

**Supplement dated November 13, 1992 to
Information Statement dated March 30, 1992**

Federal National Mortgage Association



This Supplement describes the financial condition of the Federal National Mortgage Association ("Fannie Mae" or the "Corporation") as of September 30, 1992 and contains unaudited financial statements with respect to the Corporation for the quarter and nine months ended September 30, 1992. This Supplement should be read in conjunction with the Corporation's Information Statement dated March 30, 1992 (the "Information Statement") and the Supplements dated May 15, 1992 and August 14, 1992 thereto (the "Supplements"), which are hereby incorporated by reference. The Information Statement describes the business and operations of the Corporation and contains financial data as of December 31, 1991. The May 15, 1992 and August 14, 1992 Supplements describe the financial condition of the Corporation as of March 31, 1992 and June 30, 1992, respectively, and contain unaudited financial statements with respect to the Corporation for the quarters ended March 31, 1992 and June 30, 1992, respectively. Each of the Supplements also describes legislative and regulatory developments. Fannie Mae also periodically makes available statistical information on its mortgage purchase and mortgage-backed securities volumes as well as other relevant information about Fannie Mae. Copies of the Corporation's current Information Statement, any supplements thereto and other available information can be obtained without charge from Paul Paquin, Senior Vice President—Investor Relations, Fannie Mae, 3900 Wisconsin Avenue, N.W., Washington, D.C. 20016 (telephone: 202-752-7115).

In conjunction with its securities offerings, the Corporation may incorporate this Supplement by reference in one or more other documents describing the securities offered thereby, the selling arrangements therefor, and other relevant information. Such other documents may be called an Offering Circular, Prospectus, Guide to Debt Securities or otherwise. This Supplement does not itself constitute an offer to purchase such securities.

Fannie Mae is a federally chartered corporation. Its principal office is located at 3900 Wisconsin Avenue, N.W., Washington, D.C. 20016 (202/752-7000). Its Internal Revenue Service employer identification number is 52-0883107.

At the close of business on October 30, 1992, 273,087,153 shares of the Corporation's common stock (without par value) were outstanding.

The delivery of this Supplement at any time shall not under any circumstances create an implication that there has been no change in the affairs of the Corporation since the date hereof or that the information contained herein is correct as of any time subsequent to its date.

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SELECTED FINANCIAL DATA

The following selected financial data for the three-month and nine-month periods ended September 30, 1992 and 1991 are unaudited and include, in the opinion of management, all adjustments (consisting of normal accruals) necessary for a fair presentation. Operating results for the periods ended September 30, 1992 are not necessarily indicative of the results expected for the entire year.

(Dollars in millions, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1992	1991	1992	1991
Income Statement Data:				
Interest income	\$ 3,390	\$ 3,158	\$ 10,013	\$ 9,428
Interest expense	2,883	2,702	8,499	8,107
Net interest income	507	456	1,514	1,321
Guaranty fees	215	173	612	492
Income from tax settlement	—	—	—	239
Gain (loss) on sales of mortgages, net	14	5	25	(45)
Miscellaneous income, net	51	28	132	70
Provision for losses	(80)	(80)	(240)	(290)
Administrative expenses	(97)	(81)	(278)	(231)
Income before federal income taxes and extraordinary item	610	501	1,765	1,556
Provision for federal income taxes	(188)	(150)	(544)	(468)
Income before extraordinary item	422	351	1,221	1,088
Extraordinary loss:				
Early extinguishment of debt	(9)	—	(24)	(86)
Net income	<u>\$ 413</u>	<u>\$ 351</u>	<u>\$ 1,197</u>	<u>\$ 1,002</u>
Per share:				
Earnings before extraordinary item:				
Primary	\$ 1.54	\$ 1.28	\$ 4.45	\$ 3.99
Fully diluted	1.54	1.28	4.45	3.98
Net earnings:				
Primary	1.51	1.28	4.36	3.67
Fully diluted	1.51	1.28	4.36	3.66
Cash dividends .....	.34	.26	.98	.74
September 30,				
	1992	1991		
Balance Sheet Data:				
Mortgage portfolio, net	\$142,683	\$122,331		
Total assets	170,055	139,619		
Borrowings:				
Due within one year	46,236	34,599		
Due after one year	108,996	92,901		
Total liabilities	163,602	134,352		
Stockholders' equity	6,453	5,267		
September 30,				
	1992	1991	1992	1991
Other Data:				
Net interest margin	1.33%	1.44%	1.39%	1.42%
Return on average equity	26.3	27.5	26.7	28.0
Return on average assets	1.0	1.0	1.0	1.0
Ratio of earnings to fixed charges	1.20:1	1.18:1	1.20:1	1.18:1
Dividend payout ratio	22.5%	20.2%	22.4%	19.9%
Equity to assets ratio	3.8	3.7	3.8	3.5
Mortgage purchases	\$ 14,621	\$ 9,284	\$ 50,713	\$ 25,381
MBS issued	41,332	31,904	136,369	79,781
MBS outstanding at period end(1)	429,935	351,917	429,935	351,917

(1) Included are Fannie Mae MBS held in the mortgage portfolio totaling \$18.4 billion and \$15.4 billion at September 30, 1992 and 1991, respectively.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS FOR THE THREE-MONTH AND
NINE-MONTH PERIODS ENDED SEPTEMBER 30, 1992**

Results of Operations

In the third quarter of 1992, Fannie Mae reported record earnings and business volumes as net income increased \$62 million or 18 percent from the \$351 million earned in the third quarter of 1991. For the first nine months of 1992, net income increased \$195 million or 19 percent from the \$1.002 billion earned in the first nine months of 1991. The improvement in net income for the three-month and nine-month periods ended September 30, 1992 was primarily the result of increases in net interest income, guaranty fees and miscellaneous income. In addition, net income for the first nine months of 1991 included a pre-tax loss of \$59 million from the sale of low-coupon mortgages, an extraordinary loss of \$86 million after-tax from the early extinguishment of debt and \$239 million of income as a result of the resolution of a tax case.

Net interest income in the third quarter of 1992 increased 11 percent compared with the third quarter of 1991, primarily due to a 15 percent growth in the average net mortgage portfolio. The increase in income generated by higher average balances in the mortgage portfolio was partially offset by the impact of prefunding of mortgage purchases in the third quarter of 1992. Net interest income increased 15 percent in the first nine months of 1992 compared with 1991, due primarily to a 15 percent increase in average interest-earning assets; the net interest margin declined two basis points in the same period, primarily attributable to lower reinvestment rates on short-term investment balances.

The following table presents an analysis of net interest income for the three-month and nine-month periods ended September 30, 1992 and 1991.

Net Interest Income and Average Balances

(Dollars in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1992	1991	1992	1991
Interest income:				
Mortgage portfolio	\$ 3,168	\$ 2,932	\$ 9,383	\$ 8,645
Investments and cash equivalents	222	226	630	783
Total interest income	<u>3,390</u>	<u>3,158</u>	<u>10,013</u>	<u>9,428</u>
Interest expense	<u>2,883</u>	<u>2,702</u>	<u>8,499</u>	<u>8,107</u>
Net interest income	507	456	1,514	1,321
Tax equivalent adjustment(1)	29	31	87	94
Net interest income tax equivalent basis	<u>\$ 536</u>	<u>\$ 487</u>	<u>\$ 1,601</u>	<u>\$ 1,415</u>
Average balances:				
Interest-earning assets:				
Mortgage portfolio, net(2)	\$140,083	\$121,295	\$135,765	\$118,228
Investments and cash equivalents	20,870	14,164	18,186	15,128
Total interest-earning assets	<u>\$160,953</u>	<u>\$135,459</u>	<u>\$153,951</u>	<u>\$133,356</u>
Interest-bearing liabilities	\$148,935	\$126,622	\$141,942	\$125,301
Interest-free funds	12,018	8,837	12,009	8,055
Total interest-bearing liabilities and interest-free funds	<u>\$160,953</u>	<u>\$135,459</u>	<u>\$153,951</u>	<u>\$133,356</u>
Average interest rates(1):				
Interest-earning assets:				
Mortgage portfolio, net	9.07%	9.72%	9.25%	9.81%
Investments and cash equivalents	4.26	6.50	4.67	7.03
Total interest-earning assets	<u>8.44</u>	<u>9.39</u>	<u>8.71</u>	<u>9.50</u>
Interest-bearing liabilities	7.69	8.51	7.92	8.61
Investment spread .....	.75	.88	.79	.89
Interest-free return(3) .....	.57	.56	.62	.52
Miscellaneous .....	.01	—	(.02)	.01
Net interest margin	<u>1.33%</u>	<u>1.44%</u>	<u>1.39%</u>	<u>1.42%</u>

- (1) Reflects pro forma adjustments to permit comparison of yields on tax-advantaged and taxable assets.
- (2) Includes average balance of nonperforming loans of \$1.1 billion and \$0.9 billion, for both the three-month and nine-month periods ended September 30, 1992 and 1991, respectively.
- (3) The return on that portion of the investment portfolio funded by equity and non-interest-bearing liabilities.

The following rate/volume analysis shows the relative contribution of asset and debt growth and interest rate changes to changes in net interest income for the three-month and nine-month periods ended September 30, 1992 and 1991.

Rate/Volume Analysis

(Dollars in millions)

	Third Quarter 1992 vs. Third Quarter 1991			First Nine Months 1992 vs. First Nine Months 1991		
	Increase (Decrease)	Attributable to Changes in (1)		Increase (Decrease)	Attributable to Changes in (1)	
		Volume	Rate		Volume	Rate
Interest income:						
Mortgage portfolio	\$236	\$434	\$(198)	\$ 738	\$1,231	\$(493)
Investments and cash equivalents ...	(4)	122	(126)	(153)	140	(293)
Total interest income	232	556	(324)	585	1,371	(786)
Interest expense	181	447	(266)	392	1,018	(626)
Net interest income	<u>\$ 51</u>	<u>\$109</u>	<u>\$(58)</u>	<u>\$ 193</u>	<u>\$ 353</u>	<u>\$(160)</u>

(1) Combined rate/volume variances, a third element of the calculation, are allocated to the rate and volume variances based on their relative size.

Guaranty fee income in the third quarter increased by \$42 million, or 24 percent, to \$215 million, resulting from a 23 percent increase in average Mortgage-Backed Securities ("MBS") outstanding when compared with the third quarter of 1991. For the first nine months of 1992, guaranty fee income increased by \$120 million, or 24 percent, to \$612 million, also resulting from a 24 percent increase in average MBS outstanding over the comparable period in 1991.

In the third quarter of 1992, miscellaneous income rose 83 percent to \$51 million versus \$28 million in the third quarter of 1991. For the first nine months of 1992, miscellaneous income rose 88 percent to \$132 million versus \$70 million in the first nine months of 1991. The increase in miscellaneous income was primarily a result of increased REMIC fee income and other MBS related fees which were derived from the continued increases in REMIC and MBS issuances. The increase in REMIC issuances was due to increased availability of collateral and increased investor demand.

The following table summarizes REMIC activity for the three-month and nine-month periods ended September 30, 1992 and 1991.

REMIC Issuances and Fees

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1992	1991	1992	1991
REMIC issuances (in billions)	\$50	\$31	\$125	\$68
Net fee income (in millions)	29	15	73	37

Administrative expenses for the quarter ended September 30, 1992 were \$97 million, compared with \$81 million during the same period in 1991. For the nine months ended September 30, 1992, administrative expenses were \$278 million, compared with \$231 million for the same period in 1991. Increased salaries and compensation-related expenses were the primary reasons for the overall increases. Compensation expense was \$53 million (55 percent of administrative expenses) in the third quarter of 1992, compared with \$47 million (58 percent) in the third quarter of 1991. For the first nine months of 1992, compensation expense was \$154 million (55 percent of administrative expenses), compared with \$136 million (59 percent) in the first nine months of 1991. The ratio of

administrative expenses to the average mortgage portfolio plus average MBS outstanding was .07 percent (annualized) for each of the periods presented.

The effective federal income tax rate for the three-month and nine-month periods ended September 30, 1992 was 31 percent, compared with 30 percent for the respective periods in 1991.

In the third quarter of 1992, the Corporation had an extraordinary loss of \$14 million (\$9 million after tax) from the repurchase or call of debt. There was no loss from the repurchase or call of debt in the third quarter of 1991. An extraordinary loss of \$37 million (\$24 million after tax) was reported in the first nine months of 1992 from the repurchase or call of debt compared with a loss of \$131 million (\$86 million after tax) in the same period in 1991.

Credit Data

The following table shows the Corporation's serious delinquencies, foreclosures and net charge-offs as of September 30, 1992 and 1991.

	Delinquency Rate (1)		Number of Properties Acquired				Net Charge-offs (Dollars in millions)			
			Three Months Ended		Nine Months Ended		Three Months Ended		Nine Months Ended	
	September 30, 1992	September 30, 1991	September 30, 1992	September 30, 1991	September 30, 1992	September 30, 1991	September 30, 1992	September 30, 1991	September 30, 1992	September 30, 1991
Single-family .....	.61%	.61%	2,470	1,913	7,099	5,545	\$54	\$35	\$144	\$107
Multifamily	2.81	2.96	10	9	19	23	9	20	34	46
Total							\$63	\$55	\$178	\$153

(1) Single-family serious delinquency rates are based on the number of loans delinquent 90 days or more and all delinquent loans in foreclosure or in relief. Multifamily serious delinquency rates are based on the unpaid principal balance of loans delinquent 60 days or more. All serious delinquency rates are based on loans in portfolio and underlying MBS for which the Corporation has the primary risk of loss.

Due to the increasing volume of loans outstanding and the likely effects of previous quarters' higher levels of delinquent loans, management expects an increase in acquisitions of foreclosed properties during the last quarter of 1992.

The inventory of single-family properties was 4,001 as of September 30, 1992, compared with 3,306 properties as of September 30, 1991. The inventory of multifamily properties was 32 as of September 30, 1992, compared with 28 properties as of September 30, 1991.

Balance Sheet Analysis

Mortgage Portfolio

The Corporation purchased \$14.6 billion of mortgages at an average yield of 7.55 percent in the third quarter of 1992, compared with \$9.3 billion of mortgages at an average yield of 9.03 percent in the third quarter of 1991. In the first nine months of 1992, mortgage purchases were \$50.7 billion at an average yield of 7.91 percent, compared with \$25.4 billion at an average yield of 9.14 percent in the first nine months of 1991. The increase in mortgage purchases in 1992 has been primarily due to an increase in the number of mortgages offered for sale in the secondary market, resulting, in large part, from the high level of refinancing activity because of a significant decline in mortgage rates.

Mortgage loan repayments during the third quarter of 1992 totaled \$8.6 billion, compared with \$4.1 billion in the third quarter of 1991. During the first nine months of 1992, mortgage loan repayments were \$25.7 billion compared with \$11.5 billion in the first nine months of 1991. The increase in loan repayments was primarily due to the high level of refinancing activity. Sales from portfolio totaled \$3.1 billion for the third quarter of 1992 compared with \$2.9 billion for the third

quarter of 1991, while sales from portfolio totaled \$8.5 billion for the first nine months of 1992 compared with \$5.0 billion for the first nine months of 1991.

As of September 30, 1992, the net mortgage portfolio totaled \$142.7 billion with a yield (before deducting the allowance for losses) of 8.95 percent, compared with \$126.5 billion at 9.54 percent as of December 31, 1991 and \$122.3 billion at 9.68 percent as of September 30, 1991. The decrease in yield was primarily due to a decline in conventional mortgage purchase yields as interest rates declined.

At September 30, 1992, the Corporation had mandatory delivery commitments and lender option commitments outstanding to purchase \$9.2 billion and \$10.1 billion of mortgage loans, respectively, compared with \$4.7 billion and \$5.6 billion, respectively, of such commitments outstanding at December 31, 1991.

Financing and Other Activities

The following table sets forth the amount and average cost of debt issued and repaid during the three-month and nine-month periods ended September 30, 1992 and 1991, and the debt outstanding at September 30 for each of those periods.

Debt Issued, Repaid and Outstanding

(Dollars in millions)

	Three Months Ended September 30,				Nine Months Ended September 30,			
	1992		1991		1992		1991	
	Amount	Average Cost	Amount	Average Cost	Amount	Average Cost	Amount	Average Cost
Debt Issued								
Short-term	\$ 42,572	2.84%	\$ 35,065	5.51%	\$135,635	3.57%	\$113,719	5.93%
Long-term	8,875	5.77	6,572	8.05	22,886	6.34	19,213	8.21
	<u>\$ 51,447</u>	<u>3.36%</u>	<u>\$ 41,637</u>	<u>5.96%</u>	<u>\$158,521</u>	<u>3.98%</u>	<u>\$132,932</u>	<u>6.26%</u>
Debt Repaid								
Short-term	\$ 40,124	3.24%	\$ 35,925	5.79%	\$123,440	3.77%	\$115,036	6.32%
Long-term	5,184	8.51	5,051	8.17	13,514	8.82	14,063	8.56
	<u>\$ 45,308</u>	<u>3.85%</u>	<u>\$ 40,976</u>	<u>6.08%</u>	<u>\$136,954</u>	<u>4.27%</u>	<u>\$129,099</u>	<u>6.56%</u>
Debt Outstanding at September 30	<u>\$155,232</u>	<u>7.49%</u>	<u>\$127,460</u>	<u>8.49%</u>	<u>\$155,232</u>	<u>7.49%</u>	<u>\$127,460</u>	<u>8.49%</u>

The average cost of debt outstanding at September 30, 1992, December 31, 1991 and September 30, 1991 was 7.49 percent, 8.25 percent and 8.49 percent, respectively.

The Corporation's statutory debt-to-capital ratio at September 30, 1992 was 17.7:1, compared with 15.7:1 at September 30, 1991. A statutory debt-to-capital ratio is no longer required because of the legislation described in the "Recent Legislative and Regulatory Developments" section.

The Corporation's shareholders' equity at September 30, 1992 was \$6.5 billion, compared with \$5.5 billion at December 31, 1991.

On October 20, 1992, the Board of Directors approved an increase in the dividend on the Corporation's common stock to 40 cents per share for the quarter ended September 30, 1992 from 34 cents per share. As of September 30, 1992, there were 273 million shares of common stock outstanding.

Mortgage-Backed Securities

The Corporation issued \$41.3 billion of MBS during the third quarter of 1992, compared with \$31.9 billion in the third quarter of 1991. MBS issued in the first nine months of 1992 totaled \$136.4

billion compared with \$79.8 billion in the first nine months of 1991. The increase in MBS issuances was primarily due to the high level of refinancing activity which resulted from lower interest rates.

The following table summarizes MBS activity for the three-month and nine-month periods ended September 30, 1992 and 1991.

Summary of MBS Activity

(Dollars in millions)

Three Months Ended September 30,	Issued				Outstanding (1)		
	Lender Originated (1)			Total	Lender Risk (2)	Fannie Mae Risk (3)	Total (4)
	Lender Risk	Fannie Mae Risk	Fannie Mae Originated				
1992	\$2,556	\$ 35,647	\$ 3,129	\$ 41,332	\$85,191	\$344,744	\$429,935
1991	2,368	24,774	4,762	31,904	95,848	256,069	351,917
Nine Months							
Ended September 30,							
1992	\$9,286	\$115,415	\$11,668	\$136,369			
1991	7,145	65,103	7,533	79,781			

- (1) This table classifies lender originated MBS issued and MBS outstanding based on primary default risk category; however, Fannie Mae bears the ultimate risk of default on all MBS. MBS outstanding includes MBS that have been pooled to back Megas, SMBS, or REMICs.
- (2) Included in lender risk are \$40.9 billion and \$39.1 billion at September 30, 1992 and 1991, respectively, on which the lender or a third party agreed to bear default risk limited to a certain portion or percentage of the loans delivered and, in some cases, the lender has pledged collateral to secure that obligation.
- (3) Included are \$8.3 billion at September 30, 1992 and \$9.5 billion at September 30, 1991, which are backed by government insured or guaranteed mortgages.
- (4) Included are \$18.4 billion and \$15.4 billion at September 30, 1992 and 1991, respectively, of Fannie Mae MBS in portfolio.

The increase in MBS outstanding where Fannie Mae has primary default risk is primarily due to lender reaction to capital rules that require lenders to have more capital for MBS where they bear default risk.

New Accounting Standard

On April 28, 1992, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants issued *Statement of Position No. 92-3, "Accounting for Foreclosed Assets."* The new accounting standard is described in the August 14, 1992 Supplement.

RECENT LEGISLATIVE AND REGULATORY DEVELOPMENTS

Public Law 102-550, which includes the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the "Act"), was signed by the President of the United States on October 28, 1992. The Act establishes capital standards for Fannie Mae and Freddie Mac and establishes an independent Office of Federal Housing Enterprise Oversight within the Department of Housing and Urban Development ("HUD") to oversee regulatory and capital requirements. Portions of the Act became effective when the Act was signed. Other portions will become effective on January 1, 1993, and others at dates relating to the appointment of the Director of the new regulatory office.

Under the Act, Fannie Mae and Freddie Mac will be tested against three capital "enforcement" levels. The risk-based capital level will be 130 percent of the amount necessary to withstand 10 years

during which there are severe credit stresses on the corporations' mortgages nationwide and substantial increases or decreases in interest rates, with the extra 30 percent designed to protect against management and operations risk. Both corporations also will be required to have equity that equals or exceeds a minimum level equal to 2.5 percent of on-balance-sheet assets, plus .45 percent of outstanding mortgage-backed securities and equivalent instruments and a percentage (determined by the Director of the Federal Housing Enterprise Oversight Office (the "Director")) of other off-balance-sheet assets, excluding commitments in excess of 50 percent of the average amount of commitments outstanding over the 12-month period immediately preceding the date for which the amount is being computed. The corporations also will be required to meet a critical equity capital level equal to 1.25 percent of on-balance-sheet assets plus .25 percent of off-balance-sheet mortgage-backed securities outstanding and equivalent instruments and a Director-determined percentage of other off-balance-sheet assets. During the first 18 months after enactment of this Act, capital requirements will equal the sum of 2.25 percent of on-balance-sheet assets, 0.4 percent of outstanding mortgage-backed securities and equivalent instruments, and a Director-determined percentage of other off-balance-sheet assets, excluding commitments to purchase mortgages or issue securities in excess of 50 percent of the average amount of commitments outstanding over the 12-month period immediately preceding the date for which the amount is being computed. The Act further provides that, until one year after the regulations establishing the risk-based level go into effect, Fannie Mae and Freddie Mac shall be deemed to meet the risk-based capital level as long as they meet the minimum equity level. If capital falls below the risk-based capital level, regulatory oversight will become more intense and the Director could take such measures as limiting dividend payments. If capital also falls below the minimum equity level, the Director could also limit the increase in obligations and growth in assets. The Director is given enforcement powers that include the power to impose temporary and final cease-and-desist orders and civil penalties on Fannie Mae or Freddie Mac and on a director or executive officer of Fannie Mae or Freddie Mac.

The Act also provides for new affordable housing requirements. The Secretary of HUD is required to set goals for (1) low- and moderate-income housing, (2) housing in central cities, rural areas, and other underserved areas, and (3) "special affordable housing" for low- and very low-income families. During the first two years after enactment (the "transition period"), the Act sets initial interim targets for each of the first two goals (units could qualify to meet both goals) equal to 30 percent of the total number of units financed. Thereafter, the Secretary of HUD is authorized to set annual goals, which could be higher or lower than the interim targets. During the transition period, the special affordable housing goals for Fannie Mae and Freddie Mac total \$2 billion and \$1.5 billion, respectively, of mortgage purchases, divided equally between 1-to-4 family and multifamily housing. Thereafter, the Secretary of HUD is authorized to set an annual special affordable housing goal that is not less than one percent of the dollar amount of the applicable corporation's mortgage purchases in the previous year. The Act expressly provides that in certain cases if either Fannie Mae or Freddie Mac failed to meet any housing goal or failed to comply with related reporting requirements, the Secretary of HUD could, after determining whether meeting the goal was indeed feasible, require the corporation to submit a housing plan indicating how it intended to meet the goal. The Secretary of HUD could, after a formal hearing on the record, impose cease and desist orders and civil money penalties on the corporation for failure to submit a plan or to make a good faith effort to meet an approved plan.

The Act also provides that the Secretary of HUD must approve any new program that is significantly different from those previously approved or engaged in. The Secretary is required to approve any new program unless it is not authorized by the charter act of the corporation or the Secretary finds that it is not in the public interest. However, until one year after the final regulations establishing the risk-based capital test are in effect, the Secretary must disapprove a new program if the Director determines that the program "would risk significant deterioration of the financial condition" of the corporation.

The Act also made other changes that affect the description of government regulation of Fannie Mae under "Government Regulation and Charter Act" in the Information Statement. Approval of the Secretary of HUD is no longer required for the Corporation's issuance of stock and securities convertible into stock, but the Director could require that the Director approve such issuances if the Corporation fails to meet certain minimum capital standards. The Secretary of HUD also no longer has authority to audit and examine the books and financial transactions of the Corporation, but the Director has authority to do so. The General Accounting Office also has authority to audit the Corporation's programs, activities, receipts, expenditures and financial transactions.

The Act also eliminated the Charter Act provisions regarding the authority of the Corporation to require nonrefundable capital contributions from mortgage sellers and requiring that each servicer of the Corporation own a minimum amount of common stock. The Corporation was not imposing a capital contribution requirement on mortgage sellers at the time the Act was enacted, and the common stock ownership requirement for servicers at that time was only one share.

The Act further provides that one of the members of the Corporation's Board of Directors appointed by the President of the United States must be from an organization that has represented consumer or community interests for not less than two years, or a person who has demonstrated a career commitment to providing housing for low-income households. The Act also provides that the President of the United States may remove for good cause only members of the Corporation's Board of Directors who were appointed by the President.

In addition, the Act amended the stated purposes of the Corporation in the Charter Act by adding an additional purpose providing that the Corporation is "to promote access to mortgage credit throughout the Nation (including central cities, rural areas, and underserved areas) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing." One of the Corporation's purposes also is to provide ongoing assistance to the secondary market for home mortgages, including mortgages securing housing for low- and moderate-income families involving "a reasonable economic return" to the Corporation, by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for home mortgage financing. The Act amended that stated purpose by adding that "a reasonable economic return" may be less than the return earned on the Corporation's other activities.

Management believes that the Act creates a workable regulatory framework that sets tough, but fair, requirements for the capital that the Corporation needs to cover the risks of its business.

Under the Comprehensive National Energy Policy Act of 1992 (H.R. 776), effective for payments on or after January 1, 1993 on securities the Corporation has issued, the federal backup withholding tax rate has been increased from 20% to 31%.

LEGAL PROCEEDINGS

A trial in the Tax Court was held in April 1992, and legal briefs were filed in July and September 1992, with respect to the litigation between the Internal Revenue Service ("IRS") and Fannie Mae involving hedging transactions in 1984 and 1985 that is described in the Information Statement.

In May 1992, the IRS completed its audit of the Corporation's tax returns for 1986 and 1987. The Corporation has begun the IRS administrative appeal procedure relating to the proposed deficiencies described in the Information Statement.

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FEDERAL NATIONAL MORTGAGE ASSOCIATION
INTERIM FINANCIAL STATEMENTS
CONDENSED STATEMENTS OF INCOME

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30	
	1992	1991	1992	1991
	(Dollars in millions, except per share amounts)			
Interest income	\$3,390	\$3,158	\$10,013	\$9,428
Interest expense	2,883	2,702	8,499	8,107
Net interest income	507	456	1,514	1,321
Guaranty fees	215	173	612	492
Income from tax settlement	—	—	—	239
Gain (loss) on sales of mortgages, net	14	5	25	(45)
Miscellaneous income, net	51	28	132	70
Provision for losses	(80)	(80)	(240)	(290)
Administrative expenses	(97)	(81)	(278)	(231)
Income before federal income taxes and extraordinary item	610	501	1,765	1,556
Provision for federal income taxes	(188)	(150)	(544)	(468)
Income before extraordinary item	422	351	1,221	1,088
Extraordinary loss — early extinguishment of debt	(9)	—	(24)	(86)
Net income	<u>\$ 413</u>	<u>\$ 351</u>	<u>\$ 1,197</u>	<u>\$1,002</u>
Per share:				
Earnings before extraordinary item:				
Primary	\$ 1.54	\$ 1.28	\$ 4.45	\$ 3.99
Fully diluted	1.54	1.28	4.45	3.98
Net earnings:				
Primary	1.51	1.28	4.36	3.67
Fully diluted	1.51	1.28	4.36	3.66
Cash dividends	0.34	0.26	0.98	0.74

CONDENSED BALANCE SHEETS

(Unaudited)

	September 30, 1992	December 31, 1991
		(Dollars in millions)
Assets		
Mortgage portfolio, net	\$142,683	\$126,486
Investments	14,334	10,999
Cash and cash equivalents	7,398	3,194
Other assets	5,640	6,393
Total assets	<u>\$170,055</u>	<u>\$147,072</u>
Liabilities		
Debentures		
Due within one year	\$ 46,236	\$ 34,608
Due after one year	108,996	99,329
Other liabilities	8,370	7,588
Total liabilities	163,602	141,525
Stockholders' equity	6,453	5,547
Total liabilities and stockholders' equity	<u>\$170,055</u>	<u>\$147,072</u>

See Notes to Interim Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION
CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

	<u>Three Months</u> <u>Ended</u> <u>September 30,</u>		<u>Nine Months</u> <u>Ended</u> <u>September 30,</u>	
	<u>1992</u>	<u>1991</u>	<u>1992</u>	<u>1991</u>
	(Dollars in millions)			
Net cash provided by operating activities	\$ 1,349	\$ 778	\$ 3,046	\$ 2,585
Cash flows from investing activities:				
Purchase of mortgages	(14,737)	(9,260)	(50,760)	(25,268)
Proceeds from sales of mortgages	3,115	2,888	8,534	4,986
Mortgage principal repayments	8,803	4,161	26,201	11,886
Net decrease (increase) in investments	<u>(5,544)</u>	<u>1,127</u>	<u>(3,335)</u>	<u>1,063</u>
Net cash used by investing activities	<u>(8,363)</u>	<u>(1,084)</u>	<u>(19,360)</u>	<u>(7,333)</u>
Cash flows from financing activities:				
Cash proceeds from issuance of debt	51,332	41,414	157,793	132,135
Cash payments to retire debt	(45,317)	(40,976)	(136,978)	(129,185)
Other	<u>(92)</u>	<u>(69)</u>	<u>(297)</u>	<u>315</u>
Net cash provided by financing activities	<u>5,923</u>	<u>369</u>	<u>20,518</u>	<u>3,265</u>
Net increase (decrease) in cash and cash equivalents ...	(1,091)	63	4,204	(1,483)
Cash and cash equivalents at beginning of period	<u>8,489</u>	<u>2,632</u>	<u>3,194</u>	<u>4,178</u>
Cash and cash equivalents at end of period	<u>\$ 7,398</u>	<u>\$ 2,695</u>	<u>\$ 7,398</u>	<u>\$ 2,695</u>

NOTES TO INTERIM FINANCIAL STATEMENTS
(Unaudited)

Basis of Presentation

The accompanying unaudited condensed financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month and nine-month periods ended September 30, 1992 are not necessarily indicative of the results that may be expected for the year ending December 31, 1992. The unaudited interim financial statements should be read in conjunction with the audited financial statements and notes to financial statements that are presented in the Information Statement dated March 30, 1992.

NOTES TO INTERIM FINANCIAL STATEMENTS (Continued)

Commitments and Contingencies

The Corporation had outstanding commitments to purchase mortgages and to issue MBS as shown below:

	<u>September 30, 1992</u> (Dollars in billions)
Commitments to purchase mortgages:	
Mandatory delivery	\$ 9.2
Lender option(1)	8.3
Average net yield on mandatory delivery	7.27%
Commitments to issue MBS:	
Mandatory delivery(1)	\$ 1.0
Lender option(1)	6.0
Master commitments(2)	57.5

(1) Excludes commitments attached to master commitments, which are included in the total for master commitments.

(2) Under a master commitment, a lender must either deliver under an MBS contract at a specified guaranty fee or enter into a mandatory portfolio commitment with the yield established upon executing the portfolio commitment.

The Corporation also guarantees timely payment of principal and interest on outstanding MBS as summarized below:

	<u>September 30, 1992</u> (Dollars in billions)
Total MBS outstanding	\$429.9
Amount for which the Corporation has primary foreclosure loss risk(1):	
Conventional	336.4
Government-insured or guaranteed	8.3

(1) The Corporation, however, assumes the ultimate risk of loss on all MBS.

Extraordinary Loss

In the third quarter of 1992, the Corporation reported an extraordinary loss of \$14 million (\$9 million after tax) from the repurchase or call of debt. There was no loss on the repurchase or call of debt in the third quarter of 1991. An extraordinary loss of \$37 million (\$24 million after tax) was reported in the first nine months of 1992 from the repurchase or call of debt compared with an extraordinary loss of \$131 million (\$86 million after tax) in the first nine months of 1991.

Income From Resolution of Tax Case

In April 1991, the Supreme Court denied the IRS's petition for certiorari in the Corporation's case relating to concurrent mortgage sales. As a result, the Corporation recognized \$239 million of income in the second quarter of 1991.

COMPUTATION OF EARNINGS PER SHARE

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1992	1991	1992	1991
	(In millions, except per share data)			
Primary Earnings Per Share:				
Average common shares outstanding	273.0	272.9	273.1	268.4
Effect of common stock equivalents	<u>1.1</u>	<u>1.6</u>	<u>1.1</u>	<u>4.5</u>
Average primary shares outstanding	<u>274.1</u>	<u>274.5</u>	<u>274.2</u>	<u>272.9</u>
Income before extraordinary item	\$ 422	\$ 351	\$1,221	\$1,088
Net income	413	351	1,197	1,002
Primary earnings per share before extraordinary item	\$ 1.54	\$ 1.28	\$ 4.45	\$ 3.99
Primary earnings per share	1.51	1.28	4.36	3.67
Fully Diluted Earnings Per Share:				
Average common shares outstanding	273.0	272.9	273.1	268.4
Effect of common stock equivalents	<u>1.2</u>	<u>1.8</u>	<u>1.3</u>	<u>5.2</u>
Average fully diluted shares outstanding	<u>274.2</u>	<u>274.7</u>	<u>274.4</u>	<u>273.6</u>
Income before extraordinary item	\$ 422	\$ 351	\$1,221	\$1,088
Net income	413	351	1,197	1,002
Fully diluted earnings per share before extraordinary item	\$ 1.54	\$ 1.28	\$ 4.45	\$ 3.98
Fully diluted earnings per share	1.51	1.28	4.36	3.66