FEDERAL HOME LOAN MORTGAGE CORP
Form 10-Q
August 07, 2009

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the quarterly period ended June 30, 2009

or

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

For the transition period from to

Commission File Number: 000-53330

Federal Home Loan Mortgage Corporation
(Exact name of registrant as specified in its charter)

Freddie Mac

Federally chartered corporation *(State or other jurisdiction of incorporation or organization)*	**52-0904874** *(I.R.S. Employer Identification No.)*
8200 Jones Branch Drive, McLean, Virginia *(Address of principal executive offices)*	**22102-3110** *(Zip Code)*

(703) 903-2000

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). o Yes o No

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

Large accelerated filer o Accelerated filer o

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o Yes x No

As of July 31, 2009, there were 648,305,154 shares of the registrant s common stock outstanding.

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* Throughout this Quarterly Report on Form 10-Q, we use certain acronyms and terms and refer to certain accounting pronouncements which are defined in the Glossary.

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FINANCIAL STATEMENTS

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PART I FINANCIAL INFORMATION

This Quarterly Report on Form 10-Q includes forward-looking statements, which may include statements pertaining to the conservatorship and our current expectations and objectives for internal control remediation efforts, future business plans, liquidity, capital management, economic and market conditions and trends, market share, legislative and regulatory developments, implementation of new accounting standards, credit losses, and results of operations and financial condition on a GAAP, Segment Earnings and fair value basis. You should not rely unduly on our forward-looking statements. Actual results might differ significantly from those described in or implied by such forward-looking statements due to various factors and uncertainties, including those described in (i) Management s Discussion and Analysis, or MD&A, MD&A FORWARD-LOOKING STATEMENTS and RISK FACTORS in this Form 10-Q and in the comparably captioned sections of our Annual Report on Form 10-K for the year ended December 31, 2008, or 2008 Annual Report, and our Form 10-Q for the first quarter of 2009 and (ii) the BUSINESS section of our 2008 Annual Report. These forward-looking statements are made as of the date of this Form 10-Q and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date of this Form 10-Q, or to reflect the occurrence of unanticipated events.

Throughout PART I of this Form 10-Q, including the Financial Statements and MD&A, we use certain acronyms and terms and refer to certain accounting pronouncements which are defined in the Glossary.

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

EXECUTIVE SUMMARY

You should read this MD&A in conjunction with our consolidated financial statements and related notes for the three and six months ended June 30, 2009 and our 2008 Annual Report.

Overview

Freddie Mac was chartered by Congress in 1970 with a public mission to stabilize the nation s residential mortgage market and expand opportunities for home ownership and affordable rental housing. Our statutory mission is to provide liquidity, stability and affordability to the U.S. housing market. Our participation in the secondary mortgage market includes providing our credit guarantee for residential mortgages originated by mortgage lenders and investing in mortgage loans and mortgage-related securities. Through our credit guarantee activities, we securitize mortgage loans by issuing PCs to third-party investors. We also resecuritize mortgage-related securities that are issued by us or Ginnie Mae as well as private, or non-agency, entities. We also guarantee multifamily mortgage loans that support housing revenue bonds issued by third parties and we guarantee other mortgage loans held by third parties. Securitized mortgage-related assets that back PCs and Structured Securities that are held by third parties are not reflected as our assets. We earn management and guarantee fees for providing our guarantee and performing management activities (such as ongoing trustee services, administration of pass-through amounts, paying agent services, tax reporting and other required services) with respect to issued PCs and Structured Securities.

We had net income attributable to Freddie Mac of $0.8 billion for the second quarter of 2009 and total equity of $8.2 billion as of June 30, 2009. Net loss attributable to common stockholders was $374 million for the second quarter of 2009, reflecting the payment of $1.1 billion of dividends in cash on the senior preferred stock. As discussed below, total equity benefited from the cumulative effect of a change in accounting principle, which increased total equity by $5.1 billion. Our financial results for the second quarter of 2009 reflect the favorable impact on the fair value of our

derivatives and on our investment activities of the steepening of the yield curve, as short-term rates decreased and long-term rates increased, as well as spread tightening. This favorable impact was partially offset by large credit-related expenses and losses on loans purchased due to loan modification. Second quarter net income also reflects a decrease in our provision for credit losses that we estimate to be approximately $1.4 billion related to an enhancement to our methodology for estimating loan loss reserves.

We expect a variety of factors will place downward pressure on our financial results in future periods, and could cause us to incur GAAP net losses. Key factors include the potential for continued deterioration in the housing market, which could increase credit-related expenses and security impairments, adverse changes in interest rates and spreads, which could result in mark-to-market losses, and our efforts under the MHA Program and other government initiatives, some of which are expected to have an adverse impact on our financial results. We believe that the recent modest home price improvements were largely seasonal, and expect home price declines in future periods. Consequently, our provisions for credit losses will likely remain high during the remainder of 2009 and increase above the level recognized in the second quarter. To the extent we incur GAAP net losses in future periods, we will likely need to take additional draws under the Purchase Agreement. In addition, due to the substantial dividend obligation on the senior

preferred stock, we expect to continue to record net losses attributable to common stockholders in future periods. For a discussion of factors that could result in additional draws, see LIQUIDITY AND CAPITAL RESOURCES Capital Adequacy .

On July 21, 2009, we announced that our Board of Directors named Charles E. Haldeman, Jr. as our Chief Executive Officer. We expect that Mr. Haldeman s employment will begin on August 10, 2009. We also announced that Mr. Haldeman was elected as a member of the Board, effective the date his employment commences. Mr. Haldeman will succeed John A. Koskinen, who has been serving as our Interim Chief Executive Officer and performing the function of principal financial officer and who will return to the position of Non-Executive Chairman of the Board.

Business Objectives

We continue to operate under the conservatorship that commenced on September 6, 2008, conducting our business under the direction of FHFA as our Conservator. During the conservatorship, the Conservator has delegated certain authority to the Board of Directors to oversee, and to management to conduct, day-to-day operations so that the company can continue to operate in the ordinary course of business.

We have changed certain business practices and other non-financial objectives to provide support for the mortgage market in a manner that serves public policy, but that may not contribute to profitability. Some of these changes increase our expenses, while others require us to forego revenue opportunities in the near term. In addition, the objectives set forth for us under our charter and by our Conservator, as well as the restrictions on our business under the Purchase Agreement with Treasury, may adversely impact our results, including our segment results.

There is significant uncertainty as to whether or when we will emerge from conservatorship, as it has no specified termination date, and as to what changes may occur to our business structure during or following our conservatorship, including whether we will continue to exist. However, we are not aware of any current plans of our Conservator to significantly change our business structure in the near-term. As discussed below in Legislative and Regulatory Matters *Pending and Proposed Legislation and Related Matters*, Treasury and HUD, in consultation with other government agencies, are expected to develop legislative recommendations for the future of the GSEs.

Our current focus and purpose is to meet the urgent liquidity needs of the U.S. mortgage market, lower costs for borrowers and support the recovery of the housing market and U.S. economy. Through our role in the Obama Administration s initiatives, including the MHA Program, we are working to meet the needs of the mortgage market, in line with our mission, by making homeownership and rental housing more affordable, minimizing foreclosures and helping families keep their homes.

MHA Program and Other Efforts to Assist the Housing Market

We are working with our Conservator to help distressed homeowners through initiatives that support the MHA Program (previously known as the Homeowner Affordability and Stability Plan), which was announced by the Obama Administration in February 2009. We have also implemented a number of other initiatives to assist the U.S. residential mortgage market and help families keep their homes, some of which were undertaken at the direction of FHFA. The more significant initiatives are discussed below.

The MHA Program includes:

Home Affordable Refinance, which gives eligible homeowners with loans owned or guaranteed by Freddie Mac or Fannie Mae an opportunity to refinance into more affordable monthly payments. The Freddie Mac Relief Refinance Mortgage[sm] is our implementation of Home Affordable Refinance. We began purchasing loans under

our program in April 2009, and as of June 30, 2009 we had purchased approximately 28,500 loans totaling $5.1 billion in unpaid principal balance originated under this initiative. The Administration s Home Affordable Refinance effort is targeted at borrowers with current LTV ratios above 80%; however, our implemented program also allows borrowers with LTV ratios below 80% to participate. In July 2009, we announced that borrowers who have mortgages with current LTV ratios up to 125% would be allowed to participate in this program.

Home Affordable Modification Program, or HAMP, which commits U.S. government, Freddie Mac and Fannie Mae funds to avoid foreclosure and keep eligible homeowners in their homes through mortgage modifications. We are working with servicers and borrowers to pursue modifications under HAMP, which requires that each borrower complete a three month trial period before the modification becomes effective. Based on information provided by certain of our largest servicers who service a majority of our loans, approximately 16,000 loans that we own or guarantee started the trial period portion of the HAMP process as of June 30, 2009. We expect a significant increase in the number of loans in the trial period as HAMP expands and we receive additional results from our servicers. Freddie Mac will bear the full cost of the monthly payment reductions related to

modifications of loans we own or guarantee, and all servicer and borrower incentive fees, and we will not receive a reimbursement of these costs from Treasury.

Second Lien Program, also known as 2MP, which will offer incentive payments to borrowers, servicers and investors (other than us and Fannie Mae), for modifications and principal reductions on second lien mortgages in certain circumstances. This program is intended to help facilitate greater modifications of second lien mortgages, but has not yet been implemented.

Short Sale and Deed-in-Lieu Program, which will offer borrowers who are ineligible to participate in HAMP the ability to sell their homes for amounts that are not sufficient for a full payoff of the borrower s mortgage debt and for lenders to accept such amounts. This program has not yet been implemented.

At present, it is difficult for us to predict the full impact of the MHA Program on us. However, to the extent our borrowers participate in HAMP in large numbers, it is likely that the costs we incur, including the servicer and borrower incentive fees, will be substantial. In addition, we continue to devote significant internal resources to the implementation of the various initiatives under the MHA Program. It is not possible at present to estimate the extent to which costs, incurred in the near term, may be offset, if at all, by the prevention or reduction of potential future costs of loan defaults and foreclosures due to these initiatives.

Our other efforts to assist the U.S. housing market include:

Increase in our Mortgage Portfolio Activity. Since we entered into conservatorship in September 2008, we have been providing additional liquidity to the mortgage market, including by acquiring and holding increased amounts of mortgage loans and mortgage-related securities in our mortgage-related investments portfolio, subject to the limitation on the size of such portfolio as set forth in the Purchase Agreement. However, our mortgage-related investments portfolio decreased during the second quarter of 2009, due to a relative lack of favorable investment opportunities.

Temporary Foreclosure and Eviction Suspensions. In order to allow our mortgage servicers time to implement our more recent modification programs and provide additional relief to troubled borrowers, we temporarily suspended all foreclosure transfers of occupied homes for certain periods. On March 7, 2009, we suspended foreclosure transfers on owner-occupied homes where the borrower may be eligible to receive a loan modification under HAMP. In addition, we temporarily suspended the eviction process for occupants of foreclosed homes from November 26, 2008 through April 1, 2009.

Increased Foreclosure Alternatives. In the second quarter of 2009, we completed approximately 29,400 foreclosure alternative agreements, excluding loans in trial-period payment plans under HAMP, with borrowers out of the estimated 415,000 single-family loans in our single-family mortgage portfolio that were or became delinquent (90 days or more past due or in foreclosure) during the second quarter of 2009.

Government Support for our Business

We are dependent upon the continued support of Treasury and FHFA in order to continue operating our business. We also receive substantial support from the Federal Reserve. Our ability to access funds from Treasury under the Purchase Agreement is critical to keeping us solvent and avoiding the appointment of a receiver by FHFA under statutory mandatory receivership provisions.

Significant recent developments with respect to the support we receive from the government include the following:

On May 6, 2009, FHFA, acting on our behalf in its capacity as Conservator, and Treasury amended the Purchase Agreement to, among other items: (i) increase the funding available under the Purchase Agreement from $100 billion to $200 billion; (ii) increase the limit on our mortgage-related investments portfolio (which is based on the carrying value of such assets as reflected on our GAAP balance sheet) as of December 31, 2009 from $850 billion to $900 billion; and (iii) revise the limit on our aggregate indebtedness and the method of calculating such limit. The amendment also expands the category of persons covered by the restrictions on executive compensation contained in the Purchase Agreement.

On June 30, 2009 and March 31, 2009, we received $6.1 billion and $30.8 billion, respectively, in funding from Treasury under the Purchase Agreement, which increased the aggregate liquidation preference of the senior preferred stock to $51.7 billion as of June 30, 2009. We received these funds pursuant to draw requests made to address the deficits in our net worth as of March 31, 2009 and December 31, 2008, respectively. On June 30, 2009 and March 31, 2009, we paid dividends of $1.1 billion and $370 million, respectively, in cash on the senior preferred stock to Treasury for the three months ended June 30, 2009 and March 31, 2009, respectively, at the direction of the Conservator.

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According to information provided by Treasury, it held $151.1 billion of mortgage-related securities issued by us and Fannie Mae as of June 30, 2009 under the purchase program it announced in September 2008.

According to information provided by the Federal Reserve, as of July 29, 2009 it had net purchases of $246.3 billion of our mortgage-related securities under the purchase program it announced in November 2008 and held $39.6 billion of our direct obligations.

At June 30, 2009, our assets exceeded our liabilities by $8.2 billion. Because we had a positive net worth as of June 30, 2009, FHFA has not submitted a draw request on our behalf to Treasury for additional funding under the Purchase Agreement. The aggregate liquidation preference of the senior preferred stock is $51.7 billion and the amount remaining under the Treasury s funding agreement is $149.3 billion as of June 30, 2009. The corresponding annual cash dividends payable to Treasury are $5.2 billion, which exceeds our annual historical earnings in most periods. We expect to make additional draws under the Purchase Agreement in future periods due to a variety of factors that could affect our net worth.

For more information on the terms of the conservatorship, the powers of our Conservator and certain of the initiatives, programs and agreements described above, see BUSINESS Conservatorship and Related Developments in our 2008 Annual Report.

Housing and Economic Conditions and Impact on Second Quarter 2009 Results

Our financial results for the second quarter of 2009 reflect the continuing adverse economic conditions in the U.S., which deteriorated dramatically during the last half of 2008 and have continued to deteriorate in 2009. During the first half of 2009, there have been some positive housing market developments, including higher volumes of home sales and modest improvements in national home prices, which we believe to be largely seasonal. However, the U.S. recession has deepened, and there were significant increases in unemployment rates which, coupled with declines in household wealth, have contributed to increases in residential mortgage delinquency rates. Much of the increase in home sales reflects distressed home sales, including higher short sales and sales of foreclosed properties in the market. As a result, we continue to experience significant credit-related expenses, and our provision for credit losses was $5.2 billion in the second quarter of 2009, principally due to increased estimates of incurred losses caused by the deteriorating economic conditions, which were evidenced by our increased rates of delinquency, the significant volume of REO acquisitions and an increase in our single-family non-performing assets.

Although home prices nationwide increased an estimated 3.2% in the second quarter of 2009 (and an estimated 1.4% during the first half of 2009) based on our own internal index, which is based on properties underlying our single-family mortgage portfolio, home prices have suffered significant declines in nearly all regions and states in the last 12 months. The percentage decline in home prices in the last 12 months has been particularly large in the states of California, Florida, Arizona and Nevada, where we have significant concentrations of mortgage loans. The second quarter of the year is historically a strong period for home sales. This seasonal strength, combined with the fact that many financial institutions have maintained foreclosure suspensions during the first half of 2009, may have contributed to the increase in home prices during the period. We expect that when these temporary foreclosure suspensions are lifted and the seasonal peak in home sales has passed, there will likely be further downward pressure on home prices over the remainder of the year, which would likely result in increased credit related expenses. Unemployment rates have worsened significantly in the second quarter of 2009, and the national unemployment rate increased to 9.5% at June 30, 2009 as compared to 8.5% at March 31, 2009. Certain states have experienced much higher unemployment rates, such as California, Florida, Michigan and Nevada, where the unemployment rate reached 11.6%, 10.6%, 15.2% and 12.0%, respectively, at June 30, 2009. These states comprise approximately 25% of loans in our single-family mortgage portfolio as of June 30, 2009. Many financial institutions have continued to remain

cautious in their lending activities during the second quarter of 2009. Although there was overall improvement in credit and liquidity conditions during the second quarter, credit spreads for both mortgage and corporate loans remained higher than before the start of the recession.

These macroeconomic conditions and other factors, such as our temporary suspensions of foreclosure transfers of occupied homes, contributed to a substantial increase in the number and aging of delinquent loans in our single-family mortgage portfolio during the second quarter of 2009. While temporary suspensions of foreclosure transfers and recent loan modification efforts reduced the rate of growth in our charge-offs and REO acquisitions during the second quarter of 2009, our provision for credit losses includes expected losses on those foreclosures currently suspended. We also observed a continued increase in market-reported delinquency rates for mortgages serviced by financial institutions, not only for subprime and Alt-A loans but also for prime loans, and we experienced significant increases in delinquency rates for all product types during the second quarter of 2009. Additionally, as the slump in the U.S. housing market has

persisted for approximately two years, increasing numbers of borrowers that previously had significant equity are now underwater, or owing more on their mortgage loans than their homes are currently worth.

Multifamily housing fundamentals have also further deteriorated during the second quarter of 2009, reflecting the increasing unemployment rate and tightened credit of consumers and institutional borrowers. Home ownership is also becoming more affordable, due to home price declines that have occurred over the past several years. Consequently, multifamily properties have experienced declining rent levels and vacancy rates have recently risen to multi-year highs, which has negatively impacted multifamily property cash flows. As a result, our multifamily delinquency rate increased from 9 basis points as of March 31, 2009 to 11 basis points as of June 30, 2009. Despite challenging conditions, in June 2009 we completed a structured securitization transaction with multifamily mortgage loans totaling approximately $1 billion, which was one of the first large commercial mortgage bond issuances in the CMBS market this year.

The continued weakness in housing market conditions during the second quarter of 2009 also led to a further decline in the performance of the non-agency mortgage-related securities in our mortgage-related investments portfolio. Mortgage-related securities backed by subprime, MTA Option ARM, Alt-A and other loans, have significantly greater concentrations in the states that are undergoing the greatest stress, including California, Florida, Arizona and Nevada. As a result of these and other factors, we recorded $2.2 billion of net impairments of available-for-sale securities recognized in earnings during the second quarter of 2009.

There were some other positive signs of economic recovery in the U.S. during the second quarter of 2009, including a significant wave of single-family loan refinancing as mortgage interest rates dipped to near record lows in March and April. Approximately 87% of our single-family mortgage purchases were refinance loans during the second quarter of 2009 as compared to 66% during the second quarter of 2008.

Consolidated Results of Operations Second Quarter 2009

We adopted FSP FAS 115-2 and FAS 124-2 effective April 1, 2009. FSP FAS 115-2 and FAS 124-2 amends the recognition, measurement and presentation of other-than-temporary impairments of debt securities, and is intended to bring greater consistency to the timing of impairment recognition and provide greater clarity to investors about the credit and non-credit components of impaired debt securities that are not expected to be sold. This guidance changes (a) the method of determining whether an other-than-temporary impairment exists, and (b) the amount of an impairment charge to be recorded in earnings. See NOTE 4: INVESTMENTS IN SECURITIES to our consolidated financial statements for further disclosures regarding our investments in securities and other-than-temporary impairments.

Net income (loss) was $767 million and $(819) million for the second quarters of 2009 and 2008, respectively. Net income increased in the second quarter of 2009 compared to the second quarter of 2008, principally due to higher net interest income, derivative gains and fair value gains on trading securities, compared to these items during the second quarter of 2008. These income and gains for the second quarter of 2009 were partially offset by increased credit-related expenses, which consist of the provision for credit losses and REO operations expense, and increased losses on loans purchased, compared to the second quarter of 2008. Although we reported net income in the second quarter of 2009, the dividends on the senior preferred stock resulted in net loss attributable to common stockholders for the period.

Net interest income was $4.3 billion for the second quarter of 2009, compared to $1.5 billion for the second quarter of 2008. As compared to the second quarter of 2008, we held higher amounts of fixed-rate agency mortgage-related securities in our mortgage-related investments portfolio and had lower funding costs, due to significantly lower interest rates on our short- and long-term borrowings during the three months ended June 30, 2009.

Non-interest income was $3.2 billion for the three months ended June 30, 2009, compared to non-interest income of $56 million for the three months ended June 30, 2008. The increase in non-interest income in the second quarter of 2009 was primarily due to a decrease in losses on investment activity of $1.9 billion as well as increased gains on our guarantee asset of $0.7 billion and derivatives portfolio, excluding foreign-currency related effects, of $1.2 billion. The decrease in losses on investment activity during the second quarter of 2009 was principally attributed to fair value gains on mortgage-related securities classified as trading of $0.6 billion compared to fair value losses on trading securities of $2.3 billion during the second quarter of 2008. This was partially offset by higher impairment-related losses primarily recognized on available-for-sale non-agency mortgage-related securities backed by subprime, MTA Option ARM, Alt-A and other loans during the quarter, which increased to $2.2 billion in the second quarter of 2009, compared to $1.0 billion in the second quarter of 2008.

Non-interest expenses increased to $6.9 billion in the second quarter of 2009 from $3.4 billion in the second quarter of 2008 due to higher credit-related expenses and losses on loans purchased. Credit-related expenses totaled $5.2 billion and $2.8 billion for the second quarters of 2009 and 2008, respectively, and included our provision for

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credit losses of $5.2 billion and $2.5 billion, respectively. The increase in provision for credit losses was due to continued credit deterioration in our single-family mortgage portfolio, primarily from further increases in delinquency rates and higher loss severities on a per-property basis. During the second quarter of 2009, we enhanced our model for estimating credit losses on single-family loans. We estimate this change reduced our estimate of loan loss reserves, and consequently our provision for credit losses, by approximately $1.4 billion in the second quarter of 2009. See CONSOLIDATED RESULTS OF OPERATIONS Provision for Credit Losses for additional information on these changes to our loan loss reserve model. Losses on loans purchased increased to $1.2 billion for the second quarter of 2009, compared to $120 million for the second quarter of 2008, due to a higher volume of purchases of modified loans out of PCs during the second quarter of 2009. Administrative expenses totaled $383 million for the second quarter of 2009, down from $404 million for the second quarter of 2008, primarily due to a reduction in short-term compensation expenses and other cost reduction measures.

Segment Earnings

Our operations consist of three reportable segments, which are based on the type of business activities each performs Investments, Single-family Guarantee and Multifamily. Certain activities that are not part of a segment are included in the All Other category. We manage and evaluate performance of the segments and All Other using a Segment Earnings approach, subject to the conduct of our business under the direction of the Conservator. Segment Earnings differ significantly from, and should not be used as a substitute for, net income (loss) as determined in accordance with GAAP.

Table 1 presents Segment Earnings by segment and the All Other category and includes a reconciliation of Segment Earnings to net income (loss) prepared in accordance with GAAP.

Table 1 Reconciliation of Segment Earnings to GAAP Net Income (Loss)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Segment Earnings, net of taxes:				
Investments	$ 158	$ 793	$ (1,414)	$ 906
Single-family Guarantee	(3,552)	(1,388)	(9,037)	(1,846)
Multifamily	50	118	190	216
All Other	(8)	144	(8)	140
Reconciliation to GAAP net income (loss):				
Derivative- and foreign-currency denominated debt-related adjustments	2,800	527	4,358	(667)
Credit guarantee-related adjustments	2,354	1,818	956	1,644
Investment sales, debt retirements and fair value-related adjustments	900	(3,096)	928	(1,571)
Fully taxable-equivalent adjustments	(98)	(105)	(198)	(215)
Total pre-tax adjustments	5,956	(856)	6,044	(809)
Tax-related adjustments[1]	(1,836)	368	(4,858)	421

Total reconciling items, net of taxes	4,120	(488)	1,186	(388)
Net income (loss) attributable to Freddie Mac	$ 768	$ (821)	$ (9,083)	$ (972)

(1) Includes a non-cash charge, net related to the establishment of a partial valuation allowance against our deferred tax assets, net of approximately $(184) million and $2.9 billion that is not included in Segment Earnings for the three and six months ended June 30, 2009, respectively.

Segment Earnings is calculated for the segments by adjusting GAAP net income (loss) for certain investment-related activities and credit guarantee-related activities. Segment Earnings includes certain reclassifications among income and expense categories that have no impact on net income (loss) but provide us with a meaningful metric to assess the performance of each segment and our company as a whole. Segment Earnings does not include the effect of the establishment of the valuation allowance against our deferred tax assets, net. For more information on Segment Earnings, including the adjustments made to GAAP net income (loss) to calculate Segment Earnings and the limitations of Segment Earnings as a measure of our financial performance, see CONSOLIDATED RESULTS OF OPERATIONS Segment Earnings and NOTE 16: SEGMENT REPORTING to our consolidated financial statements.

Consolidated Balance Sheets Analysis

During the six months ended June 30, 2009, total assets increased by $41.3 billion to $892.3 billion while total liabilities increased by $2.5 billion to $884.1 billion. Total equity (deficit) was $8.2 billion at June 30, 2009 compared to $(30.6) billion at December 31, 2008. See below for the key drivers of these changes in our consolidated balance sheet as of June 30, 2009.

Our cash and other investments portfolio increased by $9.1 billion during the six months ended June 30, 2009 to $73.3 billion, primarily due to an $11.9 billion increase in non-mortgage-related trading securities. On June 30, 2009,

we received $6.1 billion from Treasury under the Purchase Agreement pursuant to a draw request that FHFA submitted to Treasury on our behalf to address the deficit in our net worth as of March 31, 2009. The unpaid principal balance of our mortgage-related investments portfolio increased 3%, or $25.1 billion, during the six months ended June 30, 2009 to $829.8 billion. The increase in our mortgage-related investments portfolio resulted from our acquiring and holding increased amounts of mortgage loans and mortgage-related securities to provide additional liquidity to the mortgage market, and, to a lesser degree, favorable investment opportunities for agency securities, primarily in the first quarter of 2009, as a result of continued lack of liquidity in the market. Deferred tax assets, net increased $1.5 billion during the six months ended June 30, 2009 to $16.9 billion, primarily attributable to the increase in the net loss in AOCI, net of taxes, as discussed below.

Short-term debt decreased by $91.0 billion during the six months ended June 30, 2009 to $344.1 billion, and long-term debt increased by $84.9 billion to $492.8 billion. As a result, our outstanding short-term debt, including the current portion of long-term debt, has decreased as a percentage of our total debt outstanding to 41% at June 30, 2009 from 52% at December 31, 2008. The increase in our long-term debt reflects the improvement during the first half of 2009 of spreads on our debt and our increased access to the debt markets primarily as a result of the Federal Reserve s purchases in the secondary market of our long-term debt under its purchase program. Additionally, our reserve for guarantee losses on PCs increased by $9.4 billion to $24.4 billion during the six months ended June 30, 2009 as a result of probable incurred losses, primarily attributable to the overall macroeconomic environment with declining home values, higher mortgage delinquency rates, and increasing unemployment.

Total equity (deficit) increased from $(30.6) billion at December 31, 2008 to $8.2 billion at June 30, 2009, reflecting the $36.9 billion we received from Treasury under the Purchase Agreement during the first six months of 2009 and a net increase in retained earnings (accumulated deficit) as a result of the adoption of FSP FAS 115-2 and FAS 124-2. Upon our adoption of this accounting guidance, we recognized a cumulative-effect adjustment of $15.0 billion to our opening balance of retained earnings (accumulated deficit) on April 1, 2009, and a corresponding adjustment of $(9.9) billion, net of tax, to AOCI. The cumulative effect adjustment reclassified the non-credit component of other-than-temporary impairments on our non-agency mortgage-related securities from retained earnings (accumulated deficit) (i.e., previously expensed) to AOCI. The difference between these adjustments of $5.1 billion represents an increase in total equity primarily resulting from the release of the valuation allowance previously recorded against the deferred tax asset that is no longer required related to the cumulative-effect adjustment. These increases in total equity (deficit) were partially offset by a $9.1 billion net loss and $1.5 billion of senior preferred stock dividends for the six months ended June 30, 2009. In addition, the net loss in AOCI, net of taxes, increased by $2.5 billion, resulting largely from the cumulative-effect adjustment of the adoption of FSP FAS 115-2 and FAS 124-2, partially offset by the unrealized gains on our agency mortgage-related securities and the recognition of other-than-temporary impairments in earnings related to our non-agency mortgage-related securities.

Consolidated Fair Value Results

During the three months ended June 30, 2009, the fair value of net assets, before capital transactions, increased by $5.4 billion compared to no change during the three months ended June 30, 2008. The fair value of net assets as of June 30, 2009 was $(70.5) billion, compared to $(80.9) billion as of March 31, 2009. Included in our fair value results for the three months ended June 30, 2009 are the $6.1 billion of funds received from Treasury on June 30, 2009 under the Purchase Agreement, partially offset by the $1.1 billion of dividends paid in cash to Treasury on our senior preferred stock. The increase in the fair value of our net assets, before capital transactions, during the second quarter of 2009 was principally related to an increase in the fair value of our mortgage-related investments portfolio, resulting from higher core spread income and net tightening of mortgage-to-debt OAS.

Liquidity and Capital Resources

Liquidity

Our access to the debt markets has improved since the height of the credit crisis in the fall of 2008. We attribute this improvement to the continued support of Treasury and the Federal Reserve. During the second quarter of 2009, the Federal Reserve continued to be an active purchaser in the secondary market of our long-term debt under its purchase program as discussed below and, as a result, spreads on our debt remained favorable. Debt spreads generally refer to the difference between the yields on our debt securities and the yields on a benchmark index or security, such as LIBOR or Treasury bonds of similar maturity. During the second quarter of 2009, we were able to increase our use of long-term and callable debt to fund our operations, and reduce our use of short-term debt. See MD&A LIQUIDITY AND CAPITAL RESOURCES Liquidity in our 2008 Annual Report for more information on our debt funding activities and risks posed by current market challenges and RISK FACTORS in our 2008 Annual Report for a discussion of the risks to our business posed by our reliance on the issuance of debt to fund our operations.

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Treasury and the Federal Reserve have taken a number of actions affecting our access to debt financing, including the following:

- Treasury entered into the Lending Agreement with us on September 18, 2008, under which we may request funds through December 31, 2009. As of June 30, 2009, we had not borrowed under the Lending Agreement. As such, use of the Lending Agreement has not been tested as a component of our liquidity contingency plan.

- The Federal Reserve has implemented a program to purchase, in the secondary market, up to $200 billion in direct obligations of Freddie Mac, Fannie Mae, and the FHLBs.

Our improved access to the unsecured debt markets may not continue upon completion or termination of the government actions noted above. Any reduction in government support for our debt funding program could adversely affect our ability to issue long-term debt. The Lending Agreement is scheduled to expire on December 31, 2009. Upon expiration of the Lending Agreement, we will not have a liquidity backstop available to us (other than Treasury s ability to purchase up to $2.25 billion of our obligations under its permanent authority) if we are unable to obtain funding from issuances of debt or other conventional sources. Absent an extension of the Lending Agreement, if backstop liquidity is needed after December 31, 2009, we will need to seek alternative sources for it. At present, we are not able to predict the likelihood that a liquidity backstop will be needed, or to identify the alternative sources that might then be available to us, other than draws from Treasury under the Purchase Agreement or its ability to purchase up to $2.25 billion of our obligations under its permanent authority.

Our annual dividend obligation on the senior preferred stock exceeds our annual historical earnings in most periods, and will result in increasingly negative cash flows in future periods, if we continue to pay the dividends in cash. In addition, the potential for continued deterioration in the housing market and future net losses in accordance with GAAP make it more likely that we will have additional draws under the Purchase Agreement in future periods, which will make it more difficult to pay senior preferred dividends in cash in the future.

Capital Adequacy

On October 9, 2008, FHFA announced that it was suspending capital classification of us during conservatorship in light of the Purchase Agreement.

The Purchase Agreement provides that, if FHFA, as Conservator, determines as of quarter end that our liabilities have exceeded our assets under GAAP, upon FHFA s request on our behalf, Treasury will contribute funds to us in an amount equal to the difference between such liabilities and assets, up to the maximum aggregate amount that may be funded under the Purchase Agreement. At June 30, 2009, our assets exceeded our liabilities by $8.2 billion. Because we had a positive net worth as of June 30, 2009, FHFA has not submitted a draw request on our behalf to Treasury for any additional funding under the Purchase Agreement. We received $6.1 billion on June 30, 2009 under the Purchase Agreement in accordance with the draw request submitted by FHFA on May 12, 2009 to address the deficit in our net worth as of March 31, 2009. The aggregate liquidation preference of the senior preferred stock is $51.7 billion and the amount remaining under the Treasury s funding agreement is $149.3 billion as of June 30, 2009.

Treasury is entitled to annual cash dividends of $5.2 billion based on the current amount of the aggregate liquidation preference of the senior preferred stock. To date, we have paid $1.7 billion in cash in senior preferred stock dividends under the Purchase Agreement. This dividend obligation, combined with potentially substantial commitment fees payable to Treasury starting in 2010 (the amounts of which must be determined by December 31, 2009) and limited flexibility to pay down draws under the Purchase Agreement, will have an adverse impact on our future financial position and net worth. In addition, we expect to make additional draws under the Purchase Agreement in future periods, due to a variety of factors that could materially affect the level and volatility of our net worth. For instance, if

the housing market conditions continue to deteriorate, increasing the possibility of our incurring GAAP net losses in the future, we will likely need to take additional draws, which would increase our senior preferred dividend obligation. For additional information concerning the potential impact of the Purchase Agreement, including taking additional draws, see RISK FACTORS in our 2008 Annual Report. For additional information on our capital management during conservatorship and factors that could affect the level and volatility of our net worth, see LIQUIDITY AND CAPITAL RESOURCES Capital Adequacy and NOTE 9: REGULATORY CAPITAL to our consolidated financial statements.

Risk Management

Credit Risks

Overview

Our total mortgage portfolio is subject primarily to two types of credit risk: mortgage credit risk and institutional credit risk. Mortgage credit risk is the risk that a borrower will fail to make timely payments on a mortgage we own or

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guarantee. We are exposed to mortgage credit risk on our total mortgage portfolio because we either hold the mortgage assets or have guaranteed mortgages in connection with the issuance of a PC, Structured Security or other mortgage-related guarantee. Institutional credit risk is the risk that a counterparty that has entered into a business contract or arrangement with us will fail to meet its obligations.

Mortgage and credit market conditions deteriorated significantly during 2008 and remained challenging in the first half of 2009. These conditions were brought about by a number of factors, which have increased our exposure to both mortgage credit and institutional credit risks. Factors that have negatively affected the mortgage and credit markets included:

- the effect of changes in other financial institutions underwriting standards in past years, which allowed for the origination of significant amounts of new higher-risk mortgage products in 2006 and 2007 and the early months of 2008. These mortgages have performed particularly poorly during the current housing and economic downturn, and have defaulted at historically high rates. However, even with the tightening of underwriting standards, economic conditions will continue to negatively impact recent originations;
- increases in unemployment;
- declines in home prices nationally and regionally during the last two years;
- higher incidence of institutional insolvencies;
- higher levels of mortgage foreclosures and delinquencies;
- significant volatility in interest rates;
- significantly lower levels of liquidity in institutional credit markets;
- wider credit spreads;
- rating agency downgrades of mortgage-related securities and financial institutions; and
- declines in market rents and increased vacancy rates affecting multifamily housing operators and investors.

The deteriorating economic conditions discussed above and uncertainty concerning the effect of current or any future government actions to remedy them have increased the uncertainty of future economic conditions, including unemployment rates and home price changes. While our assumption for home prices, based on our own index, continues to be for a decline during the second half of 2009, there continues to be divergence among economists about the future outlook and whether a sustained recovery in home prices may occur.

Single-Family Mortgage Portfolio

The following statistics illustrate the credit deterioration of loans in our single-family mortgage portfolio, which consists of single-family mortgage loans in our mortgage-related investments portfolio and those backing our PCs, Structured Securities and other mortgage-related guarantees.

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Table 2 Credit Statistics, Single-Family Mortgage Portfolio[1]

	As of				
	06/30/09	03/31/2009	12/31/2008	09/30/2008	06/30/2008
Delinquency rate[2]	2.78%	2.29%	1.72%	1.22%	0.93%
Non-performing assets, on balance sheet (in millions)	$ 14,981	$ 13,445	$ 11,241	$ 9,840	$ 9,220
Non-performing assets, off-balance sheet (in millions)[3]	$ 61,936	$ 49,881	$ 36,718	$ 25,657	$ 18,260
REO inventory (in units)	34,699	29,145	29,340	28,089	22,029

	For the Three Months Ended				
	06/30/09	03/31/2009	12/31/2008	09/30/2008	06/30/2008
	(in units, unless noted)				
Loan modifications[4]	15,603	24,623	17,695	8,456	4,687
REO acquisitions	21,997	13,988	12,296	15,880	12,410
REO disposition severity ratio[5]	39.8%	36.7%	32.8%	29.3%	25.2%
Single-family credit losses (in millions)[6]	$ 1,906	$ 1,318	$ 1,151	$ 1,270	$ 810

(1) See OUR PORTFOLIOS and GLOSSARY for information about our portfolios.

(2) Single-family delinquency rate information is based on the number of loans that are 90 days or more past due and those in the process of foreclosure, excluding Structured Transactions. Mortgage loans whose contractual terms have been modified under agreement with the borrower are not included if the borrower is less than 90 days delinquent under the modified terms. Delinquency rates for our single-family mortgage portfolio including Structured Transactions were 2.89% and 1.83% at June 30, 2009 and December 31, 2008, respectively.

(3) Consists of delinquent loans in our single-family mortgage portfolio which underlie our issued PCs and Structured Securities, based on unpaid principal balances that are past due for 90 days or more.

(4) The number of executed modifications under agreement with the borrower during the period. Excludes forbearance agreements, which are made in certain circumstances and under which reduced or no payments are required during a defined period, as well as repayment plans, which are separate agreements with the borrower to repay past due amounts and return to compliance with the original terms. Also excludes loans that entered the three-month trial period for the modification process under HAMP during the second quarter of 2009.

(5) Calculated as the aggregate amount of our losses recorded on disposition of REO properties during the respective quarterly period divided by the aggregate unpaid principal balances of the related loans with the borrowers. The amount of losses recognized on disposition of the properties is equal to the amount by which the unpaid principal balance of loans exceeds the amount of net sales proceeds from disposition of the properties. Excludes other related credit losses, such as property maintenance and costs, as well as related recoveries from credit enhancements, such as mortgage insurance.

(6) Consists of REO operations expense plus charge-offs, net of recoveries from third-party insurance and other credit enhancements. Excludes other market-based fair value losses, such as losses on loans purchased and other-than-temporary impairments of securities.

As the table above illustrates, we have experienced continued deterioration in the performance of our single-family mortgage portfolio due to several factors, including the following:

The expansion of the housing and economic downturn has reached a broader group of borrowers. The unemployment rate in the U.S. rose from 7.2% at December 31, 2008 to 9.5% as of June 30, 2009. In the first half of 2009 we experienced a significant increase in delinquency rate of fixed-rate amortizing loans, which represents a more traditional mortgage product. The delinquency rate for single-family 30-year fixed-rate amortizing loans increased to 2.76% at June 30, 2009 as compared to 2.25% at March 31, 2009 and 1.69% at December 31, 2008.

Certain loan groups within the single-family mortgage portfolio, such as Alt-A and interest-only loans, as well as 2006 and 2007 vintage loans, continue to be larger contributors to our worsening credit statistics than other, more traditional loan groups. These loans have been more affected by macroeconomic factors, such as declines in home prices, which have resulted in erosion in the borrower s equity. These loans are also concentrated in the West region. The West region comprised 27% of the unpaid principal balances of our single-family mortgage portfolio as of June 30, 2009, but accounted for 46% of our REO acquisitions in the first half of 2009, based on the related loan amount prior to our acquisition. In addition, states in the West region (especially California, Arizona and Nevada) and Florida tend to have higher average loan balances than the rest of the U.S. and were most affected by the steep home price declines during the last two years. California and Florida were the states with the highest credit losses in the first half of 2009, comprising 45% of our single-family credit losses on a combined basis.

Loss Mitigation

As discussed above, we have taken several steps during 2008 and continuing in 2009 designed to support homeowners and mitigate the growth of our non-performing assets. We continue to expand our efforts to increase our use of foreclosure alternatives, and have expanded our staff to assist our seller/servicers in completing loan modifications and other outreach programs with the objective of keeping more borrowers in their homes.

Currently, we are primarily focusing on initiatives that support the MHA Program. We also serve as the compliance agent under the MHA Program for certain foreclosure prevention activities, and we advise and consult with Treasury about the design, results and future improvement of the MHA Program.

Our more recent loss mitigation activities have created fluctuations in our credit statistics. For example, our temporary suspensions of foreclosure transfers of occupied homes temporarily reduced the rate of growth of our REO inventory and of charge-offs, a component of our credit losses, in certain periods since November 2008, but caused our

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reserve for guarantee losses to rise. This also has created an increase in the number of delinquent loans that remain in our single-family mortgage portfolio, which results in higher reported delinquency rates than without the suspension of foreclosure transfers. In addition, the implementation of HAMP in the second quarter of 2009 contributed to a temporary decrease in the number of loan modifications since there is a three month trial-period before these modifications become effective. It is not possible at present to estimate the extent to which the costs of this program, incurred in the near term, may be offset, if at all, by the prevention or reduction of potential future costs of loan defaults and foreclosures due to these changes in business practices.

Investments in Non-Agency Mortgage-Related Securities

Our investments in non-agency mortgage-related securities also were affected by the deteriorating credit conditions in 2008 and continuing into the first half of 2009. The table below illustrates the increases in delinquency rates for subprime first lien, MTA Option ARM and Alt-A loans that back $105.1 billion of the $186.2 billion of non-agency mortgage-related securities in our mortgage-related investments portfolio as of June 30, 2009. Given the forecast for home price declines in the remainder of 2009, the performance of the loans backing these securities could continue to deteriorate.

Table 3 Credit Statistics, Non-Agency Mortgage-Related Securities Backed by Subprime, MTA Option ARM and Alt-A Loans

	As of				
	06/30/2009	**03/31/2009**	**12/31/2008**	**09/30/2008**	**06/30/2008**
Delinquency rates:[1]					
Non-agency mortgage-related securities backed by:					
Subprime first lien	44%	42%	38%	35%	31%
MTA Option ARM	40	36	30	24	18
Alt-A[2]	22	20	17	14	12
Cumulative collateral loss:[3]					
Non-agency mortgage-related securities backed by:					
Subprime first lien	10%	7%	6%	4%	2%
MTA Option ARM	4	2	1	1	
Alt-A[2]	3	2	1	1	
Gross unrealized losses, pre-tax (in millions)[4][5]	$ 41,157	$ 27,475	$ 30,671	$ 22,411	$ 25,858
Total other-than-temporary impairment of available-for-sale securities[5]	$ 10,380	$ 6,956	$ 6,794	$ 8,856	$ 826
Portion of other-than-temporary impairment recognized in AOCI[5]	8,223				
Net impairment of available-for-sale securities recognized in earnings for the three months ended (in millions)[5]	$ 2,157	$ 6,956	$ 6,794	$ 8,856	$ 826

(1) Based on the number of loans that are 60 days or more past due. Mortgage loans whose contractual terms have been modified under agreement with the borrower are not included if the borrower is less than 60 days delinquent

under the modified terms.

(2) Excludes non-agency mortgage-related securities backed by other loans primarily comprised of securities backed by home equity lines of credit.

(3) Based on the actual losses incurred on the collateral underlying these securities. Actual losses incurred on the securities that we hold are less than the losses on the underlying collateral as presented in this table, as a majority of the securities we hold include significant credit enhancements, particularly through subordination.

(4) Gross unrealized losses, pre-tax, represent the aggregate of the amount by which amortized cost exceeds fair value measured at the individual lot level.

(5) Includes mortgage-related securities backed by subprime, MTA Option ARM, Alt-A and other loans. Upon the adoption of FSP FAS 115-2 and FAS 124-2 on April 1, 2009, the amount of other-than-temporary impairment related to intent to sell or where it is more likely than not that we will be required to sell and credit losses is recognized in our consolidated statements of operations as net impairment on available-for-sale securities recognized in earnings. The amount of other-than-temporary impairment related to all other factors is recognized in AOCI. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Change in Accounting Principles *Additional Guidance and Disclosures for Fair Value Measurements and Change in the Impairment Model for Debt Securities* *Change in the Impairment Model for Debt Securities* to our consolidated financial statements.

We held unpaid principal balances of $109.5 billion of non-agency mortgage-related securities backed by subprime, MTA Option ARM, Alt-A and other loans in our mortgage-related investments portfolio as of June 30, 2009, compared to $119.5 billion as of December 31, 2008. This decrease is due to the monthly remittances of principal repayments we received on these securities of $4.9 billion and $10.0 billion during the three and six months ended June 30, 2009, respectively, representing a partial return of our investment in these securities. We have recorded net impairment of available-for-sale securities recognized in earnings on non-agency mortgage-related securities backed by subprime, MTA Option ARM, Alt-A and other loans of approximately $2.2 billion and $9.1 billion for the three and six months ended June 30, 2009, respectively. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Change in Accounting Principles *Additional Guidance and Disclosures for Fair Value Measurements and Change in the Impairment Model for Debt Securities* *Change in the Impairment Model for Debt Securities* to our consolidated financial statements for information on how other-than-temporary impairments are recorded on our financial statements commencing in the second quarter of 2009. Gross unrealized losses, pre-tax, on securities backed by subprime, MTA Option ARM, Alt-A and other loans reflected in AOCI increased during the first half of 2009 by $10.4 billion to $41.2 billion at June 30, 2009. This increase in unrealized losses includes $15.3 billion, pre-tax,

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($9.9 billion, net of tax) of other-than-temporary impairment losses reversed as a result of the second quarter 2009 adoption of FSP FAS 115-2 and FAS 124-2. These losses more than offset the unrealized gains in our non-agency mortgage-related securities that occurred during the first half of 2009.

Interest Rate and Other Market Risks

Our mortgage-related investments portfolio activities expose us to interest rate risk and other market risks arising primarily from the uncertainty as to when borrowers will pay the outstanding principal balance of mortgage loans that we hold or underlie securities in our mortgage-related investments portfolio, known as prepayment risk, and the resulting potential mismatch in the timing of our receipt of cash flows related to our assets versus the timing of payment of cash flows related to our liabilities. As interest rates fluctuate, we use derivatives to adjust the interest rate characteristics of our debt funding in order to more closely match those of our assets.

The recent market environment has been increasingly volatile. Throughout 2008 and into 2009, we adjusted our interest rate risk models to reflect rapidly changing market conditions. In particular, prepayment models were adjusted during the first half of 2009 to more accurately reflect prepayment expectations under our implementation of the MHA Program as well as refinancing expectations in the current interest rate environment. During the second quarter of 2009, we purchased put swaptions to replace maturing positions in order to partially hedge our exposure to increasing negative convexity.

Operational Risks

Operational risks are inherent in all of our business activities and can become apparent in various ways, including accounting or operational errors, business interruptions, fraud, failures of the technology used to support our business activities, difficulty in filling executive officer and key business unit vacancies and other operational challenges from failed or inadequate internal controls. These operational risks may expose us to financial loss, interfere with our ability to sustain timely financial reporting, or result in other adverse consequences. Management of our operational risks takes place through the enterprise risk management framework, with the business areas retaining primary responsibility for identifying, assessing and reporting their operational risks.

As a result of management s evaluation of our disclosure controls and procedures, our Interim Chief Executive Officer, who is also performing the functions of principal financial officer on an interim basis, has concluded that our disclosure controls and procedures were not effective as of June 30, 2009, at a reasonable level of assurance. We continue to work to improve our financial reporting governance process and remediate material weaknesses and other deficiencies in our internal controls. While we are making progress on our remediation plans, our material weaknesses have not been fully remediated at this time. In view of our mitigating activities, including our remediation efforts through June 30, 2009, we believe that our interim consolidated financial statements for the quarter ended June 30, 2009, have been prepared in conformity with GAAP.

We face significant operational risks related to the process and systems changes we will be required to implement as a result of the FASB s issuance of SFAS 166 and SFAS 167 (which will be effective as of January 1, 2010), including that it may be difficult for us to complete the changes in time to ensure we prepare timely financial reports in a controlled manner. These new accounting standards require us to consolidate our PC trusts in our financial statements, which could have a significant impact on our net worth.

Off-Balance Sheet Arrangements

We enter into certain business arrangements that are not recorded on our consolidated balance sheets or may be recorded in amounts that differ from the full contract or notional amount of the transaction. Most of these

arrangements relate to our financial guarantee and securitization activity for which we record guarantee assets and obligations, but the related securitized assets are owned by third parties. These off-balance sheet arrangements may expose us to potential losses in excess of the amounts recorded on our consolidated balance sheets.

Our maximum potential off-balance sheet exposure to credit losses relating to our PCs, Structured Securities and other mortgage-related guarantees is primarily represented by the unpaid principal balance of the related loans and securities held by third parties, which was $1,411 billion and $1,403 billion at June 30, 2009 and December 31, 2008, respectively. Based on our historical credit losses, which in the first half of 2009 averaged approximately 34 basis points of the aggregate unpaid principal balance of our PCs and Structured Securities, we do not believe that the maximum exposure is representative of our actual exposure on these guarantees.

Legislative and Regulatory Matters

Legislation

On May 20, 2009, President Obama signed into law the Helping Families Save Their Homes Act of 2009, which, among other things, provides a safe harbor from liability for servicers engaging in certain loss mitigation activities,

requires borrowers to be notified when their mortgage loans are sold or transferred. The Protecting Tenants at Foreclosure Act, enacted as part of the Helping Families Save Their Homes Act, provides certain foreclosure protections for tenants by also requiring immediate successors in interest of foreclosed properties to give bona fide, non-owners at least 90 days advance notice before they are evicted from the premises. Freddie Mac is prohibited from evicting a bona fide tenant who was occupying the foreclosure property at the time of the sale before the expiration of a written lease agreement. We currently do not expect the impact of these provisions of the Act on us to be significant, because they are similar to our existing leasing policy.

On May 20, 2009, President Obama also signed into law the Fraud Enforcement and Recovery Act of 2009, which establishes a commission designated to examine the causes of the current financial crises, including the role of Freddie Mac and Fannie Mae. The commission is composed of ten members appointed by the House and Senate majority and minority leaders.

Pending and Proposed Legislation and Related Matters

On March 5, 2009, the House of Representatives passed a bill that, among other items, includes a provision allowing bankruptcy judges to modify the terms of mortgages on principal residences for borrowers in Chapter 13 bankruptcy. Specifically, the House bill would allow bankruptcy judges to adjust interest rates, extend repayment terms and lower the outstanding principal amount to the current estimated fair value of the underlying property. On May 6, 2009, the Senate passed a similar housing-related bill that did not include provisions allowing bankruptcy judges to modify the terms of mortgages. It is unclear when, or if, the Senate will reconsider other alternative bankruptcy-related legislation. If enacted, this legislation could cause the volume of bankruptcy filings to rise, potentially increasing charge-offs for mortgages in our single-family mortgage portfolio and increasing our losses on loans purchased, which are recognized on our consolidated statements of operations.

On May 7, 2009, the House of Representatives passed a bill that, among other things, would require originators to retain a level of credit risk for certain mortgages that they sell, enhance consumer disclosures, impose new servicing standards, allow for assignee liability and require lenders to determine that a borrower has a reasonable ability to repay home loans. If enacted, the legislation would impact Freddie Mac and the overall residential mortgage market. However, it is unclear when, or if, the Senate will consider comparable legislation.

On June 17, 2009, the Obama Administration announced a plan to overhaul the regulatory structure of the financial services industry. While the plan does not contain specific recommendations regarding the GSEs, many recommendations in the plan will, if implemented, cause significant changes in the regulation of the financial services industry. We cannot predict the impact of these potential changes on our business and operations. In addition, under the plan, Treasury and HUD are expected to develop recommendations for the future of the GSEs, in consultation with other government agencies, and will report to Congress on such recommendations at the time of the President s 2011 budget, which is currently targeted for February 2010.

On June 26, 2009, the House of Representatives passed comprehensive energy legislation that would, among other things, require FHFA to provide Freddie Mac and Fannie Mae with extra affordable housing goals credit for purchases of certain energy-efficient and location-efficient mortgages. The legislation would also create a new duty to serve underserved markets for energy-efficient and location-efficient mortgages. It is currently unclear when, or if, the Senate will consider comparable legislation.

On July 16, 2009, the House of Representatives passed the appropriations bill for financial services and general government for fiscal year 2010. The House Committee on Appropriations report accompanying the bill directs Treasury to report to Congress on its plans to ensure that taxpayers receive repayment of their investment in Freddie Mac and Fannie Mae, as well as companies that received funds from the Troubled Asset Relief Program and other

companies receiving taxpayer funds.

On July 23, 2009, the House of Representatives passed the appropriations bill for HUD for fiscal year 2010. The bill includes a provision that would extend the temporary high-cost conforming loan limits through September 2010.

The House of Representatives has passed several bills that would impact executive and employee compensation paid by companies receiving federal financial assistance, including Freddie Mac. One bill would impose a 90% tax on the aggregate bonuses received by certain executives and employees of such companies. Another bill would prohibit unreasonable and excessive compensation by certain companies that have received federal financial assistance and would prohibit these companies from paying non-performance based bonuses. Under this bill, Treasury would be required to establish certain standards regarding compensation payments. It is unclear when, or if, the Senate will consider comparable legislation. The adoption of any legislation that results in a significant tax on compensation or that imposes significant compensation restrictions would likely have an adverse impact on Freddie Mac s ability to

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recruit and retain executives and employees whose compensation would be limited or reduced as a result of such legislation.

On July 31, 2009, the House of Representatives passed a bill that would require certain publicly traded companies to hold non-binding shareholder votes on executive compensation; would require certain publicly traded companies to take steps to ensure that their compensation committees are independent; would require specified financial institutions, including Freddie Mac, to disclose certain compensation structures to regulators; and would permit federal regulators to prohibit specified financial institutions, including Freddie Mac, from using certain types of compensation structures that the regulators determine encourage inappropriate risks.

Proposed and Interim Final Regulations

On June 5, 2009, FHFA published proposed executive compensation rules. The proposed rules, which would replace FHFA s current executive compensation regulations, would establish procedural requirements and processes related to the compensation of executive officers at Freddie Mac, Fannie Mae, the FHLBs and the Office of Finance of the FHLBs and would implement certain compensation oversight authorities established by the Reform Act.

On June 17, 2009, FHFA published a proposed rule that would require Freddie Mac, Fannie Mae and the FHLBs to report to FHFA any fraud or possible fraud relating to any loans or other financial instruments that the entity has purchased or sold. The proposed rule would implement the Reform Act s fraud reporting provisions and would replace the existing mortgage fraud regulation.

On June 29, 2009, FHFA published proposed rules that would set forth standards for permissible and prohibited golden parachute payments and indemnification payments to entity-affiliated parties by Freddie Mac, Fannie Mae, the FHLBs and the Office of Finance of the FHLBs. The proposed rules would implement FHFA s statutory authority to regulate or prohibit golden parachute and indemnification payments, and would specify requirements that are closely related to the limitations that already exist for insured depository institutions under comparable banking regulations.

On July 2, 2009, FHFA published an interim final rule on prior approval of new products, implementing the new product provisions for Freddie Mac and Fannie Mae in the Reform Act. The rule establishes a process for Freddie Mac and Fannie Mae to provide prior notice to the Director of FHFA of a new activity and, if applicable, to obtain prior approval from the Director if the new activity is determined to be a new product. Under the rule, if the Director determines that a new activity of Freddie Mac is a new product, a description of the new product must be published for public comment, after which the Director will approve the new product if the Director determines that the new product is: (a) authorized by our charter; (b) in the public interest; and (c) consistent with the safety and soundness of Freddie Mac and the mortgage finance and financial system. We cannot currently predict the impact that the interim final rule will have on our business, financial position or results of operations.

Regulation Z

In July 2008, the Federal Reserve published a final rule amending Regulation Z (which implements the Truth in Lending Act). According to the Federal Reserve, one of the goals of the amendments is to protect consumers in the mortgage market from unfair, abusive, or deceptive lending and servicing practices while preserving responsible lending and sustainable homeownership. Most of the provisions of the final rule are effective on October 1, 2009. On July 23, 2009, the Federal Reserve proposed amendments to Regulation Z intended to improve the disclosures consumers receive in connection with certain mortgages and home-equity lines of credit. For more information, see RISK MANAGEMENT Credit Risks *Mortgage Credit Risk* *Underwriting Standards and Quality Control Process*.

State Actions

Several states have enacted laws that permit localities to impose new assessments to allow homeowners to finance energy efficient home improvements. The assessments are generally treated like property tax assessments and may result in the creation of a new lien that is senior to Freddie Mac s lien. The ultimate impact of these new laws is currently unclear.

Various state and local governments have been taking actions that could delay or otherwise change their foreclosure processes. These actions could increase our expenses, including by potentially delaying the final resolution of delinquent mortgage loans and the disposition of non-performing assets. For example:

During the period from July 5, 2009 to July 5, 2011, the state of Michigan is temporarily restricting servicers from executing foreclosure acquisitions for a 90-day period, from the date default notices are mailed to

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homeowners, to allow servicers the opportunity to pursue loan modifications and other workout options with homeowners as alternatives to foreclosure.

During the 90-day period commencing on June 1, 2009, the state of California is temporarily restricting loan servicers from executing foreclosure acquisitions unless they have an established modification program meeting certain criteria. We have not been significantly impacted by this restriction since we pursue modifications and other foreclosure alternatives with eligible borrowers before executing our foreclosure acquisitions.

Affordable Housing Goals

Under the Reform Act, the annual housing goals for Freddie Mac and Fannie Mae in place for 2008 remain in effect for 2009, except that within 270 days from July 30, 2008, FHFA must review the 2009 housing goals to determine the feasibility of such goals in light of current market conditions and, after seeking public comment for up to 30 days, FHFA may make adjustments to the 2009 goals consistent with market conditions.

On July 28, 2009, FHFA issued a final rule that adjusts the affordable housing goals and home purchase subgoals for 2009 to the levels set forth in Table 4 below. Except for the multifamily special affordable volume target, FHFA decreased all of the goals and subgoals, as compared to those in effect for 2008.

Table 4 Housing Goals and Home Purchase Subgoals for 2009(1)

	Housing Goals
Low- and moderate-income goal	43%
Underserved areas goal	32
Special affordable goal	18
Multifamily special affordable volume target (in billions)	$ 4.60

	Home Purchase Subgoals
Low- and moderate-income subgoal	40%
Underserved areas subgoal	30
Special affordable subgoal	14

(1) An individual mortgage may qualify for more than one of the goals or subgoals. Each of the goal and subgoal percentages will be determined independently and cannot be aggregated to determine a percentage of total purchases that qualifies for these goals or subgoals.

The rule permits loans we own or guarantee that are modified in accordance with the MHA Program to be treated as mortgage purchases and count toward the housing goals. In addition, the rule excludes from the 2009 housing goals loans with original principal balances that exceed the base nationwide conforming loan limits (*e.g.*, $417,000 for a one-unit single-family property) in certain high-cost areas and exceed 150% of the nationwide conforming loan limits in Alaska, Guam, Hawaii and the Virgin Islands, which we refer to as super-conforming mortgages.

We expect that market conditions and the tightened credit and underwriting environment will make achieving our affordable housing goals and subgoals for 2009 challenging.

Effective beginning calendar year 2010, the Reform Act requires that FHFA establish, by regulation, four single-family housing goals and one multifamily special affordable housing goal. In addition, the Reform Act establishes a duty for Freddie Mac and Fannie Mae to serve three underserved markets, manufactured housing, affordable housing preservation and rural areas, by developing loan products and flexible underwriting guidelines to facilitate a secondary market for mortgages for very low-, low-and moderate-income families in those markets. Effective for 2010, FHFA is required to establish a manner for annually: (1) evaluating whether and to what extent Freddie Mac and Fannie Mae have complied with the duty to serve underserved markets; and (2) rating the extent of compliance.

New York Stock Exchange Matters

On November 17, 2008, we received a notice from the NYSE that we had failed to satisfy one of the NYSE s standards for continued listing of our common stock. Specifically, the NYSE advised us that we were below criteria for the NYSE s price criteria for common stock because the average closing price of our common stock over a consecutive 30 trading-day period was less than $1 per share. On December 2, 2008, we advised the NYSE of our intent to cure this deficiency, and that we may undertake a reverse stock split in order to do so.

On February 26, 2009, the NYSE suspended the application of its minimum price listing standard until June 30, 2009 (subsequently extended until July 31, 2009). The suspension period expired on July 31, 2009, and we have not regained compliance with the minimum price standard. Under applicable NYSE rules, we now have until October 20, 2009 to bring our share price and our average share price for the 30 consecutive trading days preceding October 20, 2009, above $1. If we fail to do so, NYSE rules provide that the NYSE will initiate suspension and delisting procedures.

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The delisting of our common stock would likely also result in the delisting of our NYSE-listed preferred stock. The delisting of our common stock or NYSE-listed preferred stock would require any trading in these securities to occur in the over-the-counter market and could adversely affect the market prices, trading volume and liquidity of the markets for these securities. As a result, it could be more difficult for our shareholders to sell their shares, especially at prices comparable to those in effect prior to delisting. We will work with our Conservator to determine the specific action or actions that may be taken to cure the deficiency, but there is no assurance that any such actions will be taken or that any actions taken will be successful. The average share price of our common stock for the 30 consecutive trading days ended as of the filing of this Form 10-Q was less than $1 per share.

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SELECTED FINANCIAL DATA[1]

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(dollars in millions, except share related amounts)			
Statement of Operations Data				
Net interest income	$ 4,255	$ 1,529	$ 8,114	$ 2,327
Non-interest income	3,215	56	127	670
Non-interest expense	(6,887)	(3,434)	(18,446)	(5,417)
Net income (loss) attributable to Freddie Mac	768	(821)	(9,083)	(972)
Net loss attributable to common stockholders	(374)	(1,053)	(10,603)	(1,476)
Loss per common share:				
Basic	$ (0.11)	$ (1.63)	$ (3.26)	$ (2.28)
Diluted	$ (0.11)	$ (1.63)	$ (3.26)	$ (2.28)
Weighted average common shares outstanding (in thousands):[2]				
Basic	3,253,716	646,868	3,254,815	646,603
Diluted	3,253,716	646,868	3,254,815	646,603
Dividends per common share	$	$ 0.25	$	$ 0.50

	June 30, 2009	December 31, 2008
	(dollars in millions)	
Balance Sheet Data		
Total assets	$ 892,290	$ 850,963
Short-term debt	344,135	435,114
Long-term senior debt	488,329	403,402
Long-term subordinated debt	4,514	4,505
All other liabilities	47,080	38,576
Total equity (deficit)	8,232	(30,634)
Portfolio Balances		
Mortgage-related investments portfolio[3]	829,837	804,762
Total PCs and Structured Securities issued[4]	1,851,124	1,827,238
Total mortgage portfolio	2,240,483	2,207,476
Non-performing assets	77,519	48,385

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008

Ratios[5]				
Return on average assets[6]	0.3%	(0.4)%	(2.1)%	(0.2)%
Non-performing assets ratio[7]	3.9	1.5	3.9	1.5
Equity to assets ratio[8]	0.1	1.7	(1.3)	2.4
Preferred stock to core capital ratio[9]	N/A	38.0	N/A	38.0

(1) See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Change in Accounting Principles to our consolidated financial statements for information regarding accounting changes impacting the current period. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Recently Adopted Accounting Standards in our 2008 Annual Report for information regarding accounting changes impacting previously reported results.

(2) For the three and six months ended June 30, 2009, includes the weighted average number of shares that are associated with the warrant for our common stock issued to Treasury as part of the Purchase Agreement. This warrant is included in basic loss per share for the second quarter of 2009, because it is unconditionally exercisable by the holder at a cost of $.00001 per share.

(3) The mortgage-related investments portfolio presented on our consolidated balance sheets differs from the mortgage-related investments portfolio in this table because the consolidated balance sheet amounts include valuation adjustments, discounts, premiums and other deferred balances. See CONSOLIDATED BALANCE SHEETS ANALYSIS Table 19 Characteristics of Mortgage Loans and Mortgage-Related Securities in our Mortgage-Related Investments Portfolio for more information.

(4) Includes PCs and Structured Securities that are held in our mortgage-related investments portfolio. See OUR PORTFOLIOS Table 54 Freddie Mac s Total Mortgage Portfolio and Segment Portfolio Composition for the composition of our total mortgage portfolio. Excludes Structured Securities for which we have resecuritized our PCs and Structured Securities. These resecuritized securities do not increase our credit-related exposure and consist of single-class Structured Securities backed by PCs, REMICs, and principal-only strips. The notional balances of interest-only strips are excluded because this line item is based on unpaid principal balance. Includes other guarantees issued that are not in the form of a PC, such as long-term standby commitments and credit enhancements for multifamily housing revenue bonds.

(5) The return on common equity ratio is not presented because total Freddie Mac stockholders equity (deficit) is less than zero for all periods presented. The dividend payout ratio on common stock is not presented because we are reporting a net loss attributable to common stockholders for all periods presented.

(6) Ratio computed as annualized net income (loss) attributable to Freddie Mac divided by the simple average of the beginning and ending balances of total assets.

(7) Ratio computed as non-performing assets divided by the ending unpaid principal balances of our total mortgage portfolio, excluding non-Freddie Mac securities.

(8) Ratio computed as the simple average of the beginning and ending balances of Total Freddie Mac stockholders equity (deficit) divided by the simple average of the beginning and ending balances of total assets.

(9) Ratio computed as preferred stock (excluding senior preferred stock), at redemption value divided by core capital. Senior preferred stock does not meet the statutory definition of core capital. Ratio is not computed for periods in which core capital is less than zero. See NOTE 9: REGULATORY CAPITAL to our consolidated financial statements for more information regarding core capital.

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CONSOLIDATED RESULTS OF OPERATIONS

The following discussion of our consolidated results of operations should be read in conjunction with our consolidated financial statements including the accompanying notes. Also see CRITICAL ACCOUNTING POLICIES AND ESTIMATES for more information concerning our more significant accounting policies and estimates applied in determining our reported financial position and results of operations.

Table 5 Summary Consolidated Statements of Operations GAAP Results

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Net interest income	$ 4,255	$ 1,529	$ 8,114	$ 2,327
Non-interest income:				
Management and guarantee income	710	757	1,490	1,546
Gains (losses) on guarantee asset	1,817	1,114	1,661	(280)
Income on guarantee obligation	961	769	1,871	1,938
Derivative gains (losses)	2,361	115	2,542	(130)
Gains (losses) on investments:				
Impairment-related[(1)]:				
Total other-than-temporary impairment of available-for-sale securities	(10,473)	(1,040)	(17,603)	(1,111)
Portion of other-than-temporary impairment recognized in AOCI	8,260		8,260	
Net impairment of available-for-sale securities recognized in earnings	(2,213)	(1,040)	(9,343)	(1,111)
Other gains (losses) on investments	797	(2,287)	2,983	(997)
Total gains (losses) on investments	(1,416)	(3,327)	(6,360)	(2,108)
Gains (losses) on debt recorded at fair value	(797)	569	(330)	(816)
Gains (losses) on debt retirement	(156)	(29)	(260)	276
Recoveries on loans impaired upon purchase	70	121	120	347
Low-income housing tax credit partnerships	(167)	(108)	(273)	(225)
Trust management income (expense)	(238)	(19)	(445)	(16)
Other income	70	94	111	138
Non-interest income	3,215	56	127	670
Non-interest expense:				
Administrative expense	(383)	(404)	(755)	(801)
Provision for credit losses	(5,199)	(2,537)	(13,990)	(3,777)
REO operations expense	(9)	(265)	(315)	(473)

Other	(1,296)	(228)	(3,386)	(366)
Non-interest expense	(6,887)	(3,434)	(18,446)	(5,417)
Income (loss) before income tax benefit	583	(1,849)	(10,205)	(2,420)
Income tax benefit	184	1,030	1,121	1,452
Net income (loss)	$ 767	$ (819)	$ (9,084)	$ (968)
Less: Net (income) loss attributable to noncontrolling interest	1	(2)	1	(4)
Net income (loss) attributable to Freddie Mac	$ 768	$ (821)	$ (9,083)	$ (972)

(1) We adopted FSP FAS 115-2 and FAS 124-2 effective April 1, 2009. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Change in Accounting Principles to our consolidated financial statements for further information.

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Net Interest Income

Table 6 presents an analysis of net interest income, including average balances and related yields earned on assets and incurred on liabilities.

Table 6 Net Interest Income/Yield and Average Balance Analysis

	Three Months Ended June 30,					
	2009			2008		
	Average Balance[1][2]	Interest Income (Expense)[1]	Average Rate	Average Balance[1][2]	Interest Income (Expense)[1]	Average Rate
	(dollars in millions)					
Interest-earning assets:						
Mortgage loans[3]	$ 127,863	$ 1,721	5.38%	$ 89,813	$ 1,320	5.88%
Mortgage-related securities[4]	702,693	8,235	4.69	664,727	8,380	5.04
Total mortgage-related investments portfolio	830,556	9,956	4.79	754,540	9,700	5.14
Non-mortgage-related securities[4]	16,594	288	6.96	26,935	223	3.31
Cash and cash equivalents	57,401	62	0.42	27,126	178	2.60
Federal funds sold and securities purchased under agreements to resell	29,542	13	0.17	20,660	119	2.29
Total interest-earning assets	934,093	10,319	4.42	829,261	10,220	4.93
Interest-bearing liabilities:						
Short-term debt	293,475	(571)	(0.77)	240,119	(1,637)	(2.70)
Long-term debt[5]	582,998	(5,211)	(3.57)	569,443	(6,711)	(4.71)
Total interest-bearing liabilities	876,473	(5,782)	(2.63)	809,562	(8,348)	(4.11)
Expense related to derivatives[6]		(282)	(0.13)		(343)	(0.17)
Impact of net non-interest-bearing funding	57,620		0.17	19,699		0.10
Total funding of interest-earning assets	$ 934,093	(6,064)	(2.59)	$ 829,261	(8,691)	(4.18)
Net interest income/yield		4,255	1.83		1,529	0.75
Fully taxable-equivalent adjustments[7]		99	0.04		105	0.05
Net interest income/yield (fully taxable-equivalent basis)		$ 4,354	1.87		$ 1,634	0.80

	Six Months Ended June 30,					
	2009			2008		
	Average Balance[1][2]	Interest Income (Expense)[1]	Average Rate	Average Balance[1][2]	Interest Income (Expense)[1]	Average Rate
	(dollars in millions)					
Interest-earning assets:						
Mortgage loans[3]	$ 123,209	$ 3,301	5.36%	$ 87,052	$ 2,563	5.89%
Mortgage-related securities[4]	700,578	16,995	4.85	646,724	16,513	5.11
Total mortgage-related investments portfolio	823,787	20,296	4.93	733,776	19,076	5.20
Non-mortgage-related securities[4]	13,896	499	7.19	28,750	536	3.73
Cash and cash equivalents	53,666	138	0.51	18,008	266	2.92
Federal funds sold and securities purchased under agreements to resell	31,574	31	0.20	17,548	238	2.71
Total interest-earning assets	922,923	20,964	4.54	798,082	20,116	5.04
Interest-bearing liabilities:						
Short-term debt	328,020	(1,693)	(1.03)	222,385	(3,681)	(3.27)
Long-term debt[5]	552,075	(10,575)	(3.83)	553,869	(13,436)	(4.85)
Total interest-bearing liabilities	880,095	(12,268)	(2.79)	776,254	(17,117)	(4.40)
Expense related to derivatives[6]		(582)	(0.13)		(672)	(0.17)
Impact of net non-interest-bearing funding	42,828		0.14	21,828		0.13
Total funding of interest-earning assets	$ 922,923	(12,850)	(2.78)	$ 798,082	(17,789)	(4.44)
Net interest income/yield		8,114	1.76		2,327	0.60
Fully taxable-equivalent adjustments[7]		201	0.04		212	0.05
Net interest income/yield (fully taxable-equivalent basis)		$ 8,315	1.80		$ 2,539	0.65

(1) Excludes mortgage loans and mortgage-related securities traded, but not yet settled.
(2) For securities, we calculated average balances based on their unpaid principal balance plus their associated deferred fees and costs (*e.g.*, premiums and discounts), but excluded the effect of mark-to-fair-value changes.
(3) Non-performing loans, where interest income is recognized when collected, are included in average balances.
(4) Interest income (expense) includes the portion of impairment charges recognized in earnings expected to be recovered.
(5) Includes current portion of long-term debt.
(6) Represents changes in fair value of derivatives in cash flow hedge relationships that were previously deferred in AOCI and have been reclassified to earnings as the associated hedged forecasted issuance of debt and mortgage purchase transactions affect earnings. 2008 also includes the accrual of periodic cash settlements of all derivatives in qualifying hedge accounting relationships.
(7)

The determination of net interest income/yield (fully taxable-equivalent basis), which reflects fully taxable-equivalent adjustments to interest income, involves the conversion of tax-exempt sources of interest income to the equivalent amounts of interest income that would be necessary to derive the same net return if the investments had been subject to income taxes using our federal statutory tax rate of 35%.

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Net interest income and net interest yield on a fully taxable-equivalent basis increased during the three and six months ended June 30, 2009 compared to the three and six months ended June 30, 2008 primarily due to: (a) a decrease in funding costs as a result of the replacement of higher cost short- and long-term debt with new lower cost debt; (b) a significant increase in the average size of our mortgage-related investments portfolio, including an increase in our holdings of fixed-rate assets; and (c) $968 million of income, primarily recognized in the three months ended March 31, 2009, related to the accretion of other-than temporary impairments of investments in available-for-sale securities recorded primarily during the second half of 2008. Upon our adoption of FSP FAS 115-2 and FAS 124-2 on April 1, 2009, previously recognized non-credit related other-than-temporary impairments were reclassified from retained earnings to AOCI and these amounts are no longer accreted into net interest income. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES to our consolidated financial statements for a discussion of the impact of these accounting changes.

During the three and six months ended June 30, 2009, both our floating-rate long-term and our short-term debt funding average balances increased significantly when compared to the three and six months ended June 30, 2008. Our use of floating-rate long-term debt funding and short-term debt funding has been driven by varying levels of demand for our long-term and callable debt in the worldwide financial markets commencing in the second half of 2008. During the first half of 2009, the Federal Reserve was an active purchaser in the secondary market of our long-term debt under its purchase program and, as a result, spreads on our debt and access to the debt markets improved. Due to our limited ability to issue long-term and callable debt during the second half of 2008 and the first few months of 2009, we increased our use of the strategy of combining derivatives and floating-rate long-term debt or short-term debt to synthetically create the substantive economic equivalent of various longer-term fixed rate debt funding structures. See Non-Interest Income (Loss) *Derivative Overview* for additional information. As discussed in LIQUIDITY AND CAPITAL RESOURCES Liquidity *Debt Securities*, our access to the debt markets has improved.

The increase in our mortgage-related investments portfolio resulted from our acquiring and holding increased amounts of mortgage loans and mortgage-related securities to provide additional liquidity to the mortgage market. Also, primarily during the first quarter of 2009, continued liquidity concerns in the market resulted in more favorable investment opportunities for agency mortgage-related securities at wider spreads. In response, our net purchase activities resulted in an increase in the average balance of our interest-earning assets.

The increases in net interest income and net interest yield on a fully taxable-equivalent basis during the three and six months ended June 30, 2009 were partially offset by the impact of declining short-term interest rates on floating rate assets held in our mortgage-related investments portfolio. We also increased our cash and other investments portfolio during the three and six months ended June 30, 2009 compared to the three and six months ended June 30, 2008, as we replaced higher-yielding, longer-term non-mortgage-related securities with lower-yielding, shorter-term cash and cash equivalents and securities purchased under agreements to resell. This shift, in combination with lower short-term rates, also partially offset the increase in net interest income and net interest yield.

Non-Interest Income (Loss)

Management and Guarantee Income

Table 7 provides summary information about management and guarantee income. Management and guarantee income consists of contractual amounts due to us (reflecting buy-ups and buy-downs to base management and guarantee fees) as well as amortization of pre-2003 delivery and buy-down fees received by us that were recorded as deferred income as a component of other liabilities. Beginning in 2003, delivery and buy-down fees are reflected within income on guarantee obligation as the guarantee obligation is amortized.

Table 7 Management and Guarantee Income

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009		2008		2009		2008	
	Amount	Rate	Amount	Rate	Amount	Rate	Amount	Rate
	(dollars in millions, rates in basis points)							
Contractual management and guarantee fees[1]	$ 776	17.3	$ 778	17.5	$ 1,558	17.4	$ 1,535	17.5
Amortization of deferred fees included in other liabilities	(66)	(1.5)	(21)	(0.5)	(68)	(0.8)	11	0.1
Total management and guarantee income	$ 710	15.8	$ 757	17.0	$ 1,490	16.6	$ 1,546	17.6
Unamortized balance of deferred fees included in other liabilities, at period end	$ 250		$ 403		$ 250		$ 403	

(1) Consists of management and guarantee fees related to all issued and outstanding guarantees, including those issued prior to adoption of FIN 45 in January 2003, which did not require the establishment of a guarantee asset.

Management and guarantee income decreased for the three and six months ended June 30, 2009 compared to the three and six months ended June 30, 2008 primarily due to the reversal of amortization of pre-2003 deferred fees in the

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2009 periods. Amortization of deferred fees declined due to our expectations of increasing interest rates and slowing prepayments in the future, which resulted in our recognizing a catch-up, or, in this case, reversal of previous amortization. The unpaid principal balance of our issued PCs and Structured Securities was $1.85 trillion at June 30, 2009 compared to $1.82 trillion at June 30, 2008, an increase of 1.5%. Although there were higher average balances of our issued guarantees during the three and six months ended June 30, 2009, compared to the same periods in 2008, the effect of this increase was offset by declines in the average rate of contractual management and guarantee fees. Our average management and guarantee fee rates have declined slightly in the second quarter and first half of 2009, compared to the same periods in 2008, due primarily to portfolio turnover in these periods, since newly issued PCs generally had lower average contractual guarantee fee rates than the previously outstanding PCs that were liquidated. This rate decline was primarily caused by the impact of our market-pricing on new business purchases and a decrease in higher-risk mortgage composition in our purchases that was partially offset by an increase in the preference for buy-ups in rates by our customers.

Gains (Losses) on Guarantee Asset

Upon issuance of a financial guarantee, we record a guarantee asset on our consolidated balance sheets representing the fair value of the management and guarantee fees we expect to receive over the life of our PCs and Structured Securities. Subsequent changes in the fair value of the future cash flows of our guarantee asset are reported in the current period income as gains (losses) on guarantee asset.

Gains (losses) on guarantee asset reflect:

- reductions related to the management and guarantee fees received that are considered a return of our recorded investment in our guarantee asset; and
- changes in the fair value of management and guarantee fees we expect to receive over the life of the financial guarantee.

Contractual management and guarantee fees shown in Table 8 represent cash received in each period for those financial guarantees with an established guarantee asset. A portion of these contractual management and guarantee fees is attributed to imputed interest income on the guarantee asset.

Table 8 Attribution of Change Gains (Losses) on Guarantee Asset

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Contractual management and guarantee fees	$ (731)	$ (720)	$ (1,464)	$ (1,409)
Portion attributable to imputed interest income	251	243	500	458
Return of investment on guarantee asset	(480)	(477)	(964)	(951)
Change in fair value of future management and guarantee fees	2,297	1,591	2,625	671
Gains (losses) on guarantee asset	$ 1,817	$ 1,114	$ 1,661	$ (280)

Contractual management and guarantee fees and imputed interest income increased slightly in the three and six months ended June 30, 2009 as compared to the three and six months ended June 30, 2008, primarily due to increases in the average balance of our PCs and Structured Securities issued.

As shown in the table above, the change in fair value of management and guarantee fees was $2.3 billion in the second quarter of 2009 compared to $1.6 billion in the second quarter of 2008. The increase in the gain on our guarantee asset in the second quarter and first half of 2009 was principally attributed to a greater increase in interest rates during the 2009 periods, compared to the increase in interest rates that occurred during the same periods of 2008.

Income on Guarantee Obligation

Upon issuance of our guarantee, we record a guarantee obligation on our consolidated balance sheets representing the estimated fair value of our obligation to perform under the terms of the guarantee. Our guarantee obligation is amortized into income using a static effective yield determined at inception of the guarantee based on forecasted repayments of the principal balances on loans underlying the guarantee. See CRITICAL ACCOUNTING POLICIES AND ESTIMATES Application of the Static Effective Yield Method to Amortize the Guarantee Obligation in our 2008 Annual Report for additional information on application of the static effective yield method. The static effective yield is periodically evaluated and amortization is adjusted when significant changes in economic events cause a shift in the pattern of our economic release from risk. When this type of change is required, a cumulative catch-up adjustment, which could be significant in a given period, will be recognized. In the first quarter of 2009, we enhanced our methodology for evaluating significant changes in economic events to be more in line with the current economic

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environment and to monitor the rate of amortization on our guarantee obligation so that it remains reflective of our expected duration of losses.

Table 9 provides information about the components of income on guarantee obligation.

Table 9 Income on Guarantee Obligation

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Amortization income related to:				
Static effective yield	$ 741	$ 681	$ 1,516	$ 1,261
Cumulative catch-up	220	88	355	677
Total income on guarantee obligation	$ 961	$ 769	$ 1,871	$ 1,938

Basic amortization under the static effective yield method increased in both the three and six months ended June 30, 2009, compared to the same periods in 2008 primarily due to upward adjustments to the basic rates at the end of 2008, which were due to significant declines in home prices late in the year. Higher liquidation, or prepayment, rates on the related loans, which was attributed to higher refinance activity during the 2009 periods, also resulted in increased static effective yield amortization in the 2009 periods, compared to the 2008 periods.

Cumulative catch-up amortization was higher for the second quarter of 2009 compared to the second quarter of 2008 principally due to higher prepayment rates. We recognized much higher cumulative catch-up adjustments in the first half of 2008 than in the first half of 2009 due to home price declines during the first half of 2008 compared to an increase in national home prices during the first half of 2009, which resulted in catch-up adjustments in the 2008 period. We estimate a slight increase of 1.4% during the first half of 2009 in national home prices, based on our own index of our single family mortgage portfolio, compared to an estimated decrease of 2.9% during the first half of 2008.

Derivative Overview

During 2008, we designated certain derivative positions as cash flow hedges of changes in cash flows associated with our forecasted issuances of debt, consistent with our risk management goals, in an effort to reduce interest rate risk related volatility in our consolidated statements of operations. In conjunction with our entry into conservatorship on September 6, 2008, we determined that we could no longer assert that the associated forecasted issuances of debt were probable of occurring and, as a result, we ceased designating derivative positions as cash flow hedges associated with forecasted issuances of debt. The previous deferred amount related to these hedges remains in our AOCI balance and will be recognized into earnings over the expected time period for which the forecasted issuances of debt impact earnings. Any subsequent changes in fair value of those derivative instruments are included in derivative gains (losses) on our consolidated statements of operations. As a result of our discontinuance of this hedge accounting strategy, we transferred $27.6 billion in notional amount and $(488) million in fair value from open cash flow hedges to closed cash flow hedges on September 6, 2008. During 2008, we also elected cash flow hedge accounting relationships for certain commitments to sell mortgage-related securities; however, we discontinued hedge accounting

for these derivative instruments in December 2008. For a discussion of the impact of derivatives on our consolidated financial statements and our discontinuation of derivatives designated as cash flow hedges see NOTE 10: DERIVATIVES to our consolidated financial statements.

Table 10 presents the gains and losses related to derivatives that were not accounted for in hedge accounting relationships. Derivative gains (losses) represents the change in fair value of derivatives not accounted for in hedge accounting relationships because the derivatives did not qualify for, or we did not elect to pursue, hedge accounting, resulting in fair value changes being recorded to earnings. Derivative gains (losses) also includes the accrual of periodic settlements for derivatives that are not in hedge accounting relationships. Although derivatives are an important aspect of our management of interest-rate risk, they generally increase the volatility of reported net income (loss), particularly when they are not accounted for in hedge accounting relationships.

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Table 10 Derivative Gains (Losses)

Derivatives not Designated as Hedging Instruments under SFAS 133[2]	Derivative Gains (Losses)[1] Three Months Ended June 30, 2009	2008	Six Months Ended June 30, 2009	2008
	(in millions)			
Interest-rate swaps:				
Receive-fixed				
Foreign-currency denominated	$ (63)	$ (490)	$ 124	$ (297)
U.S. dollar denominated	(10,187)	(7,204)	(11,990)	2,299
Total receive-fixed swaps	(10,250)	(7,694)	(11,866)	2,002
Pay-fixed	18,524	11,259	25,229	(3,874)
Basis (floating to floating)	(116)	(23)	(115)	(21)
Total interest-rate swaps	8,158	3,542	13,248	(1,893)
Option-based:				
Call swaptions				
Purchased	(5,910)	(2,542)	(9,297)	698
Written	94	27	211	21
Put swaptions				
Purchased	1,002	72	1,047	(53)
Written	(370)	(93)	(357)	(90)
Other option-based derivatives[3]	(240)	(88)	(215)	(64)
Total option-based	(5,424)	(2,624)	(8,611)	512
Futures	(252)	(154)	(224)	493
Foreign-currency swaps[4]	583	(48)	10	1,189
Forward purchase and sale commitments	140	(243)	(272)	268
Credit derivatives	(6)	10	(5)	14
Swap guarantee derivatives	9	(1)	(22)	(1)
Subtotal	3,208	482	4,124	582
Accrual of periodic settlements:				
Receive-fixed interest rate swaps[5]	1,380	648	2,468	721
Pay-fixed interest rate swaps	(2,269)	(1,118)	(4,211)	(1,595)
Foreign-currency swaps	22	101	71	158
Other	20	2	90	4
Total accrual of periodic settlements	(847)	(367)	(1,582)	(712)
Total	$ 2,361	$ 115	$ 2,542	$ (130)

(1) Gains (losses) are reported as derivative gains (losses) on our consolidated statements of operations.
(2) See NOTE 10: DERIVATIVES to our consolidated financial statements for additional information about the purpose of entering into derivatives not designated as hedging instruments and our overall risk management

strategies.

(3) Primarily represents purchased interest rate caps and floors, purchased put options on agency mortgage-related securities, as well as certain written options, including guarantees of stated final maturity of issued Structured Securities and written call options on agency mortgage-related securities.

(4) Foreign-currency swaps are defined as swaps in which the net settlement is based on one leg calculated in a foreign-currency and the other leg calculated in U.S. dollars.

(5) Includes imputed interest on zero-coupon swaps.

We use receive- and pay-fixed interest rate swaps to adjust the interest-rate characteristics of our debt funding in order to more closely match changes in the interest-rate characteristics of our mortgage-related assets. We also use derivatives to synthetically create the substantive economic equivalent of various debt funding structures. For example, the combination of a series of short-term debt issuances over a defined period and a pay-fixed interest rate swap with the same maturity as the last debt issuance is the substantive economic equivalent of a long-term fixed-rate debt instrument of comparable maturity. Due to limits on our ability to issue long-term and callable debt in the second half of 2008 and the first few months of 2009, we pursued this strategy and thus increased our use of pay-fixed interest rate swaps. However, the use of these derivatives may expose us to additional counterparty credit risk and increased volatility reported in our GAAP net income (loss). For a discussion regarding our ability to issue debt see LIQUIDITY AND CAPITAL RESOURCES Liquidity *Debt Securities*. During the three months ended June 30, 2009, fair value gains on our pay-fixed interest rate swaps of $18.5 billion were partially offset by losses on our receive-fixed interest rate swaps of $10.3 billion as longer-term swap interest rates increased, resulting in an overall gain recorded for derivatives. During the three months ended June 30, 2008, fair value gains on our pay-fixed swaps of $11.3 billion contributed to an overall gain recorded for derivatives. The gains were partially offset by losses on our receive-fixed swaps of $7.7 billion as swap interest rates increased.

Additionally, we use swaptions and other option-based derivatives to adjust the characteristics of our debt in response to changes in the expected lives of mortgage-related assets in our mortgage-related investments portfolio. We recorded losses of $5.9 billion and $2.5 billion on our purchased call swaptions during the three months ended June 30, 2009 and 2008, respectively. The losses during the three months ended June 30, 2009 and 2008 were primarily attributable to increasing swap interest rates, partially offset by increases in implied volatility.

During the six months ended June 30, 2009, we recognized derivative gains of $2.5 billion as compared to derivative losses of $130 million during the six months ended June 30, 2008. During the six months ended June 30, 2009, swap interest rates increased resulting in a gain on our pay-fixed swap positions, partially offset by losses on our receive-fixed swaps. The increase in swap interest rates more than offset the increase in volatility, resulting in a loss related to our purchased call swaptions for the six months ended June 30, 2009. During the six months ended June 30, 2008, shorter term swap interest rates declined, resulting in a loss on our pay-fixed swap positions, partially offset by gains on our receive-fixed swaps. The decrease in shorter term swap interest rates during the six months ended June 30, 2008, combined with an increase in volatility, resulted in a gain related to our purchased call swaptions for the six months ended June 30, 2008.

As a result of our election of the fair value option for our foreign-currency denominated debt, foreign-currency translation gains and losses and fair value adjustments related to our foreign-currency denominated debt are recognized on our consolidated statements of operations as gains (losses) on debt recorded at fair value. We use a combination of foreign-currency swaps and foreign-currency denominated receive-fixed interest rate swaps to hedge the changes in fair value of our foreign-currency denominated debt related to fluctuations in exchange rates and interest rates, respectively.

For the three and six months ended June 30, 2009, we recognized fair value gains (losses) of $(797) million and $(330) million, respectively, on our foreign-currency denominated debt. These amounts included fair value gains (losses) related to translation of $(655) million and $(75) million, respectively, and gains (losses) relating to interest-rate and instrument-specific credit risk adjustments of $(142) million and $(255) million, respectively. For the three and six months ended June 30, 2009, derivative gains (losses) on foreign-currency swaps of $583 million and $10 million, respectively, partially offset fair value translation gains (losses) of $(655) million and $(75) million, respectively, on our foreign-currency denominated debt. In addition, derivative gains (losses) of $(63) million and $124 million on foreign-currency denominated receive-fixed interest rate swaps partially offset the interest-rate and instrument-specific credit risk adjustments included in gains (losses) on debt recorded at fair value for the three and six months ended June 30, 2009, respectively.

For the three and six months ended June 30, 2008, we recognized fair value gains (losses) of $569 million and $(816) million, respectively, on our foreign-currency denominated debt. These amounts included fair value gains (losses) related to translation of $88 million and $(1.1) billion, respectively, and gains (losses) relating to interest-rate and instrument-specific credit risk adjustments of $481 million and $310 million, respectively. For the three and six months ended June 30, 2008, derivative gains (losses) on foreign-currency swaps of $(48) million and $1.2 billion, respectively, largely offset fair value translation gains (losses) of $88 million and $(1.1) billion, respectively, on our foreign-currency denominated debt. In addition, derivative gains (losses) of $(490) million and $(297) million on foreign-currency denominated receive-fixed interest rate swaps largely offset the interest-rate and instrument-specific credit risk adjustments included in gains (losses) on debt recorded at fair value for the three and six months ended June 30, 2008, respectively.

For a discussion of the instrument-specific credit risk and our election to adopt the fair value option on our foreign-currency denominated debt see NOTE 17: FAIR VALUE DISCLOSURES Fair Value Election *Foreign-Currency Denominated Debt with the Fair Value Option Elected* in our 2008 Annual Report.

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Gains (Losses) on Investments

Gains (losses) on investments include gains and losses on certain assets where changes in fair value are recognized through earnings, gains and losses related to sales, impairments and other valuation adjustments. Table 11 summarizes the components of gains (losses) on investments.

Table 11 Gains (Losses) on Investments

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Impairment-related[1]:				
Total other-than-temporary impairment of available-for-sale securities	$ (10,473)	$ (1,040)	$ (17,603)	$ (1,111)
Portion of other-than-temporary impairment recognized in AOCI	8,260		8,260	
Net impairment of available-for-sale securities recognized in earnings	(2,213)	(1,040)	(9,343)	(1,111)
Other:				
Gains (losses) on trading securities[2]	622	(2,279)	2,753	(1,308)
Gains (losses) on sale of mortgage loans[3]	143	(5)	294	66
Gains (losses) on sale of available-for-sale securities	205	38	256	253
Lower-of-cost-or-fair-value adjustments	(102)	(41)	(231)	(8)
Gains (losses) on mortgage loans elected at fair value	(71)		(89)	
Total gains (losses) on investments	$ (1,416)	$ (3,327)	$ (6,360)	$ (2,108)

(1) We adopted FSP FAS 115-2 and FAS 124-2 effective April 1, 2009. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Change in Accounting Principles to our consolidated financial statements for further information.
(2) Includes mark-to-fair value adjustments recorded in accordance with EITF 99-20 on securities classified as trading.
(3) Represents gains (losses) on mortgage loans sold in connection with securitization transactions.

Impairments on Available-For-Sale Securities

We adopted FSP FAS 115-2 and FAS 124-2 on April 1, 2009, which provides guidance designed to create greater clarity and consistency in accounting for and presenting impairment losses on securities. Under the guidance set forth in these pronouncements, the non-credit-related portion of the other-than-temporary impairment (that portion which relates to securities not intended to be sold or which it is not more likely than not we will be required to sell) is recorded in AOCI and not recognized in earnings. See NOTE 4: INVESTMENTS IN SECURITIES to our consolidated financial statements for additional information regarding these accounting principles and other-than-temporary impairments recorded during the three and six months ended June 30, 2009 and 2008. See NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Change in Accounting Principles *Additional Guidance and Disclosures for Fair Value Measurements and Change in the Impairment Model for Debt Securities*

Change in the Impairment Model for Debt Securities to our consolidated financial statements for information on how other-than-temporary impairments are recorded on our financial statements commencing in the second quarter of 2009.

See CONSOLIDATED BALANCE SHEETS ANALYSIS Mortgage-Related Investments Portfolio *Other-Than-Temporary Impairments on Available-for-Sale Mortgage-Related Securities* for additional information.

Gains (Losses) on Trading Securities

We recognized net gains on trading securities of $0.6 billion and $2.8 billion for the three and six months ended June 30, 2009, respectively, as compared to net losses of $(2.3) billion and $(1.3) billion for the three and six months ended June 30, 2008, respectively. The unpaid principal balance of our securities classified as trading increased to $240 billion at June 30, 2009 compared to $157 billion at June 30, 2008, primarily due to our increased purchases of agency mortgage-related securities. The increased balance in our trading portfolio, combined with tightening OAS levels, contributed $0.4 billion and $1.5 billion to the gains on these trading securities for the three and six months ended June 30, 2009, respectively. In addition, during the three and six months ended June 30, 2009, we sold agency securities classified as trading with unpaid principal balances of approximately $51 billion and $87 billion, respectively, which generated realized gains of $0.2 billion and $1.3 billion, respectively.

For the three and six months ended June 30, 2008, an increase in interest rates contributed to the losses on trading securities which were partially offset by gains on our interest-only securities classified as trading.

Gains (Losses) on Debt Recorded at Fair Value

We elected the fair value option for our foreign-currency denominated debt effective January 1, 2008. Accordingly, foreign-currency translation exposure is a component of gains (losses) on debt recorded at fair value. We manage the exposure associated with our foreign-currency denominated debt related to fluctuations in exchange rates and interest rates through the use of derivatives, and changes in the fair value of such derivatives are recorded as derivative gains (losses) in our consolidated statements of operations. For the three and six months ended June 30, 2009, we recognized fair value gains (losses) of $(797) million and $(330) million, respectively, due primarily to the

U.S. dollar weakening relative to the Euro. For the three months ended June 30, 2008, we recognized fair value gains of $569 million on our foreign-currency denominated debt primarily due to an increase in interest rates and the U.S. dollar strengthening relative to the Euro. However, the U.S. dollar weakened relative to the Euro during the six months ended June 30, 2008, contributing to our recognition of fair value losses of $816 million on our foreign-currency denominated debt. See *Derivative Overview* for additional information about how we mitigate changes in the fair value of our foreign-currency denominated debt by using derivatives.

Gains (Losses) on Debt Retirement

Gains (losses) on debt retirement were $(156) million and $(260) million during the three and six months ended June 30, 2009, respectively, compared to $(29) million and $276 million for the three and six months ended June 30, 2008, respectively. The three and six months ended June 30, 2009 include losses of $21 million related to our June 2009 tender offer for certain of our debt securities with maturity dates ranging between September 2009 and August 2010. In addition, during June 2009, we made a tender offer for our euro-denominated debt securities with maturity dates ranging between September 2010 and January 2014. There was no gain or loss recorded on these securities as foreign-currency denominated debt is recorded at fair value. For more information on these tender offers, see LIQUIDITY AND CAPITAL RESOURCES Liquidity *Debt Securities* *Debt Retirement Activities*. Also contributing to the increased losses was a decreased level of call activity involving our debt with coupon levels that increase at pre-determined intervals.

Recoveries on Loans Impaired Upon Purchase

Recoveries on loans impaired upon purchase represent the recapture into income of previously recognized losses on loans purchased and provision for credit losses associated with purchases of delinquent loans under our financial guarantee. Recoveries occur when a non-performing loan is repaid in full or when at the time of foreclosure the estimated fair value of the acquired property, less costs to sell, exceeds the carrying value of the loan. For impaired loans where the borrower has made required payments that return the loan to less than 90 days delinquent, the recovery amounts are instead accreted into interest income over time as periodic payments are received.

During the three months ended June 30, 2009 and 2008, we recognized recoveries on loans impaired upon purchase of $70 million and $121 million, respectively. For the six months ended June 30, 2009 and 2008, our recoveries were $120 million and $347 million, respectively. Our recoveries on impaired loans decreased in the first half of 2009 due to a lower rate of loan payoffs and a higher proportion of modified loans among those loans purchased, as compared to the same period in 2008. In addition, home prices in states having the greatest concentration of our impaired loans have remained weak during the first half of 2009, which limited our recoveries on foreclosure transfers.

Trust Management Income (Expense)

Trust management income (expense) represents the amounts we earn as administrator, issuer and trustee, net of related expenses, related to the management of remittances of principal and interest on loans underlying our PCs and Structured Securities. Trust management income (expense) was $(238) million and $(19) million for the three months ended June 30, 2009 and 2008, respectively, and $(445) million and $(16) million for the six months ended June 30, 2009 and 2008, respectively. We experienced trust management expenses associated with shortfalls in interest payments on PCs, known as compensating interest, which significantly exceeded our trust management income during the three and six months ended June 30, 2009. The increase in expense for these shortfalls was attributable to significantly higher refinance activity and lower interest income on trust assets, which we receive as fee income, in the first half of 2009, as compared to the first half of 2008. If mortgage interest rates remain low and refinance activity remains elevated, then our trust management expenses will continue to exceed our related income in the second half of 2009. See MD&A CONSOLIDATED RESULTS OF OPERATIONS Segment Earnings-Results *Single-Family*

Guarantee in our 2008 Annual Report for further information on compensating interest.

Other Income (Losses)

Other income (losses) primarily consists of resecuritization fees, net hedging gains and losses, fees associated with servicing and technology-related programs, and various other fees received from mortgage originators and servicers. Other income (losses) declined to $70 million in the second quarter of 2009, compared to $94 million in the second quarter of 2008, and totaled $111 million and $138 million in the six months ended June 30, 2009 and 2008, respectively. The decline in other income in both the second quarter and first half of 2009, as compared with the same periods of 2008, reflects a decline in income associated with termination of long-term standby commitments. Following these terminations, we securitized the mortgage loans as PCs or Structured Transactions. We terminated $5.7 billion and $18.8 billion of these long-term standby commitments during the first half of 2009 and 2008, respectively.

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Non-Interest Expense

Table 12 summarizes the components of non-interest expense.

Table 12 Non-Interest Expense

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Administrative expenses:				
Salaries and employee benefits	$ 221	$ 241	$ 428	$ 472
Professional services	64	55	124	127
Occupancy expense	15	18	33	33
Other administrative expenses	83	90	170	169
Total administrative expenses	383	404	755	801
Provision for credit losses	5,199	2,537	13,990	3,777
REO operations expense	9	265	315	473
Losses on loans purchased	1,199	120	3,211	171
Other expenses	97	108	175	195
Total non-interest expense	$ 6,887	$ 3,434	$ 18,446	$ 5,417

Administrative Expenses

Administrative expenses decreased for the three and six months ended June 30, 2009, compared to the three and six months ended June 30, 2008, in part due to a decrease in the number of full-time employees as well as other cost reduction measures. The decrease in salaries and benefits expense for the three and six months ended June 30, 2009 also reflected reductions in short-term performance compensation.

Provision for Credit Losses

Our reserves for mortgage loan and guarantee losses reflect our best projection of defaults we believe are likely as a result of loss events that have occurred through June 30, 2009. The substantial weakness in the national housing market, the uncertainty in other macroeconomic factors, such as trends in unemployment rates and home prices, and the uncertainty of the effect of current or any future government actions to address the economic and housing crisis makes forecasting of default rates imprecise. Our reserves also include the impact of our projections of the results of strategic loss mitigation initiatives, including our temporary suspensions of certain foreclosure transfers, a higher volume of loan modifications, and projections of recoveries through repurchases by seller/servicers of defaulted loans due to failure to follow contractual underwriting requirements at the time of the loan origination. An inability to realize the benefits of our loss mitigation plans, a lower realized rate of seller/servicer repurchases or default rates that exceed our current projections would cause our losses to be significantly higher than those currently estimated.

The provision for credit losses was $5.2 billion in the second quarter of 2009, compared to $2.5 billion in the second quarter of 2008, as continued weakness in the housing market and a rapid rise in unemployment affected our single-family mortgage portfolio. A portion of our provision relates to the delinquent interest on loans remaining in PC pools while they remain past due. During the second quarter of 2009, we enhanced our methodology for estimating our loan loss reserves to consider a greater number of loan characteristics and revisions to (1) the effects of home price changes on borrower behavior, and (2) the impact of our loss mitigation actions, including our temporary suspensions of foreclosure transfers and loan modification efforts. We estimate the impact of this enhancement reduced our provision for credit losses by approximately $1.4 billion during the second quarter of 2009. For more information regarding how we derive our estimate for the provision for credit losses, see MD&A CRITICAL ACCOUNTING POLICIES AND ESTIMATES in our 2008 Annual Report. See EXECUTIVE SUMMARY Table 2 Credit Statistics, Single-Family Mortgage Portfolio for quarterly trends in our other credit-related statistics. Our provision for credit losses was $14.0 billion and $3.8 billion for the six months ended June 30, 2009 and 2008, respectively. In the three and six months ended June 30, 2009, we recorded a $2.5 billion and $9.6 billion increase, respectively, in our loan loss reserve, which is a combined reserve for credit losses on loans within our mortgage-related investments portfolio and mortgages underlying our PCs, Structured Securities and other mortgage-related guarantees. This resulted in a total reserve balance of $25.2 billion at June 30, 2009. The primary drivers of these increases are outlined below:

- increased estimates of incurred losses on single-family mortgage loans that are expected to experience higher default rates. In particular, our estimates of incurred losses are higher for single-family loans we purchased or guaranteed during 2006, 2007 and to a lesser extent 2005 and 2008. We expect such loans to continue experiencing higher default rates than loans originated in earlier years. We purchased a greater percentage of higher-risk loans in 2005 through 2008, such as Alt-A, interest-only and other such products, and these mortgages have performed particularly poorly during the current housing and economic downturn;

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a significant increase in the size of the non-performing single-family loan portfolio for which we maintain loan loss reserves. This increase is primarily due to deteriorating market conditions and initiatives to prevent or avoid foreclosures. Our single-family non-performing assets increased to $76.9 billion at June 30, 2009, compared to $48.0 billion and $27.5 billion at December 31, 2008 and June 30, 2008, respectively;

an observed trend of increasing delinquency rates, foreclosure starts, which is the number of loans that enter the foreclosure process, and foreclosure timeframes. We have experienced more significant increases in delinquency rates and foreclosure starts concentrated in certain regions and states within the U.S. that have been most affected by home price declines, as well as loans with second lien, third-party financing. For example, as of June 30, 2009, at least 14% of loans in our single-family mortgage portfolio had second lien, third-party financing at the time of origination and we estimate that these loans comprise 23% of our delinquent loans, based on unpaid principal balances; and

increases in the estimated average loss per loan, or severity of losses, net of expected recoveries from credit enhancements, driven in part by declines in home sales and home prices in the last two years. The states with the largest declines in home prices in the last 12 months and highest severity of losses include California, Florida, Nevada and Arizona.

Our model estimates indicate that recent modest national home price improvements, which we believe to be largely seasonal, during the second quarter of 2009, helped slow the rate of growth in our loan loss reserves in the quarter. However, we expect home price declines in future periods, which will result in increasing default frequency and loss severity and would likely require us to further increase our loan loss reserves. Consequently, we expect our provisions for credit losses will likely remain high during the remainder of 2009 and to increase above the level recognized in the second quarter. The likelihood that our provision for credit losses will remain high beyond 2009 will depend on a number of factors, including the impact of the MHA Program on our loss mitigation efforts, changes in property values, regional economic conditions, including unemployment rates, third-party mortgage insurance coverage and recoveries and the realized rate of seller/servicer repurchases.

REO Operations Expense

REO operations expense was $9 million during the three months ended June 30, 2009, as compared to $265 million during the three months ended June 30, 2008, and was $315 million and $473 million during the six months ended June 30, 2009 and 2008, respectively. REO operations expense decreased in the second quarter of 2009 primarily as a result of a reduction in our holding period allowance. We recognize an allowance for estimated changes in REO fair value during the period properties are held, which is included in REO operations expense. During the second quarter of 2009, our carrying values and disposition values were more closely aligned due to more stable national home prices, reducing the size of our holding period allowance. Single-family REO disposition losses, excluding our holding period allowance, totaled $304 million and $183 million for the three months ended June 30, 2009 and 2008, respectively, and were $610 million and $292 million during the six months ended June 30, 2009 and 2008, respectively. The reduction in our holding period allowance substantially offset the impact of our REO disposition losses during the second quarter of 2009. We expect REO operations expense to fluctuate in the remainder of 2009, as single-family REO acquisition volume increases and home prices remain under downward pressure.

Losses on Loans Purchased

Losses on delinquent and modified loans purchased from the mortgage pools underlying PCs and Structured Securities occur when the acquisition basis of the purchased loan exceeds the estimated fair value of the loan on the date of purchase. As a result of increases in delinquency rates of loans underlying our PCs and Structured Securities and our increasing efforts to reduce foreclosures, the number of loan modifications increased significantly during the first half

of 2009, as compared to the first half of 2008. When a loan underlying our PCs and Structured Securities is modified, we generally exercise our repurchase option and hold the modified loan in our mortgage-related investments portfolio. See *Recoveries on Loans Impaired upon Purchase* and RISK MANAGEMENT Credit Risks Table 46 Changes in Loans Purchased Under Financial Guarantees for additional information about the impacts of these loans on our financial results.

During the three and six months ended June 30, 2009, the market-based valuation of non-performing loans continued to be adversely affected by the expectation of higher default costs and reduced liquidity in the single-family mortgage market. Our losses on loans purchased were $1.2 billion and $120 million for the three months ended June 30, 2009 and 2008, respectively, and totaled $3.2 billion and $171 million for the six months ended June 30, 2009 and 2008, respectively. The increase in losses on loans purchased is attributed both to the increase in volume of our optional repurchases of delinquent and modified loans underlying our guarantees as well as a decline in market valuations for these loans as compared to the first half of 2008. The growth in volume of our purchases of delinquent

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and modified loans from our PC pools temporarily slowed in the second quarter of 2009 due to our implementation of the loan modification process under HAMP. Loans that we would have otherwise purchased instead remained in the PC pools while the borrowers began the three-month trial period payment plan under HAMP. However, we expect these losses to increase for the remainder of 2009, as we continue to increase modifications and purchases of loans currently in PCs.

Income Tax (Expense) Benefit

For the three months ended June 30, 2009 and 2008, we reported an income tax benefit of $184 million and $1.0 billion, respectively. For the six months ended June 30, 2009 and 2008 we reported an income tax benefit of $1.1 billion and $1.5 billion, respectively. See NOTE 12: INCOME TAXES to our consolidated financial statements for additional information.

Segment Earnings

Our operations consist of three reportable segments, which are based on the type of business activities each performs Investments, Single-family Guarantee and Multifamily. Certain activities that are not part of a segment are included in the All Other category; this category consists of certain unallocated corporate items, such as costs associated with remediating our internal controls and near-term restructuring costs, costs related to the resolution of certain legal matters and certain income tax items. We manage and evaluate performance of the segments and All Other using a Segment Earnings approach, subject to the conduct of our business under the direction of the Conservator. The objectives set forth for us under our charter and by our Conservator, as well as the restrictions on our business under the Purchase Agreement with Treasury, may negatively impact our Segment Earnings and the performance of individual segments.

Segment Earnings is calculated for the segments by adjusting GAAP net income (loss) for certain investment-related activities and credit guarantee-related activities. Segment Earnings also includes certain reclassifications among income and expense categories that have no impact on net income (loss) but provide us with a meaningful metric to assess the performance of each segment and our company as a whole. We continue to assess the methodologies used for segment reporting and refinements may be made in future periods. Segment Earnings does not include the effect of the establishment of the valuation allowance against our deferred tax assets, net. See NOTE 16: SEGMENT REPORTING to our consolidated financial statements for further information regarding our segments and the adjustments and reclassifications used to calculate Segment Earnings, as well as the allocation process used to generate our segment results.

Segment Earnings Results

Investments

Our Investments segment is responsible for investment activity in mortgages and mortgage-related securities, other investments, debt financing, and managing our interest rate risk, liquidity and capital positions. We invest principally in mortgage-related securities and single-family mortgages.

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Table 13 presents the Segment Earnings of our Investments segment.

Table 13 Segment Earnings and Key Metrics Investments

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(dollars in millions)			
Segment Earnings:				
Net interest income	$ 2,454	$ 1,481	$ 4,468	$ 1,780
Non-interest income (loss)	(2,084)	(125)	(6,390)	(110)
Non-interest expense:				
Administrative expenses	(119)	(130)	(239)	(261)
Other non-interest expense	(8)	(7)	(15)	(16)
Total non-interest expense	(127)	(137)	(254)	(277)
Segment Earnings (loss) before income tax (expense) benefit	243	1,219	(2,176)	1,393
Income tax (expense) benefit	(85)	(426)	762	(487)
Segment Earnings (loss), net of taxes	158	793	(1,414)	906
Reconciliation to GAAP net income (loss):				
Derivative- and foreign-currency denominated debt-related adjustments	2,798	530	4,388	(653)
Investment sales, debt retirements and fair value-related adjustments	907	(3,096)	952	(1,571)
Fully taxable-equivalent adjustment	(98)	(105)	(198)	(215)
Tax-related adjustments[1]	111	1,004	750	992
Total reconciling items, net of taxes	3,718	(1,667)	5,892	(1,447)
GAAP net income (loss)	$ 3,876	$ (874)	$ 4,478	$ (541)
Key metrics Investments:				
Growth:				
Purchases of securities Mortgage-related investments portfolio:[2][3]				
Guaranteed PCs and Structured Securities	$ 46,599	$ 91,054	$ 130,779	$ 112,598
Non-Freddie Mac mortgage-related securities:				
Agency mortgage-related securities	10,796	24,688	42,117	34,071
Non-agency mortgage-related securities	19	1,024	95	1,884
Total purchases of securities Mortgage-related investments portfolio	$ 57,414	$ 116,766	$ 172,991	$ 148,553

Growth rate of mortgage-related investments portfolio (annualized)		(20.14)%	46.9%	5.32%	19.5%
Return:					
Net interest yield	Segment Earnings basis	1.16%	0.80%	1.07%	0.50%

(1) 2009 includes an allocation of the non-cash charge related to the establishment of the partial valuation allowance against our deferred tax assets, net that is not included in Segment Earnings.
(2) Based on unpaid principal balance and excludes mortgage-related securities traded, but not yet settled.
(3) Excludes single-family mortgage loans.

Segment Earnings for our Investments Segment decreased $635 million for the three months ended June 30, 2009 compared to the three months ended June 30, 2008, and decreased $2.3 billion for the six months ended June 30, 2009 compared to the six months ended June 30, 2008. Net impairment of available-for-sale securities recognized in earnings increased to $2.2 billion and $6.6 billion during the three and six months ended June 30, 2009, respectively, due to an increase in expected credit-related losses on our non-agency mortgage-related securities, compared to $142 million and $144 million of net impairment of available-for-sale securities recognized in earnings during the three and six months ended June 30, 2008, respectively. Among the securities impaired during the three months ended June 30, 2009 are securities backed by subprime, MTA Option ARM, Alt-A and other loans impaired as a result of the adoption of FSP FAS 115-2 and FAS 124-2. Security impairments that reflect expected or realized credit-related losses are realized in earnings immediately pursuant to GAAP and in Segment Earnings. In contrast, non-credit-related security impairments are recorded in our GAAP results in AOCI, but are not recorded in Segment Earnings. Impairments on securities we intend to sell or more likely than not will be required to sell prior to anticipated recovery are also excluded from Segment Earnings. Segment Earnings net interest income increased $1.0 billion and Segment Earnings net interest yield increased 36 basis points to 116 basis points for the three months ended June 30, 2009 compared to the three months ended June 30, 2008. Segment Earnings net interest income increased $2.7 billion and Segment Earnings net interest yield increased 57 basis points to 107 basis points for the six months ended June 30, 2009 compared to the six months ended June 30, 2008. The primary drivers underlying the increases in Segment Earnings net interest income and Segment Earnings net interest yield were (a) a decrease in funding costs as a result of the replacement of higher cost short- and long-term debt with lower cost debt and (b) a significant increase in the average size of our mortgage-related investments portfolio including an increase in our holdings of fixed-rate assets. Partially offsetting these increases was an increase in derivative interest carry expense on net pay-fixed interest rate swaps, which is recognized within net interest income in Segment Earnings. In addition, certain terminated derivative positions resulted in losses that are amortized prospectively within net interest income in Segment Earnings.

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During the six months ended June 30, 2009, the mortgage-related investments portfolio of our Investments Segment grew at an annualized rate of 5.3%, compared to 19.5% for the six months ended June 30, 2008. The unpaid principal balance of the mortgage-related investments portfolio of our Investments Segment increased from $732 billion at December 31, 2008 to $752 billion at June 30, 2009. The portfolio grew because we acquired and held increased amounts of mortgage loans and mortgage-related securities in our mortgage-related investments portfolio to provide additional liquidity to the mortgage market and, to a lesser degree, due to more favorable investment opportunities for agency securities, primarily in the first quarter of 2009, due to liquidity concerns in the market. While our mortgage-related investments portfolio increased overall during the six months ended June 30, 2009, it decreased during the second quarter of 2009, due to forward sale commitments of our mortgage-related securities at March 31, 2009 that settled during the second quarter of 2009 and a relative lack of favorable investment opportunities.

We held $72.9 billion of non-Freddie Mac agency mortgage-related securities and $186.2 billion of non-agency mortgage-related securities as of June 30, 2009 compared to $70.9 billion of non-Freddie Mac agency mortgage-related securities and $197.9 billion of non-agency mortgage-related securities as of December 31, 2008. The decline in the unpaid principal balance of non-agency mortgage-related securities is due to the receipt of monthly principal repayments on these securities. Agency securities comprised approximately 68% of the unpaid principal balance of the Investments Segment mortgage-related investments portfolio at both June 30, 2009 and December 31, 2008. See CONSOLIDATED BALANCE SHEETS ANALYSIS Mortgage-Related Investments Portfolio for additional information regarding our mortgage-related securities.

The objectives set forth for us under our charter and conservatorship and restrictions set forth in the Purchase Agreement may negatively impact our Investments segment results over the long term. For example, the required reduction in our mortgage-related investments portfolio balance to $250 billion, through successive annual 10% declines commencing in 2010, will cause a corresponding reduction in our net interest income. This may negatively affect our Investments segment results.

Single-Family Guarantee Segment

In our Single-family Guarantee segment, we guarantee the payment of principal and interest on single-family mortgage-related securities, including those held in our mortgage-related investments portfolio, in exchange for monthly management and guarantee fees and other up-front compensation. Earnings for this segment consist primarily of management and guarantee fee revenues less the related credit costs (*i.e.*, provision for credit losses) and operating expenses. Earnings for this segment also include the interest earned on assets held in the Investments segment related to single-family guarantee activities, net of allocated funding costs and amounts related to expected net float benefits.

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Table 14 presents the Segment Earnings of our Single-family Guarantee segment.

Table 14 Segment Earnings and Key Metrics Single-Family Guarantee

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(in millions)			
Segment Earnings:				
Net interest income	$ 28	$ 58	$ 53	$ 135
Non-interest income:				
Management and guarantee income	942	840	1,864	1,735
Other non-interest income	88	103	171	207
Total non-interest income	1,030	943	2,035	1,942
Non-interest expense:				
Administrative expenses	(206)	(212)	(406)	(416)
Provision for credit losses	(6,285)	(2,630)	(15,226)	(3,979)
REO operations expense	(1)	(265)	(307)	(473)
Other non-interest expense	(30)	(29)	(52)	(48)
Total non-interest expense	(6,522)	(3,136)	(15,991)	(4,916)
Segment Earnings (loss) before income tax expense	(5,464)	(2,135)	(13,903)	(2,839)
Income tax (expense) benefit	1,912	747	4,866	993
Segment Earnings (loss), net of taxes	(3,552)	(1,388)	(9,037)	(1,846)
Reconciliation to GAAP net income (loss):				
Credit guarantee-related adjustments	2,356	1,822	953	1,648
Tax-related adjustments[1]	(1,338)	(638)	(4,316)	(577)
Total reconciling items, net of taxes[1]	1,018	1,184	(3,363)	1,071
GAAP net income (loss)	$ (2,534)	$ (204)	$ (12,400)	$ (775)
Key metrics Single-family Guarantee:				
Balances and Growth (in billions, except rate):				
Average securitized balance of single-family credit guarantee portfolio[2]	$ 1,787	$ 1,764	$ 1,783	$ 1,746
Issuance Single-family credit guarantees[2]	$ 154	$ 132	$ 258	$ 245
Fixed-rate products Percentage of issuances[3]	96.7%	90.0%	97.9%	91.3%
Liquidation Rate Single-family credit guarantees (annualized rate)[4]	30.7%	20.8%	26.0%	18.9%
Credit:				
Delinquency rate[5]	2.78%	0.93%		
Delinquency transition rate[6]	24.7%	22.8%		

REO inventory (number of units)	34,699	22,029	34,699	22,029
Single-family credit losses, in basis points (annualized)	41.7	18.1	35.4	15.1
Market:				
Single-family mortgage debt outstanding (total U.S. market, in billions)[7]	$ 10,465	$ 11,227	$ 10,465	$ 11,227
30-year fixed mortgage rate[8]	5.0%	6.1%	5.1%	6.0%

(1) 2009 includes an allocation of the non-cash charge related to the partial valuation allowance recorded against our deferred tax assets, net that is not included in Segment Earnings.
(2) Based on unpaid principal balance.
(3) Excludes Structured Transactions, but includes interest-only mortgages with fixed interest rates.
(4) Includes the effect of terminations of long-term standby commitments.
(5) Represents the percentage of loans in our single-family credit guarantee portfolio, based on loan count, which are 90 days or more past due at period end and excluding loans underlying Structured Transactions. See RISK MANAGEMENT Credit Risks *Credit Performance Delinquencies* for additional information.
(6) Represents the percentage of loans that have been reported as 90 days or more delinquent or in foreclosure in the same quarter of the preceding year that have transitioned to REO. The rate excludes other dispositions that can result in a loss, such as short-sales and deed-in-lieu transactions.
(7) Source: Federal Reserve Flow of Funds Accounts of the United States of America dated July 11, 2009.
(8) Based on Freddie Mac s PMMS rate. Represents the national average mortgage commitment rate to a qualified borrower exclusive of the fees and points required by the lender. This commitment rate applies only to conventional financing on conforming mortgages with LTV ratios of 80% or less.

Segment Earnings (loss) for our Single-family Guarantee segment declined to a loss of $(3.6) billion for the second quarter of 2009, compared to a loss of $(1.4) billion for the second quarter of 2008. This decline reflects an increase in credit-related expenses of $3.4 billion due to higher delinquency rates, higher volumes of non-performing loans and foreclosure transfers, higher severity of losses on a per-property basis and other regional economic conditions. Segment Earnings management and guarantee income increased for the three and six months ended June 30, 2009, compared to the same periods in 2008, primarily due to higher credit fee amortization which was accelerated as a result of increased liquidation, or prepayment, rates on the related loans, which is attributed to higher refinance activity in the 2009 periods. Higher credit fee amortization in the 2009 periods was partially offset by slightly lower average contractual management and guarantee rates as compared to the three and six months ended June 30, 2008.

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Table 15 below provides summary information about Segment Earnings management and guarantee income for this segment. Segment Earnings management and guarantee income consists of contractual amounts due to us related to our management and guarantee fees as well as amortization of credit fees.

Table 15 Segment Earnings Management and Guarantee Income Single-Family Guarantee

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009		2008		2009		2008	
	Amount	Average Rate	Amount	Average Rate	Amount	Average Rate	Amount	Average Rate
	(dollars in millions, rates in basis points)							
Contractual management and guarantee fees	$ 697	15.2	$ 708	15.8	$ 1,404	15.3	$ 1,415	16.0
Amortization of credit fees included in other liabilities	245	5.3	132	2.9	460	5.1	320	3.6
Total Segment Earnings management and guarantee income	942	20.5	840	18.7	1,864	20.4	1,735	19.6
Adjustments to reconcile to consolidated GAAP:								
Reclassification between net interest income and management and guarantee fee[1]	61		56		118		94	
Credit guarantee-related activity adjustments[2]	(315)		(156)		(535)		(317)	
Multifamily management and guarantee income[3]	22		17		43		34	
Management and guarantee income, GAAP	$ 710		$ 757		$ 1,490		$ 1,546	

(1) Management and guarantee fees earned on mortgage loans held in our mortgage-related investments portfolio are reclassified from net interest income within the Investments segment to management and guarantee fees within the Single-family Guarantee segment. Buy-up and buy-down fees are transferred from the Single-family Guarantee segment to the Investments segment.
(2) Primarily represent credit fee amortization adjustments.
(3) Represents management and guarantee income recognized related to our Multifamily segment that is not included in our Single-family Guarantee segment.

For the six months ended June 30, 2009 and 2008, the annualized growth rates of our single-family credit guarantee portfolio were 2.6% and 9.5%, respectively. Our mortgage purchase volumes are impacted by several factors, including origination volumes, mortgage product and underwriting trends, competition, customer-specific behavior, contract terms, and governmental initiatives concerning our business activities. Origination volumes are also affected by government programs, such as the MHA Program. Single-family mortgage purchase volumes from individual

customers can fluctuate significantly. Despite these fluctuations, our share of the overall single-family mortgage origination market was higher in the first half of 2009 as compared to the first half of 2008, as mortgage originators have generally tightened their credit standards, causing conforming mortgages to be the predominant product in the market during the first half of 2009. We have also tightened our own guidelines for mortgages we purchase and we have seen improvements in the credit quality of mortgages delivered to us in 2009. We experienced an increase in refinance activity in both the second quarter and first half of 2009 caused by declines in mortgage interest rates during those periods as well as our support of Home Affordable Refinance under the MHA Program.

Our Segment Earnings provision for credit losses for the Single-family Guarantee segment increased to $6.3 billion for the three months ended June 30, 2009 compared to $2.6 billion for the three months ended June 30, 2008, due to continued credit deterioration in our single-family credit guarantee portfolio. Segment Earnings provision for credit losses was $15.2 billion and $4.0 billion for the six months ended June 30, 2009 and 2008, respectively. Mortgages in our single-family credit guarantee portfolio experienced significantly higher delinquency rates, higher transition rates to foreclosure, as well as higher loss severities on a per-property basis in the first half of 2009 than in the first half of 2008. During the second quarter of 2009, we enhanced our methodology for estimating our loan loss reserves to consider a greater number of loan characteristics and revisions to (1) the effects of home price changes on borrower behavior, and (2) the impact of our loss mitigation actions, including our temporary suspensions of foreclosure transfers and loan modification efforts. Our provision for credit losses is based on our estimate of incurred losses inherent in both our single-family credit guarantee portfolio and the single-family mortgage loans in our mortgage-related investments portfolio using recent historical performance, such as trends in delinquency rates, recent charge-off experience, recoveries from credit enhancements and other loss mitigation activities.

The delinquency rate on our single-family credit guarantee portfolio, excluding Structured Transactions, increased to 2.78% as of June 30, 2009 from 1.72% as of December 31, 2008. Increases in delinquency rates occurred in all product types for the three and six months ended June 30, 2009. Increases in delinquency rates have been more severe in the states of Nevada, Florida, Arizona and California. The delinquency rates for loans in our single-family mortgage portfolio, excluding Structured Transactions, related to the states of Nevada, Florida, Arizona and California were 7.87%, 7.73%, 5.12% and 4.23%, respectively, as of June 30, 2009. We expect our delinquency rates will continue to rise in the remainder of 2009.

Charge-offs, gross, for this segment increased to $2.4 billion in the second quarter of 2009 compared to $0.7 billion in the second quarter of 2008, primarily due to an increase in the volume of REO properties we acquired through foreclosure transfers after our temporary suspension of foreclosure transfers ended in March. Declining home prices during the last 12 months resulted in higher charge-offs, on a per property basis, during the second quarter of 2009 compared to the second quarter of 2008, and we expect growth in charge-offs to continue in the remainder of 2009. See RISK MANAGEMENT Credit Risks Table 50 Single-Family Credit Loss Concentration Analysis for additional delinquency and credit loss information.

Single-family Guarantee REO operations expense declined during the three and six months ended June 30, 2009, compared to the same periods in 2008. REO operations expense decreased in the second quarter of 2009 as a result of a reduction in our holding period allowance. During the second quarter of 2009, our existing and newly acquired REO required fewer market-based write-downs due to stabilizing home prices during the period. We expect REO operations expense to fluctuate in the remainder of 2009, as single-family REO acquisition volume increases and home prices remain under downward pressure.

During the first half of 2009, we experienced significant increases in REO activity in all regions of the U.S., particularly in the states of California, Florida, Nevada and Arizona. The West region represented approximately 34% and 26% of our REO property acquisitions during the first half of 2009 and the first half of 2008, respectively, based on the number of units. The highest concentration in the West region is in the state of California. At June 30, 2009, our REO inventory in California comprised 16% of total REO property inventory, based on units, and approximately 25% of our total REO property inventory, based on loan amount prior to acquisition. California has accounted for a significant amount of our credit losses and losses on our loans in this state comprised approximately 32% and 31% of our total credit losses in the second quarter of 2009 and the second quarter of 2008, respectively. We temporarily suspended all foreclosure transfers on occupied homes from November 26, 2008 through January 31, 2009 and from February 14, 2009 through March 6, 2009. On March 7, 2009, we suspended foreclosure transfers on owner-occupied homes where the borrower may be eligible to receive a loan modification under the MHA Program; however, we have continued with initiation and other preclosing steps in the foreclosure process. As a result of our suspension of foreclosure transfers, we experienced an increase in single-family delinquency rates and a slow-down in the growth of REO acquisitions and REO inventory during the first half of 2009, as compared to what we would have experienced without these actions. Our suspension or delay of foreclosure transfers and any imposed delay in foreclosures by regulatory or governmental agencies also causes a delay in our recognition of credit losses and our loan loss reserves to increase. See RISK MANAGEMENT Credit Risks *Loss Mitigation Activities* for further information on these programs.

Approximately 27% of loans in our single-family credit guarantee portfolio had estimated current LTV ratios above 90%, excluding second liens by third parties, at June 30, 2009, compared to 15% at June 30, 2008. In general, higher total LTV ratios indicate that the borrower has less equity in the home and would thus be more likely to default in the event of a financial hardship. There was a slight increase in national home prices during the first half of 2009; however, we expect that home prices are likely to decline during the second half of 2009. We expect that declines in home prices combined with the deterioration in rates of unemployment and other factors will result in higher credit losses for our Single-family Guarantee segment during the remainder of 2009. The implementation of any governmental actions or programs that expand the ability of delinquent borrowers to obtain modifications with concessions of past due principal or interest amounts, including proposed changes to bankruptcy laws, could lead to higher charge-offs.

Multifamily Segment

Through our Multifamily segment, we purchase multifamily mortgages for investment and guarantee the payment of principal and interest on multifamily mortgage-related securities and mortgages underlying multifamily housing

revenue bonds. The mortgage loans of the Multifamily segment consist of mortgages that are secured by properties with five or more residential rental units. We typically hold multifamily loans for investment purposes. In 2008, we began holding multifamily mortgages designated held-for-sale as part of our initiative to offer securitization capabilities to the market and our customers, and we executed the first of these securitizations in the second quarter of 2009. We may consider executing additional securitization transactions using multifamily loans we hold in our portfolio in the future, as market conditions permit.

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Table 16 presents the Segment Earnings of our Multifamily segment.

Table 16 Segment Earnings and Key Metrics Multifamily

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
	(dollars in millions)			
Segment Earnings:				
Net interest income	$ 112	$ 98	$ 230	$ 173
Non-interest income (loss):				
Management and guarantee income	22	17	43	34
LIHTC partnerships	(167)	(108)	(273)	(225)
Other non-interest income	5	7	8	15
Total non-interest income (loss)	(140)	(84)	(222)	(176)
Non-interest expense:				
Administrative expenses	(52)	(49)	(101)	(98)
Provision for credit losses	(57)	(7)	(57)	(16)
REO operations expense	(8)		(8)	
Other non-interest expense	(7)	(5)	(12)	(9)
Total non-interest expense	(124)	(61)	(178)	(123)
Segment Earnings (loss) before income tax benefit	(152)	(47)	(170)	(126)
LIHTC partnerships tax benefit	148	149	299	298
Income tax benefit	54	16	60	44
Less: Net (income) loss noncontrolling interest			1	
Segment Earnings, net of taxes	50	118	190	216
Reconciliation to GAAP net income (loss):				
Derivative and foreign-currency denominated debt-related adjustments	2	(3)	(30)	(14)
Credit guarantee-related adjustments	(2)	(4)	3	(4)
Investment sales, debt retirements and fair value related adjustments	(7)		(24)	
Tax-related adjustments[1]	(41)	2	(704)	6
Total reconciling items, net of taxes[1]	(48)	(5)	(755)	(12)
GAAP net income (loss)	$ 2	$ 113	$ (565)	$ 204
Key metrics Multifamily:				
Balances and Growth:				
Average balance of Multifamily loan portfolio[2]	$ 77,650	$ 62,706	$ 75,946	$ 60,759
Average balance of Multifamily guarantee portfolio[2]	$ 15,819	$ 13,209	$ 15,666	$ 12,274

Purchases Multifamily loan portfolio[2]	$ 4,303	$ 4,189	$ 7,951	$ 8,252
Issuances Multifamily guarantee portfolio[2]	$ 1,127	$ 1,105	$ 1,304	$ 3,487
Liquidation Rate Multifamily loan portfolio (annualized rate)	3.4%	7.9%	3.5%	6.9%
Credit:				
Delinquency rate[3]	0.11%	0.04%	0.11%	0.04%
Allowance for loan losses	$ 330	$ 78	$ 330	$ 78

(1) 2009 includes an allocation of the non-cash charge related to the partial valuation allowance recorded against our deferred tax assets, net that is not included in Segment Earnings.
(2) Based on unpaid principal balance.
(3) Based on net carrying value of mortgages 90 days or more delinquent as well as those in the process of foreclosure and excluding Structured Transactions.

Segment Earnings for our Multifamily segment decreased to $50 million for the second quarter of 2009 compared to $118 million for the second quarter of 2008. Segment Earnings for the Multifamily segment were $190 million and $216 million for the six months ended June 30, 2009 and 2008, respectively. The declines in Segment Earnings for the three and six months ended June 30, 2009 as compared to the corresponding periods in 2008 were primarily due to higher non-interest expenses and higher LIHTC partnership losses, partially offset by higher net interest income. Net interest income increased $14 million, or 14%, for the second quarter of 2009 compared to the second quarter of 2008, primarily driven by a 24% increase in the average balances of our Multifamily loan portfolio and significantly lower funding costs, partially offset by a decrease in prepayment fees, or yield maintenance income, and increased costs of capital reserves held for potential funding of our liquidity guarantees. See OFF-BALANCE SHEET ARRANGEMENTS for more information on our liquidity guarantees.

Non-interest income (loss) was $(140) million in the second quarter of 2009 compared to $(84) million in the second quarter of 2008. The increase in loss is attributed to higher losses on LIHTC partnerships in the second quarter of 2009. We invest as a limited partner in LIHTC partnerships formed for the purpose of providing equity funding for affordable multifamily rental properties. Our investments in LIHTC partnerships totaled $3.9 billion and $4.1 billion as of June 30, 2009 and December 31, 2008, respectively. Although these partnerships generate operating losses, we realize a return on our investment through reductions in income tax expense that result from tax credits. Our exposure is limited to the amount of our investment; however, the potential exists that we may not be able to utilize some

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previously taken or future tax credits. In consultation with our Conservator, we are considering potential transactions to realize the value of these interests, if market conditions are appropriate.

Non-interest expenses increased for the three and six months ended June 30, 2009 compared to the same periods in 2008, primarily due to increased provision for credit losses and REO operations expense. Our multifamily delinquency rates continued to increase in the second quarter and we expect further increases during the second half of 2009 as multifamily operators remain under pressure. Our REO property inventory has increased to seven properties as of June 30, 2009. REO operations expenses in the second quarter of 2009 relate to fair value write-down of the properties in inventory due to market conditions.

We continued to provide stability and liquidity for the financing of rental housing nationwide by continuing our purchases and credit guarantees of multifamily mortgage loans. In June 2009, we completed a structured securitization transaction with multifamily mortgage loans of approximately $1 billion. This Structured Transaction was backed by 62 multifamily loans and was one of the first large commercial mortgage bond issuances in the CMBS market this year. We may consider additional transactions in the future, if market conditions are appropriate.

CONSOLIDATED BALANCE SHEETS ANALYSIS

The following discussion of our consolidated balance sheets should be read in conjunction with our consolidated financial statements, including the accompanying notes. Also see CRITICAL ACCOUNTING POLICIES AND ESTIMATES for more information concerning our more significant accounting policies and estimates applied in determining our reported financial position.

Cash and Other Investments Portfolio

Table 17 provides detail regarding our cash and other investments portfolio.

Table 17 Cash and Other Investments Portfolio

	Fair Value	
	June 30, 2009	December 31, 2008
	(in millions)	
Cash and cash equivalents	$ 46,662	$ 45,326
Investments:		