonds to investors and uses the proceeds to purchase newly issued NHA MBS from approved sellers. To provide investors with a bond-like investment, Canada Housing Trust transforms the monthly cash flows from NHA MBS pools into non-amortizing bond cash flows with fixed interest payments and principal at maturity.

Original Distribution of CMB by Investor Type
(Issues in 2005)



Original Distribution of CMB by Region
(2001 through 2005)



In addition to guaranteeing timely payment on Canada Mortgage Bonds, CMHC acts as the financial services advisor to Canada Housing Trust, providing certain financial advisory services related to determining market demand for bond issuance, and engaging of an underwriting syndicate to underwrite bond issues. CMHC receives a fee from Canada Housing Trust for its services as guarantor and financial services advisor. The day-to-day activities of Canada Housing Trust are administered through a separate corporate entity serving as the trust administrator.

In 2005, the Canada Mortgage Bond Program provided fund rates that were competitive, with an average 9.2 basis point spread above equivalent 5-year Government of Canada securities. This includes a spread of 7.6 basis points at the time of the Canada Mortgage Bond issue in September — the tightest spread ever realized in the program. This indicates that investors consider the Canada Mortgage Bonds as nearly equivalent to Government of Canada bonds in terms of risk and liquidity, which is helping to make Canada Mortgage Bonds attractive to a wide range of investors in domestic markets, and increasing the bonds appeal in global markets.

In sum, a total of \$30.4 billion of mortgage-related securities were guaranteed by CMHC in 2005, bringing the total guarantees in force to \$103.7 billion, a 28% increase over 2004. At the time of planning, the assumption was that an upward trend in interest rates would cool the residential sector. However, strong demand in both housing and bond markets in 2005 accounted for much of the increase in securitization over the year.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Annual securities guaranteed (\$ millions)	29,592	18,000	30,374*	18,000

* Target met or exceeded * Target substantially met † Target not met

OUR STRENGTHS

- **Leader in secondary mortgage markets in Canada** — facilitating opportunities for high-quality, secure investments in residential mortgages.
- **Well-designed securitization programs** that minimize CMHC's exposure to the risk of default by participating financial institutions.
- **Close ties to the Canadian financial community** and good understanding of mortgage originator and investor needs.

CHALLENGES AND RISKS

- **Positioning CMHC guaranteed mortgage securitization program** in a changing housing finance landscape, which will likely result in increased demand for more sophisticated securitization products.
- **Developing innovative ways** for financial institutions to securitize a wider range of mortgages to continue to help lower the cost of homeownership for Canadians.
- **Ensuring the appropriate organizational structure and talent base** to effectively take advantage of opportunities in mortgage securitization.

NEXT STEPS

- **Implement a new directional strategy** given pending regulatory and other changes in CMHC's operating environment.
- **Continue to work with the market** to develop new securitization products, including enhanced products for smaller lenders.
- **Increase investor relations activities** with key investors and dealers.

We Expanded our Securitization Program to Better Meet the Needs of Mortgage Originators and Lenders

In 2005, the increased activity was facilitated by the first full year of issuance of floating rate Canada Mortgage Bond notes. Three issues were completed totalling \$3.07 billion, including the largest Canadian dollar floating rate note (\$1.2 billion) issued in the Canadian public market. This shows the continued commitment by Canada Housing Trust, supported by CMHC as guarantor and financial services advisor, to structure housing debt that meets the needs of both mortgage originators and investors.

CMHC also worked to expand the range of financial institutions able to securitize and fund mortgages via our securitization programs and introduced several enhancements to the NHA MBS Program and the Canada Mortgage Bond Program to help increase the supply and variety of mortgages that can be funded through these programs. By making CMHC guaranteed low-cost funding alternatives available for more financial institutions to securitize a wider range of mortgage products, we are helping to lower costs for Canadian homeowners on a wider range of mortgages. In particular, CMHC introduced new flexibilities to the Canada Mortgage Bond Program allowing for its guarantee to apply to the securitization of adjustable rate mortgages that have been very popular with Canadian homeowners, as well as introducing term flexibilities to allow the securitization of shorter term mortgages.

2.3 Provide Comprehensive, Timely and Relevant Information to Enable Canadian Consumers and the Housing Sector to Make Informed Decisions

■ WHAT WE DO

As Canada's housing expert, we provide a wide range of objective, and reliable housing information.

■ WHY IT MATTERS

We help industry participants make informed business decisions.

We help consumers make informed choices, whether purchasing, renting, renovating, or maintaining their home.

■ HOW WE GET IT DONE

We work with academics, other government organizations, and industry experts to produce top quality data and research.

We share our knowledge and expertise with the housing industry through conferences, seminars and media releases.

We offer ready access to our information products through our Canadian Housing Information Centre (CHIC) at 1 800 668-2642 and on our website.



1947

CMHC begins providing the industry with valuable statistics on housing starts and completions and information on new construction technologies.

CMHC TOOLBOX

We draw on the following tools to achieve this strategic priority:

Research Publications

- *Canadian Housing Observer*
- *Research Highlights* series
- *About Your House* fact sheet series
- Variety of topical reference materials, such as:
 - *Canadian Wood-Frame House Construction*
 - *Homeowner's Manual*
 - *Home Care: A Guide to Repair and Maintenance*
 - *Your Guide to Renting a Home*
 - *Guide to Cooperative Housing*

Research Initiatives

- Directed Research Program
- External Research Program
- National Housing Research Committee
- Housing Awards Program
- Affordability and Choice Today Program
- Information transfer — seminars, presentations, electronic newsletters

Market Analysis Products

- *Housing Market Outlook* series
- *Housing Now* series
- Housing statistics series
- Rental market reports
- Time series data
- Housing Outlook conferences/seminars

For additional information on CMHC's programs and services, visit our website, **www.cmhc.ca**

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

Housing is a Key Component of the Canadian Economy

After several very strong years, housing-related spending in current dollars grew 5.4% in 2005, compared to growth of 6.3% for the rest of the economy. Employment in the construction industry continued to grow faster than in most other industries.

Despite a dip in consumer confidence that accompanied the spike in fuel prices in the wake of the Gulf coast hurricanes in the early fall, consumer confidence has been very strong over the year. We expect this strong consumer sentiment to prevail throughout 2006 as interest rates remain low, and income gains continue. Going forward, rising consumer sentiment is expected to be reflected in stronger consumer spending. This should keep the demand for home-ownership and home renovations fairly strong.

Housing is a Significant Determinant of Quality of Life

Adequate, affordable and quality housing is a major determinant of the health and well being of society. Educational attainment, crime levels, and overall population health are all linked to housing supply and conditions. Information on housing options, markets, costs, efficiency, durability, indoor air quality and other areas of interest help maximize the social benefits associated with housing investments.

Industry, consumers, policy analysts, and other housing stakeholders require information and market intelligence to ensure that Canadians continue to be well housed, to ensure sound decisions are made for the benefit of all, and to ensure that housing-related issues are considered when broader policy decisions are made.

ANALYSIS OF OUR PERFORMANCE

We Provided Important Housing Research to Canadians and the Housing Sector

Relevant, timely and comprehensive information helps Canadians make informed decisions about their housing choices, and supports the well-being of Canada's housing sector. That's why we offer a full range of information, from market analysis and forecasting information through technical information aimed at builders and renovators, to how-to guides for consumers.

OUR STRENGTHS

- Premier source of reliable and objective housing information in Canada.
- Extensive database and knowledge gathered over 60 years of collecting housing data and researching housing issues.
- Ability to inform consumers, municipal government leaders and other industry stakeholders on key issues related to housing.

CHALLENGES AND RISKS

- Using research and information products as tools for developing and delivering on public policy.
- Promoting the vast array of CMHC resources and products to the general public and targeting consumers with specific needs.
- Effectively sharing our expertise to increase awareness of key housing-related issues among industry participants.

NEXT STEPS

- Continue to adapt information products to meet the needs of clients as we understand them based on our ongoing client satisfaction surveys.
- Review the housing survey methodologies related to housing starts and completions and rental markets.
- Review the market analysis suite of products and services to ensure the product offering continues to be relevant to clients.

In 2005, CMHC developed or revised 113 research information products. We published 56 *Research Highlights*, which provide relevant information on a diverse range of socioeconomic and technical topics. In addition, we continued to prepare and publish *About Your House* fact sheets, addressing common housing questions, issues and problems.

Additional examples of our housing research publications in 2005 include:

- *The Canadian Housing Observer*, third edition
- *Canadian Wood-Frame House Construction* (revised)
- *Your Guide to Renting a Home* (revised)
- *Guide to Cooperative Housing* (new)

To bring the benefits of CMHC's housing expertise and research programs to a broader range of individuals and encourage more informed housing choices, we delivered 350 presentations on a variety of topics, reaching a combined audience of almost 17,000 individuals. Participants in our information transfer seminars found the seminars and presentations to be useful, with the seminars receiving an overall satisfaction rate of 94%, significantly above our target of 70%. As the measure and target were newly introduced in 2005, future targets will be adjusted accordingly.

In 2005, for example, we held 26 *Build & Renovate to Avoid Mold and Indoor Air Quality Investigator* workshops, with the objective of increasing the capacity of the housing industry (i.e., builders, renovators, inspectors, health professionals, and building officials) to deal with indoor air problems. We also offered a variety of workshops dealing with flexible design concepts, as well as accessible and barrier-free design, to inform Canadians, industry participants and other specialists on a range of relatively low-cost home modifications to make a home accessible to seniors and people with special requirements.



1992

The Healthy Housing™ concept is introduced and demonstrated in Toronto.

Corporate Performance Measures	2004 Results ¹	2005 Target	2005 Results	2006 Target
Recipients of newly-published <i>Research Highlights</i> who found them useful (%)	70	70	69*	70
Recipients of newly-published <i>About Your House</i> fact sheets who found them useful (%)	84	80	83*	80
Information transfer seminar attendees who found them useful (%)	n/a	70	94*	70

* Target met or exceeded * Target substantially met † Target not met

¹ 2004 data represents the results of the baseline survey administered to establish targets for 2005. The targets for 2006 will remain the same as a significant data sample is required prior to implementing any changes.

We Offered Reliable Housing Market Information to Canada's Housing Sector

The Corporation's market analysis function tracks housing markets and provides national, regional and local housing forecasts, analysis and data to consumers, industry and government. Reliable market information is critical to helping the housing industry and consumers make sound investment decisions. In 2005, CMHC ranked 2nd among 17 Canadian housing forecasters, representing an improvement of two ordinals over 2004.

To encourage wider distribution of our print publications, the electronic editions of our standardized national suite of publications became free and accessible on our website in November 2005.

In 2005, we continued to expand the range of information that we collect and provide to our clients. We implemented changes to the rental market survey to begin collecting rental availability data, as distinct from rental vacancies, in all centres with a population greater than 10,000. The results were publicly released in December, providing clients with a more complete view of the availability of rental accommodation.

We also concluded a feasibility study of indicators of the secondary rental market (such as rented condominiums, duplexes and secondary suites), and conducted pilot surveys based on the results of the feasibility study. If pilot results support broader implementation, we will be able to provide clients with more complete information on all aspects of the rental market.

CMHC's Housing Outlook Conferences and other market analysis presentations offer a range of opportunities for housing industry participants to discuss CMHC's market analysis and forecasts directly with CMHC experts and to network with other industry participants. Our events were attended by record numbers in 2005, with more than 29,000 people participating in the 20 conferences and seminars and 354 presentations held across the country.

The market analysis publications and Housing Outlook Conferences were rated highly by users, with 95% and 99% of survey respondents rating the publications and events, respectively, as useful. Results for these new measures are both significantly above our initial target of 70%, which will be revisited next year and as more data becomes available in subsequent years.

Going forward, we will complete additional pilot surveys which will explore new sources of housing data, and conclude the final stages of a review of products and services to ensure that they continue to be responsive to client needs.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Forecast accuracy for housing starts (%)	-14	Within 10% of actual	-6.8*	Within 10% of actual
Ranking of housing start forecast accuracy among forecasters	4th among 17	CMHC rank within top quartile	2nd among 17*	CMHC rank within top quartile
Recipients of market analysis publications who found them useful (%)	n/a [†]	70	95*	70
Attendees at Housing Outlook Conferences who found them useful (%)	n/a [†]	70	99*	80

* Target met or exceeded * Target substantially met † Target not met

[†] 2005 was the first year of data collection.



**PROUD PAST
BRIGHT FUTURE**

Throughout our history, we have conducted research and collected extensive information and expertise on a host of housing-related issues. We have also been at the forefront of providing timely and reliable information on housing markets. In 1947, CMHC initiated surveys and the release of housing statistics, becoming the foundation for the Market Analysis Centre created in 1987. Researching critical housing issues and sharing our knowledge and expertise to improve housing in Canada continue to be a key focus of our activities. Our flagship information product — the *Canadian Housing Observer* — is an annual publication which provides a comprehensive statistical portrait of how well Canadians are housed, and charts key trends and developments affecting this important sector of Canada's economy. In 2006 and beyond, we will continue to develop and position our products as important resources for policy development.

Objective Three

ENSURE THE CANADIAN HOUSING SYSTEM REMAINS ONE OF THE BEST IN THE WORLD



As Canada's national housing agency, CMHC plays a lead role in ensuring that the Canadian housing system remains among the best in the world. Over the past 60 years, we have been continually evolving to meet the changing needs of Canadians. We promote housing and housing development that is sustainable and healthy, providing lasting value to Canadians. We continually examine the functioning of the housing system to identify gaps which may leave some Canadians unable to access suitable and affordable housing. And we work with our government, community and industry partners to address these gaps.

Because we understand the value that our housing system brings to Canadians, we sell our expertise to countries around the world who are interested in adapting our housing solutions to meet their needs and realities. We promote Canadian housing technologies and building practices through our support to housing exporters.

To continue to play a leadership role in housing at home and abroad, we ensure that CMHC is a strong organization able to fulfill our mandate and meet the challenges we face in the future.

RESOURCES

\$91.7 million in operating expenses

686 Staff Years

3.1 Ensure Canada's Housing System Remains One of the Best in the World

■ WHAT WE DO

We advise the Government of Canada on matters of housing policy.

We are a leader in promoting the concept of healthy housing and sustainable communities.

■ WHY IT MATTERS

We work to ensure that the Canadian housing system remains one of the best in the world, and that all Canadians reap the benefits of our world-class housing system.

A healthy house is one that is good for the people who live in it, good for the community and good for the planet.

Sustainable neighbourhood designs and land use reduce infrastructure costs and environmental impacts, while maintaining community liveability.

■ HOW WE GET IT DONE

We develop and implement housing policy and programs that ensure government, communities and the housing sector are working together to meet the needs of all Canadians.

We work with academia, industry, governments and other housing stakeholders to develop and share examples of best practices in design, development and standards.

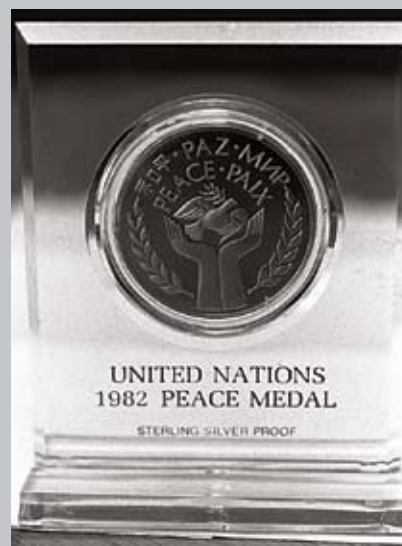
We work directly with communities in developing innovative, sustainable development solutions, tailor-designed to meet their unique needs.

We encourage energy efficiency and offer readily accessible, practical tips for your home.

CMHC TOOLBOX

We draw on the following tools to achieve this strategic priority:

- Housing policy development
- Net Zero Energy Healthy Housing demonstration initiative
- Sustainable development and community design workshops
- Mortgage Loan Insurance for Energy-Efficient Homes
- Range of information products and services



1983

CMHC is awarded the United Nations 1982 Peace Medal for promoting a better understanding among people of the ECE (Economic Commission for Europe) countries as host of a study tour on housing, buildings and planning.

For additional information on CMHC's programs and services, visit our website, www.cmhc.ca

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

While Canada has One of the Best Housing Systems in the World, There is a Need for Periodic Review so that Canadians Continue to Reap the Benefits of Evolution and Renewal

Because Canada has a well-functioning housing system, approximately 86% of Canadians are able to meet their housing needs. Nonetheless, many Canadians require some housing assistance — 14% of Canadians are unable to access safe, affordable housing, and almost 150,000 are estimated to be homeless.

Through a series of consultations held in late 2004 and early 2005, housing industry stakeholders consistently expressed that there was a need for a community-based, partnership approach that would build on existing housing programs and introduce new initiatives to create a complete toolbox of programs to respond to the needs of all Canadians. Following the consultations, expectations among housing stakeholders are high, and municipalities are pressing for action on affordable housing.



2003

The Seabird Island First Nation Sustainable Community Demonstration Project on Seabird Island Reserve, Agassiz, British Columbia is funded under the guidelines of CMHC's On-Reserve Housing Program. The project combines the latest concepts in housing construction and design while honouring Aboriginal culture.

Sustainable Housing and Communities Contribute to a Strong Canadian Housing System

Housing is a key element of environmental sustainability and quality of life because it is such a heavy consumer of resources in its construction, maintenance and operation. It also lasts for a long time, affecting energy consuming activities and other key facets of our lives, such as transportation, infrastructure, community, employment, and health. The residential sector accounts for some 18% of Canada's total energy demand and much of the infrastructure costs faced by municipalities relate to servicing low-density urban development patterns.

Better building practices will continue to be critically important in slowing Canada's total demand for energy, which is projected to increase by 1.5% per year to 2025 due primarily to population and economic growth. Developments in construction techniques and building materials, and the increasing market share for energy-efficient household appliances have significantly improved the energy efficiency of homes. Although total residential energy use increased by 3.7% between 1990 and 2001, the increase would have been six times higher without improvements in energy efficiency and conservation. On average, houses built between 2001 and 2004 use approximately half the amount of energy as those built before 1946.

Housing industry participants generally acknowledge that the costs of ineffective and unsustainable building and planning practices are too high to ignore, and this is motivating many communities to look for new approaches to planning that involve all parties in the process.

ANALYSIS OF OUR PERFORMANCE RESULTS

We Played a Key Role in Consultations and Policy Development to Renew Canada's National Housing Strategy

As Canada's national housing agency, we play a lead role in ensuring that the Canadian housing system remains among the best in the world, continually evolving to meet the changing housing needs of all Canadians. We regularly examine the functioning of the housing system to identify gaps that may leave some Canadians unable to access adequate and affordable housing, and develop and recommend policies and programs to effectively address the gaps.

In 2005, we worked with our partners to create a long-term national housing strategy, with a vision of adapting Canada's housing system to the changing needs of Canadians. We assisted in the organization of eleven community forums, five expert roundtables and an urban Aboriginal roundtable to achieve broad-based agreement on the way forward. The consultations called for all levels of government, community organizations and the private sector to work together to better integrate existing programs and broaden the tools available to local communities in addressing the root causes of housing affordability problems and homelessness. Discussions on the development of a new Canadian housing framework were also carried out with provincial and territorial Housing Ministers and officials in September 2005.

We Focused a Great Deal of Our Research on Sustainable Development to Help Ensure that Canadians Remain Among the Best Housed People in the World

In 2005, CMHC contributed \$1 million to launch the first phase of a Canadian Net Zero Energy Healthy Housing (NZEHH) initiative. This government/industry partnership builds a vision for reduced energy consumption and healthy communities through the application of healthy housing principles. It is also an important next step towards creating sustainable communities and healthy cities in Canada.

In 2006, a national competitive process to select design/development teams for the pilot NZEHH demonstration projects will take place. The design and construction of Net Zero Energy Healthy Housing demonstrations will follow in all regions across Canada. The initiative also includes creating and delivering information products to build consumer awareness and industry capacity for the broad-scale, long-term delivery of quality NZEHH communities in all regions in Canada.

We encouraged energy efficiency in Canadian homes

To encourage Canadians to adopt energy-efficient practices and technologies, CMHC, in partnership with Natural Resources Canada, took steps to begin delivery of the new EnerGuide for Low-Income Households. The program was designed to assist low-income Canadians to cope with high energy costs by funding certain energy retrofits and to be delivered through CMHC's existing delivery network for our renovation programs. The program was also designed to complement initiatives with provinces and territories.

OUR STRENGTHS

- A rich expertise base arising from over 60 years as Canada's national housing agency.
- A depth of recognized experience in housing policy development.
- Broad network of established relationships with other levels of government, private and non-profit stakeholders.
- Extensive, well-organized community delivery network.
- Experience in applying research knowledge base to stimulate the development of designs and technologies.

CHALLENGES AND RISKS

- Ensuring that all Canadians benefit from a well functioning housing system.
- Making the link between housing and key policy matters such as the environment and infrastructure.
- Developing programs and technical criteria that meet the needs of various stakeholders.

NEXT STEPS

- Manage the federal, provincial and territorial consultation process and facilitate enhancements to the Canadian housing system.
- Continue to develop policy proposals on new or improved tools, including possible enhancements to existing programs.
- Contribute to a better understanding of the environmental performance of housing.

In 2005, CMHC provided technical and financial support to develop an energy management plan for Ontario's social and non-profit housing stock. This investment in energy efficiency upgrades supports the renewal of the housing stock, as well as improved occupant health and comfort, enhanced durability, and reduced operating costs. It also supports efforts to maintain and sustain existing energy distribution networks and to slow the need for new energy infrastructure.

We worked with municipalities to encourage sustainable development

In 2005, we continued to examine issues related to brownfield redevelopment, and identified two communities to pilot risk-sharing projects in 2006. If successful, the pilots will form a model for residential intensification through risk-sharing approaches to brownfield redevelopment.

In 2005, we continued our focus on small communities to provide them with the resources needed to make informed planning decisions. We developed and delivered the Sustainable Development Workshop for Small Municipalities across the country, reaching 300 municipal councillors and staff. The workshops increased awareness of the benefits of sustainable community planning and development and of the available options and resources to meet their objectives.

We also supported and participated in integrated design workshops in various communities across the country, including in northern communities. These innovative brainstorming workshops bring together multiple stakeholders and design experts over a period of several days in order to develop solutions to complex site specific issues. They increase community learning, inspire more innovative solutions, evolve greater understanding and support of plans, and enable more effective stakeholder involvement in the sustainable community planning and building design process.



**PROUD PAST
BRIGHT FUTURE**

CMHC's leadership in the 50's and 60's helped expand the government role in housing to include urban renewal and planning, in response to increased urbanization and concern for the housing conditions of low-income families. Neighbourhood improvement initiatives shifted the focus from building homes to building communities — affordable, mixed income communities that later incorporated sustainability as a key focus. Building on this rich tradition, CMHC has recently enhanced its role in community development. Moving forward, we will continue to build on our partnership efforts and our tool kit to better address housing issues and create community-based sustainable housing solutions across the country.

3.2 Support and Promote Canada's World-class Housing Products, Services and System Internationally

■ WHAT WE DO

We act as consultants, developing and implementing solutions to the housing and housing finance challenges faced by our international clients.

We support Canadian exporters in the housing industry, promoting Canadian products and services in countries around the world.

We represent Canada on housing matters both domestically and abroad.

■ WHY IT MATTERS

We enhance the quality of life and improve the housing conditions in developing countries and emerging economies.

We contribute to the strength and innovative capacity of the Canadian housing export industry.

We help create jobs from coast to coast, which contributes to a vibrant Canadian economy.

We participate in the United Nations and contribute to important initiatives such as the Middle East Peace Process.

■ HOW WE GET IT DONE

We present the benefits of Canadian housing solutions and assist clients to make decisions aimed at strengthening their economies.

We support Canadian businesses in their search for diversified markets and new housing export opportunities.

We promote awareness, recognition and access for Canadian housing products, services and technologies abroad by working in partnership with industry and government.

We host foreign delegations to Canada to enhance their understanding and awareness of Canadian housing solutions.

CMHC TOOLBOX

We draw on the following tools to achieve this strategic priority:

- CMHC International Housing Export Services
- CMHC International Consulting Services
- CMHC International Relations



1966

CMHC won a \$2.1 million contract to build 173 CMHC-designed houses in Harlow, England.

*For additional information on CMHC's programs and services, visit our website, **www.cmhc.ca***

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

Economic Conditions Generally Favour Canadian Exporters

Several key factors are pointing to continued growth in Canadian exports. First, the world economy is in good shape with above average growth experienced in 2004 and 2005, and expected again in 2006. World economic strength has resulted in increased demand for Canadian goods and services, partially offsetting the negative impact of the Canadian dollar's strong appreciation since 2003. Second, exporters are poised to realize considerable productivity gains as a result of both investments in machinery and equipment, which should translate into improvements in labour productivity. This should offset the effects of a rising Canadian dollar on demand and profits.

Risks to the Overall Export Outlook Remain

There are some key risks to the overall outlook for Canadian exports. The foremost risk remains the continued rise of the Canadian dollar against the American dollar. Export goods priced in Canadian dollars are made more expensive and, therefore, less attractive, in foreign markets. In addition, to the extent that Canadian export goods are priced in American dollars at international market prices, Canadian exporters realize lower profits in Canadian dollar terms.

There is also the potential for rising energy and gasoline prices to curb consumer confidence and spending in the US and in other key international markets.

Canadian Exporters are Pursuing Growth Opportunities in Developing Nations

Although the US remains the primary destination for Canadian exports, with a 94% share of the total, Canadian exporters are looking to new markets for growth opportunities. Markets with the greatest growth potential tend to be in developing and emerging economies. And, Canadian exporters are increasingly doing business in these nations. While trade with developing and emerging economies is providing new opportunities for Canadian export goods and services, it also poses many challenges as Canadian exporters and policy makers adjust to changing competitive and political landscapes.

As a result, support for exporters is becoming increasingly important to ensure that Canadian businesses are able to take advantage of expanding market potential and international opportunities. Government and industry are continuing to strengthen access to North American markets, while acknowledging that Canada's economic interests extend well beyond North America and that the nation's future prosperity depends on working with partners to open up markets with strong potential.

Housing Exports Add to Economic Growth

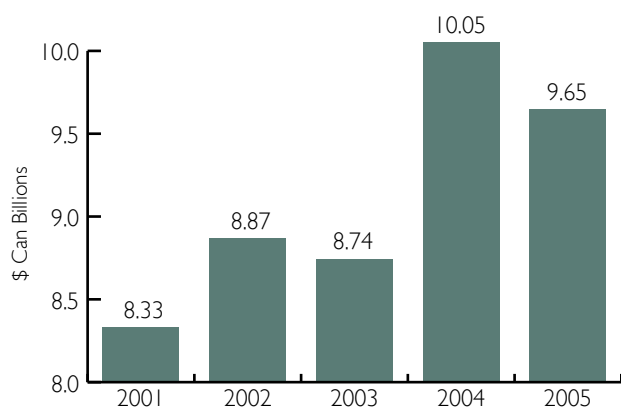
Canada sells a variety of housing-related materials to other countries to assist them in providing new housing and renovating existing housing. These include building materials, manufactured components and complete building systems, as well as a range of expertise in urban planning, and in designing and building homes. The exports of value-added, housing-related products in 2005 remained unchanged, at \$9.65 billion, compared to a year earlier. The US continues to dominate as the primary destination for Canadian exports, accounting for 70% of all prefabricated building.

There is Some Potential for Weakness in Global Housing Markets in 2006

The potential for weakness exists in global housing markets, including the US and the UK. Elevated levels of consumer debt may become problematic, particularly when rising gasoline and home heating costs are considered. The impact of rising energy and production costs on inflation has also increased the likelihood that interest rates may rise in the near term. These risks are somewhat mitigated in the US, however, because homeowners are locking in their mortgages at low rates, sheltering them somewhat from rising interest rates.

Canadian Housing-Related Building Products Export

(Excluding Lumber Industries)



ANALYSIS OF OUR PERFORMANCE

We Offered Housing Solutions Around the World

Through our international consulting services, we offer, on a commercial basis, housing and housing finance solutions to countries around the world to improve housing affordability and accessibility. We often work with international financing institutions, foreign governments and other international public and private agencies, in partnership with other Canadian companies and organizations whenever possible. Our consulting services have had a significant impact on the capacity of numerous nations to address their most pressing housing challenges. We have helped China and Latvia to review their approaches to accessible and affordable housing finance, assisted Algerian banks to develop their mortgage markets, and worked in India, Mali and West Bank/Gaza to enhance their emerging mortgage markets.

In 2005, we achieved our target of \$1.2 million in revenues for consulting services in the areas of housing and housing finance. We also signed a significant number of new contracts in 2005 that will deliver future revenues. These new contracts include countries in which CMHC has not worked before, such as Oman, Jordan, Thailand and South Korea. CMHC has also been called upon to provide advice and services in areas of expertise that we have not previously delivered in an international arena, such as helping Egypt build capacity to produce a National Urban Observatory that will include elements similar to CMHC's Canadian Housing Observer, and developing housing policy and a residential rehabilitation program in West Bank/Gaza.

In 2006 and beyond, we will continue to contribute to Canada's broader foreign policy of supporting the economic and social development of emerging economies, while at the same time generating prosperity at home.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Revenue from selling CMHC's expertise abroad (\$ millions)	1.3	1.2	1.3 *	1.5

* Target met or exceeded

† Target substantially met

‡ Target not met

OUR STRENGTHS

- Excellent reputation on the international scene as a reliable and knowledgeable consulting partner.
- Strong relationships and partnerships with key international players, such as the World Bank.
- Excellent client focus: Housing export clients indicate that they are highly satisfied with our services.
- Ability to produce tangible results for exporters, who indicate that we partnered in the creation of almost 3,000 jobs and \$260 million in export sales over the past four years.

CHALLENGES AND RISKS

- Helping relatively small Canadian housing export companies compete in the highly competitive world market.
- Overcoming a strong Canadian dollar and potential economic weakness within some key markets.
- Dealing with increased trade protectionism.
- Working in developing countries and emerging economies that are experiencing a degree of political and economic instability.

NEXT STEPS

- Share best practices with an international audience when CMHC organizes the 26th World Congress of the International Union for Housing Finance and Canada hosts the World Urban Forum in 2006.
- Support the development of efficient housing finance systems and housing policies in emerging economies.
- Expand Super E export sales by matching Canadian prefabricated housing suppliers with large developers in the United Kingdom, and establishing a program in China.

We Worked with Canadian Housing Exporters to Expand their Businesses Internationally

While expansion in the US remains important, CMHC's objective is to diversify Canada's exports by encouraging companies to expand to high-potential markets. The growing interest in healthy and energy-efficient housing is establishing a strong position for the Canadian housing industry and Canadian housing know-how, particularly the Super E brand, in key markets.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Overall satisfaction rate of key export clients (%)	79	70	84*	75 [†]
Value of CMHC-facilitated sales reported by key clients (\$ millions)	67.8	55.2	66.7*	71.4

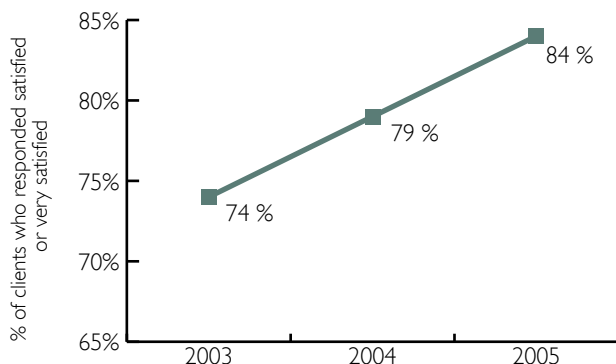
* Target met or exceeded * Target substantially met † Target not met

[†] The record level of satisfaction in 2005 was higher than was anticipated when the 2006 target was established, but will be reflected in the 2007 target when it is set.

In 2005, 87 key clients reported total sales of almost \$67 million (121% of the annual target) that they acknowledge as having been facilitated by CMHC International. This number reflects the excellent alignment of CMHC efforts in markets that are of particular interest to our clients. While progress is slow in some emerging markets, it is a known fact that longer time-lines are required for significant results in these countries. In 2005, these were counter-balanced by unique and unexpected successes in markets such as Russia.

In an annual survey, CMHC International's export clients gave CMHC a satisfaction rating of 84%, the highest ever. The results show that CMHC International clients are very satisfied with the services they are receiving, particularly with the quality of service provided by CMHC International representatives. CMHC International's efforts are not only leading to sales, but are also developing closer ties with clients, gaining the trust of potential foreign buyers, deepening understanding of international markets, and building relationships

CMHC Export clients are increasingly more satisfied with the service they receive



with partner agencies. These steps will help to position Canadian exporters for success and greater breakthroughs in the future.

Our long-term goal is to increase Canadian housing exports, leading to job creation in the sector. Over the next 4–5 years, our activities are expected to create or maintain approximately 4,000 domestic person-years of employment in the housing sector. We will continue to help key clients identify business opportunities by offering market intelligence, matchmaking events, market access strategies and customized business missions. To assist in gaining market entry, CMHC will continue to promote awareness and recognition of Canadian housing codes and standards, and facilitate the attaining of certification and home warranties for the Canadian housing system.

**PROUD PAST
BRIGHT FUTURE**

Our solid credibility as Canada's national housing agency led naturally to CMHC becoming the face and voice of the Canadian government in the international housing arena. Through the decades, CMHC has developed bilateral relations with other national governments and their agencies to help increase housing affordability and quality, and promote sustainability in response to intense urban growth around the world. In 1983, CMHC was awarded the United Nations 1982 Peace Medal for promoting a better understanding of housing, building and planning issues. CMHC's recent international efforts are focused on promoting Canada's housing products, technologies, expertise and services across the globe. In 2006 and beyond, we will continue to promote our housing finance system, which is considered a best practice in many parts of the world for its ability to provide safe, quality and affordable housing for its citizens.

3.3 Ensure that CMHC is a strong organization able to fulfill its mandate

■ WHAT WE DO

We ensure that we remain a strong, responsible and progressive organization, drawing on our 60 years of experience to serve the housing needs of Canadians.

■ WHY IT MATTERS

We provide benefits to Canadians that are fundamental to their quality of life and well being.

Effective management of resources and efficient operations mean greater value for Canadians.

■ HOW WE GET IT DONE

We manage our business in an ethical and accountable way, recognizing that our human resources are our greatest asset.

We use sound financial, administrative, and technology processes and systems.



For additional information on CMHC's programs and services, visit our website, www.cmhc.ca

WHAT FACTORS INFLUENCED OUR PERFORMANCE?

A Strong Need for Robust Governance and Accountability Frameworks

Following recent corporate failures in Canada and the US, accounting standards and guidelines are being reviewed and revised by standards-setting bodies to ensure transparency in reporting. New rules related to internal controls have also arisen to improve the quality and reliability of financial reporting, maintain investor confidence, and enhance overall governance of public companies. Canadian rules are being developed, and Treasury Board Secretariat is considering their application to Crown corporations.

Emphasis on Effective Risk Management Continues to Grow

Market and regulatory developments in relation to accounting standards, capital adequacy guidelines, and compliance have emphasized the need to improve corporate governance through effective risk management. Boards are increasingly involved in risk management and are demanding improvements in risk policy, compliance and financial reporting. The continued emphasis on risk management trends by regulators, notably through the Bank for International Settlements, and by rating agencies and investors support ongoing advancements and continued interest in enterprise risk management and the role it can play in organizations.



1952

CMHC National Office opens its doors on Montréal Road in Ottawa.

Increased Competition for Skilled Workers

The modern labour market is in the midst of change. Just as an aging population is affecting housing needs and preferences across the country, the pending retirement of many from the baby-boom generation is beginning to create talent management issues for organizations. In Canada, the number of men and women age 55 and over who are employed increased by 35% between 2001 and 2004, and this population now makes up 13 per cent of the employed workforce. Conversely, there continues to be fewer workers to take the place of those that are retiring.

As a result of these workforce demographics, growing international competition and the rapid pace of technological development and innovation, many employers are increasingly aware and concerned about possible skill shortages and the need to foster skills development and learning among new labour market entrants as well as the existing workforce. These same factors are also reinforcing the need to adopt competitive human resource management practices to attract and retain a skilled workforce, who find themselves increasingly in demand.

**PROUD PAST
BRIGHT FUTURE**

Since our beginnings, we have been at the forefront of human resources practices, introducing leading edge programs and policies, and flexible benefits packages and options to respond to employee life changes and lifestyle choices. Our current focus on succession management reflects our desire to ensure we have the skills and expertise required to fulfill our mandate and provide valuable programs and services to Canadians. In 2006 and beyond, we will continue this focus to ensure our employees have the most up-to-date tools to succeed in their jobs and the supportive environment needed to advance. Our solid tradition of ethics and our values will also continue to underpin our activities as we move forward.

ANALYSIS OF OUR PERFORMANCE

We Introduced Innovations in Human Resource Management

CMHC has put in place a suite of human resources products that benchmark favourably against the best practices of external organizations. Our organization benefits considerably from the strength of our human resources product suite, which includes flexible work policies, progressive leave policies, competitive compensation package, and a values and ethics program.

In 2005, a high priority was placed on ensuring a good succession management framework for the Corporation. We brought greater precision to the succession management process by identifying corporate critical positions with vulnerable incumbents at all levels of the Corporation. This analysis was supplemented with an assessment of potential successors, and action plans are now being implemented for these positions. We also began to widen the scope of succession management through the design of an integrated talent management framework, which will be completed in the upcoming year.

Overall, the need to continue to focus on the development and recruitment of employees is demonstrated by the slight decline in the retention of new recruits over last year. CMHC will continue to monitor our retention rates as a means of gauging the effectiveness of our human resources practices, including the new talent management framework, and as a guide to how effectively we are keeping pace with the competitive labour market.

A significant portion of training investment originally slated for 2005 was deferred to 2006 in order that training initiatives could be better targeted to the corporate needs and priorities identified through the implementation of the succession management framework.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Training investment per staff year (\$)	2,090	2,546	1,857 [†]	n/a
Retention rate of recent recruits (%)	96.0	Maintain 96% for 1-year retention	94.1 [†]	93% for 3–5 year retention

* Target met or exceeded

* Target substantially met

† Target not met

OUR STRENGTHS

- Strong, well-accepted values that guide all activities.
- Demonstrated evidence that the Corporation is well-managed, through four Special Examinations conducted by the joint examiners.
- Enhanced priority-setting exercise ensures alignment of priorities with resources.
- Comprehensive risk framework and extensive business performance reporting against corporate objectives and targets.

CHALLENGES AND RISKS

- Ensuring processes are in place to strengthen management's ability to respond to challenges in meeting objectives by reprioritizing and redirecting resources where needed.
- Developing enhanced methodologies and metrics to better demonstrate the value that CMHC's suite of programs and services bring to Canadians.
- Competing for individuals with the skills that CMHC requires in a public sector environment.

NEXT STEPS

- Complete the implementation of succession management plans for all critical positions at CMHC and launch the talent management initiative.
- Complete an asset allocation review of the Insurance and Securitization funds to allow better matching of assets with liabilities and better return optimization.

We promoted the value of CMHC to Canadians

As Canada's national housing agency, we believe that it is important for Canadians to comprehend the contribution of the federal government to housing and the value of quality housing in their lives. As such, the growth of awareness of CMHC programs and services remains a priority for the Corporation.

In 2005, we conducted spring and fall advertising campaigns targeting Canadian homebuyers and homeowners. The campaigns promoted the range of products and tools that we have made available to help Canadians make informed housing decisions and support energy efficiency. Unaided awareness of CMHC as Canada's housing agency increased to 27% in the fall of 2005 from 21% the year before, while overall awareness increased slightly to 81% from 80% a year earlier.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Percentage of overall awareness of CMHC	80%	76%	81%*	76%
Percentage of unaided awareness of CMHC	21%	18%	27%*	18%

* Target met or exceeded * Target substantially met † Target not met

We invested in proven and reliable technologies

Because technological investments help Canadians get their mortgages approved faster, and provide fast and flexible online access to the wealth of expertise the Corporation has to offer, CMHC strives to invest in technologically advanced reliable systems. In 2005, CMHC's information technology systems were available for business essentially at all times as reflected in its overall indicator of technical excellence, the technology reliability index, which remained steady at 99.8% in 2005.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Technology reliability index for key systems (%)	99.8	99.7	99.8*	99.7
Operating budget spent on information technology (%)	16.7	16.0	15.9*	16.0

* Target met or exceeded * Target substantially met † Target not met

BUSINESS HIGHLIGHTS

The following table summarizes the Corporation's results and projections for key business areas.

CORPORATE RESULTS	2001 Actual	2002 Actual	2003 Actual	2004 Actual	2005 Actual
Total Assets (in millions of dollars)*	28,465	41,430	59,925	81,008	101,093
Total Liabilities (in millions of dollars)*	27,200	39,621	57,449	77,582	96,665
Total Equity (in millions of dollars)	1,265	1,809	2,476	3,426	4,428
Total Revenue (in millions of dollars)*	4,106	4,634	5,563	6,560	7,334
Total Expenses (in millions of dollars)*	3,543	3,779	4,556	5,161	5,870
Operating Expenses (in millions of dollars)*	214	257	294	305	303
Net Income After Income Taxes (in millions of dollars)	345	544	667	950	1,002
Reserve Fund (in millions of dollars)	42	56	91	134	143
Staff Years	1,736	1,772	1,799	1,814	1,804
INSURANCE AND SECURITIZATION					
Annual Insurance Units Approved	507,237	583,225	517,795	652,573	746,157
Insurance in Force (in millions of dollars)	211,500	224,345	230,000	243,800	273,700
Net Insurance Claims Expense (in millions of dollars)	335	139	188	51	119
Annual Securities Guaranteed (in millions of dollars)	8,489	20,642	27,017	29,592	30,374
Securitization Guarantees in Force (in millions of dollars)	34,684	45,473	59,994	80,800	103,709
Premiums and Fees Received (in millions of dollars)	1,049	1,330	1,263	1,512	1,560
Investments (including cash) (in millions of dollars)**	4,914	6,021	6,910	8,097	9,380
Net Income After Income Taxes (in millions of dollars)	323	530	632	907	993
Unappropriated Retained Earnings (in millions of dollars)	260	348	123	155	854
Retained Earnings Set Aside for Capitalization (in millions of dollars)	938	1,380	2,237	3,112	3,406
HOUSING PROGRAMS					
New Commitments Under Renovation Programs (units)	23,800	24,850	18,467	25,539	21,990
New Commitments On-Reserve Non-Profit Units	1,050	1,050	968	978	1,045
Estimated Households Assisted Through Long-Term Commitments	640,800	638,850	635,900	632,650	633,000
Housing Program Expenses (in millions of dollars) (excluding operating expenses)	1,789	1,828	1,972	2,006	1,973
LENDING					
Loans and Investments in Housing Programs (in millions of dollars)	15,239	14,586	14,075	13,669	13,170
Borrowings from Capital Markets (in millions of dollars)	11,081	10,242	10,244	9,212	9,467
Borrowings from the Government of Canada (in millions of dollars)	5,692	5,474	5,232	5,045	4,899
Net Income After Income Taxes (in millions of dollars)	22	14	35	43	9
CANADA HOUSING TRUST					
Canada Housing Trust Assets (in millions of dollars)	4,716	18,125	35,422	54,975	73,208
Canada Housing Trust Liabilities (in millions of dollars)	4,716	18,125	35,422	54,975	73,208

* Historical results and future year plans have been restated to reflect the consolidation of Canada Housing Trust which took effect on 1 January 2005.

** Excluding investments related to repurchase activities.

*** 2006 plans were revised following November 2005 announcement of one-year extension of the renovation programs.

AND OUTLOOK

CORPORATE RESULTS	2005 Plan	2006 Plan	2007 Plan	2008 Plan	2009 Plan	2010 Plan
Total Assets (in millions of dollars)*	88,588	107,111	109,534	104,243	106,344	107,354
Total Liabilities (in millions of dollars)*	84,430	101,802	103,223	96,889	97,911	97,779
Total Equity (in millions of dollars)	4,158	5,309	6,311	7,354	8,433	9,575
Total Revenue (in millions of dollars)*	7,069	7,968	8,137	8,141	8,069	8,168
Total Expenses (in millions of dollars)*	5,859	6,538	6,652	6,596	6,470	6,476
Operating Expenses (in millions of dollars)*	368	384	383	391	398	406
Net Income After Income Taxes (in millions of dollars)	817	965	1,002	1,043	1,079	1,142
Reserve Fund (in millions of dollars)	133	139	136	133	129	125
Staff-Years	1,902	1,917	1,857	1,863	1,862	1,874
INSURANCE AND SECURITIZATION						
Annual Insurance Units Approved	564,589	574,633	571,691	568,220	571,267	575,130
Insurance in Force (in millions of dollars)	254,900	264,027	271,911	277,634	282,805	287,335
Net Insurance Claims Expense (in millions of dollars)	202	171	201	217	236	231
Annual Securities Guaranteed (in millions of dollars)	18,000	18,000	18,000	18,000	18,000	18,000
Securitization Guarantees in Force (in millions of dollars)	91,800	104,700	105,900	98,700	98,300	90,300
Premiums and Fees Received (in millions of dollars)	1,503	1,442	1,467	1,508	1,556	1,606
Investments (including cash) (in millions of dollars)**	9,007	10,075	11,167	12,239	13,394	14,631
Net Income After Income Taxes (in millions of dollars)	805	964	1,005	1,046	1,083	1,147
Unappropriated Retained Earnings (in millions of dollars)	182	1,497	2,201	3,089	4,019	5,094
Retained Earnings Set Aside for Capitalization (in millions of dollars)	3,819	3,648	3,949	4,107	4,260	4,331
HOUSING PROGRAMS						
New Commitments Under Renovation Programs (units)	22,675	19,054***	904	904	904	904
New Commitments On-Reserve Non-Profit Units	892	4,007	922	922	922	922
Estimated Households Assisted Through Long-Term Commitments	632,000	632,000	626,200	622,000	615,600	611,200
Housing Program Expenses (in millions of dollars) (excluding operating expenses)	2,103	2,059	1,883	1,913	1,875	1,862
LENDING						
Loans and Investments in Housing Programs (in millions of dollars)	13,348	13,186	12,934	12,811	12,651	12,443
Borrowings from Capital Markets (in millions of dollars)	9,317	9,146	9,124	9,342	9,405	9,419
Borrowings from the Government of Canada (in millions of dollars)	4,848	4,651	4,446	4,235	4,025	3,822
Net Income After Income Taxes (in millions of dollars)	12	1	(3)	(4)	(4)	(4)
CANADA HOUSING TRUST						
Canada Housing Trust Assets (in millions of dollars)	63,686	81,016	82,429	76,019	76,978	76,978
Canada Housing Trust Liabilities (in millions of dollars)	63,686	81,016	82,429	76,019	76,978	76,978

MANAGEMENT'S DISCUSSION AND ANALYSIS

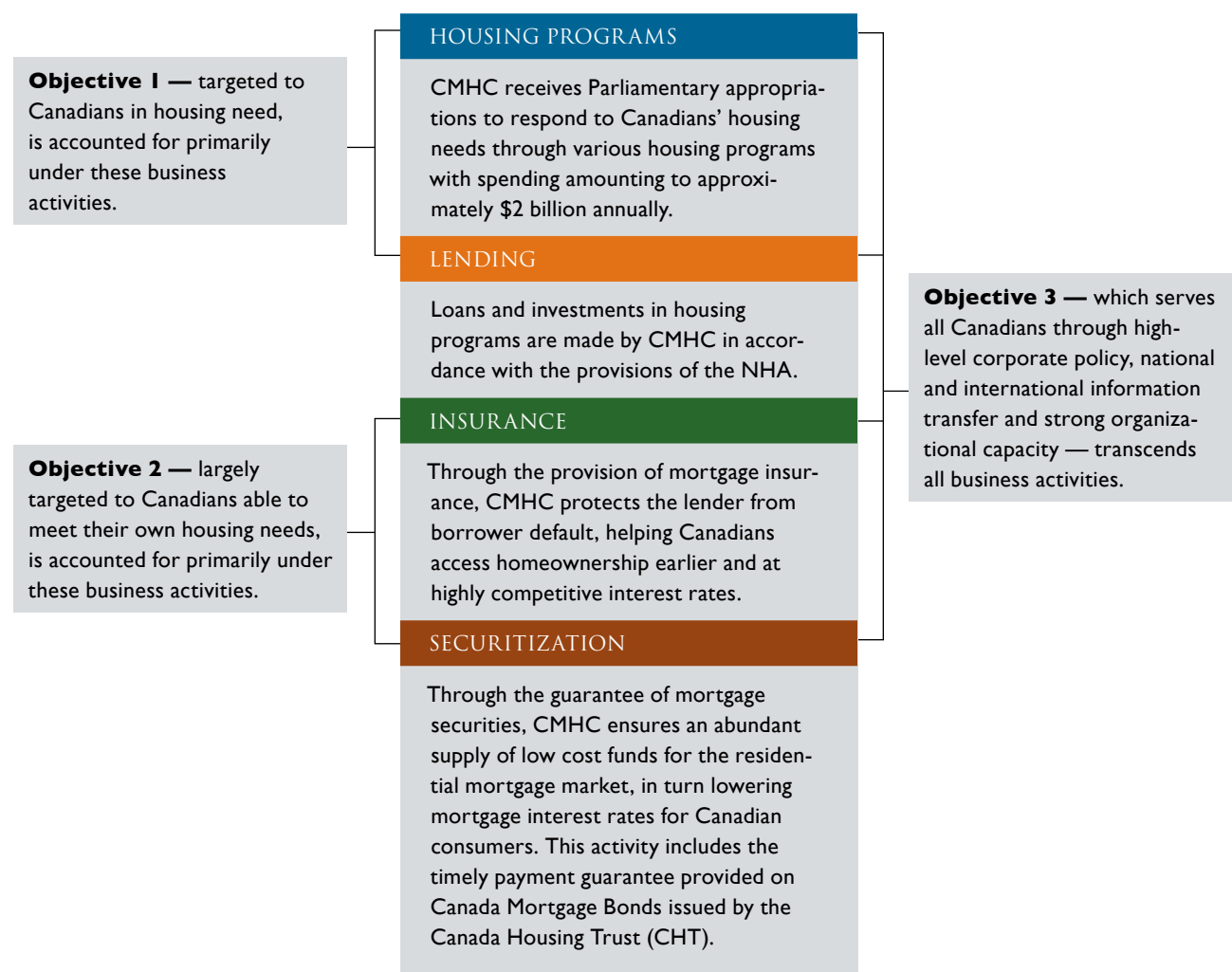
Financial Analysis of Operations

Risk Management

FINANCIAL ANALYSIS OF OPERATIONS

CMHC has four business activities that account for the full range of its business lines and support functions. These business activities capture all business transactions, investments, Parliamentary appropriations and spending.

The financial results comprise all of our varied activities, ranging from housing programs for those in need to insurance and securitization activities that facilitate access to more affordable housing through the Canadian housing finance system. While the Corporation's activities that help Canadians in need are operated on a break-even basis, other activities aimed at the efficiency of the housing finance markets are operated, as required by our mandate, on a more commercial basis. Accordingly, net income is predominantly a function of the Insurance and Securitization activities while revenues and expenses reflect the entire breadth of CMHC activities.



Significant Accounting Standards Implemented in 2005

Effective 1 January 2005, the Corporation adopted *Accounting Guideline 15: Consolidation of Variable Interest Entities* (AcG-15), issued by the Canadian Institute of Chartered Accountants, which requires the consolidation of certain variable interest entities that are subject to control on a basis other than through ownership of a majority of voting interest. This change in accounting policy has been applied retroactively and prior years' figures have been restated.

AcG-15 defines a variable interest entity as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. Canada Housing Trust (CHT) is such a variable interest entity. AcG-15 requires the primary beneficiary to consolidate variable interest entities and considers an entity to be the primary beneficiary if it is exposed to the majority of the expected losses or will receive the majority of the expected residual returns, or both. CMHC is considered the primary beneficiary of Canada Housing Trust. Therefore, for accounting purposes, Canada Housing Trust is consolidated with the financial statements of CMHC.

The Trustee of Canada Housing Trust has entered into agreements with a number of parties, including CMHC, to provide various services to Canada Housing Trust. Under one such agreement, CMHC, as agent of Canada, has guaranteed the timely payment of the interest payments and the principal at maturity on all Canada Mortgage Bonds issued by Canada Housing Trust to date. Once provided, the guarantee becomes an obligation of the Government of Canada and is irrevocable until full repayment of the Canada Mortgage Bond at maturity (typically within five years of issuance). In addition, under a Financial Services Advisor Agreement, CMHC gauges market demand for bond issuance and assesses the potential supply of housing loans available to be packaged for sale to Canada Housing Trust.

Pursuant to the purchase agreements and other relevant program agreements, Canada Housing Trust purchases ownership interest in pools of *National Housing Act* Mortgage-Backed Securities (NHA MBS), which are pledged as security for Canada Mortgage Bonds issued by Canada Housing Trust to finance the purchases. The assets of Canada Housing Trust are neither owned by, nor held for the benefit of, CMHC. Consequently, the assets are not available to CMHC for its general corporate purposes or to satisfy any liabilities of CMHC. Details of Canada Housing Trust's interest in the NHA MBS and the Canada Mortgage Bonds issued to finance the purchases are disclosed in the notes to the financial statements.

The impact from the consolidation of Canada Housing Trust on the consolidated financial statements at 31 December 2005 is an increase of \$72,751 million (2004 — \$54,336 million) in consolidated assets and liabilities, as well as a \$2,617 million (2004 — \$1,906 million) increase in both revenues and expenses. As a result, there is no impact on consolidated net income or consolidated retained earnings.

The impact of the consolidation of Canada Housing Trust on the 2005 financial statements is outlined in the table below.

Results (in millions of dollars)	CMHC	CHT	Elimination entries	Consolidated FS
Revenues	4,717	2,675	(58)	7,334
Expenses	3,253	2,675	(58)	5,870
Income Taxes	462	—	—	462
Net Income	1,002	—	—	1,002
Assets	28,342	73,208	(457)	101,093
Liabilities	23,914	73,208	(457)	96,665
Retained Earnings	4,403	—	—	4,403

CORPORATE FINANCIAL RESULTS

(in millions of dollars)	2004 Actual*	2005 Plan	2005 Actual	Results Against Plan	2006 Plan
Revenues	6,560	7,067	7,334	104%	7,968
Expenses	5,161	5,857	5,870	100%	6,538
Income Taxes	449	393	462	118%	465
Net Income	950	817	1,002	123%	965
Retained Earnings	3,401	4,133	4,403	107%	5,284
Resource Management**					
Operating Expenses	305	368	303	82%	384
Staff Years	1,814	1,902	1,804	95%	1,917

* Historical results and future year plans have been restated to reflect the consolidation of Canada Housing Trust which took effect on 1 January 2005.

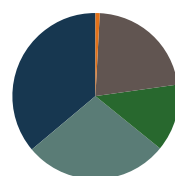
** Canada Housing Trust has no staff years and all operating expenses are reimbursed by the swap counterparties.

Net Income

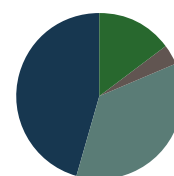
Net income exceeded the \$1.0 billion threshold for the first time in our 60 year history, led by Insurance's \$951 million of net income as this activity continues to reap the benefits of a commitment to operational excellence and favourable economic conditions. The higher than planned revenue came about due to lower long-term mortgage rates creating sustained demand in many housing markets across the country. The resultant increase in sales combined with rising house prices contributed significantly to the net income result.

In 2006, net income is expected to moderate slightly after the record breaking 2005 year, but will continue to benefit from strong housing markets.

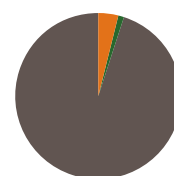
2005 Revenues



2005 Expenses



2005 Net Income



■ Canada Housing Trust
 ■ Lending Programs
■ Securitization
 ■ Housing Programs
■ Insurance

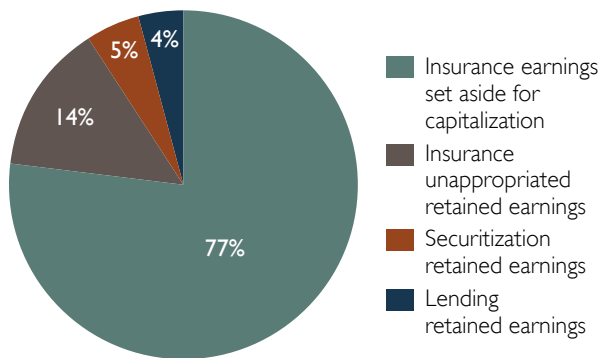
Financial Plan Assumptions	2004 Actual	2005 Plan	2005 Actual	2006 Plan
MLS® Average Resale Price (\$)	226,283	236,500	249,311	238,000
Mortgage Rate (%)				
1-year	4.59	5.09	5.06	6.47
5-year	6.23	6.77	5.99	7.81
Unemployment Rate (%)	7.2	7.2	7.2	7.2

Retained Earnings

As a federal Crown corporation, CMHC's financial results are an integral part of the Government of Canada's financial results and budgetary projections. Both budgeted and actual federal annual surplus figures include CMHC's net income (planned and actual respectively) for the fiscal year in question.

CMHC's retained earnings are the result of an accumulation of past profits (net income) and losses, and therefore our retained earnings represent the federal government's investment in CMHC.

The use of CMHC's retained earnings is governed by the CMHC Act and the National Housing Act. In particular, Insurance and Securitization retained earnings may only be used for the capitalization of CMHC's Insurance and Securitization operations, for payment of a dividend to the Government of Canada, for purposes of the National

Retained Earnings by Business Activities in 2005

Housing Act or the *CMHC Act* or any other purposes authorized by Parliament relating to housing, and for retention. To date, Insurance retained earnings have been used for capitalization and any excess used for retention (unappropriated retained earnings). Securitization retained earnings have also been used for retention.

Because of the fact that CMHC's annual net income is accounted for by the Government of Canada, use of Insurance or Securitization retained earnings for purposes other than capitalization, payment of a dividend or retention effectively represents a new expenditure by the Government of Canada. Lending retained earnings are subject to statutory limits which, when exceeded, trigger a dividend to the Government of Canada.

Effective 1 January 2005, the Board of Directors approved a 15% decrease to the target level of insurance capital in accordance with the guidelines set out by the Office of the Superintendent of Financial Institutions (OSFI). The decrease was supported by dynamic financial analysis techniques that ensured that minimum OSFI capital levels would only be breached in extreme adverse housing market conditions, in accordance with the guidelines set out by OSFI. This decrease brings the insurance capital target more in line with industry levels.

The CMHC target level of capital reflects the fact that CMHC insurance products and services are offered in less well served markets and/or in support of specific government priorities, where the insurance risk is often higher.

In 2005, CMHC achieved its targeted level of capitalization. This will ensure there is sufficient capital available to meet future risks and follows prudent business practices. While the current economic and housing conditions are very favourable to the mortgage insurance business, economic conditions are cyclical, and insurance providers need to recognize this in managing their business over the long term. In addition, the capital requirement must be viewed in the context of an insurance business with \$274 billion of policies in force.

CMHC expects to maintain 100% of its target level of capital for the foreseeable future due to the expected continued strong performance of the insurance business.

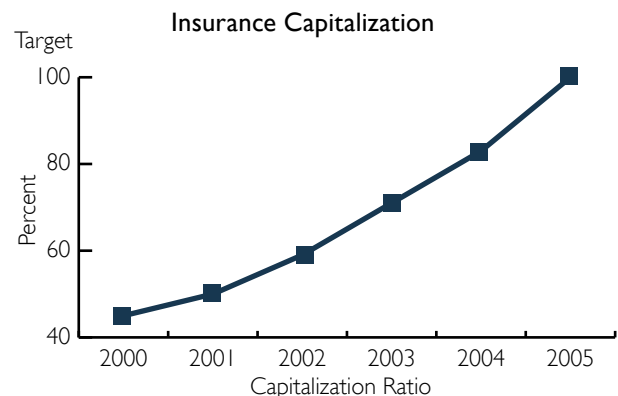
The strength in housing markets that helped expand Insurance retained earnings by a record amount in 2005 is expected to moderate in the future but still remain positive for the mortgage insurance activity. Under these conditions retained earnings could more than double over the next five years while capitalization requirements would increase by approximately one third. An economic downturn or the entry of new competitors or the use of Insurance and Securitization retained earnings pursuant to the *National Housing Act* would result in lower retained earnings going forward.

Resource Management

Efficiency and cost effectiveness are a long-standing focus at CMHC. With personnel costs comprising approximately 65% of operating expenses, staff-year consumption largely drives costs. In 2005, staff years increased by less than 1% despite record business volumes and the introduction of new products. Operating costs also grew modestly. Canada Housing Trust has no staff years and all operating expenses are reimbursed by the swap counterparties.

Income Taxes

CMHC is a taxable federal Crown corporation and as such pays federal income tax but is not subject to provincial income tax. In 2005, CMHC paid close to half a billion dollars in income taxes, a level comparable to 2004 and similar tax payments are anticipated for the foreseeable future. Canada Housing Trust is subject to federal and provincial income taxes on the amount of taxable income for the period and is permitted a deduction for all amounts paid or payable to Canada Housing Trust's beneficiary in determining their taxable income. As all income was distributed to the beneficiary, no provision for income taxes has been reflected in the consolidated financial statements.



FINANCIAL ANALYSIS BY CORPORATE OBJECTIVE

While all of our activities help us achieve each of our three broad corporate objectives, the Lending and Housing Programs activities are aimed primarily at “Helping Canadians in need” and the Insurance and Securitization activities are instrumental in “Facilitating access to more affordable, better quality housing for all Canadians.” Accordingly, the discussion of financial results of each activity is discussed only once and as a whole under the primary objective served by the activity.

OBJECTIVE ONE — HELP CANADIANS IN NEED

CMHC aids Canadians in need through grants and contributions for housing and the provision of loans at below market rates. Approximately 21% of our resources are devoted to developing and delivering housing solutions for Canadians in need and preserving the existing stock of affordable housing.

Housing Programs

While the Canadian economy remains one of the strongest in the world, many Canadians remain in core housing need across the country including a disproportionate amount of Aboriginals, recent immigrants and seniors. CMHC continues to address the situation through a variety of programs, delivery mechanisms and partnerships. These include the existing social housing agreements with the provinces and territories, the Affordable Housing Initiative, on-reserve and non-profit housing agreements, as well as renovation and partnership programs.

Results Highlights (in millions of dollars)	2004 Actual	2005 Plan	2005 Actual	Results Against Plan	2006 Plan
Housing Program Expenses	2,006	2,103	1,973	94%	2,059
Operating Expenses	101	105	103	98%	108
Appropriations	2,107	2,208	2,076	94%	2,167

In total, the Corporation spends over \$2 billion annually responding to Canadians' housing needs through these various programs. Of the total spent, approximately \$1.7 billion is related to long-term commitments made in prior years with approximately \$1 billion of that amount being transferred to provinces/territories under Social Housing Agreements. The Corporation is reimbursed for these expenditures, including interest rate losses incurred by the Lending activity, through Parliamentary appropriations approved annually by the Government of Canada.

In addition, as announced in the 2005 Federal Budget, the Government has authorized the Corporation, in conjunction with Indian and Northern Affairs Canada, to make an investment of \$295 million over five years in First Nations housing on reserves. The funding is to be used to facilitate the construction of an estimated 6,400 new housing units, the creation of approximately 5,400 serviced lots and the renovation of an estimated 1,500 existing housing units.

Housing program expenses are lower than plan by 6% or \$130 million and comparable to 2004. Approximately half of the variance to plan is due to lower than planned interest costs due to lower than expected interest rates. The balance relates primarily to spending in the Affordable Housing Initiative and Renovation programs due to some delays in commitment activity and the shortage of available contractors (due to strong renovation markets) in some regions. CMHC's plan for 2006 provides for full utilization of the approximately \$2 billion of government appropriations.

Lending

CMHC makes loans and investments in housing projects in accordance with the provisions of the *National Housing Act*. Operated on a break-even basis, CMHC lending programs provide low-cost financing for social housing projects, thus maximizing the effectiveness of government housing subsidies. With the exception of interest losses arising from prepayment and mortgage rate renewal risks that exist in certain loans granted prior to 1993, the programs were designed to cover funding and administrative costs.

Results Highlights (in millions of dollars)	2004 Actual	2005 Plan	2005 Actual	Results Against Plan	2006 Plan
Interest and Investment Income	1,011	887	909	102%	856
Interest Expense	939	864	898	104%	835
Operating Expenses	19	22	18	82%	21
Net Income	43	12	9	75%	1
Reserves	134	133	143	108%	139

In 2005, both the number of new loans initiated and renewals of existing loans were significantly above target. The \$197 million in new business loans exceeded its target by 25% largely due to increased commitments on reserve. Subsequent renewals also exceeded target by 13% due to several unexpected loan renewals in 2005.

While direct lending loans were above planned levels, in general, these programs have been declining over the last several years, replaced by other, more flexible mechanisms to assist Canadians in need. Thus, there is a downward trend in both the loan portfolio and the debt issued to fund the loans, which currently stand at some \$13 billion (\$14 billion in 2004). The number of loans increased slightly while the average size is decreasing resulting in an overall decreasing portfolio. This means that the average costs per dollar of loan being administered is increasing. The loans were funded by borrowings from the Government of Canada up to the end of 1992. Since then, the Corporation has borrowed solely from the capital markets as an agent of Canada.

The main source of income for the Lending Activity is interest earned on its loans and investments while its biggest expense is its borrowing cost.

Net income derived from the Lending Activity is small relative to the Corporation's overall performance and can be significantly affected by the recovery of prepayment and repricing losses from the Government (nil in 2005 compared to \$9 million planned in 2005 and \$24 million in 2004) and fluctuations in income due to the application of hedge accounting standards as set out in Accounting Guideline 13 (AcG-13), (\$5 million in 2005 compared to \$1 million planned and \$16 million in 2004). The Corporation did not recover any prepayment losses in 2005 as it would have then exceeded its reserve fund limit. CMHC's derivative financial instruments mitigate market risks related to loans and borrowings, but many of them do not meet the criteria for hedge accounting specified in AcG-13. As a result, many derivatives are now adjusted to current fair value on the Balance Sheet, with gains and losses resulting from the changes in fair value recognized in income, causing income volatility from year to year.

CMHC is authorized to retain its annual net income from the Lending activity in a Reserve Fund which currently has a limit of \$175 million, \$50 million of which is designated for fluctuations resulting from the application of AcG-13. Amounts in the general reserve over the \$125 million must be returned to the Government of Canada. As of 31 December 2005, the Reserve Fund stands at \$143 million of which \$21 million results from the impact of AcG-13.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Annual direct lending — new business (in millions of dollars)	158.2	158 to 170	197*	313 to 337
Annual direct lending — subsequent renewals (in millions of dollars)	1,161	1,628 to 1,750	1,843*	1,653 to 1,778

* Target met or exceeded * Target substantially met † Target not met

As shown, the Corporation exceeded both targets for direct lending in 2005 and was well above 2004 results. This was due to a more concerted effort by the Corporation to obtain new business while retaining the existing business. The 2006 plan for new business is nearly double the 2005 amount as a result of additional investments for on-reserve housing. The 2006 plan for renewals is based on the total loans up for renewal in 2006.

OBJECTIVE TWO — FACILITATE ACCESS TO MORE AFFORDABLE, BETTER QUALITY HOUSING FOR ALL CANADIANS

The Corporation helps Canadians access affordable mortgages through its commercial activities in the housing finance sector. Approximately 44% of our resources are dedicated to the execution of its market housing activities, primarily in Insurance.

Insurance

CMHC protects lenders from borrower default through the provision of mortgage insurance thus assisting the Canadian housing finance market to function effectively and providing an efficient and cost-effective means of facilitating market-based housing solutions. The vast majority of Canadians are, as a direct result, able to access affordable housing choices quicker and at lower interest rates than they would be able to without mortgage insurance within a highly stable, predictable and geographically invariant Canadian housing finance system.

Results Highlights (in millions of dollars)	2004 Actual	2005 Plan	2005 Actual	Results Against Plan	2006 Plan
Premium and Fees Revenue	1,095	1,110	1,175	106%	1,249
Investment Income	397	424	468	110%	465
Operating Expenses	136	160	137	86%	166
Net Claims Expense	51	202	119	59%	171
Net Income	875	775	951	123%	928
Earnings Set Aside for Capitalization	3,112	3,819	3,406	89%	3,648
Unappropriated Retained Earnings	—	—	657	n/a	1,274

The main sources of revenues are insurance premiums (collected once at inception of the mortgage and valid for as long as the mortgage is outstanding), application fees and investment income earned on the investment portfolio. CMHC is mandated to operate the insurance business on a commercial basis meaning that premiums and fees collected over time will cover related claims and other expenses and provide for a reasonable rate of return to the Government of Canada thus ensuring a fair playing field with private sector insurance providers. Accordingly, the mortgage insurance activity continues to be operated at no cost to Canadian taxpayers.

The economy has a significant influence on the performance of CMHC's insurance business. Economic conditions and more specifically housing market conditions over the past several years have been exceptional, which has meant increased opportunities for home-ownership for Canadians. For CMHC, these economic factors along with the introduction of new products and CMHC's commitment to service excellence have resulted in successive years of escalating business volumes and corresponding premiums revenues as well as lower than expected net claim losses. This has also meant that CMHC has remained Canada's mortgage insurer of choice despite vigorous competition. In addition, CMHC has ensured that borrowers are charged a fair price as demonstrated by the 15% reduction in the premium for first time homebuyers, the second such premium reduction in two years.

Mortgage insurance approvals for 2005 reached an all-time high of 746,157 units, a 14% increase over the previous high of 652,573 units in 2004. Premiums received in 2005 were over \$1.4 billion compared to \$1.35 billion in 2004 despite the April 2005 premium reduction.

Since premiums are deferred and recognized over the life of the insured mortgage, some 93% of the 2005 premium revenue is attributable to premiums received prior to 2005.

Net claims expense is also affected by the economic conditions. It has two components. The first component is the actual loss on claims paid during the year. The other component is the change in the provision or estimate of claims that have already occurred but for which no claim has yet been filed with CMHC. This estimate is based upon historical experience, prevailing legal, economic, social and regulatory trends, and expectations as to future developments (primarily in the next 12 to 18 months). It is evaluated annually by an external actuary who reviews historical experience to determine if changes are required to assumptions regarding expected claim outcomes. In 2005, both of these components contributed to lower than planned net claims expense. Net claims expense, however, follows a cyclical trend. As recently as 2001, it was \$335 million representing 45 per cent of premium and fees revenue that year. This year, the expense was \$119 million representing 10 per cent of premium and fees revenue. While net claims expense declines in good economic times, it will undoubtedly rise again when a market downturn occurs. Since the last general economic downturn, CMHC's outstanding insurance in force has risen from about 20% of residential mortgage debt to more than 40% today.

Having benefited from strong economic conditions of the last several years, net income is expected to moderate slightly in 2006. In addition, the pending introduction of a new mortgage insurer will put pressure on the Corporation to be innovative and efficient in order to remain Canada's mortgage insurer of choice and meet its 2006 projections.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Short-term profitability:	12.8%	<14.7%	11.7%*	13.4%
Operating expense ratio for mortgage insurance (%)				

* Target met or exceeded * Target substantially met † Target not met

The 2005 operating expense ratio was lower than planned due to additional revenues generated by greater than planned business volumes together with somewhat lower expenses. The lower expenses were due to the Corporation's ability to efficiently manage changing initiation and claims settlement business volumes. The 2005 operating expense ratio was lower than the 2004 ratio due to the additional revenues.

Securitization

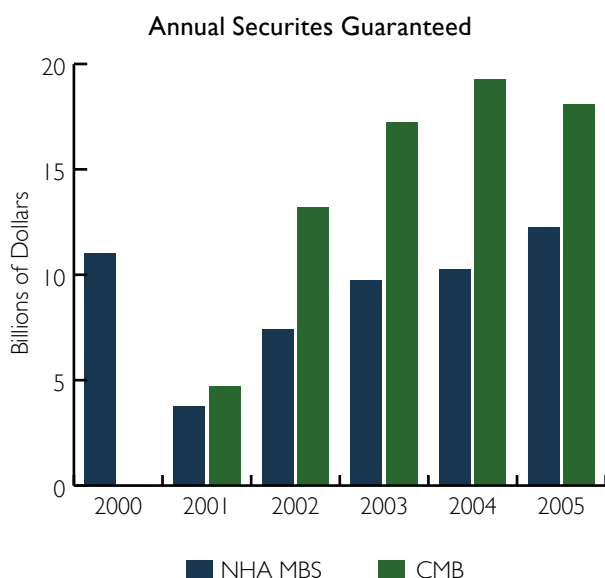
Through the guarantee of mortgage backed securities, CMHC ensures an abundant supply of low cost funds for the residential mortgage market. This in turn means Canadians benefit from lower mortgage interest rates than they would otherwise enjoy in the absence of CMHC's presence within the secondary mortgage market. The results of Canada Housing Trust are also included in this activity.

Results Highlights (in millions of dollars)	2004 Actual	2005 Plan	2005 Actual	Results Against Plan	2006 Plan
Canada Housing Trust Revenue	1,970	2,432	2,675	110%	3,207
Fees Revenue	40	40	49	123%	47
Investment Income	12	11	16	146%	14
Canada Housing Trust Expense	1,970	2,432	2,675	110%	3,207
Operating Expenses	5	6	5	83%	6
Net Income	32	30	42	140%	36
Retained Earnings	155	182	197	108%	223

Canada Housing Trust's main source of revenue is income from the investments it holds and its main expense is interest on outstanding Canada Mortgage Bonds. The Trust is designed to have zero net income. The higher than expected Canada Mortgage Bonds volumes have resulted in higher than planned revenues and expenses.

The main source of revenues for CMHC's guarantee activity are guarantee fees, application fees and investment income earned on its investment portfolio. As CMHC is mandated to operate its securitization business on a commercial basis, guarantee fees collected over time are expected to cover related expenses and provide for a reasonable rate of return to the Government of Canada. Similar to the insurance business, securitization is operated at no cost to Canadian taxpayers.

Securitization volumes have grown in recent years, particularly since the inception of the Canada Mortgage Bond Program in 2001. The 2005 revenues were positively impacted by growth in recent years benefiting, in part, from the introduction of a new product, variable rate Mortgage-Back Securities, in 2004. The guarantee fees are received at inception of the related security issue and recognized as income over the term of the security issue (typically five years). Accordingly, approximately 90% of the 2005 guarantee fee revenue is attributable to fees received prior to 2005.



As a result of the application of AcG-15, the CMB guarantees also appear as a liability on the Consolidated Balance Sheet.

In 2005, net income was \$42 million, 40% higher than plan and 31% higher than 2004. The increase in net income versus plan and 2004 actual is mainly driven by higher issuance activity resulting in higher guarantee fees earned. In 2006, the Corporation expects to guarantee \$14 billion of Canada Mortgage Bond issuances, \$4 billion lower than the 2005 level. However, it is possible that the plan figure will be exceeded should there be continued strength in the Canadian mortgage markets. As a result of this projected decrease, net income is expected to be slightly lower in 2006.

Actual performance in 2005 is substantially better than 2005 plan and 2004 actual due mainly to the significant overachievement of revenues.

Corporate Performance Measures	2004 Results	2005 Target	2005 Results	2006 Target
Short-term profitability: Operating expense ratio for securitization (%) ¹	12.5%	<13.8%	8.6%*	11.7%

* Target met or exceeded * Target substantially met † Target not met

¹ Ratio of operating expenses over revenues excluding investment income, exclusive of Canada Housing Trust expenses and revenues.

OBJECTIVE THREE — ENSURE THE CANADIAN HOUSING SYSTEM REMAINS ONE OF THE BEST IN THE WORLD

CMHC continues to plan for the future by providing and disseminating research to support the continued evolution of Canada's housing markets and housing finance system, and to share its expertise with countries who wish to enhance their own housing systems. Approximately 35% of its resources are directed to this area of activity, with the vast majority of this directed to the domestic front. CMHC also prepares the way forward by ensuring a strong and solid corporation.

CMHC continued its commitment to research through the expenditure of \$49 million on research and information dissemination in 2005. CMHC also continued to sell its expertise abroad, resulting in revenues of \$1.3 million.

Future Accounting and Reporting Changes

The Corporation expects to adopt the following accounting standards in the future.

Financial Instruments, Hedges and Comprehensive Income

The Canadian Institute of Chartered Accountants has issued three new accounting standards — *Financial Instruments — Recognition and Measurement*, *Hedges* and *Comprehensive Income*. The Corporation will be implementing these standards on 1 January 2007. The principal impacts of the standards are detailed below.

- Other comprehensive income will be a new component of the equity of Canada and a new statement entitled Statement of Comprehensive Income will be added to the Corporation's Consolidated Financial Statements.
- Financial assets will be required to be classified as available for sale, held to maturity, held for trading, or as loans and receivables.
- For fair value hedges, where the Corporation is hedging changes in the fair value of assets, liabilities or firm commitments, the change in the value of derivatives and hedged items will be recorded in the Consolidated Statement of Income.
- For cash flow hedges where the Corporation is hedging the variability in cash flows related to variable rate assets, liabilities or forecasted transactions, the effective portion of the changes in the fair values of the derivative instruments will be recorded through other comprehensive income until the hedged items are recognized in the Consolidated Statement of Income.

RISK MANAGEMENT

CMHC is dedicated to achieving our public policy mandate and objectives, and applying rigorous commercial and regulatory risk management principles and best practices to identify, monitor, control and manage risks. Our commitment to enterprise risk management underlies our approach to effective senior management and Board governance. Enterprise risk management enables the Board and senior management to comprehensively assess and act on corporate risks and opportunities within CMHC's strategic planning efforts. It is a tool to facilitate alignment of priority objectives and resources to address stakeholder perspectives.

In 2005, CMHC acted to strengthen core elements of this process, focusing resources on the key criteria underlying effective enterprise risk management, as established by leading financial and regulatory institutions, as well as international rating agencies. This has included specific focus on enhancing governance and enterprise risk management processes in relation to strategic planning, and developing additional risk and performance measurement, control and reporting.

GOVERNANCE AND RISK MANAGEMENT OVERVIEW

The responsibility for risk management is shared between the Board of Directors, senior management, and operational units. The Board oversees CMHC's risks at the governing level, approving risk policies and ensuring that required processes and systems are in place to effectively manage risk. CMHC's senior management monitors risks and reports to the Board on CMHC's overall risk profile, recommends financial and non-financial risk policies and oversees CMHC's financial positions, risk exposures, financial strategies and performance. At the operating level, specialized risk functions exist to address legal, security, insurance and other specific financial and non-financial risks.

This structure is used in setting priorities, allocating resources and making effective decisions regarding risk management. CMHC's governance structure ensures that risks of significance are elevated from the operating activities and oversight functions to the senior management committees and the Board.

The consolidation of the Canada Housing Trust does not change how the Corporation manages the guarantee of mortgage-related securities, including Canada Mortgage Bonds.

2005 ACHIEVEMENTS

- Integration of enterprise risk management more directly with corporate planning, resource allocation and reporting processes.
- Establishment of a Chief Compliance Officer with a focus on treasury and investments-related activities.
- Continued focus on capital management through development of a credit exposure framework linking risk tolerances more closely with the capitalization and business requirements of its respective business activities.
- Enhanced performance metrics and planning efforts to more effectively incorporate capital and value management considerations.
- Industry leadership to implement fraud management strategies in mortgage lending.
- Business continuity planning updated to ensure appropriateness for unplanned contingencies.
- Concrete actions to protect sensitive information and data exchange.

CMHC's enterprise risk management process is a dynamic approach aimed at facilitating the identification of key risks that could have an impact on the development and achievement of corporate objectives and strategies. Given the mandate of CMHC and the commercial tools and strategies utilized to help fulfill that mandate, CMHC is exposed to a number of different risks across its businesses, classified into 13 enterprise risks, which are organized within three broad categories: strategic, infrastructure and specific (including financial) risks.

GOVERNING

Board of Directors — Risk oversight and policy approval

Audit Committee — Monitors financial activities and provides advice to the Board and approves the corporate risk landscape

MANAGING

Management Committee — Monitors risks and updates risk policies

Asset-Liability Committee — Recommends financial and non-financial risk policies and oversees asset/liability management

Investment Committee — Provides technical expertise and supports CMHC's investment strategies

Chief Compliance Officer — Proactively ensures that effective controls are in place, and that compliance issues are identified and reported

OPERATING

Specific activities are carried out by the:

- Enterprise Risk Management Office
- Risk Management Division
- Insurance (Risk Analysis)
- Actuarial Analysis Division of Finance
- Legal Division
- Audit and Evaluation Services
- Security Office

STRATEGIC RISKS

The identification and monitoring of strategic risks are important for moving CMHC forward and can significantly impact the achievement of corporate objectives.

Who Manages Strategic Risks

The Board of Directors has the ultimate responsibility for strategic direction and risk tolerance of CMHC. The senior management team, through the Management Committee, manages CMHC's strategic risks. The Management Committee is comprised of the President, Vice Presidents, General Managers and Executive Directors, representing the major business units and oversight functions. Each strategic risk has assigned responsibility to one, and in some cases, multiple members of the senior management team. Managers of business units and functional areas have a role to manage strategies within their area and must work with senior management to ensure strategies are aligned with the high level corporate objectives.

How We Manage Strategic Risks

Strategic risks are considered by senior management and the Board of Directors when evaluating and establishing overall corporate direction and strategy. CMHC's overall strategy is formulated by the President and senior management, in consultation with and subject to approval by the Board of Directors and the Minister responsible for CMHC. On an annual basis, the Board holds a strategic planning meeting to analyze and address strategic issues facing CMHC, and to renew and update the corporate objectives and priorities. The Board receives quarterly reports on plans and initiatives, and semi-annual risk landscape reviews containing an overview of future strategic risks and opportunities.

STRATEGIC RISKS

■ Mandate

Delivering the mandate and influencing changes to the mandate.

■ Business Environment

Understanding and managing business environment impact.

■ Relational

Managing key relationships, improving client service.

■ Organizational

Aligning corporate efforts to achieve objectives responsibly.

Key Strategic Risks

The corporate objectives provide direction for CMHC's strategic initiatives and activities. Identifying, monitoring and managing strategic risks in terms of CMHC's corporate objectives is therefore important. As CMHC's management of strategic risks is fully integrated in our strategic planning and priority setting process, the discussion of these risks is offered in greater detail in the Performance section of this report beginning on page 20, with a brief overview of key issues presented below.

Overview of key strategic risks

Developments in the Canadian mortgage insurance industry, including increasing competitive pressures, mean that CMHC must continue to develop appropriate strategies and products in order to maintain its market leader position and remain the insurer of choice. Efforts in this regard will be impacted by potential changes to the *Bank Act* review as well as implications of Basel II to mortgage portfolios of regulated financial institutions. In addition, the Department of Finance's review of a centralized borrowing model may impact future funding and hedging activities.

Organizational changes that occurred in 2005 will provide more specialized focus in delivering on corporate objectives. Some of these changes have included an improved focus on Aboriginal housing, merging of funding and securitization activities, investment staff consolidation, and a better focus on key business accounts. In 2006, changes will be implemented to realign resource allocation and planning processes to adjust more nimbly to changing business conditions and events.

INFRASTRUCTURE RISKS

Infrastructure risks relate to the risk of loss of corporate knowledge (people risk), loss resulting from deficiencies in internal business processes and controls (process risk), or disruption in information systems or processing facilities (technology risk). These are the risks that primarily impact internal operating activities and the resources necessary to keep the organization functioning and delivering on objectives. They are important elements in achieving an effective and efficient organization, particularly in this period of change in our operating environment.

Who Manages Infrastructure Risks

Management Committee, with specialized committees such as the Human Resources Council and operational units such as IT Strategy and Security groups, manages CMHC's infrastructure risks. Audit and Evaluation Services also support the management of infrastructure

INFRASTRUCTURE RISKS

■ People

Ability to have the right people in the right place at the right time.

■ Process

Managing current processes and adapting processes to support business needs.

■ Technology

Providing reliable technology and information systems to support business needs.

risks through its role of independently reviewing functions and related processes. Directors and Managers of all functional areas play a role in managing people, their business processes and related technology to carry out their responsibilities. As with strategic risks, each infrastructure risk has assigned responsibility to members of the senior management team.

How We Manage Infrastructure Risks

Effective management of CMHC's human capital is managed through corporate initiatives such as talent and succession management, learning and development, and techniques to ensure a representative workplace. Compensation is reviewed regularly against the marketplace to ensure it remains competitive. In addition, ethics principles and awareness are integrated into the organizational culture. Analysis of demographic trends, training programs for managers and employee orientation are additional examples of efforts CMHC puts forth to ensure effective management of key resources.

Effective internal processes must be in place and continually reviewed to ensure sound and timely decision making. As technology and the business environment continuously evolve CMHC remains committed to ongoing business process efficiency reviews and to the implementation of process improvement where needed. Periodic audits are conducted by Audit and Evaluation Services Division. Results from the "efficiency of operations review for multiples insurance" will be implemented in 2006–07. CMHC is also subject to a Special Examination every five years, as required by the *Financial Administration Act*. The last such Examination, which was completed by the joint examiners in 2004, indicated that no significant deficiencies were found in the systems and practices examined.

CMHC is faced with the ongoing challenge of maintaining and supporting key business systems such as those related to automated underwriting, securitization, treasury and risk management. Redundant sites and processes are continually updated to ensure that mission critical systems are available under virtually all circumstances. Strategic direction is provided through a specialized strategy and security group who identify strategic projects to improve overall business performance by leveraging current technologies. Management Committee sets the priorities for information technology initiatives and Audit and Evaluation Services Division conducts periodic audits.

Key Infrastructure Risks

The loss of corporate knowledge is a key risk for CMHC as it faces increasing retirements over the next few years. Consequently, CMHC will be focusing its attention on the last stages of a succession management strategy designed to identify potential successors for key positions and to provide them with the skills development, training and mentoring necessary to ensure an effective transfer of knowledge.

The risks, and the challenges of ensuring business processes are operating effectively to support sound and timely decision making are important for CMHC as it continuously strives to improve its internal processes. In 2005, a requisitioning, purchasing and procurement system was successfully piloted to support fairness, transparency, competition and best value in the procurement of goods and services. The system is now close to being rolled out. CMHC is also ready to roll-out a document management system that will classify and retain electronic records, thereby helping to mitigate the loss of corporate data or records.

The potential impact from a loss of service of systems that support mission critical functions is significant. Considerable work was completed in 2005 to implement redundant facilities to mitigate the risk and ensure that essential business processes continue to operate in an uninterrupted manner. An alternate mainframe will be moved to outside central Canada in 2006 to further ensure business continuity for CMHC's key systems and activities. This would mitigate the risk of a power failure across an entire power grid. CMHC's Information Technology Division has also established a strategy group to identify projects designed to improve overall business performance by taking advantage of current technology.

KEY FINANCIAL RISKS

Who Manages Financial Risks

CMHC's Asset/Liability Committee (ALCO) provides specialized expertise in relation to the management of investment credit risks, market risks and other financial risks for each of its lending, insurance and securitization activities. The Board of Directors is responsible for approving corporate risk policies, ensuring that the main risks of CMHC's activities have been identified and that appropriate systems to manage the risks are implemented. Other divisions, functions and committees involved in managing key financial risks include Finance, Risk Management Division, Actuarial Analysis Division, Insurance (Risk Analysis), Investments, Securitization and Treasury, Portfolio and Agreement Administration Division (loan portfolio), Chief Compliance Officer, Multiple Underwriting Committee, and the Investment Committee.

How We Manage Financial Risks

CMHC is exposed to credit, market and other financial risks from various sources, including directly from its investment, lending and hedging activities, and indirectly from potential claims arising from insurance and securitization activities. CMHC evaluates and manages its financial risks to ensure appropriate diversification, asset-liability matching, and optimization of returns, subject to risk tolerances approved by management and the Board.

The consolidation of the financial statements of Canada Housing Trust and CMHC does not alter the financial risks facing CMHC in relation to the Canada Mortgage Bond Program. Due to the significant differences in the financial risks of CMHC and Canada Housing Trust, they are discussed separately in this report.

FINANCIAL RISKS

■ Credit

Risk of loss associated with a counterparty or borrower failing to meet its obligations.

■ Market

Risk associated with fluctuations in market conditions including interest and currency rates.

■ Other Financial

Risk associated with operations, liquidity and achieving returns.

Credit Risk

Credit risk is the risk of loss arising from a counterparty's failure to fulfill its contractual obligations. Credit risk includes default risk, settlement risk, and downgrade risk and encompasses both the probability of loss, and the probable size of the loss, net of recoveries and collateral over appropriate time horizons. CMHC is directly exposed to credit risk from various sources including through its loans, investments and financial derivative instruments, and indirectly from potential claims arising from insurance and securitization activities.

Senior management regularly receives exposure information on a consolidated corporate-wide basis for its largest exposures in order to monitor potential concentrations to individual or affiliated groups of entities.

Corporate Investment & Hedging Exposures

Credit exposures associated with investment and hedging transactions are limited within each of the lending, insurance, and securitization activities.

As of 31 December 2005, the estimated market value of investment and hedging exposures, including amounts associated with repurchase and reverse repurchase activity, totalled \$14.6 billion, an increase of \$2.7 billion from the year earlier (\$11.9 billion in 2004). The accompanying charts provide the distribution and trends of these exposures over the last three years and reflect the consistent quality and diversification of CMHC on the basis of credit quality, industry sectors, and terms to maturity.

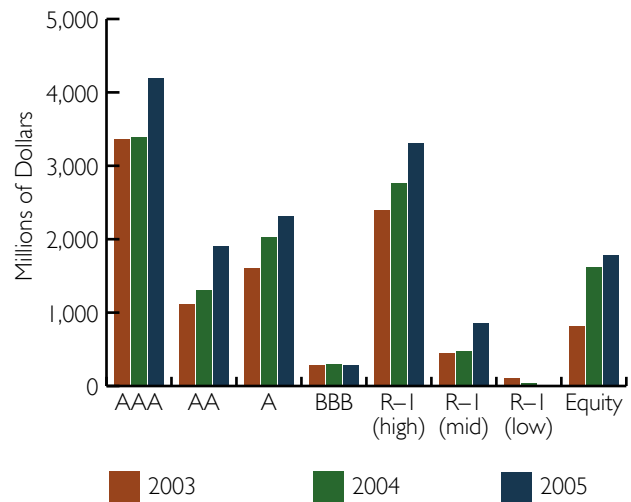
Insurance Activities

Liabilities

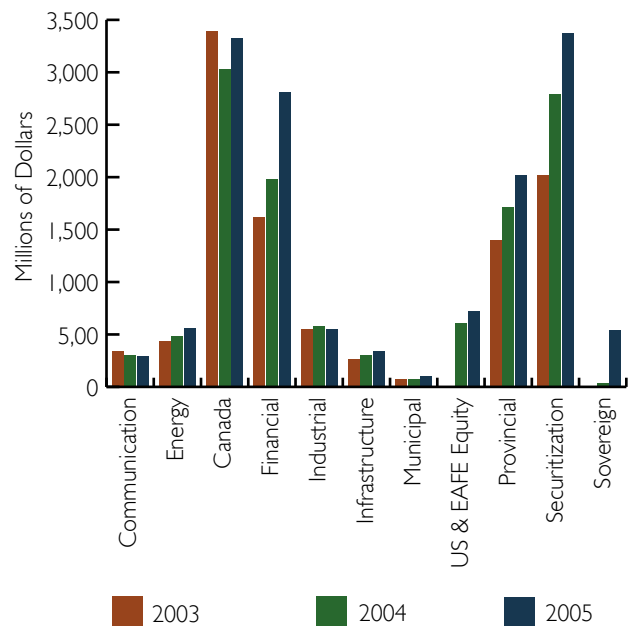
The major risk of financial loss to the insurance activity is the amount of future claims associated with insured mortgages relative to insurance premiums received. The overall performance of the economy is the main determinant of future claims patterns. Changes in house price levels and mortgage interest and unemployment rates, nationally and regionally, are key economic variables affecting the incidence of claims, as they are highly correlated to borrowers' ability to continue servicing their mortgage loans.

As part of the annual corporate planning process, CMHC analyses the sensitivity of insurance activity results using dynamic financial analysis techniques. This allows CMHC to evaluate performance under various economic scenarios such as recessions or periods of high unemployment or interest rates as well as under different business conditions such as a reduction in market share or worse than expected product performance.

Fair Value Investment and Hedging Exposure by Credit Rating



Fair Value Investment and Hedging Exposure by Sector



CREDIT RISK FROM INVESTMENTS

Credit risk is actively managed by the Corporation. As a Crown corporation, CMHC is subject to guidelines established by the Department of Finance for its investment and derivative positions. In addition, CMHC's funding, investment and risk management policies are approved annually by its Board of Directors to outline principles and limits to safeguard the Corporation's liquidity, financial strength and capital.

In relation to credit risk, CMHC's policies require that internal evaluations, exposure limits, and credit ratings be approved for each issuer and counterparty prior to transacting. Within each portfolio, limits are also established on the basis of industry sectors and credit ratings to ensure appropriate diversification. The Risk Management Division monitors investment and hedging exposures on a daily basis to ensure policy compliance as well as evaluate the ongoing appropriateness of internal ratings and limits.

The asset allocation mix for the insurance and securitization investment portfolios, as outlined in the table below, is a key factor which contributes to the high asset quality of the Corporation. Reflective of this, approximately 50.2% of the total assets supporting the insurance and securitization activities at year-end were invested in obligations issued or guaranteed by the Government of Canada or Canadian provinces.

Insurance and Securitization Investment Portfolio Asset Mix (%)

	Strategic Allocation	Insurance	Securitization
Fixed Income	78.0	77.9	78.0
Money Market	5.0	4.2	4.3
Canadian Equity	10.0	10.9	10.7
EAFE Equity	3.5	3.5	3.5
US Equity	3.5	3.5	3.5
Total	100.0	100.0	100.0

As in previous years, the conclusion of this year's sensitivity analysis is that the insurance activity remains sound over the corporate planning horizon as well as under possible adverse economic and business conditions:

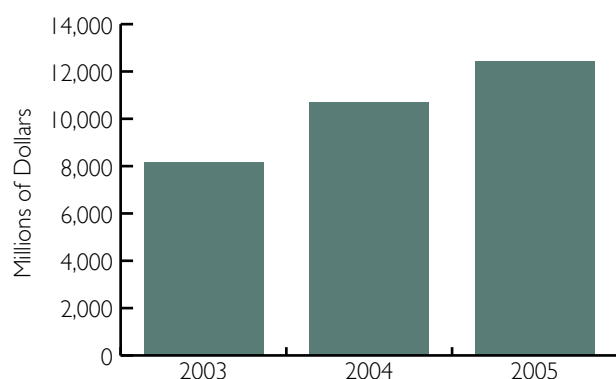
- it is highly unlikely that the insurance activity would need to seek government assistance, as there is a positive investment base;
- the risks for CMHC's insurance activity of additional entrants into the mortgage insurance business in Canada include lower cash flow, in proportion to the amount of business lost to the competitor; and a lower return on capital should the competitor target higher margin markets.

CMHC actively manages homeowner related insurance risk with its state of the art automated underwriting system, **emili**. Incorporated within **emili** are borrower, market, and property risk assessment models. Together, these automated models provide CMHC's underwriters with the tools to effectively identify higher-risk mortgage loan applications. The underwriters can then take further steps to determine if risk-mitigating actions would effectively reduce the overall risk to a level that is acceptable. The most effective risk mitigating actions are continually researched and updated for underwriters. CMHC continually monitors and, if necessary, adjusts its risk assessment models based on actual claims experience.

CMHC also manages its insurance risk through diversification. Because CMHC is active across Canada, the insured portfolio is geographically distributed as is the portfolio's mortgage default risk. Difficult economic times, which are the major factor in higher credit losses, have historically demonstrated that they are also geographically distributed. As well, CMHC manages its insurance risk through lender-based assessments within its Quality Assurance framework. Through this framework, CMHC works with lenders to maintain quality standards in the underwriting and servicing of their mortgage portfolios.

Assets

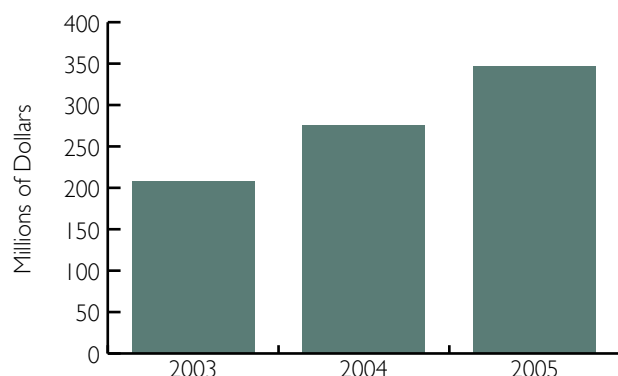
CMHC uses its insurance investment portfolio (generated from premiums received) to cover requirements associated with its provision of insurance to lenders against borrower default on residential mortgages. The objective of the portfolio is to maximize investment returns, while maintaining liquidity sufficient to meet projected business requirements and safeguarding the value of the investment portfolio, subject to appropriate levels of financial risk. According to sensitivity analysis undertaken in 2005, it is currently considered unlikely that investments would have to be liquidated prematurely to meet future adverse economic outcomes associated with the Insurance liabilities.

Fair Value Insurance Investment Exposure

In 2005, the insurance investment portfolio grew by \$1.7 billion, from \$8.0 billion to \$9.7 billion, due primarily to positive net cash inflows and growth from overall market movements. Credit exposures in the above chart include investments in highly-rated short-term instruments associated with the Insurance Activity's repurchase and reverse repurchase activity. This represented \$2.7 billion as of 31 December 2005, up from \$2.4 billion the previous year.

Securitization Activities*Liabilities*

Through its securitization programs, *National Housing Act* Mortgage-Backed Securities (NHA MBS) and Canada Mortgage Bonds, CMHC guarantees timely payment of principal and interest to investors. Total principal obligations to investors guaranteed as of 31 December 2005 were \$103.7 billion, which includes \$72.5 billion guaranteed under the Canada Mortgage Bond Program. Issuances of NHA MBS are done by individual financial entities, while Canada Mortgage Bonds are issued by the Canada Housing Trust.

Fair Value Securitization Investment Exposure

The major risk of financial loss associated with this activity is the cost of funding guaranteed payments in an event of default, relative to the guarantee fees received. All securitized mortgages have full mortgage default insurance coverage. For NHA MBS, the risk associated with issuer default is mitigated by both quality assessment and monitoring of the issuers and by a minimum spread requirement between the security coupon and the lowest mortgage rate in the pool. In the event of issuer default, the minimum spread is made available to a third-party issuer for the continued servicing of both underlying mortgages and the NHA MBS payments. For Canada Mortgage Bonds, in addition to the NHA MBS mitigations above, the risk associated with swap counterparty default is mitigated through program requirements for collateralization and interest retention accounts in the event of counterparty credit ratings below specific ratings thresholds and the requirement that all principal run-off investments be rated R-1 (High) or AAA within Canada Housing Trust.

Assets

CMHC's investment portfolios which support its securitization activity are comprised of investments related to both the Mortgage-Backed Securities Program and the Canada Mortgage Bond Program. The securitization investment portfolio has the same objective as the insurance investment portfolio.

In 2005, the securitization investment portfolio grew by \$71 million, from \$276 million to \$347 million, due to similar factors which influenced the insurance investment portfolio.

Canada Housing Trust

Canada Housing Trust operates within narrowly defined parameters set by CMHC, as guarantor, at the inception of the Canada Mortgage Bond Program and approved by the Minister of Finance. Canada Housing Trust invests the proceeds of Canada Mortgage Bond issuances in NHA MBS and reinvests all prepayments and amortization of principal in eligible investments. The Canada Housing Trust investments are managed by swap counterparties, approved by CMHC, as guarantor, pursuant to contractual agreements and CMHC cannot access any of the investments except in the event of a default by a swap counterparty. Accordingly, while CMHC does not directly manage financial risks for Canada Housing Trust investments, it does mitigate financial risks through the overall Canada Mortgage Bond Program design.

Trust permitted investments are relatively risk-free investments, including NHA MBS, limited amounts of R-I (high) asset-backed commercial paper and obligations issued/backed by the Government of Canada.

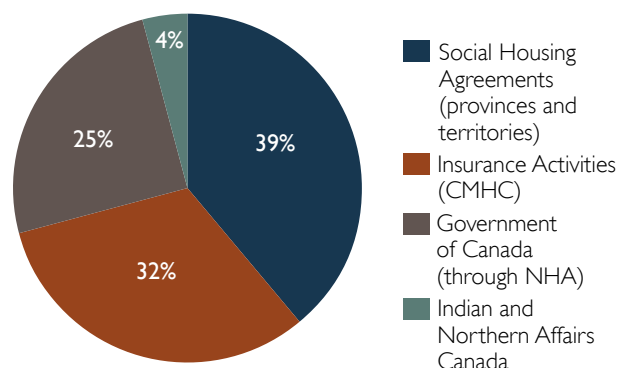
To enable CMHC to properly assess its risks as guarantor under the Canada Mortgage Bond Program, CMHC requires regular and detailed reporting from the Trust Administrator for Canada Housing Trust on the activities related to each Canada Mortgage Bond issue. The Trust Administrator's reports serve to demonstrate that they are prudently managing and monitoring the risks of Canada Housing Trust's activities by detailing all of the assets and liabilities of the Trust and providing semi-monthly mark-to-market valuations on all swap counterparties. As well, the Trustee provides CMHC with annual audited financial statements for Canada Housing Trust. In turn, CMHC relies on this information to monitor its risk exposure under the guarantee.

Lending Activity

Loans

Credit exposure, as reflected by the estimated fair value of loans arising from CMHC's lending activities, totaled \$15.4 billion on an outstanding loan portfolio (book value including accrued interest) of \$13.4 billion. As CMHC's mandate requires that it lend to a large number of non-profit entities, it is often not possible to attribute specific credit ratings established by independent credit agencies. This risk is offset by the fact that losses relating to defaults on these loans are largely recoverable from various levels of government. Approximately 25% of CMHC's loan portfolio is covered through the recovery of losses from the federal government to the extent that such recoveries are within CMHC's parliamentary appropriations. Approximately 32% of the portfolio is covered by CMHC's mortgage insurance activity. Reserves have been provided for claims that may result from these loans. Approximately 39% relates to loans covered under various social housing agreements negotiated with the provinces/territories. Under these agreements, the provinces/territories have taken on the default risk associated with all loans covered in the agreements. Finally, approximately 4% of the portfolio is covered by Indian and Northern Affairs Canada through Ministerial Loan Guarantees.

**Lending Activity
Default Recovery Mitigation**

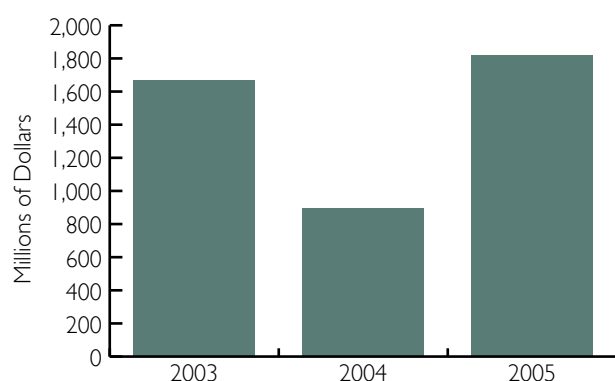


The CMHC loan portfolio has a process framework in place for default management. When a loan goes into default, a feasibility analysis is performed to determine the value of the property and collateral, and workouts are carried out on a case-by-case basis. Every effort is made for early detection, regular reporting of projects in difficulty, application of solutions to cure default and an ongoing monitoring/reporting/approval process is followed. In very rare cases where there is sufficient and compelling evidence that all possible options to cure the default have been exhausted and no viable solutions are available, CMHC will remove its support/subsidies.

Investments & Hedging

The investment assets related to the lending activity portfolio are distinct from those of the insurance and securitization activities. Investments relate to the reinvestment of mortgage principal received in advance of liabilities maturing as corporate cash management requirements. Lending activity investments are subject to more restrictive policies and guidelines in relation to acceptable levels of credit risk than the insurance and securitization activities due to the nature of this activity.

Fair Value Lending Activity Investment and Hedging Exposure



As of 31 December 2005, cash management and principal run-off investments totaled \$1,196 million, compared to \$670 million a year earlier. Credit exposures within the lending activity as of this date also included \$331 million of investments in highly-rated short-term instruments associated with repurchase and reverse repurchase activity, up from \$168 million the previous year-end.

CMHC uses interest rate and cross currency swaps to hedge market risks related to its direct lending portfolio. Counterparty credit risks related to this activity are mitigated through strict credit rating criteria and through the collection of collateral when CMHC is exposed to amounts which exceed agreed-upon ratings-based thresholds. As of 31 December 2005, the net positive mark-to-market value of swap exposures was \$20.8 million.

Ratings-Based Exposure Thresholds

Credit Rating (S&P equivalent)	Exposure Threshold (in millions of dollars)
AAA	250
AA+	200
AA	150
AA-	100
A+	75
A	35
A-	15

Market Risk

Market risk is the risk of adverse financial consequences caused by fluctuations in market conditions. It includes potential adverse impacts on CMHC's earnings and economic value due to adverse changes in such factors as interest rates, foreign exchange rates and equity prices.

The level of market risk to which CMHC is exposed fluctuates according to market dynamics as well as changes to asset and liability mixes in its portfolios. Potential adverse impacts on CMHC's earnings and economic value can arise due to adverse changes in such factors as interest rates, foreign exchange rates, residential property values, and equity prices. CMHC has policies and limits in place to monitor and limit exposure to market risks arising from its business transacting, and asset and liability management activities. These are reviewed and revised as appropriate on an annual basis. Performance against these policies and limits is reported to the Board on a quarterly basis.

CMHC limits its risk of loss from adverse movements in interest rates and foreign exchange rates through hedging, asset and liability matching, and capital market strategies.

Insurance and Securitization

CMHC's insurance activity is exposed to market risk through its Insurance investment portfolios, as well as from the impacts of interest rate and/or residential property value fluctuations which may influence the frequency and severity of claims against its insurance in force.

CMHC's insurance and securitization investment portfolios are managed by limiting price sensitivity to interest rate changes relative to benchmark indices and by appropriate asset diversification.

It should be noted that as part of CMHC's diversification strategy, the Europe, Australasia and Far East (EAFE) Equity and US equity portfolios are not hedged against currency movements.

The majority of CMHC's Insurance and Securitization investment assets are held within the fixed income portfolios. As duration management is an important part of interest rate risk mitigation in fixed income portfolios, the durations of the fixed income investment portfolios are managed within ranges relative to the duration of the Scotia Capital Universe Bond Index (SCUBI) benchmark. As at 31 December 2005, the Insurance and Securitization fixed income portfolios had durations that were marginally longer than the benchmark.

Interest rate simulations are also used as another measure of interest rate sensitivity on the Insurance Fixed Income investment portfolio versus the benchmark index. This aids in determining how much risk is taken when the portfolio characteristics (e.g., duration weighting along the rate curve or convexity) differ slightly from the index. As at the end of December 2005 the portfolio was very similar to the index in terms of interest rate sensitivity. In comparing the portfolio versus the index we see that the portfolio was structured to potentially gain 10 basis points or lose 10 basis points in the tail results over a one quarter horizon (see table below).

Fixed Income Simulation Results at the 5% Tails	Best 5% Tail (%)	Worst 5% Tail (%)
Insurance Portfolio	2.56	-3.86
Benchmark Index (SCUBI)	2.50	-3.78
Portfolio versus Index	0.10	-0.10

CMHC also conducts a 50 basis point parallel interest rate shock test to the fixed income portfolios and compares that to changes in the market values of the benchmark index. Results presented in the table below also confirm that at year end, the portfolios maintained an interest rate risk profile similar to the index.

The annualized volatility of the portfolio returns, based on rolling monthly data for the past three years ended 31 December, was 3.55% and 3.54% for the insurance and securitization fixed income portfolios. During the same period, the benchmark index recorded a volatility of 3.56%. The insurance and securitization volatilities are consistently close to that of the index, implying the insurance and securitization fixed income investment portfolios have taken on a similar risk profile as that of the benchmark index. Volatility has increased slightly over 2005 reflecting the experience of Canadian fixed income markets in general.

Lending Activity

CMHC's objective with this activity is to protect the fair value of its positions and to reduce the volatility of net interest margin over time. Valuations of all Lending Activity portfolio assets and liability positions, as well as off balance-sheet exposures, are performed at least quarterly.

CMHC is exposed to interest rate risk when asset and liability principal and interest cash flows have different interest payments or maturity dates. CMHC's exposure to interest rate risk depends on the size and direction of interest rate changes, and on the size and maturity of mismatched positions. Market risk is mitigated through the matching of assets and liabilities as well as by hedging foreign exchange rates through the use of cross-currency swaps.

CMHC's market risk is also impacted by new business volumes, loan renewals and exercise of embedded optionality such as prepayment. Exposure to prepayment and repricing risk is managed using various funding and business strategies, and covered through retaining a reserve fund to cover potential losses arising from such risks. The joint examiners reviewed CMHC's management practices related to prepayment risk during the 2004 Special Examination and found no significant deficiencies.

CMHC's interest rate sensitivity tolerance as defined in policy states that interest rate risk (defined as the maximum exposure of the interest margin to interest rate movements with 95% confidence), shall be no more than \$1.5 million over a 12 month horizon. For the lending activity portfolio, the exposure was measured as \$0.4 million as at 31 December 2005 (up from \$0.3 million at the end of 2004), which is within the market risk policy limit.

The portfolio is further subjected to 200 basis points parallel shocks to both interest margin as well as to economic value to ensure that interest rate risk does not exceed the tolerance.

Fixed Income Investment Portfolios	Duration (Years)	Duration Versus Index (Years)	Change in Portfolio Market Value with +0.50% Shock (in %)	Change in Portfolio Market Value with +0.50% Shock (in millions of dollars)	Change in Index with +0.50% Shock (in millions of dollars)
Benchmark Index (SCUBI)	6.51	—	—	—	—
Insurance	6.63	0.12	-3.31	-251.7	-247.2
Securitization	6.63	0.12	-3.31	-9.0	-8.8

Estimated Changes in Value Based on Parallel Shocks	December 31 2005 (in millions of dollars)
Lending Activity Portfolio	
+ 200 bps	29
- 200 bps	-45

CMHC also reports on a quarterly basis the lending activity portfolios' duration gaps. The duration gap is the difference between the estimated durations of portfolio assets and liabilities. Duration gap summarizes the extent to which estimated cashflows for assets and liabilities are matched, on average, over time. A positive gap indicates greater exposure to rising interest rates because it indicates that the duration of our assets exceeds the duration of the liabilities. A negative gap signals a greater exposure to declining interest rates because the duration of our assets is less than the duration of our liabilities. At year end, the duration gap for the Direct Lending portfolio was 0.05 years, and the duration gap for the existing loans portfolio was negative 0.32 years.

Canada Housing Trust

In its securitization activity, CMHC has mitigated market risks related to its guarantees regarding the Canada Housing Trust through the internal design of the Trust, where swaps are structured to transfer prepayment and reinvestment risks to highly rated swap counterparties.

Other Financial Risks

CMHC regularly reviews changes to financial regulation, including current efforts to assess the impact of ongoing tax and hedge accounting developments, as well as capital adequacy guidelines potentially impacting financial market participants. CMHC also continues to make efforts to enhance its risk framework in line with capital adequacy and value management principles, consistent with practices employed with leading financial institutions and guidelines established by regulatory agencies. This has resulted in significant improvements in the area of performance measurement and management.

CMHC's ability to meet its financial requirements is enhanced by its status as a Crown corporation. As such, its debt instruments are obligations of Canada and carry a 0 % risk weight under guidelines prescribed by the Office of the Superintendent of Financial Institutions (OSFI). CMHC has a liquidity risk policy which includes appropriate limits and ensures that CMHC has sufficient resources to meet current and projected cash requirements. In the normal course of CMHC's business activities, the commercial paper program provides liquidity to meet cash requirements on a daily basis. Further sources of liquidity associated with this policy include overdraft facilities, lines of credit with several institutions and cash and short-term investments in marketable securities. CMHC's credit ratings are outlined in the accompanying table.

Rating Agency	DBRS	Moody's	Standard & Poor's
Short-term	R-1(High)	P-1	A-1(High)
Long-term (C\$)	AAA	Aaa	AAA
Long-term (foreign currency)	AAA	Aaa	AAA

CAPITAL MANAGEMENT

CMHC, through its enabling legislation and Crown corporation status, has the sovereign creditworthiness of Canada, which is reflected by "AAA" credit ratings on its debt issuance. Subject to its public policy mandate and objectives, CMHC strives to employ private sector risk management practices appropriate for its activities.

Lending Activity

Capital Authorized and Fully Paid by the Government of Canada amounted to \$25 million as of 31 December 2005. In addition, CMHC is authorized to retain the annual net income from the Lending Activity in a Reserve Fund of up to \$175 million to protect CMHC from possible future losses. Included in this limit is an amount of \$50 million designed specifically for fluctuations in net income arising from AcG-13 (i.e., guideline to account for hedging relationships), with the remainder to cover potential prepayment loss. The current Reserve Fund stands at \$143 million, of which \$21 million results from the AcG-13 guideline.

Insurance Activity

CMHC ensures the financial viability of its insurance activity by reserving for policy liabilities in accordance with prudent actuarial practices and by setting aside earnings to be consistent with capitalization guidelines developed by OSFI. OSFI provides a risk-based capital adequacy framework which establishes regulatory capital requirements for Canadian property and casualty insurers, including mortgage insurers. Although not regulated by OSFI, CMHC follows OSFI's guidelines as a prudent business practice and to maintain a level playing field with the private industry.

An annual independent external actuarial valuation ensures that reserves for policy liabilities related to all policy holder obligations in force are appropriate in accordance with accepted actuarial practice.

Securitization Activity

CMHC does not currently appropriate retained earnings for capitalization of its securitization activity. There are no comparable regulatory capital requirements for this activity as there are for insurance. CMHC pays the Government of Canada annually a fee in recognition of its ultimate backing of the securitization guarantees. This fee is based on the amount of maximum expected losses that could be incurred for new guarantees issued each year. A one-in-twenty adverse interest rate scenario together with a swap counterparty default is used to generate maximum expected losses.

OUTLOOK

Going forward, CMHC will continue to focus on risk management from an enterprise perspective, while providing specialized focus on the risk in the business lines. CMHC is engaging its managers and employees to continue to strengthen risk management practices in a rapidly evolving business environment.

Key challenges include a changing regulatory and competitive environment, new insurance and securitization products, and new government priorities. In addition to addressing key enterprise and financial risk challenges, CMHC will work towards improving general risk knowledge and awareness among staff, and on improving risk measurement and reporting. CMHC will continue to progress with strengthening its ERM process to position its strategic planning efforts to be flexible and adaptive to handle these challenges.

CMHC will further develop and integrate risk capital concepts with reserving, pricing, risk adjusted performance measurement, resource allocation and the development of new CMHC products, services and financial strategies.

FINANCIAL STATEMENTS

Financial Statements

Notes to Financial Statements

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

YEAR ENDED 31 DECEMBER 2005

CMHC management is responsible for the integrity and objectivity of the consolidated financial statements and related financial information presented in this annual report. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles, and, consequently, include amounts which are based on the best estimates and judgement of management. The financial information contained elsewhere in this annual report is consistent with that in the consolidated financial statements.

In carrying out its responsibilities, management maintains appropriate financial systems and related internal controls and controls as guarantor of Canada Housing Trust to provide reasonable assurance that financial information is reliable, assets are safeguarded, transactions are properly authorized and are in accordance with the relevant legislation and by-laws of the Corporation, resources are managed efficiently and economically, and operations are carried out effectively. The system of internal controls is supported by internal audit, which conducts periodic audits of different aspects of the operations.

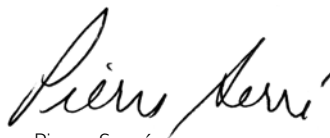
The Board of Directors, acting through the Audit Committee whose members are not officers of the Corporation, oversees management's responsibilities for financial reporting and internal control systems and controls as guarantor of Canada Housing Trust. The Board of Directors, upon the recommendation of the Audit Committee, has approved the consolidated financial statements.

Raymond Chabot Grant Thornton LLP, and Sheila Fraser, FCA, Auditor General of Canada, have audited the consolidated financial statements. The independent auditors have full access to, and meet periodically with, the Audit Committee to discuss their audit and related matters.



Karen Kinsley

President and Chief Executive Officer




Pierre Serré

Vice-President, Finance
and Chief Financial Officer

17 March 2006



Auditor General of Canada
Vérificatrice générale du Canada

Raymond Chabot Grant Thornton 

AUDITORS' REPORT

To the Minister of Human Resources and Social Development

We have audited the consolidated balance sheet of the Canada Mortgage and Housing Corporation as at 31 December 2005 and the consolidated statements of income, retained earnings and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at 31 December 2005 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the *Financial Administration Act*, we report that, in our opinion, these principles have been applied, after giving retroactive effect to the change in the method of accounting for the Canada Housing Trust as explained in Note 3 to the financial statements, on a basis consistent with that of the preceding year.

Further, in our opinion, the transactions of the Corporation that have come to our notice during our audit of the consolidated financial statements have, in all significant respects, been in accordance with Part X of the *Financial Administration Act* and regulations, the *Canada Mortgage and Housing Corporation Act*, the *National Housing Act* and the by-laws of the Corporation.

Sheila Fraser

Sheila Fraser, FCA
Auditor General of Canada

Ottawa, Canada
17 March 2006

Raymond Chabot Grant Thornton LLP

Raymond Chabot Grant Thornton, LLP
Chartered Accountants

Montreal, Canada

CONSOLIDATED BALANCE SHEET

As at 31 December

		Consolidated		CMHC		CHT	
(in millions of dollars)	Notes	2005	2004	2005	2004	2005	2004
ASSETS							
Investment in NHA Mortgage-Backed Securities	5	63,931	51,373	—	—	63,931	51,373
Loans and Investments in Housing Programs	4	13,170	13,669	13,170	13,669	—	—
Investments	5	11,242	8,637	10,021	8,594	1,672	677
Cash and Cash Equivalents		6,975	5,264	3,967	2,841	3,008	2,423
Securities Purchased Under Resale Agreements		4,040	576	112	576	3,928	—
Accrued Interest Receivable		999	829	336	332	669	502
Accounts Receivable and Other Assets		233	179	233	179	—	—
Due from the Government of Canada		212	203	212	203	—	—
Future Income Tax Assets	6	143	111	143	111	—	—
Inventory of Real Estate		74	87	74	87	—	—
Derivative-Related Amounts		74	80	74	80	—	—
		101,093	81,008	28,342	26,672	73,208	54,975
LIABILITIES							
Canada Mortgage Bonds	7	72,075	53,834	—	—	72,526	54,468
Borrowings from the Capital Markets	7	9,467	9,207	9,467	9,207	—	—
Borrowings from the Government of Canada	7	4,899	5,045	4,899	5,045	—	—
Unearned Premiums and Fees		4,694	4,355	4,694	4,355	—	—
Securities Sold Under Repurchase Agreements		3,044	2,976	3,044	2,976	—	—
Accounts Payable and Other Liabilities	9	960	870	959	869	1	1
Accrued Interest Payable		922	629	247	128	681	506
Provision for Claims	8	479	507	479	507	—	—
Securities Sold But Not Yet Purchased		111	121	111	121	—	—
Derivative-Related Amounts		14	38	14	38	—	—
		96,665	77,582	23,914	23,246	73,208	54,975
Commitments and Contingent Liabilities	20						
EQUITY OF CANADA							
Capital Authorized and Fully Paid		25	25	25	25	—	—
Retained Earnings	11	4,403	3,401	4,403	3,401	—	—
		4,428	3,426	4,428	3,426	—	—
		101,093	81,008	28,342	26,672	73,208	54,975

See accompanying notes to the consolidated financial statements.

Approved by the Board of Directors:



Dino Chiesa
Chair, Board of Directors



Sophie Joncas
Chair, Audit Committee

CONSOLIDATED INCOME STATEMENT

Year ended 31 December

(in millions of dollars)	Notes	Consolidated			CMHC			CHT		
		2005	2004	2003	2005	2004	2003	2005	2004	2003
REVENUES										
Income from NHA Mortgage-Backed Securities		2,458	1,838	1,095	—	—	—	2,458	1,838	1,095
Premiums and Fees	8	1,224	1,135	947	1,224	1,135	947	—	—	—
Interest Earned on Loans and Investments in Housing Programs	19	864	969	1,024	864	969	1,024	—	—	—
Investment Income		654	479	402	529	450	390	144	52	25
Other Income		58	32	26	24	(7)	(9)	73	80	72
		5,258	4,453	3,494	2,641	2,547	2,352	2,675	1,970	1,192
Parliamentary Appropriations for:	12,19									
Housing Programs		1,973	2,006	1,972	1,973	2,006	1,972	—	—	—
Operating Expenses		103	101	97	103	101	97	—	—	—
		2,076	2,107	2,069	2,076	2,107	2,069	—	—	—
		7,334	6,560	5,563	4,717	4,654	4,421	2,675	1,970	1,192
EXPENSES										
Housing Programs	12,19	1,973	2,006	1,972	1,973	2,006	1,972	—	—	—
Interest Expense	7	3,475	2,799	2,102	898	937	999	2,596	1,885	1,116
Operating Expenses		303	305	294	263	261	255	79	85	76
Net Claims		119	51	188	119	51	188	—	—	—
		5,870	5,161	4,556	3,253	3,255	3,414	2,675	1,970	1,192
INCOME BEFORE INCOME TAXES		1,464	1,399	1,007	1,464	1,399	1,007	—	—	—
INCOME TAXES										
Current	6	493	460	383	493	460	383	—	—	—
Future		(31)	(11)	(43)	(31)	(11)	(43)	—	—	—
		462	449	340	462	449	340	—	—	—
NET INCOME		1,002	950	667	1,002	950	667	—	—	—

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENT OF RETAINED EARNINGS (NOTE 11)

(in millions of dollars)	Unappropriated Retained Earnings	Earnings Set Aside for Capitalization	Reserve for Lending	Total
Balance 31 December 2002	348	1,380	56	1,784
Net Income	632	–	35	667
Set Aside for Capitalization	(857)	857	–	–
Balance 31 December 2003	123	2,237	91	2,451
Net Income	907	–	43	950
Set Aside for Capitalization	(875)	875	–	–
Balance 31 December 2004	155	3,112	134	3,401
Net Income	993	–	9	1,002
Set Aside for Capitalization	(294)	294	–	–
Balance 31 December 2005	854	3,406	143	4,403

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December

(in millions of dollars)	Consolidated			CMHC			CHT		
	2005	2004	2003	2005	2004	2003	2005	2004	2003
CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES									
Net Income	1,002	950	667	1,002	950	667	—	—	—
Items Not Affecting Cash or Cash Equivalents									
Amortization of Premiums and Discounts	(30)	(14)	(2)	32	12	23	(62)	(26)	(25)
Future Income Taxes	(31)	(11)	(43)	(31)	(11)	(43)	—	—	—
Market Value Adjustment for Equities	(57)	(32)	(5)	(57)	(32)	(5)	—	—	—
Gain on Sale of Investments	(54)	(53)	(46)	(54)	(53)	(46)	—	—	—
Net Change in Non-cash Operating Assets and Liabilities	364	132	382	356	129	382	8	3	—
	1,194	972	953	1,248	995	978	(54)	(23)	(25)
CASH FLOWS PROVIDED BY (USED IN) INVESTING ACTIVITIES									
Investment NHA Mortgage-Backed Securities									
Repayments	15,406	9,485	5,624	—	—	—	15,406	9,485	5,624
Purchases	(27,901)	(27,237)	(21,588)	—	—	—	(27,901)	(27,237)	(21,588)
Loans and Investments in Housing Programs									
Repayments	706	673	715	706	673	715	—	—	—
Disbursements	(211)	(267)	(204)	(211)	(267)	(204)	—	—	—
Investments									
Sales and Maturities	12,124	8,273	8,252	12,076	8,106	8,252	48	167	—
Purchases	(13,771)	(9,459)	(9,766)	(13,309)	(9,355)	(9,778)	(1,041)	(584)	(237)
Change in Securities Purchased Under Resale Agreements	(3,464)	(262)	891	464	(262)	891	(3,928)	—	—
	(17,111)	(18,794)	(16,076)	(274)	(1,105)	(124)	(17,416)	(18,169)	(16,201)
CASH FLOWS PROVIDED BY (USED IN) FINANCING ACTIVITIES									
Issuance of Canada Mortgage Bonds	17,476	18,890	16,904	—	—	—	18,055	19,370	17,153
Medium-term Borrowings from the Capital Markets									
Issuances	2,161	850	2,290	2,161	850	2,290	—	—	—
Repayments	(2,336)	(2,350)	(1,890)	(2,336)	(2,350)	(1,890)	—	—	—
Change in Short-term Borrowings from the Capital Markets	415	612	(166)	415	612	(166)	—	—	—
Repayment of Borrowings from the Government of Canada	(146)	(187)	(242)	(146)	(187)	(242)	—	—	—
Change in Securities Sold Under Repurchase Agreements	68	1,422	438	68	1,422	438	—	—	—
Change in Securities Sold But Not Yet Purchased	(10)	119	(71)	(10)	119	(71)	—	—	—
	17,628	19,356	17,263	152	466	359	18,055	19,370	17,153
Increase in Cash and Cash Equivalents	1,711	1,534	2,140	1,126	356	1,213	585	1,178	927
Cash and Cash Equivalents									
Beginning of year	5,264	3,730	1,590	2,841	2,485	1,272	2,423	1,245	318
End of year	6,975	5,264	3,730	3,967	2,841	2,485	3,008	2,423	1,245
Represented by:									
Cash	(7)	4	6	(7)	4	6	—	—	—
Cash Equivalents	6,982	5,260	3,724	3,974	2,837	2,479	3,008	2,423	1,245
	6,975	5,264	3,730	3,967	2,841	2,485	3,008	2,423	1,245
Supplementary Disclosure of Cash Flow Information									
Amount of Interest Paid During the Year	3,166	2,641	1,951	771	960	989	2,418	1,702	974
Amount of Income Taxes Paid During the Year	494	476	390	494	476	390	—	—	—

See accompanying notes to the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended 31 December 2005

1. CORPORATE MANDATE

These consolidated financial statements include the accounts of Canada Mortgage and Housing Corporation (CMHC) and Canada Housing Trust (CHT) a variable interest entity.

The Corporation's mandate is to promote the construction, repair and modernization of housing, the improvement of housing and living conditions, housing affordability and choice, the availability of low-cost financing for housing and the national well-being of the housing sector.

CMHC was established as a Crown corporation in 1946 by the *Canada Mortgage and Housing Corporation Act* (the "CMHC Act") to carry out the provisions of the *National Housing Act* (the "NHA"). It is also governed by the *Financial Administration Act* (the "FAA"), and is wholly-owned by the Government of Canada.

CHT was established in 2001 as an Issuer Trustee. CHT's functions are limited to the acquisition of interests in eligible housing loans such as *National Housing Act* Mortgage-Backed Securities (NHA MBS), the purchase of highly-rated investments, certain related financial hedging activities and the issuance of Canada Mortgage Bonds (CMB). The CMB are guaranteed by CMHC under its Securitization Activity. The beneficiaries of the Trust, after payment of all obligations, are one or more charitable organizations.

The Corporation's mandate is carried out through the following activities:

Insurance: CMHC provides insurance against borrower default on residential mortgages.

Securitization: CMHC guarantees the timely payment of principal and interest for investors in securities based on insured mortgages. The CMHC Guarantee is a direct and unconditional obligation of CMHC as an agent of Canada and carries the full faith and credit of Canada and constitutes a direct and unconditional obligation of and by the Government of Canada.

Housing Programs: CMHC receives Parliamentary appropriations which are used to fund housing programs.

Lending: CMHC makes loans and investments in housing programs which are funded by borrowings. A significant number of these loans and investments are supported with housing program subsidies.

Within the Public Accounts of Canada, the Corporation's annual Net Income increases the Government's annual surplus; its Capital and Retained Earnings reduce the Government's accumulated deficit.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (GAAP). GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and related disclosures. Actual results could differ from those estimates.

Basis of Presentation

These consolidated financial statements include the accounts of Canada Mortgage and Housing Corporation (CMHC) and, as required by *Accounting Guideline 15: Consolidation of Variable Interest Entities* (AcG-15) issued by the Canadian Institute of Chartered Accountants (see Note 3), the accounts of Canada Housing Trust (CHT), a variable interest entity (VIE) for which CMHC is considered to be the primary beneficiary. The assets and liabilities of CHT, are neither owned by nor held for the benefit of CMHC and are therefore disclosed separately in the consolidated financial statements and related notes. Revenues, expenses and cash flows relating to CHT have received similar treatment. Inter-entity balances and transactions have been eliminated in the consolidated figures.

Loans and Investments in Housing Programs

Loans are carried at cost. Where loans contain forgiveness clauses, they are recorded net of the forgiveness which is reimbursed through Parliamentary appropriations when the loans are advanced.

Investments in Housing Programs, which represent CMHC's ownership interest in various housing projects, are carried at cost less accumulated amortization. Amortization is calculated on a straight-line basis over the life of the investment. CMHC's portion of net operating losses and disposal losses is reimbursed through Parliamentary appropriations.

Interest Earned on Loans and Investments in Housing Programs is recorded on an accrual basis.

Full collection of principal and accrued interest on the majority of the Loans and Investments in Housing Programs is assured as described in Note 4.

Investments

	Carrying Value	Recognition of Realized Gains and Losses	Recognition of Impairment
Lending — Investments held for cash management purposes and investments relating to managing interest rate risk associated with lending activities.	Amortized cost. Premiums and discounts are deferred and amortized on a constant yield basis over the term of the related investments.	Gains and losses are included in income at the time of sale.	Specific securities are written down to their market value when the decline in the value of the security is other than temporary. The resulting loss is recorded in the year in which the impairment occurs.
Insurance and Securitization (excluding CHT) — Fixed income securities generally purchased with the intention to hold them to maturity to meet long-term obligations.	Amortized cost. Premiums and discounts are deferred and amortized on a constant yield basis over the term of the related investments.	Gains and losses are deferred and amortized over the remaining life of the original investment.	Specific securities are written down to their market value when the decline in the value of the security is other than temporary. The resulting loss is recorded in the year in which the impairment occurs.
Insurance and Securitization (excluding CHT) — Equities	Cost, plus a moving average market value adjustment of 5% per quarter.	Net gains and losses are deferred and amortized to Investment Income at 5% per quarter on a declining balance basis.	Written down to their market value when the decline in the value of the portfolio is other than temporary. The resulting loss is recorded in the year in which the impairment occurs.
Canada Housing Trust — Investments	Amortized cost. Premiums and discounts are deferred and amortized on a straight-line basis over the term of the related investments.	Gains and losses are included in income at the time of sale.	Specific securities are written down to their market value when the decline in the value of the security is other than temporary. The resulting loss is recorded in the year in which the impairment occurs.
Canada Housing Trust — Investment in NHA Mortgage-Backed Securities	Amortized cost. Premiums and discounts are deferred and amortized on a straight-line basis accelerated for unscheduled principal repayments.	Gains and losses are included in income at the time of sale.	Insignificant risk of impairment.

Cash and Cash Equivalents

Cash and Cash Equivalents are comprised of cash and short-term, highly liquid investments (primarily corporate entities) with terms to maturity of 98 days or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. These investments are carried at the lower of cost and market value. Gains and losses from sales of cash equivalents are included in Investment Income at the time of sale. Cash equivalents must have a minimum credit rating of R-I(Low).

Securities Purchased Under Resale Agreements and Sold Under Repurchase Agreements

Securities Purchased Under Resale Agreements (Reverse Repurchase Agreements) consist of the purchase of securities, typically government treasury bills or bonds, with the commitment to resell the securities to the original seller at a specified price and date. Securities Sold Under Repurchase Agreements (Repurchase Agreements) consist of the sale of securities with the commitment to repurchase the securities from the original buyer at a specified price and date. These items are carried at cost, plus accrued interest. Proceeds from securities sold under repurchase agreements are invested for the purpose of generating additional income. Such transactions are entered into simultaneously with matching terms to maturity. As a result, the associated interest earned and interest expense are included in income on an accrual basis.

Securities Sold But Not Yet Purchased

Securities Sold But Not Yet Purchased represent an obligation to deliver securities which are not owned at the time of sale. These obligations are recorded at fair value. Realized and unrealized gains and losses are included in Interest Expense.

Inventory of Real Estate

Inventory of Real Estate is carried at the lower of cost and fair value. Cost is determined as the acquisition cost, plus modernization and improvement costs where applicable. Fair value is calculated as the current market value of the property, less the discounted value of estimated holding and disposal costs.

For certain properties, net operating losses and disposal losses are reimbursed through Parliamentary appropriations while net operating profits and disposal gains are returned to the Government of Canada.

Borrowings from the Capital Markets

Issuance costs on borrowings from the capital markets are deferred and amortized on a straight-line basis over the term of the debt issue. Premiums and discounts on borrowings from the capital markets are deferred and amortized on a constant yield basis over the term of the debt issue.

Canada Mortgage Bonds

Canada Mortgage Bonds, which are guaranteed by CMHC, consist of interest bearing bullet bonds. Coupon interest payments are made semi-annually for fixed-rate CMB and quarterly for floating-rate CMB. Principal repayments on the bonds are made at the end of the term. These are recorded at the cash amount received and any premium or discount is amortized on a straight-line basis to interest expense over the term to maturity. Interest is taken into expense on an accrual basis. Direct costs associated with the issuance of the bonds are expensed in the year incurred. The Approved MBS Sellers reimburse CHT for the cost of arranging financing for the purchase of NHA MBS. This includes the fees paid to CMHC as Guarantor and Financial Services Advisor, underwriters and others for the distribution of CMB.

Premiums and Fees

Insurance premiums are due at the inception of the mortgage being insured at which time they are deferred and recognized as income over the period covered by the insurance contract using factors determined by an Appointed Actuary. These factors reflect the long-term pattern for default risk by age of a mortgage insurance policy.

Unearned premiums represent the portion of the premiums written that relates to the unexpired portion of the policy at the Balance Sheet date and therefore relate to claims that may occur from the Balance Sheet date to the termination of the insurance policies. Annually, the unearned premiums are compared to an estimate of total future claims on a discounted basis to ensure the amount is sufficient.

Guarantee fees from Securitization are received at the inception of the related security issue at which time they are deferred and recognized as income over the term of the security issue (typically five years) on a straight-line basis.

Application fees and costs associated with issuing mortgage insurance policies and timely payment guarantees are recorded on an accrual basis.

Provision for Claims

The Provision for Claims represents an estimate for expected claims and the related settlement expenses, net of the related expected mortgage foreclosure proceeds, for defaults from the Insurance business that have occurred on or before the Balance Sheet date. The provision takes into consideration the estimate of losses on defaults that have been incurred but not reported, the time value of money and in accordance with accepted actuarial practice, includes an explicit provision for adverse deviation.

The establishment of the Provision for Claims involves estimates, which are based upon historical trends, prevailing legal, economic, social and regulatory trends, and expectations as to future developments. The process of determining the provision necessarily involves risks that the actual results will deviate, perhaps significantly, from the estimates made.

The loss on actual mortgage defaults and the change in estimate for the Provision for Claims are recorded in Net Claims in the year in which they occur.

Housing Programs

Parliamentary appropriations for Housing Programs, and the related expenses, are recorded on an accrual basis. Those expenses incurred but not yet reimbursed are recorded as Due from the Government of Canada.

Employee Future Benefits

CMHC provides a defined benefit pension plan, a supplemental pension plan, and other post-employment benefits consisting of severance pay, life insurance and medical insurance.

Pension benefits are based on length of service and average earnings of the best five-year period as classified under defined benefit pension arrangements. The pension benefits are adjusted annually by a percentage equivalent to the increase in the average Consumer Price Index during the previous year. The obligations under employee benefit plans and the related costs are accrued, net of plan assets.

The cost of pension and other post-employment benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of expected long-term pension plan investment performance, salary increases, retirement ages of employees, mortality of members and expected health care costs. These assumptions are of a long-term nature, which is consistent with the nature of employee future benefits. Actual results could differ from these estimates.

Costs are determined as the cost of employee benefits for the current year's service, interest cost on the accrued benefit obligation, expected investment return on the fair value of plan assets and the amortization of the transitional asset/obligation, the deferred actuarial gains/losses and the deferred past service costs.

The transitional asset/obligation, and past service costs are amortized over the average remaining service period of active employees under the plans. The excess of the net actuarial gain/loss over 10% of the greater of the benefit obligation or the fair value of the plan assets is amortized over the average remaining service period of active employees under the plans.

Derivative Financial Instruments

The Corporation enters into derivative financial instruments such as interest rate swaps and foreign currency swaps in order to manage its exposures to market risks. It does not use freestanding derivative financial instruments for trading or speculative purposes.

In order for a derivative financial instrument to qualify as an eligible hedge for accounting purposes, the hedge relationship must be designated and formally documented at its inception. The particular risk management objective and strategy for the hedge, the specific asset, liability or cash flow being hedged, and how effectiveness is measured are all formally documented. Formal assessments, both at the hedge's inception and on an ongoing basis, are also done to determine whether the derivative is highly effective in offsetting either changes in fair value or future cash flows of hedged items.

For all CHT derivative financial instruments that qualify as eligible hedges, income/expenses are recorded as adjustments to Income from NHA Mortgage-Backed Securities on an accrual basis. The related amount payable to, or receivable from, swap counterparties is included in accrued interest.

For all other derivative financial instruments that qualify as eligible hedges, income/expenses are recorded as adjustments to Interest Expense on an accrual basis. The related amount payable to, or receivable from, counterparties is included in accrued interest. Translation gains/losses arising on foreign currency swaps that qualify as eligible hedges are offset by translation gains/losses on the related debt.

Hedge accounting is discontinued prospectively if the hedge relationship is no longer effective, the derivative financial instrument is no longer designated as an eligible hedge, or if the designated hedged item matures, is sold or is terminated. Deferred gains or losses associated with derivative instruments, which have been terminated or cease to be effective prior to maturity, are recognized in income in the period in which the underlying hedged transaction is recognized. In the event a designated hedged item is sold, extinguished or matures prior to the termination of the related derivative instrument, any previously deferred gain or loss on such derivative instrument is immediately recognized in income. The derivative financial instrument is then carried at fair value on the Consolidated Balance Sheet as of the date that hedge accounting is discontinued and subsequent changes in fair value are recognized in Other Income.

Derivative financial instruments that do not qualify, or have not been designated, as eligible hedges for accounting purposes are carried at fair value on the Consolidated Balance Sheet as Derivative-Related Amounts. Subsequent changes in fair value are recorded in Other Income.

Income Taxes

The Corporation follows the asset and liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are recognized based on the estimated tax effect of temporary differences in the carrying value of assets and liabilities in the financial statements and their respective tax bases, using income tax rates substantively enacted on the Balance Sheet date.

Foreign Currency Translation

All monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at exchange rates prevailing at the Balance Sheet date. Exchange gains and losses resulting from the translation of foreign denominated balances are included in Interest Expense.

Future Accounting Changes — Financial Instruments

In January 2005, the Canadian Institute of Chartered Accountants (CICA) issued three new accounting standards: Section 3855, Financial Instruments — Recognition and Measurement; Section 3865, Hedges; and Section 1530, Comprehensive Income. They are currently being assessed to determine the impact they will have when adopted in January 2007. The new requirements are as follows:

Section 3855 — prescribes standards for recognizing and measuring financial instruments on the Balance Sheet and how related gains and losses are to be presented.

Section 3865 — modifies the timing of recognizing gains or losses under Section 3855 to permit the matching of gains and losses in the Income Statement for financial instruments included in highly effective hedging transactions.

Section 1530 — introduces a new component of Shareholders' Equity and a new Statement of Comprehensive Income that will present certain gains and losses arising from the application of Sections 3855 and 3865, before they are transferred to the Income Statement.

3. CHANGE IN ACCOUNTING POLICY

Effective 1 January 2005, the Corporation adopted *Accounting Guideline 15: Consolidation of Variable Interest Entities* (AcG-15), issued by the Canadian Institute of Chartered Accountants, which requires the consolidation of certain VIEs that are subject to control on a basis other than through ownership of a majority of voting interest. This change in accounting policy has been applied retroactively and prior years' figures have been restated.

AcG-15 defines a variable interest entity as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. CHT is such a variable interest entity. AcG-15 requires the primary beneficiary to consolidate VIEs and considers an entity to be the primary beneficiary of a VIE if it is exposed to the majority of the expected losses or will receive the majority of the expected residual returns, or both. CMHC is considered the primary beneficiary of CHT. Therefore, for accounting purposes, CHT is consolidated with the financial statements of CMHC.

The Trustee of CHT has entered into agreements with a number of parties to provide various services to CHT, including CMHC. Under one such agreement, CMHC, as agent of Canada, has guaranteed the timely payment of the interest payments and the principal at maturity on all CMB issued by CHT to date. Once provided, the guarantee becomes a direct and unconditional obligation of the Government of Canada and is irrevocable until full repayment of the CMB at maturity (typically within five years of issuance). In addition, under a Financial Services Advisor (FSA) Agreement, CMHC gauges market demand for bond issuance and assesses the potential supply of housing loans available to be packaged for sale to CHT.

Pursuant to the purchase agreements and other relevant program agreements, CHT purchases ownership interest in pools of NHA MBS, which are pledged as security for CMB issued by CHT to finance the purchases. CHT assets are neither owned by nor held for the benefit of CMHC. Consequently, CHT's assets are not available to CMHC for its general corporate purposes or to satisfy any liabilities of CMHC. Details of CHT's interest in the NHA MBS and the CMB issued to finance the purchases are disclosed in Notes 5 and 7 respectively.

The impact from the consolidation of CHT on the consolidated financial statements at 31 December 2005 is an increase of \$72,751 million (2004 — \$54,336 million) in consolidated assets and liabilities, as well as a \$2,617 million (2004 — \$1,906 million) increase in both revenues and expenses. As a result, there is no impact on consolidated Net Income or consolidated Retained Earnings.

4. LOANS AND INVESTMENTS IN HOUSING PROGRAMS

CMHC makes loans and investments in housing programs either independently or jointly with provincial, territorial, and municipal authorities. These loans and investments were issued for terms up to 50 years. Of the total portfolio, \$12,969 million, or 98% (2004 — \$13,478 million or 99%) are due and payable beyond five years.

Approximately \$12,485 million, representing 95% (2004 — \$12,916 million, or 95%) of the loans and investments in housing programs, are supported with housing program subsidies.

At 31 December 2005, CMHC is assured full collection of principal and accrued interest on the majority of the portfolio from the Provinces and Territories through provisions in social housing agreements (39%), the Government of Canada through provisions in the NHA (25%), and Indian and Northern Affairs Canada through Ministerial loan guarantees (4%).

The remainder of the portfolio (32%) is underwritten through the Insurance Activity. Provision for losses on these loans is included in the determination of Provision for Claims and Unearned Premiums.

5. INVESTMENTS

The following table shows the maturity structure and average yield of Investments.

(in millions of dollars)	Term to Maturity				2005	2004
	Within 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years		
CMHC						
Fixed Income Securities						
Issued or Guaranteed by:						
Government of Canada	43	862	1,242	1,537	3,684	3,056
Provinces/Municipalities	–	300	203	1,454	1,957	1,662
Corporate/Other Entities	269	810	461	1,377	2,917	2,459
Total Fixed Income	312	1,972	1,906	4,368	8,558	7,177
Yield ⁽¹⁾	2.85%	3.96%	4.23%	4.92%	4.47%	4.64%
Equities (no specific maturity)						
Canadian Equities					798	827
US Equities					351	296
Foreign Equities					314	294
Total Equities					1,463	1,417
Yield ⁽²⁾					3.14%	2.62%
Total CMHC					10,021	8,594
CHT						
Fixed Income Securities						
Issued or Guaranteed by:						
Government of Canada	546	444	53	–	1,043	677
Corporate/Other Entities	629	–	–	–	629	–
Total CHT	1,175	444	53	–	1,672	677
Yield ⁽¹⁾	3.35%	3.45%	3.61%	–	3.38%	3.33%
Inter-entity Elimination					(451)	(634)
Grand Total					11,242	8,637

(1) Represents the weighted-average yield, which is determined by applying the weighted average of the book yields of individual securities.

(2) The weighted-average yield is determined by applying the stated dividend rates of equity securities.

Sales of investments in the Lending portfolio resulted in a net loss of \$6 million in 2005 (2004 — \$12 million gain, 2003 — \$2 million gain) which has been expensed in the current year. Sales of investments in the Insurance and Securitization portfolios resulted in a net gain of \$171 million in 2005 (2004 — \$68 million gain, 2003 — \$52 million gain) which has been deferred. These treatments are in accordance with the accounting policies described in Note 2. Cumulative deferred gains are presented in Note 9.

CHT investments are managed by swap counterparties pursuant to contractual agreements and CMHC cannot access any of the investments except in the event of a swap counterparty default.

The CHT NHA MBS maturities are estimated based on assumptions regarding mortgage prepayments and liquidations, excluding new issuance and unscheduled prepayment. The following table shows the maturity structure and average yield of CHT investments.

(in millions of dollars)	Term to Maturity				2005	2004
	Within 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years		
Investment in NHA Mortgage-Backed Securities	10,112	30,616	23,203	—	63,931	51,373
Yield ⁽¹⁾	3.88%	3.94%	3.88%	—	3.91%	3.40%

(1) Represents the weighted-average yield, which is determined by applying the weighted average of the book yields of individual securities.

6. INCOME TAXES

CMHC is subject to federal income tax. It is not subject to provincial income tax. A reconciliation of CMHC's Income Tax Expense is as follows:

(in millions of dollars)	2005	2004	2003
Income Taxes Computed at Statutory Tax Rate (2005 — 33%, 2004 — 33%, 2003 — 35%)	476	454	349
Net Reduction of Future Income Tax Assets	—	(2)	(8)
Permanent Differences	(6)	(5)	(4)
Other	(8)	2	3
Income Tax Expense	462	449	340

The tax-effected temporary differences which result in future income tax assets and liabilities are as follows:

(in millions of dollars)	2005	2004
Provisions for Actuarial Liabilities	(26)	(10)
Deferred Revenue	61	35
Deferred Expenses	13	12
Expenses Incurred But Not Yet Disbursed	7	8
Appreciation in Value of Equities	87	65
Other	1	1
Future Income Tax Assets	143	111

CHT is subject to federal and provincial income taxes on the amount of taxable income for the period and is permitted a deduction for all amounts paid or payable to CHT's beneficiary in determining income for tax purposes. As all income was distributed to the beneficiary, no provision for income taxes has been reflected in these consolidated financial statements.

7. BORROWINGS

Prior to 1993, Loans and Investments in Housing Programs were funded by Borrowings from the Government of Canada. Since that time, CMHC has made its borrowings solely from the capital markets as an agent of Canada. Legislative authority, which does not apply to borrowings of Canada Housing Trust, requires that the total indebtedness from the capital markets outstanding at any time cannot exceed \$20 billion. The Minister of Finance approves CMHC's Borrowing Plan annually and establishes limits and parameters for borrowings.

The following table summarizes the carrying value and yield for Borrowings from the Government of Canada based on repayments and for Borrowings from the Capital Markets based on term to maturity. Capital market borrowings include US denominated debt. Foreign currency principal and interest payments are fully swapped to Canadian dollar obligations.

(in millions of dollars)	2005					2004	
	Government of Canada		Capital Markets			Carrying Value	
	Carrying Value	Yield ⁽¹⁾	Foreign Currency Borrowings ⁽²⁾	Carrying Value	Yield ⁽¹⁾	Government of Canada	Capital Markets
2005	–	–	–	–	–	145	3,501
2006	198	8.09%	–	3,153	3.84%	199	1,453
2007	255	8.82%	–	1,258	4.70%	255	1,257
2008	210	8.90%	1,160	1,160	4.48%	210	1,201
2009	210	8.88%	–	1,049	3.91%	210	1,049
2010	204	8.79%	1,450	1,450	3.94%	204	–
2011–2015	1,064	8.53%	–	1,397	4.79%	1,064	746
Thereafter	2,758	9.39%	–	–	–	2,758	–
Total	4,899	9.08%	2,610	9,467	4.20%	5,045	9,207

(1) Represents the weighted-average yield, which is determined by applying the weighted average book yields of individual fixed income securities and the weighted average yields to reset of floating-rate notes.

(2) Canadian equivalent of US denominated debt (included in carrying value).

Included in capital market borrowings are commercial paper with a term to maturity less than 365 days and medium-term debt. Commercial paper outstanding is \$1,701 million and the yield on these borrowings is 3.13%. Medium-term debt includes bonds, floating-rate and fixed-rate medium-term notes, with a term to maturity ranging from two to ten years. Floating-rate notes represent \$400 million (2004 — \$550 million) of Borrowings from the Capital Markets.

The 2005 interest expense related to Borrowings from the Government of Canada is \$451 million (2004 — \$469 million, 2003 — \$488 million) and \$419 million (2004 — \$486 million, 2003 — \$522 million) for Borrowings from the Capital Markets.

Lines of Credit

At 31 December 2005, CMHC had \$450 million (2004 — \$450 million) in unused, uncommitted lines of credit. In addition, \$100 million (2004 — \$100 million) of overnight overdraft facility was available with its banker that had not been drawn.

Canada Mortgage Bonds

CMB are fixed interest semi-annual or floating interest quarterly coupon bonds issued by CHT. The principal is payable at the maturity of the bonds. CMHC guarantees timely payment of interest and principal on CMB issued by CHT. This guarantee to investors is unconditional and irrevocable until full payment of the CMB.

The following table summarizes the carrying value and yield for the CMHC guaranteed CMB based on term to maturity.

(in millions of dollars)	2005		2004
	Carrying Value	Yield ⁽¹⁾	Carrying Value
2006	2,200	5.53%	2,200
2007	12,618	4.94%	12,627
2008	20,295	4.10%	20,274
2009	13,109	4.28%	13,125
2010	19,364	3.61%	6,242
2011–2015	4,940	4.05%	–
Thereafter	–	–	–
	72,526	4.19%	54,468
Inter-entity Elimination	(451)		(634)
Total	72,075	4.18%	53,834

(1) Represents the weighted-average yield, which is determined by applying the weighted average book yields of individual fixed income securities and the weighted average yields to reset of floating-rate notes.

In order to meet the principal obligations of the bonds, the principal payments and prepayments from the underlying mortgages are held in a principal account in the name of CHT, managed and reinvested into eligible assets by the swap counterparties.

8. INSURANCE

Role of the Appointed Actuary

The actuary is appointed by CMHC's management to carry out a valuation of the policy liabilities of the mortgage insurance activity as at 30 September and to provide an opinion to management regarding their appropriateness at the valuation date. The factors and techniques used in the valuation are in accordance with accepted actuarial practice, applicable legislation, and associated regulations. The scope of the valuation encompasses the policy liabilities that consist of a Provision for Claims on the expired portion of policies and of future obligations on the unexpired portion of policies (Unearned Premiums). In performing the valuation of the liabilities for these contingent future events, which are by their very nature inherently variable, the actuary makes assumptions as to future claim rates, average loss on claims, trends, expenses and other contingencies, taking into consideration the circumstances of CMHC and the nature of the insurance policies.

CMHC determines Provisions for Claims and Unearned Premiums at 31 December using valuation factors from the 30 September valuation, taking into account premiums received and claims paid in the intervening period.

Nature of Provision for Claims

The establishment of the Provision for Claims for mortgage insurance is based on known facts and interpretation of circumstances, and is therefore a complex and dynamic process, influenced by a large variety of factors. These factors are continually evolving and changing as they are affected by underwriting and claim settlement procedures, actuarial studies, professional experience, the quality of data utilized for projection purposes, economic conditions, and general credit behaviour. Consequently, the establishment of the Provision for Claims necessarily involves risks that the actual results will deviate, perhaps significantly, from the best estimates made.

The factors affect the key actuarial assumptions as follows:

Claim emergence: Claim emergence encompasses claim frequency and claim occurrence patterns. It is based on historical trends in claims reporting and payment delays.

Claim severity: Claim severity, or average loss on claims, is dependent on the dollar value of claims, losses on sales of real estate properties, administrative expenses, and sales delays. These factors are based on historical experience.

Economic conditions: Recent past and projected economic factors, such as unemployment rates, mortgage rates, and changes in housing prices, affect the forecast of future claim levels.

The provision for claims is based on projections of future losses on claims and related expenses. The actual future claims may not develop exactly as projected and may in fact vary significantly from the projections. Further, the projections make no provision for new classes of claims categories not sufficiently recognized in the claims database.

All provisions are periodically reviewed and evaluated in light of emerging claim experience and changing circumstances. The resulting changes in estimates of the Provision for Claims are recorded in Net Claims in the year in which they are determined.

Change in Provision for Claims

(in millions of dollars)	2005	2004
Balance at 1 January	507	622
Impact of Increased Business Volumes	13	8
Change in Assumptions:		
Claim Emergence	(2)	(39)
Claim Severity	1	–
Economic Conditions	(28)	(85)
Other	(12)	1
Balance at 31 December	479	507

The Provision for Claims is mostly affected by changes in assumptions for economic conditions. Average 5-year mortgage interest rates and the unemployment rate improved by about 30 basis points in 2005 compared to 2004 and house price inflation remained high. Changes in actuarial assumptions for claim emergence and claim severity primarily have longer term impacts.

CMHC uses Dynamic Financial Analysis (DFA) to model the impact on the Insurance Activity of adverse economic shocks, including recessions. Recessions involve a combination of adverse interest rate impacts, high unemployment rate outcomes and deteriorating house prices. The DFA analysis for the 2006–2010 Corporate Plan showed that a 4-quarter recession beginning in 2006 would increase the provision for claims by more than \$100 million over current levels.

To provide a further measure of sensitivity of the change in Provision for Claims, it is estimated that for every 5% change in the estimate of future claim settlement cost or every 5% change in the estimate of future claim rate, the effect on pre-tax income would be an increase/decrease of approximately \$10 million.

These sensitivities are hypothetical and should be viewed in that light. The relationship of a change in assumption to the change in value may not be linear. Changes in one factor may result in changes in another which might magnify or counteract the sensitivities.

Insurance in Force

Under Section 11 of the NHA, the aggregate outstanding amount of mortgage insurance policies may not exceed \$300 billion. At 31 December 2005, insurance policies in force totalled \$274 billion (2004 — \$244 billion).

9. ACCOUNTS PAYABLE AND OTHER LIABILITIES

The following table presents the composition of Accounts Payable and Other Liabilities.

(in millions of dollars)	2005	2004
CMHC		
Foreign Exchange Adjustment on Foreign Currency Swaps	293	317
Deferred Gains on Disposals of Investments	228	109
Accrued Housing Program Expenses	174	166
Accrued Benefit Liability for Supplemental Pension Plan and Other Post-employment Benefits	78	67
Income Taxes Payable	59	62
Obligation Under Capital Lease	21	22
Unamortized Transitional Gain Arising from the Implementation of AcG-13 — <i>Hedging Relationships</i>	16	20
Government of Canada Fees Payable	5	25
Other Miscellaneous Liabilities	85	81
Total CMHC	959	869
CHT	1	1
Grand Total	960	870

10. SECURITIZATION

CMHC guarantees the timely payment of principal and interest for investors in securities issued, by Approved Issuers (primarily lending institutions), on the basis of housing loans through the NHA MBS program and the bonds issued by CHT through the Canada Mortgage Bonds (CMB) Program.

CMHC has determined that a provision for claims on these programs is not required. This is based on historical results and program design whereby only insured mortgages are eligible for securitization. In addition, CMHC requires that CHT only transact with swap counterparties of high creditworthiness, that collateralization occurs in the event that counterparty credit ratings fall, and that all investments are rated R-1 (High) or AAA.

Guarantees in Force

Under Section 15 of the NHA, the aggregate outstanding amount of principal guarantees may not exceed \$300 billion. At 31 December 2005, guarantees in force totalled \$104 billion (2004 — \$81 billion) which includes \$31 billion of CMHC guaranteed NHA MBS (2004 — \$26 billion) and \$73 billion of CMHC guaranteed CMB issued by CHT (2004 — \$55 billion) as disclosed in the following table.

(in millions of dollars)	2005	2004
Outstanding Balance at 31 December	72,550	54,450
Unamortized (Discount) Premium	(24)	18
	72,526	54,468
Inter-entity Elimination	(451)	(634)
Balance at 31 December	72,075	53,834

11. RETAINED EARNINGS

Earnings Set Aside for Capitalization represent the portion of cumulative Net Income generated by the Insurance Activity that has been set aside for the purposes of being consistent with capitalization guidelines developed by the Office of the Superintendent of Financial Institutions (OSFI) and is approved annually through CMHC's Corporate Plan. Unappropriated Retained Earnings represent Net Income generated by the Insurance Activity that has not been set aside for capitalization purposes, and all of the retained earnings of the Securitization Activity.

CMHC places all lending-related retained earnings in its Reserve for Lending. The components of this Reserve are outlined in the following table.

(in millions of dollars)	Authorized Limit	31 December 2005	31 December 2004
Reserve for Fluctuations in Net Income Arising from AcG-13: <i>Hedging Relationships</i>	50	21	16
Reserve for All Other Lending-Related Items	125	122	118
Reserve for Lending	175	143	134

12. HOUSING PROGRAMS

CMHC provides payments to support the following housing programs which are funded by Parliamentary appropriations.

(in millions of dollars)	2005	2004	2003
Non-Profit	586	593	589
Public Housing	483	511	502
Affordable Housing	175	173	166
Rural and Native Housing	151	158	165
Rent Assistance	142	139	143
Renovation Programs	113	114	88
Urban Native	105	94	92
On Reserve	99	100	95
Co-operatives	83	86	89
Limited Dividend	12	12	12
Research and Information Transfer	10	8	9
Other	14	18	22
Total	1,973	2,006	1,972

Of the total amount spent on housing programs in 2005, \$950 million (2004 — \$957 million, 2003 — \$961 million) was spent under programs transferred to Provinces/Territories under Social Housing Agreements. These amounts are disclosed above based on the allocation within the agreements which also provide that where there may be an over-funding in one program, the Province/Territory may spend the amount on other housing programs.

13. DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are financial contracts whose value is derived from price movements in one or more underlying securities, indices or other instruments or derivatives. The Corporation uses derivatives (interest rate swaps and foreign currency swaps) in connection with its risk management activities.

Interest rate swaps are transactions in which two parties exchange interest cash flows on a specified notional amount for a predetermined period based on agreed-upon fixed and floating rates. Notional amounts are not exchanged. The value of these swaps is derived from movements in interest rates. They are used to manage reinvestment risk, refinancing risk, or mismatches in the timing of receipts on assets versus payments on liabilities.

Foreign currency swaps are transactions in which two parties exchange currencies and interest cash flows on a specified notional amount for a predetermined period. The notional amount is exchanged at inception and at maturity. The value of these swaps is derived from movements in foreign exchange and interest rates. They are used to manage foreign exchange risk arising from foreign denominated debt.

The table below provides the notional amounts of the Corporation's derivative transactions. Notional amounts, which are off-balance sheet, serve as a point of reference for calculating payments and do not represent the fair value, or the potential gain or loss associated with the credit or market risk of such instruments.

(in millions of dollars)	Ineligible for Hedge Accounting		Eligible for Hedge Accounting	
	2005	2004	2005	2004
CMHC				
Interest Rate Swaps	15,967	15,562	300	300
Foreign Currency Swaps	—	—	2,904	2,119
Total CMHC	15,967	15,562	3,204	2,419
CHT				
Interest Rate Swaps	—	—	72,550	54,450
Grand Total — Notional	15,967	15,562	75,754	56,869

14. MARKET RISK

Market risk is the risk of adverse financial impact arising from changes in underlying market factors, including interest rates, foreign exchange rates, and equity prices.

Interest Rate Risk

CMHC manages interest rate risk through the implementation of policies which include risk limits for its investments and the Lending Activity.

The investment portfolios for Insurance and Securitization are managed taking into consideration the liability profile and by limiting price sensitivity to interest rate changes relative to benchmark indices and by appropriate asset diversification. Interest rate risk associated with the Lending Activity is managed through asset and liability matching, hedging and capital market strategies. CHT enters into swap agreements to manage the risk that the interest earned on its investments would not be sufficient to meet its CMB obligations. With these swaps, all interest payments to CHT, net of its expenses, are paid to the swap counterparties and CHT receives payments equal to the interest it is required to pay on the CMB.

The following table provides details regarding the Corporation's exposure to interest rate risk.

(in millions of dollars)	Within 3 Months ⁽¹⁾	3 Months to 1 Year	1 to 5 Years	Over 5 Years	Other ⁽²⁾	CHT	Inter-entity Elimination	2005	2004
Assets									
Investment in NHA MBS	—	—	—	—	—	63,931	—	63,931	51,373
Effective Interest Rate ⁽³⁾	—	—	—	—	—	3.91%	—	—	—
Loans and Investments in Housing Programs	861	1,316	4,977	5,982	34	—	—	13,170	13,669
Effective Interest Rate	6.00%	5.31%	4.50%	7.86%	—	—	—	—	—
Investments	—	312	3,878	4,368	1,463	1,672	(451)	11,242	8,637
Effective Interest Rate	—	2.85%	4.09%	4.92%	3.14%	3.38%	—	—	—
Cash and Cash Equivalents	3,967	—	—	—	—	3,008	—	6,975	5,264
Effective Interest Rate	3.32%	—	—	—	—	3.17%	—	—	—
Securities Purchased Under Resale Agreements	112	—	—	—	—	3,928	—	4,040	576
Effective Interest Rate	3.10%	—	—	—	—	3.10%	—	—	—
Derivative-Related Amounts Receive Side Instrument	578	1,910	5,757	2,209	74	—	—	10,528	80
Effective Interest Rate	3.59%	5.74%	4.82%	5.26%	—	—	—	—	—
Derivative-Related Amounts Pay Side Instrument	(1,179)	(1,934)	(5,525)	(1,816)	—	—	—	(10,454)	—
Effective Interest Rate	3.30%	5.11%	4.36%	4.81%	—	—	—	—	—
Other Assets	—	—	—	—	998	669	(6)	1,661	1,409
Total Assets	4,339	1,604	9,087	10,743	2,569	73,208	(457)	101,093	81,008
Liabilities									
Canada Mortgage Bonds	—	—	—	—	—	72,526	(451)	72,075	53,834
Effective Interest Rate	—	—	—	—	—	4.19%	—	—	—
Borrowings from the Capital Markets	1,725	1,427	4,918	1,397	—	—	—	9,467	9,207
Effective Interest Rate	3.10%	4.74%	4.26%	4.79%	—	—	—	—	—
Borrowings from the Government of Canada	96	94	916	3,793	—	—	—	4,899	5,045
Effective Interest Rate	8.73%	8.70%	8.92%	9.14%	—	—	—	—	—
Securities Sold Under Repurchase Agreements	3,044	—	—	—	—	—	—	3,044	2,976
Effective Interest Rate	3.01%	—	—	—	—	—	—	—	—
Securities Sold But Not Yet Purchased	—	—	—	111	—	—	—	111	121
Effective Interest Rate	—	—	—	3.89%	—	—	—	—	—
Derivative-Related Amounts Receive Side Instrument	(2,232)	(203)	(2,673)	(405)	14	—	—	(5,499)	38
Effective Interest Rate	3.26%	4.55%	4.62%	4.10%	—	—	—	—	—
Derivative-Related Amounts Pay Side Instrument	1,811	494	2,798	410	—	—	—	5,513	—
Effective Interest Rate	4.37%	5.09%	4.91%	5.64%	—	—	—	—	—
Other Liabilities and Equity of Canada	—	—	—	—	10,807	682	(6)	11,483	9,787
Total Liabilities and Equity of Canada	4,444	1,812	5,959	5,306	10,821	73,208	(457)	101,093	81,008
On-Balance Sheet Gap	(105)	(208)	3,128	5,437	(8,252)	—	—	—	—
Off-Balance Sheet Financial Instruments									
<i>Eligible for Hedge Accounting</i>									
Pay Side Instruments	—	—	3,204	—	—	72,550	—	75,754	56,869
Effective Interest Rate	—	—	4.40%	—	—	3.89%	—	—	—
Receive Side Instruments	300	—	2,904	—	—	72,550	—	75,754	56,869
Effective Interest Rate	3.36%	—	4.20%	—	—	4.12%	—	—	—
Off-Balance Sheet Gap	300	—	(300)	—	—	—	—	—	—
Total Gap	195	(208)	2,828	5,437	(8,252)	—	—	—	—

(1) On- and Off-Balance Sheet financial instruments are reported based on the earlier of their contractual repricing dates or maturity dates.

(2) Other includes all Balance Sheet items that are non-interest sensitive or that do not have a specific maturity.

(3) The effective rates shown represent historical rates for fixed rate instruments and rates to reset for floating rate instruments.

Some of CMHC's Loans and Investments in Housing Programs contain prepayment and/or repricing options. As CMHC does not have the right to prepay its borrowings from the Government of Canada without penalty, it is exposed to interest rate risk.

Currency Risk

All currency exposure arising from foreign denominated debt issuance is hedged in accordance with Corporate policy.

15. CREDIT RISK

Credit risk is the risk of loss arising from a counterparty's inability to fulfill its contractual obligations. CMHC is exposed to credit risk from various sources directly and indirectly, including directly from its investment, lending and hedging transactions and indirectly from potential claims arising from the Insurance and Securitization Activities.

Credit risk associated with the Corporation's investments and derivatives is managed through the implementation of policies which include counterparty credit limits and diversification of credit risk.

Derivative Financial Instruments

The following table presents the credit exposure of the Corporation's derivatives by term to maturity.

(in millions of dollars)	Replacement value ⁽¹⁾				Potential Future Credit Exposure ⁽²⁾	Total Credit Exposure	
	Within 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years		2005	2004
CMHC							
Interest Rate Swaps	9	15	13	38	219	294	288
Foreign Currency Swaps	—	—	—	—	27	27	—
Total CMHC	9	15	13	38	246	321	288
CHT							
Interest Rate Swaps	18	485	284	7	363	1,157	1,243
Grand Total	27	500	297	45	609	1,478	1,531

(1) Represents the total current replacement value of all outstanding contracts with a positive fair value, before factoring in the impact of master netting agreements.

(2) Represents an add-on that is an estimate of the potential change in the market value of the transaction up to maturity which is calculated in relation to the notional principal of the contracts by applying factors consistent with guidelines issued by the Office of the Superintendent of Financial Institutions.

CMHC limits its credit risk associated with derivative transacting by dealing with counterparties whose credit ratings are in accordance with Department of Finance guidelines, and through the use of master netting agreements for derivatives which have been entered into with all counterparties.

CHT has executed agreements only with counterparties with high credit worthiness and only holds investment instruments rated R-1 high or AAA.

Collateral

Collateral agreements provide for the posting of collateral by the counterparty when CMHC's exposure to that entity exceeds a certain threshold. Collateral held by CMHC as at 31 December 2005 totalled \$24 million (2004 — \$13 million).

CHT also mitigates risk through collateralization in the event of counterparties rated less than AA-. Collateral held by CHT as at 31 December 2005 totalled \$212 million (2004 — \$95 million).

16. FAIR VALUE OF FINANCIAL INSTRUMENTS

The amounts set out below represent the fair values of financial instruments using the valuation methods and assumptions referred to below. Fair value amounts are designed to represent estimates of the amounts at which instruments could be exchanged in a current transaction between willing parties.

As many of the Corporation's financial instruments lack an available trading market, fair values are based on estimates using present value and other valuation techniques. These techniques are significantly affected by the assumptions used concerning the amount and timing of estimated future cash flows and discount rates which reflect varying degrees of risk. Due to the use of subjective judgment and uncertainties, the fair value amounts should not be interpreted as being realizable in an immediate settlement of the instruments. In addition, the calculation of estimated fair value is based on market conditions at a specific point in time and may not be reflective of future fair values.

Interest rate changes are the main cause of changes in the fair value of financial instruments.

	2005												2004		
	CMHC			CHT			Inter-entity Elimination		Consolidated			Consolidated			
	Carrying Value	Fair Value	Fair Value over (under) Carrying Value	Carrying Value	Fair Value	Fair Value over (under) Carrying Value	Carrying Value	Fair Value	Carrying Value	Fair Value	Fair Value over (under) Carrying Value	Carrying Value	Fair Value	Fair Value over (under) Carrying Value	
(in millions of dollars)															
Assets															
Investment in NHA Mortgage-Backed Securities ⁽²⁾	–	–	–	63,931	63,321	(610)	–	–	63,931	63,321	(610)	51,373	51,644	271	
Loans and Investments in Housing Programs ⁽²⁾	13,170	15,300	2,130	–	–	–	–	–	13,170	15,300	2,130	13,669	15,959	2,290	
Investments ^(1,2)	10,021	10,611	590	1,672	1,683	11	(451)	(449)	11,242	11,845	603	8,637	9,107	470	
Cash and Cash Equivalents ^(1,2)	3,967	3,967	–	3,008	3,008	–	–	–	6,975	6,975	–	5,264	5,264	–	
Securities Purchased Under Resale Agreements ⁽²⁾	112	112	–	3,928	3,928	–	–	–	4,040	4,040	–	576	576	–	
Accrued Interest Receivable ⁽³⁾	336	336	–	669	669	–	(6)	(6)	999	999	–	829	829	–	
Accounts Receivable and Other Assets ⁽³⁾	233	233	–	–	–	–	–	–	233	233	–	179	179	–	
Due from the Government of Canada ⁽³⁾	212	212	–	–	–	–	–	–	212	212	–	203	203	–	
Derivative-Related Amounts ⁽³⁾	74	74	–	–	–	–	–	–	74	74	–	80	80	–	
Liabilities															
Canada Mortgage Bonds ⁽²⁾	–	–	–	72,526	72,660	134	(451)	(449)	72,075	72,211	136	53,834	54,991	1,157	
Borrowings from the Capital Markets ^(1,2)	9,467	9,514	47	–	–	–	–	–	9,467	9,514	47	9,207	9,769	562	
Borrowings from the Government of Canada ⁽²⁾	4,899	7,037	2,138	–	–	–	–	–	4,899	7,037	2,138	5,045	7,056	2,011	
Securities Sold Under Repurchase Agreements ⁽²⁾	3,044	3,044	–	–	–	–	–	–	3,044	3,044	–	2,976	2,976	–	
Accounts Payable and Other Liabilities ⁽³⁾	959	959	–	1	1	–	–	–	960	960	–	870	870	–	
Accrued Interest Payable ⁽³⁾	247	247	–	681	681	–	(6)	(6)	922	922	–	629	629	–	
Securities Sold But Not Yet Purchased ⁽³⁾	111	111	–	–	–	–	–	–	111	111	–	121	121	–	
Derivative-Related Amounts ⁽²⁾	14	14	–	–	–	–	–	–	14	14	–	38	38	–	
Off-Balance Sheet Financial Instruments⁽²⁾															
Eligible for Hedge Accounting															
Positive Fair Value	–	–	–	–	794	794	–	–	–	794	794	–	941	941	
Negative Fair Value	–	363	363	–	51	51	–	–	–	414	414	–	414	414	

(1) Fair values are determined by reference to quoted market prices.

(2) Fair values are estimated using net present value analysis.

(3) Fair values are equal to carrying values due to short-term nature.

Methodology and assumptions:

Where quoted market prices are not available, the fair value is estimated by discounting the remaining contractual cash flows at market interest rates currently offered for instruments with similar terms and risks. The fair value of Accrued Interest is disclosed separately.

For Loans and Investments in Housing Programs, the fair value is further adjusted for interest loss recovery.

The total change in fair value for Derivative-Related Amounts during the year was \$18 million (2004 — \$10 million, 2003 — not applicable). This amount is included in Other Income.

17. EMPLOYEE FUTURE BENEFITS

CMHC has a defined benefit pension plan and a supplemental pension plan. CMHC also provides other post-employment benefits.

The accrued benefit asset for the defined benefit pension plan is included in Accounts Receivable and Other Assets. The total accrued benefit liability for the supplemental pension plan and for the other post-employment benefits is included in Accounts Payable and Other Liabilities. The net benefit plan cost recognized is included in Operating Expenses.

Total cash payments for employee future benefits were \$9 million (2004 — \$14 million, 2003 — \$3 million). They include contributions by CMHC to its funded pension plan and payments for the unfunded supplemental pension plan. Also therein are disbursements for other post-employment benefits, which consist of payments to a third-party service provider on behalf of retired employees and payments made directly to employees, their beneficiaries or estates.

Information about the employee future benefits is as follows:

(in millions of dollars)	Pension Plans		Other Post-employment Benefits	
	2005	2004	2005	2004
Accrued Benefit Obligation				
Balance, Beginning of Year	984	947	98	96
Current Service Cost	18	17	2	2
Employees' Contributions	5	4	—	—
Interest Cost	56	57	6	6
Benefits Paid	(51)	(49)	(3)	(3)
Actuarial Loss (Gain)	100	8	19	(3)
Balance, End of Year	1,112	984	122	98
Fair Value of Plan Assets				
Balance, Beginning of Year	1,042	960	—	—
Actual Return on Plan Assets	137	116	—	—
Employer's Contributions	6	11	3	3
Employees' Contributions	5	4	—	—
Benefits Paid	(51)	(49)	(3)	(3)
Balance, End of Year	1,139	1,042	—	—
Funded Status — Plan Surplus (Deficit)	27	58	(122)	(98)
Unamortized Net Actuarial Loss	123	102	33	15
Unamortized Past Service Costs	53	61	—	—
Unamortized Transitional Obligation (Asset)	(150)	(180)	28	31
Accrued Benefit Asset (Liability)	53	41	(61)	(52)

Included in pension plans are amounts in respect of an unfunded supplemental pension plan as follows:

(in millions of dollars)	Supplemental Pension Plan	
	2005	2004
Fair Value of Plan Assets	—	—
Accrued Benefit Obligation	28	27
Funded Status — Plan Deficit	28	27

The plan assets and the accrued benefit obligation were measured for accounting purposes as at 31 December 2005. The most recent actuarial valuation for funding purposes was done 31 December 2005, and the next regularly scheduled valuation will be no later than 31 December 2008. In performing the actuarial valuations of the pension plans and the other post-employment benefits, the following assumptions were adopted:

	2005	2004
Accrued Benefit Obligation:		
Discount rate	5.00%	5.75%
Rate of compensation increase	2.50%	2.75%
Benefit Costs:		
Discount rate	5.75%	6.00%
Rate of compensation increase	2.75%	3.00%
Long-term rate of return on plan assets	5.75%	6.00%
Average remaining service period for Pension Plans	10 years	11 years
Average remaining service period for Other Post-employment Benefits	13 years	13 years

An 8.4% (2004 — 8.8%) increase in health care costs was assumed for 2005, with 0.4% (2004 — 0.4%) average decreases per year thereafter to an ultimate trend rate of 5.1% which is expected to be achieved by 2014.

Sensitivity Analysis:

(in millions of dollars)	Increase (Decrease) in Accrued Benefit Obligation	Increase (Decrease) in Net Benefit Costs
0.5% Increase/Decrease in Discount Rate	(81)/88	(2)/9
0.5% Increase/Decrease in Rate of Compensation Increase	13/(12)	3/(2)
0.5% Increase/Decrease in Long-Term Rate of Return on Plan Assets	—	(6)/6
1.00% Increase/Decrease in Health Care Cost Trend Rates	15/(11)	2/(1)

CMHC's defined benefit costs recognized in the year are as follows:

(in millions of dollars)	Pension Plans			Other Post-employment Benefits		
	2005	2004	2003	2005	2004	2003
Costs Incurred during the Year						
Current Service Cost, Net of Employees' Contributions	18	17	15	2	2	1
Interest Cost	56	57	59	6	6	6
Actual Return on Plan Assets	(137)	(116)	(132)	—	—	—
Actuarial (Gain) Loss on Accrued Benefit Obligation	100	8	44	19	(3)	9
Total Costs before Adjustments	37	(34)	(14)	27	5	16
Adjustments to Recognize the Long-term Nature of Employee Future Benefits Costs						
Difference between Expected and Actual Return on Plan Assets	78	59	75	—	—	—
Difference between Actuarial (Gain) Loss Recognized and Actual Actuarial (Gain) Loss on Accrued Benefit Obligation	(100)	(3)	(34)	(18)	4	(9)
Amortization of Past Service Costs	9	9	9	—	—	—
Amortization of the Transitional Obligation (Asset)	(30)	(30)	(30)	3	3	3
Total Adjustments	(43)	35	20	(15)	7	(6)
Net Benefit Plan Cost (Revenue) Recognized	(6)	1	6	12	12	10

Information on the defined benefit pension plan assets is as follows:

Category of Plan Assets	Percentage of Fair Value of Total Plan Assets	
	2005	2004
Short-term Investments	1.47%	1.62%
Bonds and Debentures	20.25%	19.09%
Equities	64.31%	65.15%
Real Return Securities	4.86%	4.91%
Real Estate	9.11%	9.23%
Total	100.00%	100.00%

At 31 December 2005, fair value of plan assets included \$111 million (2004 — \$94 million) of investments in CMHC related parties, of which \$14 million related to CHT issued CMB (2004 — \$18 million). In 2005, there was a net charge in the amount of \$4 million (2004 — \$3 million) from CMHC to the pension plans.

18. SEGMENTED INFORMATION

As described in Note 1, the Corporation carries out its mandate through the following activities: Insurance, Securitization, Housing Programs, Lending Activity and, as a result of AcG-15, the Corporation has consolidated the activities of Canada Housing Trust. The financial results of each activity are determined using the accounting policies described in Note 2.

The Lending Activity includes certain Corporate items that are not allocated to each activity. The Housing Program activity includes reimbursements to the Lending Activity as described in Note 19. These reimbursements are not eliminated in the table below.

	Insurance		Securitization		Housing Programs		Lending		Canada Housing Trust		Elimination of Inter-Segment Items		Total	
(in millions of dollars)	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
REVENUES														
Income from NHA MBS	—	—	—	—	—	—	—	—	2,458	1,838	—	—	2,458	1,838
Interest Earned on Loans and Investments in Housing Programs	—	—	—	—	—	—	864	969	—	—	—	—	864	969
Investment Income	468	397	16	13	—	—	45	42	144	52	(19)	(25)	654	479
Premiums, Fees, Parliamentary Appropriations and Other Income	1,178	1,076	48	41	2,076	2,107	22	11	73	80	(39)	(41)	3,358	3,274
	1,646	1,473	64	54	2,076	2,107	931	1,022	2,675	1,970	(58)	(66)	7,334	6,560
EXPENSES														
Interest Expense	—	—	—	—	—	—	898	939	2,596	1,885	(19)	(25)	3,475	2,799
Operating Expenses	137	136	5	5	103	101	18	19	79	85	(39)	(41)	303	305
Housing Programs and Net Claims	119	51	—	—	1,973	2,006	—	—	—	—	—	—	2,092	2,057
	256	187	5	5	2,076	2,107	916	958	2,675	1,970	(58)	(66)	5,870	5,161
Income Taxes	439	411	17	17	—	—	6	21	—	—	—	—	462	449
NET INCOME	951	875	42	32	—	—	9	43	—	—	—	—	1,002	950
ASSETS														
Investment in NHA MBS	—	—	—	—	—	—	—	—	63,931	51,373	—	—	63,931	51,373
Direct Lending Loans	—	—	—	—	—	—	8,354	8,556	—	—	—	—	8,354	8,556
Other Loans and Investments in Housing Programs	—	—	—	—	—	—	4,816	5,113	—	—	—	—	4,816	5,113
Investments	8,741	7,707	314	262	—	—	966	630	1,672	677	(451)	(639)	11,242	8,637
Other Assets	3,393	3,171	36	18	—	—	1,746	1,244	7,605	2,925	(30)	(29)	12,750	7,329
	12,134	10,878	350	280	—	—	15,882	15,543	73,208	54,975	(481)	(668)	101,093	81,008
LIABILITIES														
Canada Mortgage Bonds	—	—	—	—	—	—	—	—	72,526	54,468	(451)	(634)	72,075	53,834
Borrowings from the Capital Markets	—	—	—	—	—	—	9,467	9,212	—	—	—	(5)	9,467	9,207
Borrowings from the Government of Canada	—	—	—	—	—	—	4,899	5,045	—	—	—	—	4,899	5,045
Unearned Premiums and Fees	4,548	4,227	146	128	—	—	—	—	—	—	—	—	4,694	4,355
Other Liabilities	3,523	3,539	7	(3)	—	—	1,348	1,127	682	507	(30)	(29)	5,530	5,141
	8,071	7,766	153	125	—	—	15,714	15,384	73,208	54,975	(481)	(668)	96,665	77,582
EQUITY	4,063	3,112	197	155	—	—	168	159	—	—	—	—	4,428	3,426

19. RELATED PARTY TRANSACTIONS

The Corporation is related in terms of common ownership to all Government of Canada departments, agencies and Crown corporations. CMHC enters into transactions with certain of these entities in the normal course of business. All material related party transactions are either disclosed below or in relevant notes.

CMHC receives reimbursements from the Government of Canada in the form of appropriations for the following:

- Payments made to support housing programs;
- Interest rate losses resulting from certain loans containing interest rate clauses lower than the interest cost on the related borrowings;
- Net operating losses on certain investments in housing programs and real estate properties;
- Net default losses on certain loans and net disposal losses on certain investments in housing programs and real estate properties; and
- Operating costs associated with the delivery of housing programs.

The following table summarizes these expenses.

(in millions of dollars)	2005	2004	2003
Housing Program Payments	1,916	1,904	1,860
Interest Rate Losses	53	97	99
Net Operating Losses	3	4	11
Net Default and Disposal Losses	1	1	2
Total Housing Program Expenses	1,973	2,006	1,972
Operating Costs	103	101	97
Total Appropriations	2,076	2,107	2,069

The reimbursement for interest rate losses is also included in Interest Earned on Loans and Investments in Housing Programs. Net operating, default and disposal losses are recorded as Due from the Government of Canada and Housing Program Expenses on an accrual basis. The reimbursement of operating costs is shown in the Consolidated Income Statement as Parliamentary Appropriations for Operating Expenses.

CMHC pays Government of Canada Fees which are incurred in recognition of the Government's financial backing for the Insurance and Securitization Activities and are recorded in Other Income at the exchange amount, which is the amount agreed to by the related parties. In 2005, the fee amounted to \$3 million (2004 — \$21 million, 2003 — \$29 million).

In exchange for real estate transferred to Canada Lands Company CLC Limited in 1998 and 1999, CMHC holds notes receivable of \$43 million (2004 — \$41 million) including accrued interest at 7.35% due by 2014.

20. COMMITMENTS AND CONTINGENT LIABILITIES

- a) Commitments outstanding for Loans and Investments in Housing Programs, net of forgiveness, amounted to \$66 million at 31 December 2005 (2004 — \$48 million) and are normally advanced within a two-year period.
- b) Commitments outstanding for advances to insured assisted housing projects in financial difficulty amounted to \$52 million at 31 December 2005 (2004 — \$56 million) and are normally advanced within a ten-year period.
- c) Total remaining contractual financial obligations for Housing Programs extend for periods up to 34 years.

Estimated obligations are as follows:

(in millions of dollars)	2006	2007	2008	2009	2010	2011 and Thereafter
	1,769	1,725	1,721	1,717	1,704	21,347

- d) In addition to the lines of credit disclosed in Note 7, at 31 December 2005 CMHC had a \$55 million (2004 — \$40 million) letter of credit outstanding.
- e) There are legal claims of \$11 million (2004 — \$14 million) against CMHC. Due to the uncertainty of the outcome of these claims, no provision for loss has been recorded.

21. COMPARATIVE FIGURES

Comparative figures have been reclassified to conform to the 2005 financial statement presentation.

GLOSSARY AND CORPORATE LISTING

Glossary of Performance Measures

Glossary of Terms

Corporate Listing

GLOSSARY & CONTACT INFORMATION

GLOSSARY OF PERFORMANCE MEASURES

CORPORATE MEASURE	DEFINITION
Affordable Housing Program expenditures (\$ millions)	Federal expenditures incurred under the \$1 billion Affordable Housing Initiative. The federal funding is matched by the provinces, territories and others, and the provinces/territories deliver the programs.
Annual direct lending — new business (\$ millions)	Loans provided to social housing sponsors at break-even levels. These loans are funded from borrowings from capital markets. New business arises as existing or new projects are financed with CMHC for the first time.
Annual direct lending — subsequent renewals (\$ millions)	Loans provided to social housing sponsors at break-even levels. These loans are funded from capital markets. Subsequent renewals consist of projects previously funded under the Direct Lending Initiative and renewing within the initiative.
Annual securities guaranteed (\$ millions)	Mortgage-Backed Securities (MBS) issued directly into capital markets plus Canada Mortgage Bonds issued for the year.
Attendees at Housing Outlook Conferences who found them useful (%)	Percentage of attendees at Housing Outlook Conferences and Seminars who rated the event as either useful or very useful (4 or 5 on a 5-point scale) on an independent market research survey administered following the event.
Delivery of on-reserve programs and services through First Nation or Aboriginal organizations (%)	<p>Percentage of CMHC Aboriginal programs and services provided by Aboriginal contractors or organizations.</p> <p>Calculated as the average of the following:</p> <ul style="list-style-type: none"> a) % of RRAP accounts delivered by Aboriginal organizations based on units; b) % of Section 95 commitment inspections and Physical Condition Reviews carried out under the Native Inspection Services Initiative based on units; c) % of Aboriginal Capacity Development service contract dollars paid to Aboriginal service providers.
Estimated number of households assisted	The estimated number of households who, in 2005, benefited from units delivered under various social housing programs, some of which date back to the early 1950's.
Forecast accuracy for housing starts	The percentage difference between CMHC's initial starts forecast for Canada and the actual annual starts for the same year.
Information transfer seminar attendees who found them useful (%)	Percentage of attendees who rated the workshop as useful or very useful (4 or 5 on a 5-point scale) on an independent market research survey administered following the event. The workshops included in the calculation are: Build & Renovate to Avoid Mold, Sustainable Planning for Small Communities, Faculty Summits (Design, Planners, Disabilities).
Mortgage insurance approvals of public-private partnership units (units)	<p>Affordable housing projects facilitated through the Partnership Centre that have accessed financing facilitated by CMHC's mortgage insurance with lower mortgage loan insurance premiums and more flexible underwriting criteria.</p> <p>Affordable housing projects are those that rent more than half the units below the 80th percentile of rental prices.</p>
On-reserve non-profit new commitments (units)	Number of new or renovated housing units approved under the non-profit rental program for First Nation communities.
Operating budget spent on information technology (%)	Ratio of information technology expenses to total planned operating expenses

CORPORATE MEASURE	DEFINITION
Overall satisfaction rate of key export clients (%)	Percent of CMHC International's clients who are satisfied with export advice and service they receive from CMHC trade consultants, as derived from a survey of CMHC's key export clients (150–200) conducted by an independent consultant. Satisfied clients rank 4 or 5 on a scale of 1 to 5 for overall satisfaction.
Percentage of overall awareness of CMHC	<p>Percentage of consumers able to recognize CMHC as Canada's national housing agency.</p> <p>Awareness is measured through telephone surveys conducted in each of the six major Census Metropolitan Areas targeted by CMHC's consumer advertising campaign. Within each of the Census Metropolitan Areas, 500 interviews are completed among consumers involved in the home-buying and/or renovation process. Awareness tracking surveys are completed within one week following the completion of the nationally planned consumer advertising campaigns. Overall awareness includes those consumers who were prompted during the survey with the following question: "CMHC, also known as Canada Mortgage and Housing Corporation, is Canada's national housing agency. Have you ever heard of CMHC?"</p>
Percentage of unaided awareness of CMHC	<p>Percentage of consumers able to name, without prompting, CMHC as the federal government agency responsible for providing housing related information to Canadians.</p> <p>Unaided awareness is measured through a telephone survey conducted in each of the six major Census Metropolitan Areas targeted by the consumer advertising campaign. Within each of the Census Metropolitan Areas, 500 interviews are completed among consumers involved in the home-buying and/or renovation process. Awareness tracking surveys are completed within one week following the completion of the nationally planned consumer advertising campaigns.</p>
Public–Private Partnership units facilitated	<p>Public–Private Partnership projects are those which have been provided with seed funding or interest-free proposal development funding loans, and/or significant CMHC Partnership staff support to assist in the development of affordable housing. Includes but is not limited to projects financed with CMHC insured loans.</p> <p>The calculation is based on the national total number of affordable housing units and beds contained in Public–Private Partnership projects.</p>
Ranking of housing start forecast accuracy among forecasters	The ranking of CMHC's annual housing starts forecast accuracy amongst other industry forecasters, where 1 is the most accurate forecast.
Recipients of market analysis publications who found them useful (%)	Percentage of recipients of market analysis publications who rated the publications as either useful or very useful (4 or 5 on a 5-point scale) during an independent market research study conducted in 2005.
Recipients of newly-published About Your House fact sheets who found them useful (%)	Percentage of clients who ordered an About Your House publication from the CMHC Order Desk who rated the fact sheets as useful or very useful (4 or 5 on a 5-point scale) during a phone survey.
Recipients of newly-published Research Highlights who found them useful (%)	Percentage of clients who are on the Research Highlight Technical and Social-Economic series distribution lists who rated the product series as useful or very useful (4 or 5 on a 5-point scale) during a phone survey.
Renovation Programs (units)	Units committed under CMHC's suite of renovation programs including the Residential Rehabilitation Assistance Program, Emergency Repair Program, Housing Adaptations for Seniors' Independence program, and Shelter Enhancement Program.

CORPORATE MEASURE	DEFINITION
Retention rate of recent recruits (%)	Percentage of regular employees hired during the reporting year who remained in CMHC's service at the end of that year.
Revenue from selling CMHC's expertise abroad (in millions of dollars)	Revenues earned from consulting services in the area of housing and housing finance provided to international clients.
Short-term profitability: Operating expense ratio for mortgage insurance (%)	The ratio of total costs to total premiums earned and fees. (Issuance cost + other administrative cost / (earned premiums + fees) * 100
Short-term profitability: Operating expense ratio for securitization (%)	The ratio of total operating expenses as a percentage of operating revenue. (Operating expenses + Canada Mortgage Bond related expenses) / (guarantee fees + application fees + Financial Services Advisor fees collected from Canada Housing Trust) * 100
Technology reliability index for key systems (%)	Weighted average of monthly availability of the key corporate systems.
Total mortgage insurance approved (units)	Total mortgage insurance applications approved (units).
Total mortgage insurance units approved to address less served markets and/or support specific government priorities (%)	Percentage of total mortgage insurance approvals in rural and northern areas, in single industry towns, on reserve, for rental accommodation (including nursing and retirement homes), for energy-efficient homes and for loans on chattels.
Training investment per staff year (\$)	Total training dollars (continuous learning, language training & corporate priorities) spent per staff year.
Value of CMHC-facilitated sales reported by key clients (\$ millions)	The value of international sales by CMHC's export clients that the clients themselves attribute to CMHC facilitation/assistance.

GLOSSARY OF TERMS

Aboriginal Capacity Development — To facilitate, by sharing CMHC knowledge and experience with Aboriginal groups, the development of appropriate infrastructure and governance capability for Aboriginal Peoples to run their own housing systems and ensure sustainability of the final product.

Benchmark Index — A benchmark provides an objective point of reference for performance measurement. CMHC's benchmarks for the insurance and securitization investment portfolios are the Scotia Capital Universe Bond Index (fixed income portfolios); the Scotia Capital 91-day Treasury-Bill Index (money market portfolios); the total return of the Standard and Poor's/Toronto Stock Exchange (S&P TSX) Composite Index (equity portfolios); the total return of the Standard & Poor's 500 (for the US equity portfolios; and the total return of the Morgan Stanley Capital International (MSCI) — Europe, Australasia, and Far East Index (for the international equity portfolios).

Brownfield redevelopment — Redevelopment/adaptive reuse of contaminated sites and buildings previously used for industrial or commercial purposes.

Canadian Centre for Public-Private Partnerships in Housing (CCPPPH) — A team of housing experts operating within CMHC which provides information, guidance and other tools to facilitate the production of affordable housing by non-profit organizations, private sector proponents and others.

Canada Housing Trust (CHT) — A special purpose trust created to issue Canada Mortgage Bonds.

Canada Mortgage Bonds (CMB) — A guaranteed semi-annual coupon, bullet-maturity (repayment of principal upon maturity) bond product issued by a special purpose trust, known as Canada Housing Trust (CHT).

Commercial Paper — A type of corporate short-term borrowing with a term to maturity of up to one year.

Compliance — A term used in reference to conformity to established policies, which define the risk tolerance of the Corporation.

Convexity — The degree of curvature (or convex) shape of the price/yield relationship for a security and defines the degree to which a security's price changes as yields change.

Credit Rating — Credit ratings are current opinions of the creditworthiness of an obligor with respect to a specific financial obligation. It takes into consideration the creditworthiness of guarantors, insurers, or other forms of credit enhancement on the obligation and takes into account the currency in which the obligation is denominated.

Derivatives — A financial derivative is an instrument whose value is derived from price movements in one or more underlying securities, interest rates, currencies, indices or other instruments or derivatives.

Direct Lending — Loans provided to social housing sponsors at break-even levels. These loans are funded through borrowings from capital markets.

Duration — A measure of the average time interval required for an expected stream of cashflows to repay the original investment (i.e., shorter duration means faster recovery of the original investment). It is also a measure of the sensitivity of fixed income securities prices in relation to changes in interest rates.

Dynamic Financial Analysis (DFA) — A systematic and holistic approach to financial modeling and sensitivity analysis for assets and liabilities that projects financial results under a variety of possible scenarios, showing how outcomes might be affected by changing business and economic conditions.

Emergency Repair Program (ERP) — This CMHC program offers financial assistance to low-income homeowners or occupants in rural areas to undertake emergency repairs required for the continued safe occupancy of their house.

Housing Adaptations for Seniors' Independence (HASI)

— This CMHC initiative assists low-income seniors who have difficulties with daily living activities in the home by providing financial assistance to carry out minor home adaptations.

Investment and Hedging Exposure — The fair value of the Corporation's financial investments (including fixed income and equity securities) and hedging positions. In relation to the Corporation's repurchase, reverse repurchase, and derivatives transactions, exposures are marked-to-market and include only positive amounts (net of collateral under respective agreements) on a counterparty basis.

Mark-to-Market — The valuing of financial instruments at market trading prices.

National Housing Act (NHA) — An Act to promote the construction of new houses, the repair and modernization of existing houses, and the improvement of housing and living conditions. CMHC was established to carry out the provisions of the NHA.

National Housing Act Mortgage-Backed Securities (NHA MBS or MBS) — An undivided interest in a pool (group) of insured residential mortgages. These financial instruments are secured by the value of underlying real estate and credit enhanced by mortgage insurance.

Residential Rehabilitation Assistance Program (RRAP) — A CMHC program offering financial assistance to low-income households on- and off-reserve to enable them to repair their dwellings. Types of assistance include Homeowner RRAP, Disabled Homeowner RRAP, Rental and Rooming House RRAP, RRAP Conversion and On-Reserve RRAP.

Repurchase and Reverse Repurchase Activity — Transactions in which the Corporation buys securities with a commitment to resell them (securities purchased under resale agreements), or sells securities with a commitment to repurchase them (securities sold under repurchase agreements).

Shelter Enhancement Program (SEP) — This CMHC program provides financial assistance to repair, rehabilitate and improve existing shelters for women, children and youth who are victims of family violence. The program also assists in the acquisition or construction of new shelters and second stage housing.

Securitization — The process of converting loans or other assets into financial securities which are sold into the capital markets providing investors with an interest in the pool of loans or assets underlying the security.

Swap — A form of derivative, an interest rate swap is a contractual agreement between two parties to exchange a series of cashflows, generally exchanging fixed and floating rate interest payments based on a notional principal value in a single currency. In the case of a currency swap, principal amounts and fixed and floating rate interest payments are exchanged in different currencies. Swaps are generally used to reduce or eliminate interest rate risk or foreign exchange risk.

Value of a Portfolio — The concept of value and how it can change under various scenarios is central to the discussion of risk management. While there are different methods for obtaining estimates of the value of a portfolio, the meaning typically refers to the sum of the projected future cash flows of a portfolio adjusted to today's value by discounting at appropriate rates.

Volatility — A measure of the spread or dispersion of observations around the average. Statistically, volatility is defined as the standard deviation of a set of observations.

CORPORATE LISTING

(as at 31 December 2005)

CMHC's National Office is located in Ottawa. The Corporation also has five Business Centres located in the following regions across Canada: Atlantic; Quebec; Ontario; Prairie and Territories; and British Columbia. CMHC also has points of service or corporate representatives in smaller communities and cities throughout the country.

National Office, the regional Business Centres and the points of service work in close cooperation to provide Canadians with front-line access to CMHC programs, products and services.

CMHC is also responsible for the management and administration of Granville Island on behalf of the Government of Canada, for which CMHC receives a management fee. Owned by the federal government, the island is a cultural, recreational and commercial development in the heart of Vancouver. It is expected to be commercially viable with the majority of revenue being rental income. Capital additions are funded through operations, grants and contributions.

Karen Kinsley
President and Chief Executive Officer

NATIONAL OFFICE

Sharon Matthews
Vice-President, Insurance

Pierre Serré
Vice-President, Finance and Chief Financial Officer

Mel Skinner
Vice-President, Human Resources

Bill Smith
Vice-President, Assisted Housing

Douglas A. Stewart
Vice-President, Policy and Planning

Berta Zaccardi
Vice-President, Corporate Services

Pierre David
Executive Director, CMHC International

Anthea English
Executive Director, Securitization and Treasury

Gilles Proulx
Executive Director, Risk Management and Investments

Joseph Choi
Director, Audit and Evaluation Services

Luc Fournier
Corporate Secretary

REGIONAL BUSINESS CENTRES

Carolyn Kavanagh
General Manager, Atlantic Region

Charles D. Chenard
General Manager, Quebec Region

Peter Friedmann
General Manager, Ontario Region

Trevor Gloyn
General Manager, Prairie and Territories Region

Nelson Merizzi
General Manager, British Columbia Region

CMHC OFFICES

NATIONAL OFFICE

700 Montreal Road
Ottawa, Ontario
Canada K1A 0P7
(613) 748-2000

REGIONAL BUSINESS CENTRES

Atlantic

1894 Barrington Street, 9th Floor
Halifax, Nova Scotia B3J 2A8
(902) 426-3530

Quebec

1100 René-Lévesque Blvd West, 1st Floor
Montreal, Quebec H3B 5J7
(514) 283-2222

Ontario

100 Sheppard Avenue East, Suite 500
Toronto, Ontario M2N 6Z1
(416) 221-2642

Prairie and Territories

Suite 200, 1000 7th Avenue SW
Calgary, Alberta T2P 5L5
(403) 515-3000

British Columbia

1111 West Georgia Street, Suite 200
Vancouver, British Columbia V6E 4S4
(604) 731-5733

OTHER KEY CONTACT NUMBERS

Market Analysis Electronic Marketplace

www.cmhc.ca/mktinfo/store
(613) 748-2313

CMHC International Centre

(613) 748-2461

NHA Mortgage-Backed Securities

mbs@cmhc.ca
(416) 250-2700

Northern Housing Centre

(403) 515-3000

TO ORDER ADDITIONAL COPIES OF THE ANNUAL REPORT

1 800 668-2642

CMHC ON THE INTERNET

www.cmhc.ca

Canada Mortgage and Housing Corporation supports the Government of Canada policy on access to information for people with disabilities. If you wish to obtain this publication in alternative formats, call 1 800 668-2642. CMHC offers a wide range of housing-related information. For details, call 1 800 668-2642 or visit our Web site at **www.cmhc.ca**

© 2006 Canada Mortgage and Housing Corporation
Catalogue no: NHI-1/2005
ISSN: 0226-0336
ISBN: 0-662-69008-7

Printed in Canada