Information Statement

Federal National Mortgage Association

This Information Statement describes the business and operations of the Federal National Mortgage Association ("Fannie Mae" or the "Corporation") as of the date hereof and its financial condition as of December 31, 1991. In conjunction with its securities offerings, the Corporation may incorporate this Information Statement 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 Information Statement does not itself constitute an offer to purchase such securities. Any incorporation of this Information Statement by reference shall be deemed to include all supplements hereto, which can be obtained as provided under "Documents Incorporated by Reference."

This Information Statement contains audited financial statements with respect to the Corporation for the year ended December 31, 1991. Fannie Mae updates its Information Statement quarterly.

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).

The Corporation's securities are not required to be registered under the Securities Act of 1933. The aggregate market value of the voting stock held by persons other than officers and directors of the Corporation, based on the closing price on the New York Stock Exchange on January 31, 1992, was approximately $17.7 billion. The number of shares outstanding of the Corporation's common stock (without par value) as of March 27, 1992 was 273,089,191.

The delivery of this Information Statement 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.

March 30, 1992

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DOCUMENTS INCORPORATED BY REFERENCE

The Corporation's Proxy Statement for the 1992 Annual Meeting of Shareholders is incorporated by reference herein under "Management—Additional Information." Any later proxy statement published by the Corporation prior to the Corporation's publication of a new Information Statement is incorporated herein by this reference. Copies of the Corporation's current Information Statement and any supplements thereto, as well as its most recent proxy statement, can be obtained without charge from Paul Paquin, Senior Vice President—Investor Relations, Fannie Mae, 3900 Wisconsin Avenue, NW, Washington, DC 20016 (telephone: 202-752-7115).

AVAILABLE INFORMATION

Copies of the Corporation's annual and quarterly reports to shareholders, the Federal National Mortgage Association Charter Act, the Corporation's bylaws, and other information regarding the Corporation can be obtained from the person indicated under "Documents Incorporated by Reference." Reports and other information concerning the Corporation also may be inspected at the offices of the New York Stock Exchange, the Midwest Stock Exchange, and the Pacific Stock Exchange. The Corporation is not subject to the periodic reporting requirements of the Securities Exchange Act of 1934.

BUSINESS

General

The Federal National Mortgage Association (the "Corporation" or "Fannie Mae") is a federally chartered and stockholder-owned corporation organized and existing under the Federal National Mortgage Association Charter Act, 12 U.S.C. § 1716 *et seq.* (the "Charter Act"). See "Government Regulation and Charter Act." It is the largest investor in home mortgage loans in the United States. The Corporation was originally established in 1938 as a United States government agency to provide supplemental liquidity to the mortgage market and was transformed into a stockholder-owned and privately managed corporation by legislation enacted in 1968.

The Corporation provides funds to the mortgage market by purchasing mortgage loans from lenders, thereby replenishing their funds for additional lending. To purchase loans, the Corporation acquires funds from various capital markets and from many capital market investors that may not ordinarily invest in mortgage loans, thereby expanding the total amount of funds available for housing. Operating nationwide, the Corporation helps to redistribute mortgage funds from capital-surplus to capital-short areas.

The Corporation also issues mortgage-backed securities ("MBS"). The Corporation receives guaranty fees for its guaranty of timely payment of principal of and interest on MBS certificates. The Corporation issues MBS primarily in exchange for pools of mortgage loans from lenders. The issuance of MBS enables the Corporation to further its statutory purpose of increasing the liquidity of residential mortgage loans.

In this document, both whole loans and participation interests in loans are referred to as "loans," "mortgage loans," and "mortgages." (The Corporation purchases participation interests that range from 50 to 99 percent.) The term "mortgage" also is used to refer to the security instrument securing a loan rather than the loan itself, and when so used also refers to a deed of trust.

Mortgage Loan Portfolio

Mortgage Loans Purchased

The Corporation purchases primarily single-family, conventional, fixed- or adjustable-rate, first mortgage loans, but it also purchases other types of residential mortgage loans for its loan portfolio, including mortgage loans insured by the Federal Housing Administration ("FHA"), mortgage loans guaranteed by the Veterans Administration ("VA"), multifamily mortgage loans (*i.e.* loans secured by more than four dwelling units) and second mortgage loans (*i.e.* loans secured by second liens). The Corporation's purchases have a variety of maturities. The Corporation's purchases of adjustable-rate mortgage loans ("ARMs"), fixed-rate loans with intermediate terms of 20 years or less, and second mortgage loans are designed to assist in mitigating the risks associated with rising interest rates, to match more closely the generally shorter maturities of its borrowings, and to provide a secondary market for a variety of loans that may be attractive to potential homeowners.

The composition of the Corporation's loan portfolio during the last five years is shown in the table in "Portfolio Composition." The composition of its purchases during the last three years is shown in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Mortgage Portfolio." Of the total single-family and multifamily mortgage loans that the Corporation purchased in 1991, approximately 46 percent were from mortgage banking companies, 18 percent were from savings and loan associations, 19 percent were from commercial and mutual savings banks, and 17 percent were from other institutions.

Principal Balance Limits. Maximum principal balance limits apply to the Corporation's mortgage loan purchases. The Corporation may not purchase conventional mortgage loans on one-family dwellings if the loan's original principal balance exceeds $202,300, except for loans secured by properties in Alaska and Hawaii. Higher principal balance limits apply to loans secured by properties

in those states or secured by two or more family dwelling units. The maximum principal balance limits applicable to such conventional mortgage loans secured by one- to four-family dwellings can be adjusted annually based on the national average price of a one-family dwelling as surveyed by the Office of Thrift Supervision. On January 1, 1992, the limitation for one-family dwellings was increased from $191,250 to the current level.

Under the Charter Act, maximum principal balance limits also apply to the Corporation's purchases of conventional multifamily mortgage loans. Such limits are affected by the location of the unit and other factors.

FHA-insured mortgage loans are subject to statutory maximum amount limitations. The Corporation will not purchase VA-guaranteed mortgage loans that have principal amounts in excess of amounts the Corporation specifies from time to time.

Fixed-Rate/Adjustable-Rate. Substantially all fixed-rate mortgage loans purchased by the Corporation provide for level monthly installments of principal and interest. Some of these loans (9% of the portfolio at December 31, 1991) have balloon payments due after 7 or 10 years, but with monthly payments based on 30-year amortization schedules. Many of the 7-year balloon mortgage loans permit the borrower to refinance the balloon payment at maturity with a 23-year fixed-rate mortgage loan.

The interest rates on ARMs are determined by formulas providing for automatic adjustment, up or down, at specified intervals in accordance with changes in a specified index. Substantially all ARMs provide for adjustments (up or down) in the amount of monthly installments after the interest rate on the loan is adjusted because of changes in the applicable index. The Corporation purchases ARMs only if the ARMs have a cap on the amount the interest rate may change over the life of the loan. A substantial number of the ARMs purchased by the Corporation provide the mortgagor with the option, at specified times or during specified periods of time, to convert the ARM to a fixed-rate mortgage loan with payment of a small fee.

In 1990, the Corporation began purchasing conventional mortgage loans that have one interest rate for the first 5 or 7 years and then adjust automatically to another interest rate for the next 25 or 23 years, respectively. Such loans, in the aggregate, represented approximately 48 percent of the Corporation's ARM purchases and approximately 6 percent of its portfolio loan purchases in 1991.

Maturity. The Corporation currently purchases conventional, single-family fixed- and adjustable-rate mortgage loans with original maturities of up to 30 years and 40 years, respectively. Only a small portion of such ARMs purchased have maturities of more than 30 years. The multifamily mortgage loans that the Corporation currently purchases generally are conventional fixed-rate loans that have an effective term not exceeding 15 years.

Repayments

The majority of the mortgage loans in the Corporation's portfolio are prepayable by the borrower (in some cases with a small penalty). Therefore, the Corporation bears the risk that prepayments may increase when interest rates decline significantly or as a result of other factors. The Corporation manages this risk as described in "Management's Discussion and Analysis of Financial Condition and Results of Operations — Management of Interest Rate and Credit Risk — Management of Interest Rate Risk."

Portfolio Composition

The following table shows the composition of the Corporation's mortgage loan portfolio and the weighted-average yield (net of servicing) on the mortgage loan portfolio. The table includes mortgage loans that back MBS held in the Corporation's mortgage loan portfolio.

Mortgage Loan Portfolio Composition

(Dollars in millions)

	Year Ended December 31,				
	1991	**1990**	**1989**	**1988**	**1987**
Unpaid Principal Balances ("UPB") at End of Period					
Single-family: Government insured or guaranteed	$ 9,900	$ 11,204	$ 11,857	$ 12,235	$13,306
Conventional: 30-year fixed-rate	57,643	50,846	47,768	43,060	43,929
Intermediate-term fixed-rate	26,534	21,409	19,036	17,937	17,384
Adjustable-rate	20,941	20,737	22,020	21,040	13,723
Second mortgage	2,069	1,885	1,614	1,561	1,421
Multifamily	11,896	10,547	8,426	7,180	6,983
Total UPB	$128,983	$116,628	$110,721	$103,013	$96,746
Average yield	9.54%	9.94%	10.03%	9.84%	9.98%

Underwriting Guidelines

The Corporation has established certain underwriting guidelines for purchases of conventional mortgage loans in an effort to reduce the risk of loss from mortgagor defaults. These guidelines are designed to assess the creditworthiness of the mortgagor as well as the value of the mortgaged home relative to the amount of the mortgage loan. The Corporation, in its discretion, accepts deviations from the guidelines. The Corporation generally relies on lender representations to ensure that the mortgage loans it purchases conform to its underwriting guidelines, which the Corporation changes from time to time.

For single-family mortgages, the Corporation generally requires that the unpaid principal amount of each conventional first mortgage loan it purchases not be greater than 80 percent of the value of the mortgaged property unless the excess over 75 percent is insured by a mortgage insurance company acceptable to the Corporation. Mortgage insurance is required for as long as the principal balance of the mortgage loan is greater than 80 percent of the original value (or of the appraised value as determined by a subsequent appraisal). The Corporation is not requiring mortgage insurance on such loans with loan-to-value ratios greater than 80 percent if the mortgage loan seller provides other credit enhancement. The Corporation bears the risk that in some cases mortgage insurers or lenders may be unable to satisfy fully their obligations. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Management of Interest Rate and Credit Risk—Management of Credit Risk."

Commitments

The Corporation issues commitments to purchase, at a later date, a specified dollar amount of mortgage loans. The Corporation purchases mortgage loans through standard product commitments with posted yields and through negotiated commitments.

The Corporation purchases most of its mortgage loans pursuant to mandatory delivery commitments. Under such commitments, lenders are obligated to sell loans to the Corporation at the commitment yield. Mandatory delivery commitments are available for standard product and negotiated transactions. If a lender is not able to deliver the mortgage loans required under a mandatory delivery commitment, the lender may buy back the commitment at any time during the commitment term for a fee.

The Corporation issues master commitments to lenders to facilitate the delivery of mortgages into MBS pools or portfolio. In order to deliver under a master commitment, a lender must either deliver MBS or convert to a mandatory delivery mortgage purchase commitment with the yield established at the time of conversion.

The Corporation also issues to lenders negotiated standby commitments that commit the Corporation to purchase a designated dollar amount of single-family mortgage loans from the lenders if they convert their standby commitments to mandatory delivery commitments. Standby commitments do not obligate the lenders to sell the loans to the Corporation; they are obligated to do so only after such commitments are converted to mandatory delivery commitments. The yield on the mortgage loans is established at the time of the conversion in the case of standby commitments. The combined term of the standby and mandatory commitments currently can be up to 14 months. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Liquidity Management."

Affordable Housing Initiative

In March 1991, the Corporation announced a four-year, $10 billion housing initiative to improve and increase the Corporation's delivery of home mortgage funds to low- and moderate-income families and others with special needs. Under this initiative, the Corporation is creating new products and expanding the use of existing ones to help meet the needs such families have in accumulating down payments and other funds to cover closing costs and monthly housing expenses. The Corporation's plan is to produce $10 billion in commitments for low- and moderate-income and other special housing needs by July 1993 and to have $10 billion in mortgage loans delivered under such commitments by December 31, 1994.

Among other things, the Corporation is offering commitments to purchase a variety of new products, including employer-assisted loans. One new product is the "3/2 Option," whereby home buyers may qualify for the minimum 5 percent down payment requirement by using 3 percent of their own funds and obtaining the remaining 2 percent in the form of a gift from a family member or a grant or unsecured loan from a non-profit organization or public entity. Under the 3/2 Option, the percentage of monthly gross income that may be used for monthly housing expenses is raised from the customary 28 percent to 33 percent of income. As part of its affordable housing initiative, the Corporation also is expanding its public finance activities with state and local housing finance agencies, increasing its tax-credit equity investments in low-income rental housing, and developing new mortgage products for the elderly and residents in rural communities.

Under proposed legislation pending in Congress, the Corporation would be required to set certain goals to promote affordable housing for low- and very low-income families consistent with the Corporation's overall mission. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments."

Servicing

The Corporation does not service mortgage loans held in the portfolio, except for government-insured multifamily loans and loans that have been foreclosed. Fannie Mae mortgage loans can be serviced only by a servicer approved by the Corporation. Lenders who sell single-family mortgage loans and conventional multifamily loans to the Corporation often retain the responsibility for servicing the mortgage loans sold, subject to the Corporation's guidelines. Servicing includes the collection and remittance of principal and interest payments, administration of escrow accounts, collection of insurance claims, and, if necessary, processing of foreclosures. The Corporation compensates servicers by permitting them to retain a specified portion of each interest payment on a serviced mortgage loan.

Mortgage-Backed Securities

MBS are guaranteed mortgage pass-through trust certificates issued by the Corporation that represent beneficial interests in pools of mortgage loans or other MBS. The Corporation serves as trustee for each trust.

MBS are backed by loans from one of three sources: a single lender, multiple lenders, or the Corporation's portfolio. Single-lender MBS generally are issued through lender swap transactions in which a lender exchanges pools of mortgage loans for MBS. Multiple-lender MBS allow several lenders to pool mortgage loans together and, in return, receive MBS (called Fannie Majors®) representing a proportionate share of a larger pool. MBS may back other securities, including Fannie Megas® ("Megas"), Stripped MBS ("SMBS"), and real estate mortgage investment conduit securities ("REMICs").

The pools of mortgage loans or MBS are not assets of the Corporation, except when acquired for investment purposes, nor are the related outstanding securities liabilities of the Corporation. The Corporation, however, is liable under its guaranty to make timely payments to investors of principal and interest on the mortgage loans in the pools, even if the Corporation has not received payments of principal or interest on the mortgage loans in the underlying pools. MBS enable the Corporation to further its statutory purpose of increasing the liquidity of residential mortgage loans and create a source of guaranty fee income to the Corporation without assuming any debt refinancing risk on the underlying pooled mortgages. Because of the Corporation's guaranties, it assumes the ultimate credit risk of borrowers' defaults on all mortgage loans underlying MBS, as it does for portfolio mortgage loans. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Management of Interest Rate and Credit Risk—Management of Credit Risk."

The Corporation issues MBS backed by single-family or multifamily first or second mortgage loans, with fixed or adjustable rates. The mortgage loans may be either conventional or FHA/VA mortgage loans. The conventional mortgage loans are subject to the maximum principal balance limits applicable to the Corporation's purchases as described under "Mortgage Loan Portfolio—Mortgage Loans Purchased—Principal Balance Limits." The mortgage loans also are subject to the same underwriting guidelines as those for mortgage loans purchased for portfolio as described under "Mortgage Loan Portfolio—Underwriting Guidelines." The majority of the Corporation's MBS outstanding represent beneficial interests in conventional fixed-rate mortgage loans on single-family dwellings.

The Corporation issues and guarantees several forms of MBS, including Fannie Majors, that involve only a single class of certificates with each investor receiving a portion of the payments of principal and interest on the underlying mortgage loans equal to its undivided interest in the pool. With a standard MBS, an investor has an undivided interest in a pool of underlying mortgage loans that generally are provided either by one lender or by the Corporation out of the Corporation's mortgage loan portfolio. Megas represent undivided interests in a pool of MBS of the same type.

The Corporation also issues and guarantees MBS that involve more than one class of certificates and, therefore, require special allocations of cash flows. SMBS are issued in series, with two or more classes that are each entitled to different cash flows and may represent (a) an undivided interest solely in the principal payments, (b) an undivided interest solely in the interest payments, or (c) different percentage interests in principal and interest payments, to be made on a pool of mortgage loans, MBS or certificates guaranteed by the Government National Mortgage Association ("GNMA certificates"). REMICs represent beneficial interests in a trust having multiple classes of certificates entitled to different cash flows from the underlying mortgage loans, MBS or GNMA certificates. Pursuant to its guaranty of REMICs, the Corporation is obligated to make timely distribution of required installments of principal and interest and to distribute the principal balance in full by a specified date, whether or not sufficient funds are available in the related REMIC trust.

The Corporation receives guaranty fees for its standard MBS and Fannie Majors. Such fees are paid monthly until the underlying mortgage loans have been repaid or otherwise liquidated from the pool (generally as a result of foreclosure). The aggregate amount of guaranty fees received by the Corporation depends upon the amount of MBS outstanding and on the guaranty fee rate. The amount of MBS outstanding is influenced by the repayment rates on the underlying mortgage loans and by the rate at which the Corporation issues new MBS. In general, when the level of interest rates declines significantly below the interest rates on loans underlying MBS, the rate of prepayments is likely to increase, although the rate of principal payments is influenced by a variety of economic, demographic and other factors. The Corporation also receives one-time fees for swapping SMBS, REMICs and Megas for standard MBS, except that no fee is charged for Megas swapped for standard MBS issued during the same month as the Mega.

In most instances, the lenders that originated the loans in an MBS pool created from the Corporation's portfolio or the lenders that exchanged the loans for the MBS (in the case of a "swap" transaction) initially service the loans. The Corporation, however, reserves the right to remove the servicing responsibility from a lender at any time if it considers such removal to be in the best interest of MBS certificate holders. In such event, the Corporation finds a replacement lender that will service the loans. The Corporation ultimately is responsible for the administration and servicing of mortgage loans underlying MBS, including the supervision of the servicing activities of lenders, the collection and receipt of payments from lenders, and the remittance of distributions and certain reports to holders of MBS certificates.

Delinquencies and REO

When a mortgage loan for which Fannie Mae bears the default risk is liquidated by foreclosure, the Corporation acquires the underlying property (such real estate owned is called "REO") and holds it for sale. The number of REO and level of delinquencies are affected by economic conditions and a variety of other factors. The Corporation manages the risk of delinquencies and REO as described in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Management of Interest Rate and Credit Risk—Management of Credit Risk."

Competition

The Corporation competes, within the limits prescribed by its Charter Act, in the purchase of mortgage loans for portfolio and the issuance of mortgage-backed securities in the secondary mortgage market. The Corporation competes primarily with the Federal Home Loan Mortgage Corporation ("Freddie Mac"), a government-sponsored enterprise regulated by the Department of Housing and Urban Development ("HUD") whose primary business consists of the issuance of mortgage-backed securities, and to a lesser extent with savings and loan associations, savings banks, commercial banks, mortgage bankers, government-sponsored corporations, and companies that pool mortgage loans for sale to investors as whole loans or mortgage-backed securities.

The Corporation's market share of loans purchased for portfolio or swapped for MBS is affected by the volume of mortgage loans offered for sale in the secondary market by loan originators and other market participants, the amount purchased by other market participants that compete with the Corporation, and the adequacy of funds to meet the demands of the housing industry. Competition has been particularly intense for ARMs because many depository institutions have purchased or retained such loans to better match the terms of their assets and liabilities. In its purchase of mortgage loans for portfolio, the Corporation competes primarily on the basis of yield, products and services offered. The Corporation and Freddie Mac compete for mortgage-backed securities business primarily on the basis of the amount of the guaranty fee or other fees charged, the relative market price of the securities, the products and services offered, and differences in such matters as delivery requirements.

Competition between the Corporation and Freddie Mac intensified beginning in the last quarter of 1990 as Freddie Mac began issuing a new mortgage-backed security called the "Gold PC." One of the most effective means of competition between the two entities is to increase the price that lenders can obtain for sale of the respective entity's securities by issuing REMICs backed by such securities in swap transactions with securities dealers (thereby increasing demand for such securities). Freddie Mac has been increasing its REMIC activity in order to support the price of its Gold PC and thereby enhance the market for such securities. The increased competition has resulted in lowering of the REMIC fees that the Corporation and Freddie Mac earn on their REMICs. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Mortgage-Backed Securities."

The ability of Fannie Mae and Freddie Mac to compete with private issuers could be affected by regulatory developments. At present, there are legislative and regulatory proposals pending that could affect Fannie Mae and Freddie Mac. See "Government Regulation and Charter Act" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments."

Corporate Indebtedness

The Corporation obtains funds for its operations primarily from the sale of its debt securities. Although the Corporation is stockholder-owned and its obligations are not backed by the United States or any agency or instrumentality thereof other than the Corporation, the Corporation's debt has traditionally been treated as "Federal Agency" debt in the U.S. marketplace. The Corporation, as a result, has historically enjoyed ready access to funds in the U.S. credit markets at rates that are slightly higher than the yields on U.S. Treasury obligations of comparable maturities.

The outstanding indebtedness of the Corporation consists of general unsecured obligations issued under section 304(b) of the Charter Act, subordinated capital debentures (including convertible capital debentures), which are unsecured subordinated general obligations issued under section 304(e) of the Charter Act, mortgage-backed bonds issued under section 304(d) of the Charter Act, and securities sold under agreements to repurchase.

Section 304(b) of the Charter Act provides that the aggregate amount of unsecured obligations outstanding under such subsection shall not exceed, at any one time, fifteen times the sum of the capital (including, for this purpose, capital debentures), capital surplus, general surplus, reserves, and undistributed earnings of the Corporation unless a greater ratio is fixed by the Secretary of HUD. Currently, the Corporation's debt-to-capital ratio may not exceed 20:1.

The Corporation is obligated to holders of certain outstanding issues of subordinated capital debentures to maintain the total principal amount of subordinated obligations issued under section 304(e) of the Charter Act at any one time outstanding at a level not more than two times the sum of (i) the capital of the Corporation represented by its outstanding common stock and (ii) its surplus and undistributed earnings at such time until such outstanding debentures mature or are redeemed. At December 31, 1991, the Corporation's subordinated debt-to-equity ratio was 0.3:1. The latest maturity date of a series of subordinated debentures containing the subordinated debt-to-equity restriction is September 30, 2002, although that series is callable at the Corporation's option. No noncallable subordinated obligations containing the subordinated debt-to-equity restriction remain outstanding. Regulations adopted by HUD provide that, at the maturity or other event requiring the payment or redemption of obligations issued under section 304(e) of the Charter Act, the permitted debt-to-capital ratio is automatically increased as necessary to permit the issuance of obligations under section 304(b) of the Charter Act in an amount sufficient to provide the proceeds required to pay the principal of and interest on the outstanding subordinated obligations required to be paid at such time.

Issuances of indebtedness pursuant to section 304(b) of the Charter Act are also subject to the condition that, at the time of any such issuance, the aggregate amount of such indebtedness then

outstanding under such section 304(b), after giving effect to the indebtedness being issued, is not greater than the Corporation's ownership, free from any liens or encumbrances, of cash, mortgages or other security holdings and obligations, participations or other investments. Unlike the debt-to-capital ratio limitation described above, this section 304(b) limitation is statutory and may not be waived or varied by the Secretary of HUD. For purposes of each of the foregoing calculations, the Corporation accounts for debt obligations issued at a discount or premium at their book value (face amount adjusted for unamortized discount or premium).

Section 304(d) of the Charter Act, pursuant to which MBS and mortgage-backed bonds are outstanding, imposes a requirement with respect to securities issued thereunder that the mortgages pledged or set aside must be sufficient at all times to make timely debt service payments on the securities. There is no other limitation on the amount of MBS and mortgage-backed bonds that may be outstanding.

For further information regarding the Corporation's debt, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis — Financing Activities."

Facilities

The Corporation owns its principal office, which is located at 3900 Wisconsin Avenue, NW, Washington, DC. The Corporation also leases approximately 369,000 square feet of office space at 4000 Wisconsin Avenue, NW, which is adjacent to the Corporation's principal office. The present lease expires in 2001, but the Corporation has options to extend the lease for up to 15 additional years, in 5-year increments. The Corporation also maintains regional offices in leased premises in Pasadena, California; Atlanta, Georgia; Chicago, Illinois; Philadelphia, Pennsylvania; and Dallas, Texas. The regional offices negotiate mortgage loan and MBS business with lenders in their regions, assist in supervising the servicing of the Corporation's mortgage loan portfolio by lenders, assist in supervising or managing the handling and disposition of REO, and provide training to the staff of lenders in their region.

Employees

At December 31, 1991 the Corporation employed approximately 2,600 full-time personnel.

GOVERNMENT REGULATION AND CHARTER ACT

The Corporation is a federally chartered and stockholder-owned corporation organized and existing under the Charter Act (12 U.S.C. § 1716 *et seq.*) whose purpose is to (1) provide stability in the secondary market for home mortgages, (2) respond appropriately to the private capital market by developing new finance and mortgage products, and (3) 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 Federal National Mortgage Association originally was incorporated in 1938 pursuant to Title III of the National Housing Act as a wholly owned government corporation and in 1954, under a revised Title III called the Federal National Mortgage Association Charter Act, became a mixed-ownership corporate instrumentality of the United States. From 1950 to 1968, it operated in the Housing and Home Finance Agency, which was succeeded by the Department of Housing and Urban Development ("HUD"). Pursuant to amendments to the Charter Act enacted in the Housing and Urban Development Act of 1968 (the "1968 Act"), the then Federal National Mortgage Association was divided into two separate institutions, the present Corporation and the Government National Mortgage Association, a wholly owned corporate instrumentality of the United States within HUD,

which carried on certain special financing assistance and management and liquidation functions. Under the 1968 Act, the Corporation was constituted as a federally chartered corporation and the entire equity interest in the Corporation became stockholder-owned.

Although the 1968 Act eliminated all federal ownership interest in the Corporation, it did not terminate government regulation of the Corporation. Under the Charter Act, approval of the Secretary of the Treasury is required for the Corporation's issuance of its debt obligations and MBS, and approval of the Secretary of HUD is required for the Corporation's issuance of stock and securities convertible into stock. Obligations of the Corporation issued under section 304(b) of the Charter Act are subject to limitations imposed by the Charter Act and regulations adopted by HUD. See "Business—Corporate Indebtedness."

In addition to specific enumerated powers, the Secretary of HUD is granted general regulatory power over the Corporation under the Charter Act, with authority to promulgate rules and regulations to carry out the purposes of the Charter Act. Also, the Secretary may require, pursuant to the Charter Act, that a reasonable portion of the Corporation's mortgage loan purchases be related to the national goal of providing adequate housing for low- and moderate-income families, but with a reasonable economic return to the Corporation. The Secretary recently published for comment proposed revisions to HUD's regulations covering the Corporation. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments."

While the Charter Act authorizes the Corporation to require entities selling mortgages to it to make nonrefundable capital contributions, as determined from time to time by the Corporation with the approval of the Secretary of HUD and subject to Charter Act restrictions, the Corporation currently imposes no such requirements on mortgage sellers.

The Charter Act requires that each servicer of the Corporation's mortgages own a minimum amount of common stock. The Secretary of HUD must approve stock holding requirements imposed upon such mortgage servicers. The common stock ownership requirement currently is one share.

The Charter Act also gives the Secretary of HUD the authority to audit and examine the books and financial transactions of the Corporation, but this authority has never been exercised. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 authorizes the General Accounting Office ("GAO") to audit the Corporation's mortgage transactions.

Thirteen members of the Corporation's eighteen-member Board of Directors are elected by the holders of the Corporation's common stock, and the remaining five members are appointed by the President of the United States. One such appointed director is required to be from each of the home building, mortgage lending, and real estate industries. Any member of the Board of Directors, including a member elected by stockholders, may be removed by the President of the United States for good cause.

In addition to placing the Corporation under federal regulation, the Charter Act also grants to the Corporation certain privileges and immunities. For instance, securities issued by the Corporation are deemed to be "exempt securities" under laws administered by the Securities and Exchange Commission ("SEC") to the same extent as securities that are obligations of, or guaranteed as to principal and interest by, the United States. Registration statements with respect to the Corporation's securities are not filed with the SEC. The Corporation also is not required to file periodic reports with the SEC. However, the SEC, the Department of the Treasury and the Board of Governors of the Federal Reserve System recently recommended that the exempt status under federal securities laws of securities issued by government-sponsored enterprises, including the Corporation, be removed by Congress. See "Recent Legislative and Regulatory Developments."

The Secretary of the Treasury of the United States has discretionary authority to purchase obligations of the Corporation up to a maximum of $2.25 billion outstanding at any one time. This facility has not been used since the Corporation's transition from government ownership in 1968.

Neither the United States nor any agency thereof is obligated to finance the Corporation's operations or to assist the Corporation in any other manner.

The Corporation is exempt from all taxation by any state or by any county, municipality, or local taxing authority except for real property taxes. The Corporation is not exempt from payment of federal corporate income taxes. Also, the Corporation may conduct its business without regard to any qualification or similar statute in any state of the United States or the District of Columbia.

The Federal Reserve Banks are authorized to act as depositaries, custodians, and fiscal agents for the Corporation, for its own account, or as fiduciary.

As discussed in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments," on September 25, 1991, the House approved proposed legislation that would set specific capital standards for Fannie Mae and an independent office within HUD to oversee regulatory and capital requirements. No comparable legislation has been reported by the Senate Banking Committee, but legislation is expected in 1992.

RECENT LEGISLATIVE AND REGULATORY DEVELOPMENTS

In 1991, the House of Representatives approved a bill that would set specific capital standards for Fannie Mae and Freddie Mac, create an independent office within HUD to oversee regulatory and capital requirements, and require Fannie Mae and Freddie Mac to set goals to promote affordable housing for low- and very low-income families consistent with each corporation's overall mission. No comparable bill has been introduced in the Senate. Also in 1991, HUD proposed revisions to its regulations relating to oversight of Fannie Mae. These legislative and regulatory developments are described in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments."

In January 1992, the SEC, the Department of the Treasury, and the Board of Governors of the Federal Reserve System released a *Joint Report on the Government Securities Market*, which was prepared after disclosure of violations by a primary dealer of Treasury Department rules governing auctions of Treasury securities and of other abuses by dealers in the government securities market. This report included a recommendation that statutory exemptions from federal securities laws for equity and unsecured debt securities of government-sponsored enterprises be eliminated, which would require the Corporation to register such securities with the SEC. This recommendation would require legislation, and no such legislation has been introduced. Statements by key members of the House and Senate indicate that passage of any such legislation in 1992 is unlikely. Management cannot predict the effect on the Corporation and its securities of any such legislation.

The Bush Administration's recommendations for the 1993 fiscal year budget contained a recommendation, carried over from the 1992 fiscal year budget recommendations, to allow HUD to establish fees and charges payable by entities that it regulates. These assessments would cover the costs of regulating and auditing such entities. It is unclear what impact, if approved, this proposal would have on Fannie Mae.

In January 1992, the Federal Financial Institutions Examination Council adopted a revised supervisory policy statement with respect to investments in zero coupon bonds, stripped mortgage-backed securities, asset-backed securities residuals, and certain other securities for depository institutions that are regulated by Council members (*i.e.*, the federal banking regulatory agencies, the National Credit Union Administration ("NCUA"), and the Office of Thrift Supervision). This statement, which Council members (other than the NCUA) adopted effective February 10, 1992, supersedes the supervisory policy statement adopted in April 1988. This policy states, in part, that mortgage derivative products, such as stripped mortgage-backed securities, collateralized mortgage obligations ("CMOs"), REMICs, and CMO and REMIC residuals, that are "high risk" securities are generally unsuitable for investment by depository institutions. In general, any such security that exhibits greater price volatility than a standard fixed-rate 30-year mortgage-backed security (as

determined pursuant to measures of average life and of average life and price sensitivity to shifts in the yield curve) is deemed to be "high-risk." However, such "high risk" products may be used for reducing overall interest-rate risk by institutions with well-managed portfolios and specific policies for interest-rate risk management. It is unclear what impact this policy statement will have on the MBS market.

The Secondary Mortgage Market Enhancement Act of 1984 (the "Act") provided that securities issued or guaranteed by Fannie Mae and Freddie Mac must be treated as obligations of the U.S. government for purposes of state investment laws. The Act, however, permitted the states to pass legislation to override the federal preemption by October 3, 1991. Approximately 21 states passed legislation to override all or part of the federal preemption of state legal investment laws in the Act. The override legislation in many states subjects insurance companies to state laws and regulations limiting the percentage of their investment portfolio that may be invested in the securities, including mortgage-backed securities, of any one issuer. It is unclear what impact such legislation may have on Fannie Mae's business or on the market for its debt and MBS.

LEGAL PROCEEDINGS

In March 1991, the Internal Revenue Service ("IRS") informed the Corporation that it intended to proceed with litigation against the Corporation in a case involving tax deductions for hedging transactions in 1984 and 1985. Although this case was filed in the United States Tax Court in June 1986, the Court permitted the case to be held pending the outcome of its companion case involving the tax treatment of concurrent mortgage sales transactions and other issues. When filed, this case also involved only the issues raised in the companion case, but in 1988, while the companion case was proceeding through the courts, the United States Supreme Court handed down a case (*Arkansas Best*) that prompted the IRS to raise the hedging issue in this case. From 1988 to 1991, the IRS worked on an administrative package to resolve the hedging issue but finally decided to seek a court resolution of the issue instead. All tax issues in this case have been resolved except the hedging issue relating to whether gains and losses on hedging transactions are capital or ordinary. A trial in the Tax Court is scheduled to begin on April 13, 1992. If the IRS prevails, the Corporation would owe taxes and interest in an amount that, as of December 31, 1991, would reduce the Corporation's net income by approximately $94 million.

The IRS is currently auditing the Corporation's tax returns for 1986 and 1987 and has proposed additional deficiencies related to certain hedging type transactions that it indicates should be recharacterized as capital losses. If the IRS' position on these proposed deficiencies in 1986 and 1987 is sustained, the Corporation's net income could be adversely affected by approximately $170 million, which includes cumulative interest, net of tax, of $48 million as of December 31, 1991.

COMMON STOCK

Section 303(a) of the Charter Act provides that the Corporation shall have common stock, without par value. The common stock is vested with all voting rights. Each share of common stock is entitled to one vote at all elections of directors and on all other matters presented for common stockholder vote. The holders of the common stock elect thirteen directors, and the President of the United States appoints the remaining five directors. Any member of the Board of Directors, including a member elected by stockholders, may be removed by the President of the United States for good cause. The Charter Act, the Corporation's governing instrument, cannot be amended by the stockholders, but only by an Act of Congress.

The Corporation also is authorized by the Charter Act to have preferred stock on such terms and conditions as the Board of Directors of the Corporation may prescribe. No common stockholder approval is required to issue preferred stock.

The Charter Act contains no limitation on the amount of stock that may be issued. except that no stock may be issued by the Corporation without the prior approval of the Secretary of Housing and Urban Development ("HUD"). At March 27, 1992, there were outstanding approximately 273 million shares of common stock.

Holders of the common stock are entitled to receive cash dividends if, as and when declared by the Board of Directors. Cash dividends on the common stock in any one fiscal year may not exceed a rate determined from time to time by the Secretary of HUD to be a fair rate of return after consideration of the current earnings and capital condition of the Corporation. The Secretary has not established any rate limitation to date. HUD has issued proposed regulations that would require that the Secretary of HUD approve annual dividend policies adopted by the Corporation's Board of Directors. The payment of dividends on common stock also is subject to the payment of dividends on any preferred stock outstanding. Dividends have been declared and paid for each quarter during the Corporation's two most recent fiscal years. See "Quarterly Results of Operations" on page 57 for quarterly dividends declared during 1990 and 1991.

In the event of liquidation of the Corporation, holders of common stock are entitled to share ratably, in accordance with their holdings, in the remaining assets of the Corporation after payment of all liabilities of the Corporation and amounts payable to the holders of preferred stock. There are no provisions under the Charter Act that would govern the liquidation of the Corporation as a corporate entity.

The common stock has no conversion or pre-emptive rights or redemption or sinking fund provisions. The outstanding shares of common stock are fully paid and nonassessable. There is no prohibition against the purchase by the Corporation of its own common stock, holding such common stock in its treasury, and reselling such stock.

This description is summarized from the Charter Act, the bylaws, and certain resolutions of the Board of Directors and stockholders of the Corporation. This description does not purport to be complete and is qualified in its entirety by reference to the Charter Act, bylaws of the Corporation, and such resolutions, copies of which are obtainable from the Corporation.

The Corporation's common stock is publicly traded on the New York, Pacific, and Midwest stock exchanges and is identified by the ticker symbol "FNM". The transfer agent and registrar for the common stock is Manufacturers Hanover Trust Company, 450 West 33rd Street, New York, New York 10001.

The following table shows, for the periods indicated, the high and low prices per share of the Corporation's common stock on the New York Stock Exchange Composite Transactions, as reported in *The Wall Street Journal*.

	1991		1990	
Quarter	**High**	**Low**	**High**	**Low**
1st	$48.50	$32.38	$37.88	$28.50
2nd	51.75	42.63	44.63	32.00
3rd	65.13	49.00	44.50	24.88
4th	69.63	54.00	36.25	26.00

On March 27, 1992, the closing price of the Corporation's common stock as so reported was $63.63.

SELECTED FINANCIAL DATA

The following selected financial data for the years 1987 through 1991 (which data are not covered by the report of independent certified public accountants) have been summarized or derived from the audited financial statements and other financial information. These data should be read in conjunction with the audited financial statements and notes to financial statements.

(Dollars in millions, except per share amounts)

	Year Ended December 31,				
Income Statement Data:	**1991**	**1990**	**1989**	**1988**	**1987**
Interest income	$ 12,593	$ 12,069	$ 11,080	$ 10,226	$ 9,843
Interest expense	10,815	10,476	9,889	9,389	8,953
Net interest income	1,778	1,593	1,191	837	890
Guaranty fees	675	536	408	328	263
Income from tax settlement	239	—	—	—	—
Gain (loss) on sales of mortgages, net	(28)	7	9	12	(81)
Miscellaneous income, net	106	107	60	69	56
Provision for losses	(370)	(310)	(310)	(365)	(360)
Administrative expenses	(319)	(286)	(254)	(218)	(197)
Income before federal income taxes and extraordinary item	2,081	1,647	1,104	663	568
Provision for federal income taxes	(626)	(474)	(297)	(156)	(192)
Income before extraordinary item	1,455	1,173	807	507	376
Extraordinary loss (1)	(92)	—	—	—	—
Net income	$ 1,363	$ 1,173	$ 807	$ 507	$ 376
Per share:					
Earnings before extraordinary item:					
Primary	$ 5.33	$ 4.50	$ 3.14	$ 2.14	$ 1.55
Fully diluted	5.31	4.49	3.10	2.11	1.54
Net earnings:					
Primary	4.99	4.50	3.14	2.14	1.55
Fully diluted	4.98	4.49	3.10	2.11	1.54
Cash dividends	1.04	0.72	0.43	0.24	0.12

	December 31,				
Balance Sheet Data:	**1991**	**1990**	**1989**	**1988**	**1987**
Mortgage portfolio, net	$126,486	$113,875	$107,756	$ 99,867	$ 93,470
Total assets	147,072	133,113	124,315	112,258	103,459
Borrowings:					
Due within one year	34,608	38,453	36,346	36,599	29,718
Due after one year	99,329	84,950	79,718	68,860	67,339
Total liabilities	141,525	129,172	121,324	109,998	101,648
Stockholders' equity	5,547	3,941	2,991	2,260	1,811

Other Data:	**1991**	**1990**	**1989**	**1988**	**1987**
Net interest margin	1.42%	1.39%	1.16%	0.89%	1.00%
Return on average equity	27.7	33.7	31.1	25.2	23.5
Return on average assets	1.0	.9	.7	.5	.4
Ratio of earnings to fixed charges (2)	1.19:1	1.15:1	1.11:1	1.07:1	1.06:1
Dividend payout ratio	20.7%	14.7%	12.8%	11.2%	7.6%
Equity to assets ratio	3.6	2.7	2.2	1.8	1.6
Mortgage purchases	$ 37,202	$ 23,959	$ 22,518	$ 23,110	$ 20,531
MBS issued	112,903	96,695	69,764	54,878	63,229
MBS outstanding at year-end	371,984	299,833	228,232	178,250	139,960

(1) Fannie Mae repurchased or called $2.2 billion of high-coupon debt, resulting in a loss of $140 million ($92 million net of tax).

(2) For the purpose of calculating the ratio of earnings to fixed charges, "earnings" consists of income before federal taxes and fixed charges. "Fixed charges" consists of interest expense and interest capitalized on real estate owned.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

In 1991, Fannie Mae again reported record earnings, business volumes, and capital growth, as well as an improvement in credit quality. Net income in 1991 was $1.363 billion or 16 percent higher than the $1.173 billion earned in 1990, while earnings per share increased to $4.98 in 1991 from $4.49 in 1990.

Fannie Mae's performance in 1991 was fueled primarily by growth of its mortgage portfolio and Mortgage-Backed Securities ("MBS") business. The Corporation's net mortgage portfolio was $126.5 billion at December 31, 1991, up 11.1 percent from the 1990 year-end level. This rate of growth was nearly double the 5.7 percent rate recorded in 1990. MBS outstanding at year-end 1991 was $372.0 billion or 24 percent higher than the $299.8 billion at year-end 1990.

The strong earnings performance, together with equity raised through the exercise of warrants and the growth in its allowance for losses, enabled the Corporation to increase its capital base by $1.8 billion in 1991, bringing total capital to $6.3 billion at December 31, 1991.

In spite of the soft economy, credit quality as measured by charge-offs and property acquisitions continued to improve. Losses on foreclosed properties were at their lowest level since 1986. Charge-offs in 1991 were $205 million, down from $234 million in 1990, and the number of conventional single-family properties acquired through foreclosure declined to 7,450 in 1991 from 8,006 in 1990. While the delinquency rates increased slightly during the latter part of 1991, management does not anticipate a significant increase in charge-offs in 1992 because of the low average balances and loan-to-value ratios of its portfolio loans and MBS.

A summary comparison of the Corporation's 1991 performance versus 1990 follows:

- Net interest income was $1.778 billion, an increase of $185 million or 12 percent from the $1.593 billion earned in 1990, primarily as a result of increases in the average investment portfolio and in the net interest margin on the average investment portfolio.

- MBS guaranty fees were $675 million in 1991, a 26 percent increase over 1990, resulting from the continued growth in MBS outstanding.

- The provision for losses in 1991 increased to $370 million from $310 million in 1990. Although charge-offs declined, management considered an increase in the provision to be prudent in light of growth in business volumes. The allowance for losses at December 31, 1991 was $704 million, up $165 million from the end of 1990 and represented loss coverage of over three times the level of 1991 charge-offs.

- In 1991, the U.S. Supreme Court issued an opinion that favored Fannie Mae's tax position involving concurrent mortgage sales. As a result, the Corporation recognized income of $239 million. In addition, the Corporation sold $800 million of low-coupon mortgages at a loss of $59 million, and repurchased or called $2.2 billion of high-coupon debt recognizing an extraordinary loss of $140 million ($92 million after tax). The combined result of these transactions did not have a material effect on the earnings of the Corporation.

- Real Estate Mortgage Investment Conduit ("REMIC") fee income of $59 million remained relatively stable when compared with $62 million in 1990 as a decline in REMIC fee rates was offset by an increase in the volume of REMIC issuances.

- The ratio of total administrative expenses to the average mortgage portfolio plus MBS outstanding continued to decline in 1991, falling to .073 percent from .079 percent in 1990.

The remainder of the Management's Discussion and Analysis section presents detailed information on the corporation's results of operations, risk management strategies, balance sheet analysis, and MBS business.

Results of Operations

Net Interest Income

Net interest income represents the excess of income from the investment portfolio — the net mortgage portfolio and other investments — over the interest paid on borrowings and other related costs. Two measures used in analyzing changes in net interest income are investment spread and net interest margin. Investment spread is the difference between the yield on interest-earning assets, adjusted for the tax benefits of nontaxable income, and the effective cost of funds on interest-bearing liabilities. Net interest margin is net interest income, on a tax equivalent basis, as a percentage of the investment portfolio. The net interest margin differs from the investment spread in that margin includes interest-free return; that is, the return on that portion of the investment portfolio funded by equity and non-interest-bearing liabilities.

The following table presents an analysis of net interest income for 1991, 1990, and 1989.

Net Interest Income and Average Balances

(Dollars in millions)

	1991	1990	1989
Interest income:			
Mortgage portfolio	$ 11,603	$ 10,958	$ 10,103
Investments and cash equivalents	990	1,111	977
Total interest income	12,593	12,069	11,080
Interest expense	10,815	10,476	9,889
Net interest income	1,778	1,593	1,191
Tax equivalent adjustment(1)	125	130	118
Net interest income tax equivalent basis	$ 1,903	$ 1,723	$ 1,309
Average balances:			
Interest-earning assets(2)			
Mortgage portfolio, net	$119,637	$110,385	$101,714
Investments and cash equivalents	14,845	13,252	10,732
Total interest-earning assets	$134,482	$123,637	$112,446
Interest-bearing liabilities	$126,069	$117,551	$107,802
Interest-free funds	8,413	6,086	4,644
Total interest-bearing liabilities and interest-free funds	$134,482	$123,637	$112,446
Average interest rates(1):			
Interest-earning assets:			
Mortgage portfolio, net	9.76%	9.98%	9.97%
Investments and cash equivalents	6.79	8.62	9.53
Total interest-earning assets	9.43	9.84	9.93
Interest-bearing liabilities	8.56	8.91	9.18
Investment spread	.87	.93	.75
Interest-free return	.54	.44	.37
Miscellaneous	.01	.02	.04
Net interest margin	1.42%	1.39%	1.16%

(1) Reflects pro forma adjustments to permit comparison of yields on tax-advantaged and taxable assets.

(2) Includes average balance of nonperforming loans of $0.9 billion, $0.7 billion, and $0.8 billion in 1991, 1990, and 1989, respectively.

The 1991 growth in net interest income resulted primarily from a 9 percent increase in the average investment portfolio and the growth in interest-free return. The average investment portfolio

grew, in part, due to the high level of refinancing activity in response to lower interest rates in 1991. While net interest margin increased as a result of the higher interest-free return, the investment spread was lower as the yield on interest-earning assets declined more than the cost of debt.

Net interest income was higher in 1990 when compared with 1989 due to both an increase in the average investment portfolio and in net interest margin.

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 1991 and 1990.

Rate/Volume Analysis

(Dollars in millions)

	Increase (Decrease)	Attributable to Changes in (1)	
		Volume	Rate
1991 vs. 1990			
Interest income:			
Mortgage portfolio	$645	$ 900	$(255)
Investments and cash equivalents	(121)	128	(249)
Total interest income	524	1,028	(504)
Interest expense	339	740	(401)
Net interest income	$185	$ 288	$(103)
1990 vs. 1989			
Interest income:			
Mortgage portfolio	$855	$ 861	$ (6)
Investments and cash equivalents	134	232	(98)
Total interest income	989	1,093	(104)
Interest expense	587	875	(288)
Net interest income	$402	$ 218	$ 184

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

Net interest income does not include interest receivable on nonperforming loans. Conventional single-family and multifamily loans are classified as nonperforming and accrued interest is reversed out of income when a payment is 90 days or more past due. Nonperforming loans outstanding totaled $1.1 billion at the end of 1991, compared with $0.7 billion at December 31, 1990 and 1989, $0.9 billion at December 31, 1988 and $1.3 billion at December 31, 1987. If nonperforming assets had been fully performing, they would have contributed an additional $77 million to net interest income in 1991, $49 million in 1990, $48 million in 1989, $89 million in 1988, and $200 million (including $55 million due principally to a change in the method of estimating uncollectible interest) in 1987.

Information on how the Corporation manages interest rate risk is presented under "Management of Interest Rate and Credit Risk."

Guaranty Fees

Guaranty fee income continued to increase in 1991, due to the growth in the amount of MBS outstanding. These fees compensate the Corporation for its guaranty of timely payment of principal and interest to MBS investors.

The following table shows guaranty fee income as a percentage of the average balance of MBS outstanding in 1991, 1990, and 1989.

Guaranty Fee Income

(Dollars in millions)

	1991	1990	1989
Guaranty fee income	$ 675	$ 536	$ 408
Average balance of MBS outstanding (1)	$321,092	$254,703	$191,037
Effective guaranty fee rate	.210%	.211%	.213%

(1) Excludes average balances of Fannie Mae MBS held in the mortgage portfolio of $13.9 billion, $11.9 billion, and $9.8 billion in 1991, 1990, and 1989, respectively.

Additional information on the Corporation's MBS and guaranty fees is presented under "Mortgage-Backed Securities."

Income from Tax Settlement

In 1991, the Corporation recognized $239 million of income as a result of the resolution of a tax case. Additional information on the tax case is presented in the Notes to the Financial Statements, "Income Taxes".

Gain (Loss) on Sales of Mortgages

Loss on sales of mortgages was $28 million in 1991, compared with gains of $7 million and $9 million in 1990 and 1989, respectively. The loss in 1991 primarily resulted from the sale of low-coupon mortgages.

Miscellaneous Income

Miscellaneous income during 1991 did not change significantly compared with 1990. Despite a decline in REMIC fee rates in response to competitive pressures, an increase in the volume of REMIC issuances resulted in relatively stable REMIC fee income.

The increase in miscellaneous income in 1990, when compared with 1989, was due to the increase in REMIC issuances resulting in a corresponding increase in REMIC fee income. The following table presents REMIC issuances and fees for 1991, 1990, and 1989.

REMIC Issuances and Fees

	December 31,			% Change	
	1991	1990	1989	1991 vs. 1990	1990 vs. 1989
Issuances (in billions)	$102	$61	$38	67%	61%
Gross fee income (in millions)	115	97	57	19	70
Net fee income (in millions)	59	62	37	(5)	68

A portion of the gross fees are deferred and amortized into income over the life of the REMIC to offset expected future administrative costs. Net fee income is the amount included in miscellaneous income.

Additional information on REMIC activity is presented under "Mortgage-Backed Securities."

Provision for Losses

The Corporation's provision for losses in 1991 increased to $370 million from $310 million in 1990 and 1989. Although charge-offs were at their lowest level since 1986, management considered an increase in the loan loss provision to be prudent in light of growth in business volumes. Additional information on how the Corporation manages credit risk is presented under "Management of Interest Rate and Credit Risk."

Administrative Expenses

Administrative expenses were $319 million in 1991, compared with $286 million and $254 million in 1990 and 1989, respectively. Increased salaries and compensation-related expenses were the primary reasons for the overall increases. Compensation expense was $187 million or 59 percent of administrative expenses in 1991, compared with $172 million (60 percent) in 1990 and $150 million (59 percent) in 1989. The ratio of total administrative expenses to the average mortgage portfolio plus average MBS outstanding continued to improve. In 1991, the ratio was .073 percent, down from .079 percent in 1990 and .087 percent in 1989.

Income Taxes

The effective federal income tax rate in 1991 was 30 percent, compared with 29 percent in 1990 and 27 percent in 1989. The effective tax rate increased in both 1991 and 1990 primarily due to the growth in taxable income without a proportionate increase in income from tax-advantaged investments. See Notes to Financial Statements, "Income Taxes," for additional information.

Extraordinary Loss

The Corporation repurchased or called $2.2 billion of high-coupon debt in 1991, resulting in an extraordinary loss of $140 million ($92 million after tax). The repurchase of high-coupon debt will favorably affect the Corporation's cost of funds in future periods.

Management of Interest Rate and Credit Risk

Over the past decade, management adopted strategies addressing two primary risks faced by the Corporation — interest rate risk and credit risk. Interest rate exposure is managed through asset/liability strategies designed to match the estimated durations of the Corporation's assets and liabilities, and to maintain this duration match throughout a wide range of interest rate environments. To mitigate credit risk, the Corporation establishes strict underwriting standards and maintains a geographically diverse business base. While active interest rate and credit risk management diminishes the prospect for significant losses, the Corporation maintains a growing capital base (equity and allowance for losses) to absorb future losses.

Management of Interest Rate Risk

The sensitivity of earnings to changes in interest rates can be measured by the duration gap, or the difference between the estimated durations of mortgage assets and those of the liabilities that fund the mortgages. Duration is a measure of the estimated weighted-average maturity of the present values of future cash flows. The Corporation's duration gap in the years 1989 through 1991 has been under eight months.

The durations of assets and liabilities may respond differently to significant changes in interest rates. For example, when interest rates decline significantly, mortgage durations also decline because of higher mortgage prepayments. The durations of non-callable liabilities, however, stay approximately the same. The resulting duration mismatch could increase earnings volatility. One way the Corporation has reduced the projected duration gap that can result when interest rates change significantly is by issuing callable and indexed sinking fund debt that better matches the optional prepayment characteristics of the mortgages it funds. Another recent financing strategy employed by the Corporation has been to enter into callable swaps that effectively convert non-callable debt to callable debt. At December 31, 1991, callable instruments equalled 36 percent of total outstanding long-term debt, up from 22 percent at the end of 1990 and 10 percent at the end of 1989. Management believes the early redemption feature of callable instruments makes them desirable for managing the interest rate risk associated with mortgage loan prepayments. Additional information on callable debt is presented under "Balance Sheet Analysis—Financing Activities".

Management of Credit Risk

The major exposure to credit risk results from the possibility that the Corporation will not recover amounts due from borrowers or lenders on its mortgage portfolio or on loans backing its MBS. The Corporation has a credit quality program structured to monitor and actively manage the three primary components of credit risk: product risk, institutional risk, and market risk.

Product risk is managed through studying the many factors that can influence how a loan will perform and making appropriate adjustments to mortgage products and underwriting standards. These factors include loan type, seasoning, loan-to-value ("LTV") ratio, occupancy status, loan term, property type, and the underwriting standards used to qualify the borrower. LTV relates to the ratio of the original loan amount to the original appraised value of the property. For example, a home with an appraised value of $100,000 on which the borrower has an $80,000 mortgage, has an LTV ratio of 80 percent. In 1991, two changes in underwriting policies in response to identified product risk were tightening underwriting criteria for adjustable-rate mortgages ("ARMs") and curtailing the purchase of limited documentation mortgage loans.

Another aspect of managing product risk relates to requiring credit enhancements on those loans that represent a higher risk to the Corporation. Credit enhancements, which partially or fully offset the Corporation's default risk, include recourse, pledged collateral, letters of credit, pool insurance, and spread accounts. Under a spread account, the lender sets aside a portion of its excess servicing income to cover future losses. At December 31, 1991, 21 percent of the total conventional single-family mortgage portfolio and MBS were supported by credit enhancements. Of the conventional single-family ARMs, which generally represent a higher risk to the Corporation, 39 percent were covered by credit enhancements. Because of risk-based capital standards for depository institutions, the proportion of Fannie Mae's total business having credit enhancements has declined and is expected to decline further as new single-family business is being transacted, for the most part, without credit enhancements. However, Fannie Mae's credit management policies are designed to prevent the Corporation from taking unacceptable levels of risk.

Institutional risk is the second component of Fannie Mae's credit management program. The two primary sources of institutional risk are the lenders that sell and service mortgages and the mortgage insurance companies that provide loss coverage in the event of default on the higher LTV loans. The Corporation manages these risks by monitoring the financial strength and performance of the lenders and mortgage insurance companies and by conducting reviews of lenders' operations. In addition, mortgage insurance companies with credit ratings of AA or better insured approximately 92 percent of the conventional single-family business for which mortgage insurance is enforced.

The third component integral to the credit management program is monitoring market risk. Fannie Mae analyzes market conditions and loan performance in over 50 metropolitan areas. Because Fannie Mae provides mortgage funds across the country at all times, management uses this market

risk information to ensure the Corporation is applying appropriate underwriting standards to new mortgage purchases and is taking steps to maintain the quality of mortgage investments in all markets. The Corporation mitigates its market risk primarily by three factors: the geographic diversification of its mortgage portfolio and MBS; favorable LTV distributions, particularly in California and the Northeast; and risk sharing on much of the higher risk business, particularly the ARM business in California.

Management measures its success in managing credit risk by evaluating three factors: the risk profile of portfolio and MBS loans, delinquency rates, and foreclosure activity. The discussion that follows will address separately these primary performance measures of credit quality as they pertain to the conventional single-family and multifamily businesses.

Single-Family

The first measure of loan quality is the risk profile of the Corporation's single-family portfolio and MBS. At December 31, 1991, 76 percent of the conventional (nongovernment insured or guaranteed) single-family loans in the Corporation's portfolio or backing MBS had an original LTV ratio not higher than 80 percent (35 percent not higher than 70 percent) and the average original LTV ratio was 73 percent. In California and New England, the average original LTV ratios were 70 percent and 68 percent, respectively, at the end of 1991.

Other significant factors contributing to the continuing high credit quality of Fannie Mae's loans in portfolio and backing MBS are the requirement that conventional loans with an LTV greater than 80 percent have mortgage insurance or other types of acceptable credit protection; the concentration of the Corporation's mortgages in fixed-rate product, which is generally less risky than ARMs; the low average loan size; and the small percentage of investor loans. The Corporation's loan limits and the lower loan balance profile of mortgages in portfolio and underlying MBS reduces the credit risk exposure when compared with the nonconforming housing markets. Nonconforming loans have an original balance in excess of the Corporation's statutory loan limits.

Because of housing initiatives announced in 1991 to help low- and moderate-income borrowers and certain changes in the FHA insurance program, management expects the percentage of its new business consisting of low down payment loans to increase in 1992. Management expects to mitigate the additional risks of low- and moderate-income business in part through the use of mortgage insurance and through techniques such as using second mortgages provided by state and local governments and through taking steps to ensure that lenders' origination and quality control systems are consistent with Fannie Mae guidelines.

Despite a slight rise in serious delinquencies (90 or more days delinquent) in 1991 due to the current economic recession, the level of serious delinquencies has declined significantly from 1986 when the level was 1.38 percent. This decline reflects, in part, the positive results of the Corporation's credit risk management strategies. The following table summarizes conventional single-family serious delinquencies by region as of December 31, 1991, 1990, and 1989.

Single-Family Serious Delinquencies (1)

	December 31,		
	1991	1990	1989
Northeast	1.00%	.74%	.65%
Southeast	.65	.63	.71
Midwest	.41	.42	.49
Southwest	.76	.96	1.37
West	.40	.30	.40
Total	.64%	.58%	.69%

(1) Single-family serious delinquencies are those loans in portfolio and underlying MBS for which the Corporation has the primary risk of loss that are 90 or more days delinquent or in relief or foreclosure. The percentages are based on the number of such loans in portfolio and underlying MBS.

California and New England are two areas of the country where the recession has had a particularly severe impact. As shown in the table, the Western region had a serious-delinquency rate well below the average for the Corporation. The Northeast region had the highest serious-delinquency rate and this has led to increased acquisitions of foreclosed properties.

The following table summarizes the number of conventional single-family properties acquired during the year and owned at year-end, including their carrying value.

Single-Family Real Estate Owned ("REO")

(Dollars in thousands)

Number of Properties	1991	1990	1989
Acquired:			
Northeast	1,069	548	284
Southeast	1,939	1,729	1,686
Midwest	747	739	908
Southwest	3,097	4,288	5,863
West	598	702	1,421
Total	7,450	8,006	10,162
In inventory at year-end	3,295	3,585	4,975
Aggregate carrying value (1)	$164,000	$146,000	$172,000
Average carrying value (1)	$ 50	$ 41	$ 35

(1) The carrying value of a property is the lower of the Corporation's net investment (after deducting any mortgage insurance proceeds) and the current estimated net realizable value.

Property acquisitions in the Northeast region represented 14 percent of Fannie Mae's total 1991 acquisitions, although the unpaid principal balance of the loan portfolio and MBS in the region equalled 24 percent of the total for the Corporation as of December 31, 1991.

Single-family foreclosures have declined since 1987 when 16,345 properties were acquired. The main reasons for the decline in the number of properties acquired are growth in homeowner equity resulting from property appreciation in most geographic areas and improved credit quality of mortgage loans in portfolio and MBS due to changes in underwriting standards primarily in late 1985. In addition, a large portion of foreclosure losses in the 1980's came from states dependent on the oil industry. The improvement in the housing market in those states is reflected in the Corporation's recent loss experience.

The following table illustrates the improvement in loan quality by presenting the cumulative rate of foreclosure for single-family conventional loans approximately three years after origination.

Conventional Single-Family Foreclosure Rates
Three Years After Origination — Portfolio and MBS

Year of Origination	Cumulative Rate of Foreclosure
1988	.32%
1987	.26
1986	.20
1985	.88
1984	2.00

The table reflects a significant reduction in the foreclosure rate between loans originated in 1984 and 1985 and loans originated in 1986 and subsequent years. For example, 2.00 percent of loans in portfolio or MBS that were originated in 1984 had gone into foreclosure three years after origination, compared with .32 percent of loans originated in 1988 at the same point in the life of the loans.

As a result of the lower rate of foreclosure, charge-offs and the ratio of charge-offs to average principal balances outstanding for single-family loans in portfolio and backing MBS have declined, as shown in the following table.

Single-Family Charge-Offs

(Dollars in millions)

	Year Ended December 31,		
	1991	1990	1989
Net charge-offs	$143	$190	$205
Net loss charge-off ratio	.03%	.05%	.07%

Due to the weak economy and the increasing volume of loans outstanding, management expects a modest increase in acquisitions of foreclosed properties and charge-offs in 1992.

Multifamily

For the majority of multifamily loans held in portfolio or that back MBS, the Corporation has full or partial recourse to the lender or others, and, in certain cases, has required pledged collateral. Fannie Mae also has a delegated underwriting and servicing ("DUS") program under which the lender is responsible for the first 5 percent of losses, with any remaining losses shared by the lender and Fannie Mae. The percentage of multifamily loans and MBS for which Fannie Mae has the primary risk of default (and which includes shared risk under DUS) as of December 31, 1991 was 44 percent, compared with 40 percent and 31 percent at December 31, 1990 and 1989, respectively. Of the total, 24 percent, 19 percent and 9 percent in 1991, 1990 and 1989, respectively, relate to the DUS program. While the Western region has a large percentage of the conventional multifamily portfolio and MBS, the majority of those loans and MBS involve collateralized recourse or shared risk.

The level of multifamily serious delinquencies had declined significantly from its peak of 6.6 percent in 1988. Multifamily serious delinquencies are those loans two months or more delinquent for which the Corporation has primary risk of loss. Delinquency percentages are based on the dollar amount of such loans in portfolio and underlying MBS. Multifamily serious delinquencies as of December 31, 1991, 1990, and 1989 were 3.6 percent, 1.7 percent, and 3.2 percent, respectively. The increase in the level of serious delinquencies in 1991 is due primarily to the national economic recession.

Multifamily foreclosure activity in 1991 was consistent with management's expectations, given the prevailing economic conditions. The following table summarizes the number of multifamily properties acquired during the year and owned at year-end, including their carrying value.

Multifamily Real Estate Owned ("REO")

(Dollars in thousands)

Number of Properties	1991	1990	1989
Acquired	27	25	23
In inventory at year-end	28	32	33
Aggregate carrying value (1)	$98,900	$111,000	$84,000
Average carrying value (1)	$ 3,500	$ 3,500	$ 2,500

(1) The carrying value of a property is the lower of the Corporation's net investment and the current estimated net realizable value.

Net charge-offs and the ratio of net charge-offs to average principal balances outstanding for multifamily loans in portfolio and underlying MBS are summarized in the following table.

Multifamily Charge-Offs

(Dollars in millions)

	Year Ended December 31,		
	1991	1990	1989
Net charge-offs	$62	$44	$38
Net loss charge-off ratio	.32%	.25%	.26%

The increase in charge-offs in 1991 and 1990 were due primarily to acquiring properties with higher unpaid principal balances and an increase in charge-offs on anticipated foreclosures. Management believes that stricter underwriting standards adopted in recent years and requirements for recourse, risk sharing, or other credit enhancement will have a mitigating effect on the level of future multifamily charge-offs.

Additional information on the Corporation's exposure to credit risk is presented in the Notes to the Financial Statements under the sections titled "Financial Instruments with Off-Balance-Sheet Risk" and "Concentrations of Credit Risk."

Allowance for Loan Losses

In evaluating the risk of loss on portfolio loans and MBS outstanding, management considers recent experience, current economic conditions, and estimates of future losses on seriously delinquent loans. The allowance for losses is established by recording an expense for the provision for losses and is reduced through charge-offs (net of recoveries) as mortgage loans are foreclosed. Estimates of losses recorded at foreclosure are adjusted to actual losses when the underlying properties are sold.

The following table summarizes changes in the allowance for losses in 1987 through 1991 for loans in the mortgage portfolio and in MBS pools.

Allowance for Losses

(Dollars in millions)

	Total
Balance, January 1, 1987	$ 271
Provision for loan losses	360
Net loan charge-offs:	
Conventional:	
Single-family	(249)
Multifamily	(23)
Government	(13)
Balance, December 31, 1987	346
Provision for loan losses	365
Net loan charge-offs:	
Conventional:	
Single-family	(272)
Multifamily	(30)
Government	(13)
Balance, December 31, 1988	396
Provision for loan losses	310
Net loan charge-offs:	
Conventional:	
Single-family	(191)
Multifamily	(38)
Government	(14)
Balance, December 31, 1989	463
Provision for loan losses	310
Net loan charge-offs:	
Conventional:	
Single-family	(175)
Multifamily	(44)
Government	(15)
Balance, December 31, 1990	539
Provision for loan losses	370
Net loan charge-offs:	
Conventional:	
Single-family	(138)
Multifamily	(61)
Government	(6)
Balance, December 31, 1991	$ 704

At December 31, 1991, the ratio of the allowance for losses to 1991 net charge-offs, or net loss coverage ratio, was 3.4:1, compared with 2.3:1, 1.9:1, 1.3:1, and 1.2:1 at December 31, 1990, 1989, 1988, and 1987, respectively.

Balance Sheet Analysis

This section discusses the Corporation's mortgage portfolio and the financing activities undertaken by the Corporation to fund mortgage purchases. Also included is a discussion of the role of liquidity management in meeting the Corporation's business requirements.

Mortgage Portfolio

As of December 31, 1991, the net mortgage portfolio totaled $126.5 billion. In comparison, the portfolio totaled $113.9 billion and $107.8 billion at December 31, 1990 and 1989, respectively. The yield on the net mortgage portfolio (before deducting the allowance for losses) was 9.54 percent as of December 31, 1991, compared with 9.94 percent as of December 31, 1990 and 10.03 percent as of December 31, 1989. The decreases in yield in the last two years were due primarily to a decline in conventional mortgage purchase yields and ARM adjustments as interest rates declined, and to an increase in the proportion of intermediate-term fixed-rate mortgages in portfolio, which generally have a lower yield relative to 30-year fixed-rate mortgages.

The following table summarizes mortgage purchases and repayments for the years 1989 through 1991.

Mortgage Purchases and Repayments

(Dollars in millions)

	Purchases			Repayments (1)		
	1991	1990	1989	1991	1990	1989
Mortgage type:						
Single-family mortgages:						
Government insured or guaranteed	$ 1,164	$ 698	$ 940	$ 1,306	$ 1,240	$ 1,342
Conventional:						
30-year fixed-rate	19,111	12,245	11,659	7,238	4,090	4,583
Intermediate-term fixed-rate	9,541	5,044	3,460	3,928	2,482	1,926
Adjustable-rate mortgages	4,892	2,826	4,492	4,253	3,651	3,262
Second mortgages	705	654	406	521	383	354
Total single-family	35,413	21,467	20,957	17,246	11,846	11,467
Multifamily	1,789	2,492	1,561	442	374	320
Total	$37,202	$23,959	$22,518	$17,688	$12,220	$11,787
Average net yield	8.89%	9.82%	9.88%	9.53%	10.20%	10.16%

(1) Includes mortgage loan prepayments, scheduled amortization, and foreclosures. Loans removed from portfolio as a result of foreclosure were $643 million, $616 million, and $786 million in 1991, 1990, and 1989, respectively.

The increase in mortgage purchases in 1991 compared with 1990 was due primarily to an increase in the number of mortgages offered for sale in the secondary market, in large part resulting from the high level of refinancing activity because of a recent significant decline in mortgage rates. The increase from 1989 to 1990 was due to increased "buy/sell" activity as well as to growth in the secondary market. Buy/sell activity refers to the Corporation's practice of committing to purchase mortgages and simultaneously committing to sell mortgages as MBS. Buy/sell activity allows the Corporation to continue to provide funds to the primary mortgage market in periods characterized by narrow spreads between mortgage yields and the Corporation's debt costs, when management does not consider it desirable to expand the size of its portfolio.

Sales from portfolio totaled $7.2 billion in 1991, compared with $5.8 billion in 1990 and $3.0 billion in 1989. The higher sales levels in 1991 and 1990 compared with 1989 reflect the Corporation's increased use of buy/sell activities. Sales in connection with buy/sell activities were $5.3 billion, $5.5 billion, and $2.8 billion in 1991, 1990, and 1989, respectively. Buy/sell activity does not materially affect net interest margin nor does it generate significant gains or losses. The

Corporation also sold $800 million of low-coupon mortgages in 1991 and incurred a loss of $59 million on the sale.

At December 31, 1991, the weighted average remaining life of the mortgage loans in the Corporation's mortgage portfolio was approximately 19 years, assuming normal scheduled amortization and no prepayments. Although the rate of principal payments is influenced by a variety of economic, demographic, and other factors, it generally increases when the level of interest rates declines significantly below the average interest rate of mortgage loans in portfolio.

Investment Portfolio

The carrying value of the Corporation's non-mortgage investment portfolio as of December 31, 1991, 1990, and 1989 was $11.0 billion, $9.9 billion, and $6.7 billion, respectively. Investments in U.S. Government and state and municipal securities represented less than one percent of the investment portfolio at the end of each of those years. Investments are carried at their historical cost adjusted for unamortized discount and premium.

The following table shows the maturities and weighted average yields as of December 31, 1991. Yields on tax-exempt securities are presented on a tax-equivalent basis.

Investment Portfolio

(Dollars in millions)

	Amortized Cost	Yield
As of December 31, 1991		
Due within one year	$ 8,435	5.50%
After 1 but within 5 years	92	8.81
After 5 but within 10 years	54	8.07
After 10 years	2	8.00
	8,583	
Asset-backed securities (1)	2,416	
Total	$10,999	

(1) Contractual maturity of the asset-backed securities may not be a reliable indicator of their expected life because borrowers have the right to repay their obligations at any time.

Financing Activities

Debt Issued and Outstanding

The average cost of debt outstanding at December 31, 1991 was 8.25 percent, compared with 8.81 percent and 9.04 percent at December 31, 1990 and 1989, respectively. These decreases were primarily the result of achieving a cost of funds on net new debt (debt issued less debt repaid) that was lower than the average cost of debt outstanding. Lower interest rates in recent years have allowed the Corporation to reduce the average cost of debt outstanding while maintaining the desired duration of its liabilities.

The following table sets forth the amount and average cost of debt issued and repaid during the last three years, and of debt outstanding at the end of each of those years.

Debt Issued, Repaid, and Outstanding

(Dollars in millions)

	1991	1990	1989
Issued during the year:			
Short-term: (1)			
Amount	$151,223	$ 94,407	$ 55,037
Average cost	5.60%	7.83%	8.46%
Long-term: (1)			
Amount	$ 30,234	$ 19,581	$ 23,531
Average cost	7.73%	8.93%	8.90%
Total debt:			
Amount	$181,457	$113,988	$ 78,568
Average cost (2)	5.96%	8.03%	8.60%
Repaid during the year:			
Amount	$171,311	$106,974	$ 68,043
Average cost (2)	6.29%	8.27%	8.77%
Outstanding at year-end:			
Due within one year:			
Net amount	$ 34,608	$ 38,453	$ 36,346
Average cost	6.59%	8.05%	8.90%
Due after one year:			
Net amount	$ 99,329	$ 84,950	$ 79,718
Average cost	8.67%	9.07%	9.00%
Total debt:			
Net amount	$133,937	$123,403	$116,064
Average cost (2)	8.25%	8.81%	9.04%

(1) Short-term refers to the face amount of debt issued with an original term of one year or less. Long-term is the face amount of debt issued with an original term greater than one year.

(2) Average cost includes the amortization of insurance costs and hedging results, and the effect of currency, debt, and interest rate swaps.

The following table presents the amount of callable debt and Indexed Sinking Fund Debentures ("ISFDs") and the notional principal amounts of callable and ISFD swaps issued and outstanding for each year.

	Year Ended December 31,		
	1991	1990	1989
	(Dollars in billions)		
Issued during period	$20.1	$13.3	$ 6.5
Percentage of total long-term debt issued (1)	63%	66%	28%
Outstanding at end of period	$41.2	$22.3	$ 9.4
Percentage of total long-term debt outstanding (1)	36%	22%	10%

(1) Includes the notional principal amount of callable and ISFD swaps.

During 1991, members of the Corporation's Debenture Selling Group acknowledged that they had inflated indications of investor interest in Fannie Mae debt issues and provided the Corporation with inaccurate reports about debt distribution. As a result, the Corporation announced revised procedures and record-keeping requirements for debenture sales and initiated a program to audit compliance with

the provisions of a revised selling group agreement. It appears that neither the Corporation nor purchasers of its securities suffered losses as a result of this unacceptable activity by its selling group members.

Capital Resources

At December 31, 1991, the Corporation's capital base (stockholders' equity plus allowance for losses) had grown to $6.3 billion, compared with $4.5 billion and $3.5 billion at the end of 1990 and 1989, respectively. At December 31, 1991, there were 273 million shares of common stock outstanding. During 1991, 33 million shares of common stock were issued upon exercise of warrants and, as a result, proceeds of $493 million were added to stockholders' equity. In 1991, the Board voted increases in the quarterly cash dividend totaling eight cents per share. The dividend payable in the fourth quarter of 1991 was 30 cents per share.

The Secretary of Housing and Urban Development requires that the Corporation's debt-to-capital ratio not exceed 20:1. Capital, for this purpose, includes stockholders' equity, subordinated debentures, and the allowance for losses. Also, the Corporation is subject to a restriction in connection with certain subordinated debenture issues, which limits the amount of such debentures outstanding to not more than two times the sum of common stock, additional paid-in capital, and retained earnings. Presented in the following table are these ratios at December 31, 1991, 1990, and 1989.

Capital Ratios

	1991	1990	1989
Debt-to-capital	15.9:1	18.9:1	19.7:1
Subordinated debt-to-equity	0.3:1	0.5:1	0.8:1

These ratios have decreased largely because of increases in retained earnings and, for the debt-to-capital ratio, a higher allowance for losses.

Regulatory Developments

On September 25, 1991, the House of Representatives voted to approve H.R. 2900, a bill that would set specific capital standards for Fannie Mae and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), and would create an independent Office of Secondary Market Examination and Oversight within the Department of Housing and Urban Development ("HUD") to oversee regulatory and capital requirements.

Under H.R. 2900, Fannie Mae and Freddie Mac would be tested against three capital "enforcement levels." The bill incorporates a risk-based capital standard that would require each company to have sufficient capital to withstand severe credit losses and interest rate changes simultaneously and to hold an additional 30 percent of the capital required for interest rate and credit risk to cover management and operations risk. Both corporations also would be required to have capital that equals or exceeds a minimum equity level equal to the sum of 2.5 percent of on-balance-sheet assets and .45 percent of the unpaid principal balance of outstanding mortgage-backed securities and other off-balance-sheet obligations, excluding commitments to purchase mortgages or issue securities. If capital fell below the risked-based capital level, regulatory oversight would become more intense and the regulators could take such measures as limiting dividend payments. If capital also fell below the minimum equity level, the regulators could also limit the increase in obligations and growth in assets.

The bill further sets a critical equity level of 1.25 percent of on-balance-sheet assets plus .25 percent of off-balance-sheet MBS outstanding and other off-balance-sheet obligations. If this level is not maintained, the result would be mandatory conservatorship by HUD. At December 31, 1991, the Corporation's capital level was sufficient to meet the minimum and critical equity levels in H.R. 2900.

H.R. 2900 further provides that, until the regulations establishing the risk-based level go into effect, the Corporation shall be deemed to meet the risk-based capital level as long as it meets the minimum equity level.

With respect to affordable housing programs, Fannie Mae and Freddie Mac would be required to set goals to promote affordable housing for low- and very low-income families consistent with each corporation's overall mission. Fannie Mae's goal for the two-year 1992-1993 period would be the purchase or securitization of such mortgages in an amount of not less than $2 billion; the goal for 1994 would be the purchase or securitization of such mortgages in an amount aggregating not less than 1 percent of the total amount of mortgage purchases of the Corporation during 1993. No comparable legislation had been reported by the Senate Banking Committee as of February 27, 1992, but legislation is expected in 1992.

In August 1991, HUD published proposed revisions to its existing regulations relating to oversight of Fannie Mae and proposed new regulations applicable to Freddie Mac. The proposed regulations would require that the Secretary of HUD approve annual dividend policies adopted by Fannie Mae's Board of Directors, any repurchases by Fannie Mae of its stock or debt or other obligations convertible into stock, and any significant and material changes in existing Fannie Mae programs (as well as new program proposals) for the purchase or securitization of conventional mortgages. They also would require that Fannie Mae meet risk-based capital requirements to be imposed by the Secretary and comply with certain other restrictions and reporting requirements, including a requirement that Fannie Mae submit annual audit reports certified by a certified public accounting firm acceptable to the Secretary. Fannie Mae submitted extensive critical comments on the proposed regulations before the November 28 deadline for comments, as did approximately 100 other entities. In almost all cases, the comments suggested that major revisions to the proposed regulations would be required in order for the regulations not to stifle innovation, slow responsiveness to market needs, diminish efficiency, impact adversely the ability of Fannie Mae and Freddie Mac to raise capital, and ultimately, increase the cost of affordable housing to American home buyers and renters. HUD has not taken any further action on the proposed regulations.

Liquidity Management

Fannie Mae's statutory mission requires that it maintain a constant secondary market for mortgage loans. The Corporation, therefore, must raise funds continually to support this mortgage purchase activity. The capital markets traditionally have treated the Corporation's obligations as "federal agency" debt. As a result, even though its debt is not guaranteed by the U.S. government, the Corporation has had ready access to funds at relatively favorable rates.

The role of liquidity management at Fannie Mae is to ensure that funds are available to meet the Corporation's regular business requirements and to take advantage of market opportunities. Fannie Mae's primary sources of cash are issuances of debt obligations, mortgage loan repayments, interest income, MBS guaranty fees, and proceeds from the sale of mortgages. In addition, at December 31, 1991, Fannie Mae had a portfolio of cash equivalents and shorter term investments totaling $14.0 billion. Primary uses of cash include the purchase of mortgages, repayment of debt, payment of interest and administrative expenses, and payment of taxes.

At December 31, 1991, the Corporation had mandatory delivery commitments and lender option commitments outstanding to purchase $4.7 billion and $5.6 billion of mortgage loans, respectively, compared with $1.9 billion and $7.7 billion, respectively, outstanding at December 31, 1990.

Mortgage-Backed Securities

MBS outstanding grew to a record $372.0 billion at December 31, 1991, compared with $299.8 billion at December 31, 1990, and $228.2 billion at December 31, 1989. MBS are backed by loans from one of three sources: a single lender, multiple lenders, or the Corporation's portfolio. Single-lender MBS generally are issued through lender swap transactions in which a lender exchanges

pools of mortgage loans for MBS. Multiple-lender MBS allow several lenders to pool mortgage loans together and, in return, receive MBS (called Fannie Majors®) representing a proportionate share of a larger pool. MBS frequently are used to back other securities, including Fannie Megas, Stripped MBS ("SMBS"), and REMICs. Fannie Megas allow investors to consolidate small or partially paid down pools of MBS of the same type and pass-through rate. In return, the investor receives a certificate representing an undivided interest in the consolidated pool.

MBS are not assets of the Corporation, except when acquired for investment purposes, nor are the related outstanding securities recorded as liabilities. However, the Corporation is liable under its guaranty to make timely payments of principal and interest to investors. The issuance of MBS creates guaranty fee income without Fannie Mae assuming any debt refinancing risk on the underlying pooled mortgages. Sellers of pools of mortgage loans may retain or transfer to one or more third parties the primary default risk on loans comprising the pools, or they may elect to transfer this credit risk to Fannie Mae for a higher guaranty fee. The Corporation, however, assumes the ultimate risk of loss on all MBS.

The following table summarizes MBS activity for the years ended December 31, 1991, 1990, and 1989.

Summary of MBS Activity

(Dollars in millions)

	Issued				Outstanding		
	Lender Originated (1)						
	Lender Risk	Fannie Mae Risk	Fannie Mae Originated	Total	Lender Risk (2)	Fannie Mae Risk (3)	Total (4)
1991	$11,578	$90,531	$10,794	$112,903	$96,208	$275,776	$371,984
1990	11,485	79,699	5,511	96,695	97,752	202,081	299,833
1989	23,925	40,471	5,368	69,764	94,343	133,889	228,232

(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 $43.3 billion, $35.9 billion, and $30.6 billion at December 31, 1991, 1990, and 1989, 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 $9.3 billion at December 31, 1991 and 1990, and $11.1 billion at December 31, 1989, which are backed by government insured or guaranteed mortgages.

(4) Included are $16.7 billion, $11.8 billion, and $11.7 billion at December 31, 1991, 1990, and 1989, respectively, of Fannie Mae MBS in portfolio.

Despite an increase in the amount of MBS on which the Corporation has the primary default risk and receives a higher guaranty fee, the effective guaranty fee rate on MBS remained relatively stable because competitive pressure caused the general decline in guaranty fee rates on MBS.

Fannie Mae issued more MBS in 1991 than in 1990, and issued more in 1990 than in 1989, primarily due to an increase in the volume of fixed-rate mortgages available in the secondary market to create MBS and an increase in the Corporation's market share. In addition, in both 1991 and 1990, higher proportions of fixed-rate mortgage originations were securitized than in the preceding year, partly in response to new risk-based capital requirements for thrifts, banks, and bank holding companies.

REMICs issued during 1991 aggregated $101.8 billion, compared with $60.9 billion in 1990 and $37.6 billion in 1989. The increase in 1991 and 1990 of REMIC issuances was the result of increased investor demand for investments with a variety of average life and prepayment characteristics and greater availability of the underlying MBS. Both Fannie Mae and Ginnie Mae certificates have been used in the issuance of REMICs by Fannie Mae. Issuance of REMICs backed by Ginnie Mae certificates provides an additional source of fee income. Because the issuance of REMICs backed by Fannie Mae MBS creates a demand for MBS, REMIC activity supports the price for Fannie Mae MBS. As a result, the increases in MBS issues in 1990 and 1991 are due, in part, to increased REMIC activity. The outstanding balance of REMICs as of December 31, 1991 was $193.3 billion, compared with $104.3 billion and $47.6 billion of REMICs outstanding as of December 31, 1990 and 1989, respectively.

FEDERAL NATIONAL MORTGAGE ASSOCIATION

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INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders
Federal National Mortgage Association

We have audited the accompanying balance sheets of Federal National Mortgage Association as of December 31, 1991 and 1990, and the related statements of income, changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 1991. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Federal National Mortgage Association at December 31, 1991 and 1990, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 1991, in conformity with generally accepted accounting principles.

KPMG PEAT MARWICK

Washington, DC
January 13, 1992

FEDERAL NATIONAL MORTGAGE ASSOCIATION

STATEMENTS OF INCOME

	Year Ended December 31,		
	1991	1990	1989
	(Dollars in millions, except per share amounts)		
Interest income:			
Mortgage portfolio	$11,603	$10,958	$10,103
Investments and cash equivalents	990	1,111	977
Total interest income	12,593	12,069	11,080
Interest expense	10,815	10,476	9,889
Net interest income	1,778	1,593	1,191
Other income:			
Guaranty fees	675	536	408
Income from tax settlement	239	—	—
Gain (loss) on sales of mortgages, net	(28)	7	9
Miscellaneous, net	106	107	60
Total other income	992	650	477
Other expenses:			
Provision for losses	370	310	310
Administrative	319	286	254
Total other expenses	689	596	564
Income before federal income taxes and extraordinary item	2,081	1,647	1,104
Provision for federal income taxes	626	474	297
Income before extraordinary item	1,455	1,173	807
Extraordinary item: loss from repurchase of debt (net of tax effect of $48 million)	92	—	—
Net income	$ 1,363	$ 1,173	$ 807
Per share:			
Earnings before extraordinary item:			
Primary	$ 5.33	$ 4.50	$ 3.14
Fully diluted	5.31	4.49	3.10
Net earnings:			
Primary	4.99	4.50	3.14
Fully diluted	4.98	4.49	3.10
Cash dividends	1.04	.72	.43
Average shares used to compute fully diluted earnings per share (in millions)	274	261	260

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

BALANCE SHEETS

Assets

	December 31, 1991	December 31, 1990
	(Dollars in millions)	
Mortgage portfolio, net	$126,486	$113,875
Investments	10,999	9,868
Cash and cash equivalents	3,194	4,178
Accrued interest receivable	1,048	1,032
Receivable from currency swaps	3,202	2,376
Acquired property and foreclosure claims, net	348	370
Other	1,795	1,414
Total assets	$147,072	$133,113

Liabilities and Stockholders' Equity

	1991	1990
Liabilities:		
Debentures, notes, and bonds, net:		
Due within one year	$ 34,608	$ 38,453
Due after one year	99,329	84,950
	133,937	123,403
Accrued interest payable	2,514	2,418
Payable from currency swaps	2,385	1,755
Other	2,689	1,596
Total liabilities	141,525	129,172
Stockholders' Equity:		
Common stock, $2.10 stated value, no maximum authorization, issued 282,167,915 shares (1991) and 248,716,569 shares (1990)	593	522
Additional paid-in capital	1,245	810
Retained earnings	3,853	2,772
	5,691	4,104
Less: treasury stock, at cost, 9,179,664 shares (1991) and 10,444,844 shares (1990)	144	163
Total stockholders' equity	5,547	3,941
Total liabilities and stockholders' equity	$147,072	$133,113

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

	Number of Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Total Stockholders' Equity
	(Dollars and shares in millions)					
Balance, January 1, 1989	79	$513	$ 781	$1,067	$ (101)	$2,260
Net income	—	—	—	807	—	807
Dividends	—	—	—	(103)	—	(103)
Three-for-one stock split	157	4	(4)	—	—	—
Conversions of convertible debentures	1	3	7	—	—	10
Treasury stock issued for stock options and benefit plans	2	—	1	—	14	15
Other	—	—	2	—	—	2
Balance, December 31, 1989	239	520	787	1,771	(87)	2,991
Net income	—	—	—	1,173	—	1,173
Dividends	—	—	—	(172)	—	(172)
Shares repurchased	(4)	—	—	—	(93)	(93)
Treasury stock issued for stock options and benefit plans	2	—	9	—	17	26
Stock warrants exercised	1	2	13	—	—	15
Other	—	—	1	—	—	1
Balance, December 31, 1990	238	522	810	2,772	(163)	3,941
Net income	—	—	—	1,363	—	1,363
Dividends	—	—	—	(282)	—	(282)
Treasury stock issued for stock options and benefit plans	2	—	13	—	19	32
Stock warrants exercised	33	71	422	—	—	493
Balance, December 31, 1991	273	$593	$1,245	$3,853	$ (144)	$5,547

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	1991	1990	1989
	(Dollars in millions)		
Cash flows from operating activities:			
Net income	$ 1,363	$ 1,173	$ 807
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for losses	370	310	310
Loss on repurchase of debt	140	—	—
Other increases, net	612	102	229
Net cash provided by operating activities	2,485	1,585	1,346
Cash flows from investing activities:			
Purchases of mortgages	(37,117)	(23,743)	(22,293)
Proceeds from sales of mortgages	7,128	5,817	2,992
Mortgage principal repayments, net of discount	16,726	11,216	10,544
Net proceeds from disposition of foreclosed properties	457	464	519
Net increase in investments	(1,131)	(1,530)	(2,873)
Net cash used in investing activities	(13,937)	(7,776)	(11,111)
Cash flows from financing activities:			
Cash proceeds from issuance of debentures	30,306	19,666	23,567
Cash payments to redeem debentures	(17,937)	(12,249)	(12,698)
Cash proceeds from issuance of short-term debt	150,174	93,245	54,084
Cash payments to redeem short-term debt, net of discount	(152,308)	(93,596)	(54,241)
Net cash proceeds (payments) for stock activities	233	(229)	(99)
Net cash provided by financing activities	10,468	6,837	10,613
Net increase (decrease) in cash and cash equivalents	(984)	646	848
Cash and cash equivalents at beginning of year	4,178	3,532	2,684
Cash and cash equivalents at end of year	$ 3,194	$ 4,178	$ 3,532

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Fannie Mae is a federally chartered and stockholder-owned corporation operating in the residential mortgage finance industry. The accounting and reporting policies of the Corporation conform with generally accepted accounting principles. Certain amounts in prior years' financial statements have been reclassified to conform with the current presentation.

Mortgage Portfolio and Investments

Mortgages and mortgage-backed securities acquired for investment are carried at their unpaid principal balances adjusted for unamortized purchase discount or premium and deferred loan fees. The Corporation uses actual principal prepayment experience and estimates of future principal prepayments in calculating the constant effective yield necessary to apply the interest method in the amortization of loan fees and discount. In evaluating prepayments, loans are aggregated by similar characteristics (e.g., loan type, acquisition date, and maturity). Factors used in determining estimates of future prepayments include historical prepayment data and expected prepayment performance under varying interest rate scenarios.

The accrual of interest on conventional mortgages, other than those that are federally insured or guaranteed, is discontinued when the mortgages become 90 days delinquent. Any accrued but uncollected interest on mortgages that are 90 days delinquent is reversed against current period interest income. Interest income on such mortgages is recognized only to the extent that cash payments are received.

Non-mortgage investments are carried at their historical cost adjusted for unamortized discount or premium. Both the mortgage portfolio and other investments are acquired with the objective of earning a net interest spread over the related cost of funds. The Corporation has the ability to hold these investments until their maturity and intends to hold them for the foreseeable future.

Guaranteed Mortgage-Backed Securities

The Corporation guarantees the timely payment of principal and interest on Fannie Mae Mortgage-Backed Securities ("MBS"). These securities represent beneficial interests in pools of mortgages or other MBS held in trust by the Corporation. The pools of mortgages or MBS are not assets of the Corporation, except when acquired for investment purposes, nor are the related outstanding securities liabilities; accordingly, neither is reflected on the accompanying balance sheets. The Corporation receives monthly guaranty fees for each MBS pool based on a percentage of the pool's outstanding balance. For MBS pools held in the Corporation's portfolio, the guaranty fee is reflected as interest income.

Allowance for Losses

The Corporation establishes an allowance for losses on the mortgage portfolio and on MBS to provide against foreclosure losses. The allowance is maintained at a level that, in management's judgment, is adequate to provide for estimated losses. This judgment is based on such factors as economic conditions, geographic concentrations, mortgage characteristics, and actual and expected loan loss experience. The allowance is increased by provisions charged as an expense in the income statement and decreased by charge-offs, net of recoveries.

Acquired Property

Real estate acquired and held for sale as a result of foreclosure is carried at the lower of the investment in the property or its estimated net realizable value. In making these estimates, current appraised values of properties, expected mortgage insurance proceeds, estimated interest carrying costs, and selling and holding expenses are considered.

Gain/Loss on Sales of Mortgages

When the Corporation places mortgages in MBS pools and sells them as securities, a gain or loss is recognized to the extent the sale proceeds differ from the recorded value of the mortgages sold. An adjustment to the gain or loss is recognized in an amount equal to the present value of the difference between the effective mortgage interest rate received by the Corporation and the sum of the pass-through rate paid to the investor and a normal guaranty fee.

Risk Management Activities

The Corporation takes positions in financial markets to hedge against changing interest rates or foreign currency fluctuations that may affect the cost of certain debt issuances. Results from activities that are designated and perform effectively as hedges are deferred and amortized as adjustments to interest expense over the term of the borrowings.

Securities Sold Under Agreements to Repurchase

The Corporation enters into sales of securities under agreements to repurchase substantially similar securities at a later date. Such transactions are treated as financings. The obligations to repurchase securities sold are reflected as liabilities on the balance sheet and the mortgage securities underlying the agreements remain in the asset accounts. The counterparty to the repurchase agreement acquires legal ownership of the securities transferred during the term of the agreement.

Securities Purchased Under Agreements to Resell

The Corporation purchases securities under agreements to resell the same securities at a later date. The securities are recorded as investment assets on the balance sheet, and the Corporation acquires legal ownership of the securities purchased during the term of the agreement. The Corporation requires the fair market value of the securities purchased to be equal to or greater than the investment amount.

Foreign Currency Translation

The Corporation issues debt securities in which principal, interest, or both are payable in a foreign currency or are determined by reference to an index that includes one or more foreign currencies. Concurrently, the Corporation enters into currency swaps that convert the proceeds of the borrowing into dollars or provide for scheduled future exchanges of the two currencies to insulate the Corporation against foreign exchange risk.

Foreign currency borrowings and the related receivables from currency swaps are translated at the market rates of exchange as of the balance sheet date.

FEDERAL NATIONAL MORTGAGE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS—(Continued)

Cash and Cash Equivalents

The Corporation considers overnight federal funds and highly liquid investment instruments with an original maturity of three months or less to be cash equivalents. Cash equivalents are carried at cost, which approximates market value.

Income Taxes

Deferred income taxes are established for timing differences between financial and taxable income. Investment and other tax credits are deferred and amortized over the lives of the related assets.

Earnings Per Share

Earnings per share are computed using the weighted-average number of common shares outstanding, including dilutive common stock equivalents. Fully diluted earnings per share are computed on the assumption that all outstanding subordinated convertible capital debentures were converted at the beginning of the year, after increasing earnings for the related interest expense, net of federal income taxes.

2. Mortgage Portfolio, Net

The mortgage portfolio consisted of the following investments at December 31.

	1991	1990
	(Dollars in millions)	
Single-family mortgages:		
Government insured or guaranteed	$ 9,900	$ 11,204
Conventional:		
30-year fixed-rate	57,643	50,846
Intermediate-term fixed-rate	26,534	21,409
Adjustable-rate mortgages	20,941	20,737
Second mortgages	2,069	1,885
	117,087	106,081
Multifamily mortgages:		
Government insured	4,090	4,243
Conventional	7,806	6,304
	11,896	10,547
Total unpaid principal balance	128,983	116,628
Less:		
Unamortized discount and deferred loan fees	2,304	2,562
Allowance for losses	193	191
	$126,486	$113,875

FEDERAL NATIONAL MORTGAGE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS—(Continued)

3. Allowance for Losses

Changes in the allowance for the years 1989 to 1991 are summarized below.

	Total (Dollars in millions)
Balance, January 1, 1989	$396
Provision	310
Net foreclosure losses charged off	(243)
Balance, December 31, 1989	463
Provision	310
Net foreclosure losses charged off	(234)
Balance, December 31, 1990	539
Provision	370
Net foreclosure losses charged off	(205)
Balance, December 31, 1991	$704

At December 31, 1991, $193 million of the allowance for losses is included in the Balance Sheet under "Mortgage portfolio, net," which represents the allocation for portfolio loan losses; $503 million is included under "Other liabilities" for estimated losses on MBS; and the remainder, or $8 million, is included in foreclosure claims. The corresponding amounts at December 31, 1990 were $191 million, $344 million, and $4 million, respectively. However, the total allowance for losses is available to absorb losses related to either the total loan portfolio or loans underlying MBS.

4. Debt Securities Held for Investment

Debt securities held for investment include certain MBS, other mortgage-related debt instruments, and the non-mortgage investment portfolio. The following table presents the amortized cost and estimated market value of these securities at December 31, 1991 and 1990, and gross unrealized gains and losses at December 31, 1991. Gross unrealized gains and losses at December 31, 1990 were $296 million and $72 million, respectively.

	1991				1990	
Account Title (1) (Security Name)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value	Amortized Cost	Estimated Market Value
	(Dollars in millions)					
Mortgage portfolio, net:						
Fannie Mae MBS	$16,452	$1,077	$16	$17,513	$11,530	$11,667
Other mortgage-related securities	2,916	129	—	3,045	2,948	2,987
	19,368	1,206	16	20,558	14,478	14,654
Investments:						
Federal funds	4,117	—	—	4,117	5,329	5,329
Asset-backed securities	2,416	79	—	2,495	1,780	1,800
Floating-rate notes	485	2	—	487	1,432	1,415
Repurchase agreements	2,195	91	—	2,286	951	996
Other	1,786	10	—	1,796	376	376
	10,999	182	—	11,181	9,868	9,916
Total	$30,367	$1,388	$16	$31,739	$24,346	$24,570

(1) Debt securities are listed according to balance sheet account classification.

The remaining maturities of debt securities held for investment at December 31, 1991 and 1990 are shown in the following table:

	1991		1990	
	Amortized Cost	Estimated Market Value	Amortized Cost	Estimated Market Value
	(Dollars in millions)			
Remaining maturity at December 31:				
Due within one year	$ 6,240	$ 6,245	$ 7,464	$ 7,498
Due after one year through five years	92	97	552	548
Due after five years through ten years	54	55	50	49
Due after ten years	2,761	2,861	2,552	2,581
	9,147	9,258	10,618	10,676
Mortgage-backed securities (1)	18,804	19,986	11,948	12,094
Asset-backed securities (1)	2,416	2,495	1,780	1,800
Total	$30,367	$31,739	$24,346	$24,570

(1) Contractual maturity of the mortgage- and asset-backed securities may not be a reliable indicator of their expected life because borrowers have the right to repay their obligations at any time.

Proceeds from sales of non-mortgage investments in debt securities during 1991 and 1990 were $34 million and $103 million, respectively. Gross realized gains and losses were not significant in either year.

5. Debentures, Notes and Bonds, Net

The average cost of all debt outstanding at December 31, 1991 and 1990 was 8.25 percent and 8.81 percent, respectively. The average effective maturity of all debt outstanding at December 31, 1991 and 1990 was 56 months and 50 months, respectively, including the effect of interest rate swaps. Interest paid during 1991, 1990, and 1989 was $10.5 billion, $10.4 billion, and $9.4 billion, respectively.

Pursuant to the Corporation's Charter Act and related regulations, no debt obligations may be issued without the approval of the Secretary of the Treasury. The Secretary of Housing and Urban Development ("HUD") currently requires that the maximum amount of the corporation's general obligations outstanding at any time, excluding those that are subordinated or secured, not exceed 20 times the sum of stockholders' equity, subordinated capital debentures, and the allowance for losses. At December 31, 1991, this ratio was 15.9:1.

FEDERAL NATIONAL MORTGAGE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS—(Continued)

Borrowings Due Within One Year

Borrowings due within one year at December 31 are summarized below. Amounts are net of unamortized discount and premium.

	1991					1990				
	Outstanding at December 31		Average Outstanding During Year		Maximum Outstanding At Any	Outstanding at December 31		Average Outstanding During Year		Maximum Outstanding At Any
	Amount	Cost(1)	Amount	Cost(1)	Month End	Amount	Cost(1)	Amount	Cost(1)	Month End
	(Dollars in millions)									
Securities sold under agreements to repurchase(2)	$ 1,348	2.39%	$ 506	4.35%	$ 1,638	$ 351	6.06%	$ 501	6.72%	$ 1,171
Short-term notes	17,516	5.17	18,531	6.30	20,795	17,594	7.71	14,086	8.07	17,594
Residential financing securities	1,130	5.79	2,689	6.98	3,556	3,814	8.08	4,693	8.46	5,771
Other short-term debt	235	4.61	245	6.37	458	358	7.43	1,046	8.51	2,061
Current portion of borrowings due after one year(3):										
Debentures	11,653	9.14				13,749	8.32			
Other	2,726	7.23				2,587	9.13			
Total due within one year	$34,608	6.59%				$38,453	8.05%			

(1) Cost includes the amortization of discounts, premiums, issuance costs, hedging results, and the effects of currency and debt swaps.

(2) MBS underlying repurchase agreements had a carrying value of $1,310 and $344 million at December 31, 1991 and 1990, respectively, and a market value of $1,369 million and $354 million at December 31, 1991 and 1990, respectively.

(3) Information on average amount and cost of debt outstanding during the year and maximum amount outstanding at any month end is not applicable. See "Borrowings Due After One Year" for additional information.

FEDERAL NATIONAL MORTGAGE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS—(Continued)

Borrowings Due After One Year

Borrowings due after one year consisted of the following at December 31,

	Maturity Date	1991 Amount Outstanding	1991 Average Cost (1)	1990 Amount Outstanding	1990 Average Cost (1)
		(Dollars in millions)			
Investment agreements	1992-2012	$ 2,149	8.04%	$ 2,310	8.05%
Long-term — other, net of $65 million of discount for 1991 ($68 million for 1990)	1992-2018	612	8.32	707	9.13
Debentures, net of $39 million of discount for 1991 ($46 million for 1990) (2)	1992-2021	82,404	8.80	76,647	9.09
Medium-term notes, includes $120 million of premium for 1991 ($127 million for 1990) (3)	1992-2021	11,233	7.61	2,140	8.59
Zero coupon securities, net of $5,551 million of discount for 1991 ($5,617 million for 1990)	1992-2014	672	10.67	611	10.63
Zero coupon subordinated capital debentures, net of $6,326 million of discount for 1991 ($6,366 million for 1990)	2019	424	10.22	384	10.22
Subordinated capital debentures, net of $12 million of discount for 1991 ($13 million for 1990)	1992-2019	1,039	9.12	1,519	9.00
		98,533	8.67%	84,318	9.07%
Adjustment for foreign currency translation	—	796		632	
		$99,329		$84,950	

(1) Cost includes the amortization of discounts, premiums, issuance costs, hedging results, and the effects of currency and debt swaps.

(2) Included in debentures are Indexed Sinking Fund Debentures ("ISFDs") totaling $3.0 billion and $3.3 billion at December 31, 1991 and 1990, respectively. ISFDs are subject to mandatory redemptions tied to certain Treasury rates after an initial nonredemption period.

(3) Medium-term notes may be fixed-rate, floating-rate, or zero coupon with maturities ranging from one day to thirty years. Interest and principal may be payable in U.S. dollars or a foreign currency and may be indexed to foreign exchange rates or other indices.

Debentures include callable debt, which generally is redeemable in whole or in part (in certain cases, at a specified premium) at the option of the Corporation any time on or after a specified date. The final maturity of callable debt is used in computing average effective maturity data. The following table summarizes the amounts and call periods of callable instruments, including Indexed Sinking Fund Debentures ("ISFDs"), and the notional amount of callable and ISFD swaps. Medium-term notes and subordinated capital debentures that are redeemable at the Corporation's option also are included in the table.

Callable Instruments

Call Date	Year of Maturity	Amount Outstanding (Dollars in millions)	Average Cost
Currently	1993-2002	$ 685	8.10%
1992	1994-2001	6,677	8.05
1993	1995-2013	6,884	8.80
1994	1996-2019	11,476	8.59
1995	1998-2020	4,350	8.85
1996	2001-2021	4,705	8.47
1997	2000-2021	195	8.96
		34,972	
ISFDs	1993-1999	3,024	9.66
Callable and ISFD swaps (notional amount)	1997-2001	3,200	—
Total		$41,196	

At December 31, 1991, principal amounts of debt maturing in the years 1993-1997 were $10.8, $14.0, $10.9, $18.7, and $9.2 billion, respectively. If callable debt is assumed to be redeemed at the initial call date, the principal amounts would be $17.7, $21.5, $12.8, $17.3, and $6.2 billion in the years 1993-1997, respectively. In 1991, $0.9 billion of debt was redeemed early pursuant to call provisions. No debt was called in 1990.

In 1991, the Corporation recorded an extraordinary loss of $140 million ($92 million after tax) on the repurchase or call of $2.2 billion of high-coupon debt.

6. Common Shares

Pursuant to the Corporation's Charter Act and related regulations, approval by HUD is required prior to the issuance of any stock of the Corporation or securities convertible into stock. The Corporation was authorized to issue shares of adjustable-rate preferred stock for exchangeable debentures that were due in 1991. The Corporation redeemed the exchangeable debentures in lieu of issuing preferred stock.

During 1991 and 1990, 33 million and 1 million common shares were issued upon exercise of warrants and, as a result, proceeds of $493 million and $15 million were added to stockholders' equity for each respective year.

7. Income Taxes

The components of the provision for federal income taxes at December 31, 1991, 1990, and 1989 are as follows:

	1991	1990	1989
	(Dollars in millions)		
Current	$ 811	$ 523	$ 358
Deferred	(185)	(49)	(61)
	626	474	297
Tax benefit of extraordinary loss	(48)	—	—
Net federal income tax provision	$ 578	$ 474	$ 297

Deferred federal income tax expense (benefit) relating to timing differences consists of the following.

Components of Deferred Taxes

	1991	1990	1989
	(Dollars in millions)		
Deferred commitment fees	$ (22)	$ 2	$ 22
Amortization of purchase discount	(18)	(35)	(59)
Losses (gains) on disposition of mortgages	(99)	10	10
Provision for losses	(58)	(60)	(58)
Benefits from tax-advantaged investments	29	29	13
Other items, net	(17)	5	11
Total deferred federal income tax benefit	$(185)	$ (49)	$ (61)

The Corporation's effective tax rates differ from statutory rates as follows.

Analysis of Effective Tax Rate

	1991	1990	1989
Statutory corporate rate	34%	34%	34%
Tax exempt interest and dividends received deductions	(4)	(5)	(7)
Effective rate	30%	29%	27%

The Corporation is exempt from state and local taxes, with the exception of real estate taxes. The Corporation made federal income tax payments, net of refunds, of $597 million, $547 million, and $222 million in 1991, 1990, and 1989, respectively.

Resolution of Tax Case

At December 31, 1990, the Corporation had pending a case before the U.S. Supreme Court involving an unresolved issue with the Internal Revenue Service ("IRS") relating to concurrent mortgage sales. Although the Supreme Court took no action regarding the corporation's case, it agreed to review the cases of two other taxpayers. The Supreme Court's decision favored the taxpayers and in April 1991, the Supreme Court denied the IRS' petition for *certiorari* in the corporation's case. This action by the Supreme Court left standing a lower court's ruling favoring the

Corporation's tax position. As a result, the Corporation received a tax refund, with interest, and recorded income of $239 million.

IRS Examinations

The IRS, in its audit report of the Corporation's 1983 through 1985 tax returns, proposed certain deficiencies relating to deductions for hedge transactions. The IRS has indicated that hedging losses taken as ordinary deductions should be recharacterized as capital losses. This issue is in litigation and the case is scheduled to be heard in Tax Court in April 1992. If the IRS' position on hedge losses in 1983 through 1985 is sustained, the Corporations' net income would be reduced by approximately $94 million, which includes cumulative interest, net of tax, of $24 million.

The IRS is currently auditing the Corporation's tax returns for 1986 and 1987 and has proposed additional deficiencies related to certain hedging type transactions that it indicates should be recharacterized as capital losses. If the IRS' position on these proposed deficiencies in 1986 and 1987 is sustained, the Corporation's net income could be adversely affected by approximately $170 million, which includes cumulative interest, net of tax, of $48 million.

The Corporation believes the positions and deductions taken in its tax returns are proper and will contest vigorously any effort to change their timing or characterization. The Corporation's tax returns for 1988 through 1991 have similar deductions that may be challenged in future IRS audits.

Proposed Accounting Standard

In 1991, the Financial Accounting Standards Board ("FASB") issued a proposal for a new standard on "Accounting for Income Taxes." The proposed standard amends Financial Accounting Standard No. 96 and would require the Corporation to adopt new accounting and disclosure rules for income taxes no later than the Corporation's fiscal year beginning in 1993. Under the proposed standard, deferred income taxes arising from temporary differences between tax and financial income will be measured using the current marginal tax rate. In addition, it permits the recognition and measurement of a deferred tax asset for temporary differences that will result in deductible amounts in future years and for carryforwards, with an allowance recognized if it is more likely than not that some portion of the deferred tax asset will not be realized. The Corporation currently is analyzing the provisions of the proposed standard, but management anticipates that the adoption of the standard will not have a material effect on the earnings or financial condition of the Corporation.

5. Employee Benefits

Stock Compensation Plan

The Federal National Mortgage Association Stock Compensation Plan authorizes certain officers to receive performance awards, which may be issued within an award period that can range from three to five years. The performance awards become actual awards only if the Corporation attains the financial goals set for the award period. At the end of such time, the awards generally are payable in common stock. The outstanding contingent grants made for the 1992-1994, 1991-1993, and 1990-1992 award periods were 81,280; 170,443; and 94,427 performance shares, respectively.

Stock options also may be granted to key employees under this plan. The options do not become exercisable until at lease one year after the grant date and generally expire ten years from the grant date. The purchase price of the common stock covered by each option is equal to the fair market value of the stock on the date the option is granted. The following table summarizes stock option activity

for the years 1989-1991. At December 31, 1991 and 1990, stock options on 764,107 shares and 745,126 shares, respectively, were exercisable.

Stock Option Plans

	1991		1990		1989	
	Number of Options	Option Price	Number of Options	Option Price	Number of Options	Option Price
Balance, January 1	1,831,910	$ 5.38-$40.56	1,522,031	$ 5.38-$40.56	1,783,683	$5.38-$15.75
Granted	852,910	43.00- 59.25	544,000	32.00- 34.50	218,550	40.56
Exercised	(333,950)	5.38- 40.56	(193,631)	5.38- 15.75	(422,482)	5.38- 15.75
Terminated	(87,383)	9.44- 40.56	(40,490)	9.44- 40.56	(57,720)	9.44- 15.75
Balance, December 31	2,263,487	$ 5.38-$59.25	1,831,910	$ 5.38-$40.56	1,522,031	$5.38-$40.56

In 1991, 78,023 shares of restricted stock (48,500 in 1990) were awarded, issued, and placed in escrow under the Stock Compensation Plan and the Restricted Stock Plan for Directors; 12,126 shares were recovered upon termination of nonvested participants; and 32,949 shares were released as vesting of participants occurred. Compensation expense is being recorded over the vesting period of the stock as services are performed.

Employee Stock Purchase Plan

The Corporation has an Employee Stock Purchase Plan that allows the Corporation to issue up to nine million shares of common stock to qualified employees at a price equal to 85 percent of the fair market value of the stock on the first day of the period in which employees can elect to purchase the stock. In 1991, the Corporation granted each qualified employee, excluding certain officers, the right to purchase in January 1992 up to 400 shares of stock. Under the 1991 offering, 943,910 shares were purchased in January 1992, at $35.43 per share compared with 653,710 shares purchased in 1991 at $25.71 per share under the plan's 1990 offering. The Board of Directors has approved a similar offering in 1992 for Fannie Mae employees that limits the number of shares to 300 per eligible employee.

Employee Stock Ownership Plan

The Corporation has an Employee Stock Ownership Plan ("ESOP") for qualified employees. The Corporation may contribute to the ESOP an amount based on defined earnings goals, not to exceed 4 percent of the aggregate base salary for all participants. The contribution is made in the subsequent year either in shares of Fannie Mae common stock or cash that is used to purchase such stock. The expense to the Corporation related to the ESOP was $2 million in 1991, 1990, and 1989.

Thrift and Savings Plan

All regular, full-time employees of the Corporation are eligible to participate in the Corporation's Thrift and Savings Plan, which includes a 401(k) option. Employees may contribute up to the lesser of 12 percent of their base salary or the current annual dollar cap established and revised annually by the IRS, with the Corporation matching such contributions up to 3 percent of base salary. The Corporation contributed $3 million in 1991 and 1990 and $2 million in 1989.

the cost of retiree medical and other benefits be accrued over employees' working lives. Most firms, including Fannie Mae, currently record the cost of non-pension retiree benefits as they are paid. For Fannie Mae, cash payments were less than $2 million in 1991 and less than $1 million in 1990 and 1989. Fannie Mae is required to adopt the new accounting and disclosure rules no later than 1993, although earlier implementation is permitted.

Fannie Mae may adopt the new standard via a cumulative catch-up adjustment or may prospectively amortize the unfunded obligation on a straight-line basis over the greater of the average remaining service period for active plan participants or 20 years. Based on a review of the composition of the Corporation's workforce and the structure of its postretirement medical and life insurance plans, the Corporation currently estimates that the accumulated postretirement benefit obligation, or cumulative effect of the implementation of FAS 106, is approximately $55 million. The Corporation estimates the annual cost for providing these post-retirement benefits will be approximately $8 million to $11 million, depending on the method of adoption.

9. Financial Instruments with Off-Balance-Sheet Risk

The Corporation is a party to transactions involving financial instruments with off-balance-sheet risk. In the normal course of business, the Corporation uses these instruments to fulfill its statutory purpose of increasing the liquidity of residential mortgage loans and to reduce its exposure to fluctuations in interest rates. These financial instruments include MBS, commitments to purchase mortgages or to issue and guarantee MBS, and certain hedge instruments. These instruments involve, to varying degrees, elements of credit and market risk in excess of the amounts recognized on the Balance Sheet.

Guaranteed Mortgage-Backed Securities

As issuer and guarantor of MBS, the Corporation is obligated to disburse scheduled monthly installments of principal and interest (at the certificate rate) and the full unpaid principal balance of any foreclosed mortgage to MBS investors, whether or not any such amounts have been received. The Corporation also is obligated to disburse unscheduled principal payments received from borrowers.

The Corporation's credit risk is mitigated to the extent sellers of pools of mortgages elect to remain at risk on the loans sold to the Corporation. Lenders have the option to retain the primary default risk, in whole or in part, in exchange for a lower guaranty fee. Fannie Mae, however, bears the ultimate risk of default.

The Corporation's exposure to credit loss, if borrowers completely fail to perform and if both the property backing the mortgage and any pledged collateral or other forms of credit enhancement posted by the lender prove to be of no value, is represented by the face value of the MBS outstanding less the allowance for loss. At December 31, 1991 and 1990, this amount was $371.5 billion and $299.5 billion, respectively. MBS outstanding with recourse to the lender or third parties was $96.2 billion and $97.8 billion at December 31, 1991 and 1990, respectively.

Commitments

At December 31, 1991, the Corporation had outstanding $50.7 billion of mandatory and $2.1 billion of optional master commitments. In order to deliver under a master commitment a lender must convert to either a mandatory delivery commitment for portfolio or MBS with the yield or guaranty fee established at the time of conversion.

In addition, the Corporation had the following commitments outstanding at December 31, 1991 that were not issued pursuant to outstanding master commitments: $4.7 billion of mandatory delivery commitments for portfolio at an average net yield of 7.98 percent, $4.8 billion of lender option commitments for portfolio, $4.3 billion of mandatory delivery commitments to issue and guaranty MBS, and $4.5 billion of optional delivery commitments to issue and guaranty MBS. For most optional commitments, the yield or guaranty fee is set at the date of conversion to a mandatory commitment.

The cost of funding future portfolio purchases generally is hedged upon issuance of, or conversion to, a mandatory commitment: therefore, the interest rate exposure for the Corporation is largely mitigated.

Hedge Instruments

The Corporation typically uses interest rate swaps, interest rate futures contracts, and short sales of Treasury securities to hedge against fluctuations in interest rate movements. Changes in the value of these hedge instruments caused by fluctuations in interest rates are expected to offset substantially changes in the value of the items hedged. Consequently, the primary risks associated with these hedging instruments are (a) that changes in the value of the item hedged will not substantially offset changes in the value of the hedge instrument, or (b) that the counterparty to the agreement will be unable to meet the terms of the agreement. The Corporation reduces counterparty risk by dealing only with institutions that meet certain credit guidelines.

Interest rate swaps are contractual agreements between two counterparties for the exchange of periodic payments generally based on a notional principal amount and agreed-upon fixed and variable rates. The Corporation has long-term interest rate swap agreements with various parties to extend the effective maturity of certain short-term debt obligations and to adjust the effective maturity of certain long-term obligations. The notional amount of long-term interest rate swap agreements outstanding at December 31, 1991 was $4.7 billion, compared with $3.5 billion at December 31, 1990. The average remaining term of these long-term swaps was six years at December 31, 1991 and 1990. The weighted-average interest rate being received under these long-term swaps was 6.12 percent and the weighted-average interest rate being paid was 9.24 percent at December 31, 1991, compared with 8.17 percent and 9.62 percent respectively, at December 31, 1990.

The Corporation also has interest rate swap agreements that are linked to specific debt issues ("debt swaps"). These swaps achieve a specific financing objective at a desired cost, usually by effectively converting floating-rate debt into fixed-rate debt. The costs and terms of the specific debt issues, as reflected in the financial statements, include the effects of the swaps. At December 31, 1991, the notional amount of debt swaps outstanding totaled $4.3 billion, compared with $1.3 billion at December 31, 1990.

Interest rate futures are contracts for future delivery of a specified instrument or cash at a specified yield or price. Futures contracts are traded on organized exchanges and require initial margin (collateral) in the form of cash or marketable securities. Holders of futures contracts look to the exchange clearinghouse for performance under the contract and not the entity holding the offsetting futures position. Accordingly, the amount at risk due to nonperformance of counterparties is minimal. The contract amounts of interest rate futures outstanding at December 31, 1991 and 1990 was $50 million and $25 million, respectively.

Short sales of Treasury securities are obligations to deliver at a future date securities that have not been purchased. These instruments differ from interest rate futures contracts in that they are transacted through a dealer as opposed to an exchange. Risk arises from the possible inability or

unwillingness of the dealer to meet the terms of the agreement and from movement in securities values and interest rate changes. If the dealer does not meet the terms of the agreement, the Corporation would have to purchase the security at the prevailing market rate to meet its obligation. Consequently, if the market value of the securities has subsequently increased, a loss would be incurred for the difference between the current market value of the securities purchased and the original sales price. Risk is controlled through evaluation of the creditworthiness of counterparties and continuous monitoring of hedge positions. The contract amounts of Treasury securities the Corporation sold short were $1.1 billion and $1.7 billion at December 31, 1991 and 1990, respectively.

The exposure to credit loss for interest rate swaps, interest rate futures, and short sales of Treasury securities can be estimated by calculating the cost, on a present value basis, to replace at current market rates all those off-balance-sheet financial instruments outstanding for which the Corporation was in a gain position. The Corporation's estimate of the exposure to credit loss for off-balance-sheet financial instruments in a gain position at December 31, 1991 was $11 million.

10. Concentrations of Credit Risk

Concentrations of credit risk exist when a significant number of counterparties engage in similar activities or are affected similarly by changes in economic conditions that could affect their ability to meet contractual obligations.

The following table presents unpaid principal balances and the general geographic distribution of properties underlying mortgages in the portfolio and MBS outstanding as of December 31, 1991 and 1990.

		Geographic Distribution					
1991	**Gross UPB** (Dollars in millions)	**Northeast**	**Southeast**	**Midwest**	**Southwest**	**West**	**Total**
Fannie Mae risk	$377,533	21%	20%	16%	13%	30%	100%
Lender risk	106,734	35	18	13	7	27	100
Total	$484,267	24%	20%	15%	12%	29%	100%

		Geographic Distribution					
1990	**Gross UPB** (Dollars in millions)	**Northeast**	**Southeast**	**Midwest**	**Southwest**	**West**	**Total**
Fannie Mae risk	$299,871	21%	20%	15%	14%	30%	100%
Lender risk	104,832	35	18	13	7	27	100
Total	$404,703	25%	19%	15%	12%	29%	100%

No significant concentration exists at the state level except for California, where as of December 31, 1991, 24 percent of total loans and MBS were located, compared with 25 percent as of December 31, 1990.

To minimize counterparty risk, the Corporation generally requires that the original loan-to-value ("LTV") ratio (unpaid principal amount of the conventional mortgage loan to the value of the mortgaged property) not be greater than 80 percent. Mortgage insurance is required on mortgage loans with LTV ratios greater than 80 percent. The following table presents the LTV ratio distribution of conventional single-family mortgages in portfolio and backing MBS at December 31.

1991	Gross UPB (Dollars in millions)	Loan-to-Value Ratio(1)						
		60% and less	61-70%	71-75%	76-80%	81-90%	over 90%	Total
Fannie Mae risk	$349,446	21%	16%	14%	25%	17%	7%	100%
Lender risk	92,978	18	14	15	30	19	4	100
Total	$442,424	20%	15%	15%	26%	17%	7%	100%

1990	Gross UPB (Dollars in millions)	Loan-to-Value Ratio(1)						
		60% and less	61-70%	71-75%	76-80%	81-90%	over 90%	Total
Fannie Mae risk	$268,121	20%	15%	14%	27%	17%	7%	100%
Lender risk	95,139	18	14	15	30	19	4	100
Total	$363,260	19%	14%	14%	28%	18%	7%	100%

(1) Represents original LTV ratios. Current LTV ratios may be higher or lower than the original LTV ratios.

FEDERAL NATIONAL MORTGAGE

QUARTERLY RESULTS OF OPERATIONS (Unaudited)

The following unaudited results of operations include, in the opinion of management, all adjustments necessary for a fair presentation of the results of operations for such periods.

	1991 Quarter Ended			
	December	September	June	March
	(Dollars in millions, except per share amounts)			
Interest income	$3,166	$3,158	$3,132	$3,137
Interest expense	2,709	2,702	2,694	2,710
Net interest income	457	456	438	427
Guaranty fees	183	173	163	156
Income from tax settlement	—	—	239	—
Gain (loss) on sales of mortgages, net	17	5	(53)	3
Miscellaneous income, net	36	28	23	19
Provision for losses	(80)	(80)	(130)	(80)
Administrative expenses	(88)	(81)	(78)	(72)
Income before income taxes and extraordinary item	525	501	602	453
Provision for federal income taxes	(158)	(150)	(185)	(133)
Income before extraordinary item	367	351	417	320
Extraordinary loss from repurchase of debt (net of tax effect of $4 million in December and $44 million in June)	(6)	—	(86)	—
Net income	$ 361	$ 351	$ 331	$ 320
Per share:				
Earnings before extraordinary item (fully diluted) (1)	$ 1.33	$ 1.28	$ 1.52	$ 1.19
Net earnings (fully diluted) (1)	1.31	1.28	1.21	1.19
Cash dividends	.30	.26	.26	.22

	1990 Quarter Ended			
	December	September	June	March
	(Dollars in millions, except per share amounts)			
Interest income	$3,074	$3,036	$3,002	$2,957
Interest expense	2,659	2,632	2,606	2,579
Net interest income	415	404	396	378
Guaranty fees	149	138	129	120
Gain on sales of mortgages, net	2	—	4	1
Miscellaneous income, net	24	32	23	28
Provision for losses	(80)	(80)	(75)	(75)
Administrative expenses	(77)	(72)	(71)	(66)
Income before federal income taxes	433	422	406	386
Provision for federal income taxes	(125)	(123)	(116)	(110)
Net income	$ 308	$ 299	$ 290	$ 276
Per share:				
Earnings (fully diluted) (1)	$ 1.19	$ 1.15	$ 1.10	$ 1.06
Cash dividends	.22	.18	.18	.14

(1) The total of the four quarters does not equal the amount for the year because the amount for each period is calculated independently based on the weighted average number of shares outstanding during that period.

MANAGEMENT

Directors

The age and background, as of March 27, 1992, of each of the members of the Board of Directors of the Corporation are as follows:

Name and Age	Principal Occupation, Business Experience, and Residence	First Became Director	Other Directorships(1)
Felix M. Beck, 66	Chairman of the Board and Chief Executive Officer, Margaretten & Co., Inc., a mortgage banking company, 1969 to present; Livingston, New Jersey	1985	
Roger E. Birk, 61	President and Chief Operating Officer of the Corporation, November 1987 until his retirement in January 1992; Chairman of the Board, International Securities Clearing Corporation, November 1986 to October 1987; Chairman of the Board, January 1981 to April 1985, Chief Executive Officer, January 1981 to July 1984, and President, July 1976 to January 1982, Merrill Lynch & Co., Inc., a financial services company; Rumson, New Jersey and Washington, D.C.	1985	New Jersey Resources Corporation; Penske Transportation
Salvador Bonilla-Mathé (2)(5), 37	President and Chief Executive Officer and Director, April 1988 to present, and Executive Vice President, September 1984 to April 1988; Gulf Bank, a financial institution, Coconut Grove, Florida	1992	
Eli Broad, 58	Chairman of the Board, 1961 to present, Chief Executive Officer, 1976 to present, and President, May 1990 to present, Broad Inc. (formerly Kaufman and Broad, Inc.); Chairman and Chief Executive Officer, SunAmerica Corporation (formerly Sun Life U.S.A., Inc., and Sun Life Group of America, Inc., where he was Chairman and Chief Executive Officer since 1987 and 1978, respectively); Chairman, 1987 to present, Sun Life Insurance Company of America, Inc.; Los Angeles, California	1984	
George L. Clark, Jr.(2), 51	President, September 1987 to present, and Vice President, 1962 to September 1987, George L. Clark, Inc., a real estate company; Brooklyn, New York	1989(3)	
Christine M. Diemer(2), 39	Executive Director, Building Industry Association of Southern California, Orange County Region, a building association, July 1989 to present; Director, January 1987 to June 1989, and Acting Director, May 1986 to January 1987, California Department of Housing and Community Development, a state housing department; Corona del Mar, California	1989	
J. Brian Gaffney (2), 59	Partner, Gaffney Law Associates, a law firm practicing in Connecticut, January 1992 to present; Partner, Gaffney, Pease & DiFabio, a law firm practicing in Connecticut, January 1989 to December 1991; Partner, Gaffney & DiFabio, a law firm practicing in Connecticut, 1975 to December 1988; New Britain, Connecticut	1989	
Thomas P. Gerrity(4), 50	Dean of The Wharton School of the University of Pennsylvania, an educational institution, July 1990 to present; President of CSC Consulting, a subsidiary of Computer Sciences Corporation, May 1989 to June 1990; Chairman and Chief Executive Officer, Index Group, a technology-oriented consulting company, 1969 to April 1989; Haverford, Pennsylvania	1991	Digital Equipment Corporation; Sun Company, Inc.

Name and Age	Principal Occupation, Business Experience, and Residence	First Became Director	Other Directorships (1)
James A. Johnson, 48	Chairman of the Board of Directors and Chief Executive Officer of the Corporation, February 1991 to present; Vice Chairman of the Board of Directors, January 1990 to January 1991; Managing Director, Shearson Lehman Hutton, Inc., an investment banking firm, April 1985 to December 1989; President, Public Strategies, a Washington, D.C.-based consulting firm, 1981 to April 1985; Washington, D.C.	1990	
Vincent A. Mai, 51	President and Chief Executive Officer, AEA Investors, Inc., an investment company, April 1989 to present; Managing Director, Shearson Lehman Hutton, Inc., an investment banking firm, 1974 to April 1989; Port Washington, New York	1991	
Richard D. Parsons, 43	Chairman of the Board and Chief Executive Officer, January 1991 to present, President and Chief Executive Officer, July 1990 to January 1991, President and Chief Operating Officer, July 1988 to June 1990, and Director, July 1988 to present, The Dime Savings Bank of New York, FSB, a financial institution; Partner, Patterson, Belknap, Webb & Tyler, a law firm practicing in New York, May 1979 to June 1988; Pocantico Hills, New York	1989	Philip Morris Companies, Inc.; Time Warner, Inc.
Franklin D. Raines, 43	Vice Chairman of the Board of Directors, September 1991 to present; Vice Chairman-Designate, July 1991 to September 1991; Limited Partner, January 1991 to June 1991, and General Partner, January 1985 to December 1990, Lazard Freres and Co., an investment banking firm; Washington, D.C.	1991	
Samuel J. Simmons, 64	President and Chief Executive Officer, The National Caucus and Center on Black Aged, Inc., a non-profit organization, 1982 to present; housing consultant, 1981 to present; Washington, D.C.	1978	
Lawrence M. Small, 50	President and Chief Operating Officer of the Corporation, February 1992 to present; President and Chief Operating Officer-Designate of the Corporation, September 1991 to January 1992; Vice Chairman, January 1990 to July 1991, Sector Executive, January 1985 to December 1989, Citicorp, a financial institution; Washington, D.C.	1991	The Chubb Corporation; Paramount Communications, Inc.
Christopher J. Sumner, 46	President and Chief Executive Officer, CrossLand Mortgage Corp., a mortgage banking corporation, May 1988 to present; Vice Chairman, April 1990 to present, and President and Director, March 1987 to April 1990, CrossLand Savings, FSB (Utah) (formerly Western Savings and Loan Company), a financial institution; President and Chief Executive Officer, Western Savings and Loan Company, a financial institution, 1980 to March 1987; Salt Lake City, Utah	1985	

Name and Age	Principal Occupation, Business Experience, and Residence	First Became Director	Other Directorships (1)
Gloria E.A. Toote (2)(6), 60	Chief Executive Officer, Trea Estates and Enterprises, Inc., a community housing rehabilitation and property management company, 1977 to present; New York, New York	1992	
Mallory Walker, 52	President, Chief Executive Officer and Director, Walker & Dunlop, Inc., a mortgage banking and real estate company, 1976 to present; Washington, D.C.	1981	
Karen Hastie Williams, 47	Partner, Crowell & Moring, a law firm practicing in the District of Columbia, 1982 to present; Washington, D.C.	1988	Crestar Financial Corporation

(1) Companies with a class of securities registered pursuant to Section 12 of the Securities Exchange Act of 1934 or subject to the requirements of Section 15(d) of that Act or any company registered as an investment company under the Investment Company Act of 1940. Certain directorships of other companies are also noted in the occupation column.

(2) Appointed by the President of the United States, who has authority to appoint five directors.

(3) From 1986 to 1987, Mr. Clark also served as a director of the Corporation appointed by the President of the United States.

(4) Mr. Gerrity was elected to the Board of Directors on September 17, 1991.

(5) The President of the United States appointed Mr. Bonilla-Mathé to the Board of Directors on February 13, 1992.

(6) The President of the United States appointed Ms. Toote to the Board of Directors on February 14, 1992.

The term of each director will end on the date of the May 1992 annual meeting of stockholders, except that the President of the United States may remove any director for good cause.

Executive Officers

The age and business experience, as of March 27, 1992, of each of the executive officers of the Corporation, are as follows:

James A. Johnson, 48, has been Chairman of the Board of Directors and Chief Executive Officer since February 1991. Mr. Johnson was Vice Chairman of the Board of Directors from January 1990 to January 1991. Mr. Johnson was a Managing Director in Corporate Finance at Shearson Lehman Hutton, Inc. from April 1985 to December 1989 and was President of Public Strategies from January 1981 to April 1985.

Lawrence M. Small, 50, has been President and Chief Operating Officer since February 1992. Mr. Small was President and Chief Operating Officer-Designate of the Corporation from September 1991 to January 1992. Prior to his employment with the Corporation, Mr. Small was Vice Chairman of Citicorp from January 1990 to July 1991 and Sector Executive of Citicorp's Institutional Bank from January 1985 to December 1989.

Franklin D. Raines, 43, has been Vice Chairman of the Board of Directors since September 1991. Mr. Raines was Vice Chairman-Designate from July 1991 to September 1991. Prior to his employment with the Corporation, Mr. Raines was a Limited Partner with Lazard Freres and Company from January 1991 to June 1991 and a General Partner with that firm from January 1985 to December 1990.

Caryl S. Bernstein, 58, has been Executive Vice President since February 1982, General Counsel since May 1981 and Secretary since July 1981.

J. Timothy Howard, 43, has been Executive Vice President and Chief Financial Officer since February 1990. Mr. Howard was Executive Vice President—Asset Management from December 1987 to February 1990, Executive Vice President—Economics, Strategic Planning, and Financial Analysis from September 1987 to December 1987, and Senior Vice President—Economics and Corporate Planning from November 1985 to September 1987.

Robert J. Levin, 36, has been Executive Vice President—Marketing since June 1990. Mr. Levin was Senior Vice President—Marketing and MBS from June 1989 to June 1990, Senior Vice President—Mortgage-Backed Securities and Portfolio Acquisition from February 1988 to June 1989, Senior Vice President—Mortgage-Backed Securities from February 1987 to February 1988, Senior Vice President and Assistant to the Chairman of the Board from May 1986 to February 1987, and Senior Vice President—Corporate Finance from November 1985 to May 1986.

Michael A. Smilow, 54, has been Executive Vice President and Chief Credit Officer since March 1989. Mr. Smilow was Executive Vice President—Marketing and Customer Services from January 1988 to March 1989 and Executive Vice President—Mortgage Operations from July 1984 through December 1987.

Glenn T. Austin, Jr., 43, has been Senior Vice President—Southeastern Regional Office since May 1985.

Douglas M. Bibby, 45, has been Senior Vice President—Administration since October 1988. Mr. Bibby was Senior Vice President and Assistant to the Chairman of the Board from March 1987 until October 1988, and Senior Vice President—Corporate Affairs from October 1983 to March 1987.

John Buckley, 35, has been Senior Vice President—Communications since November 1991. Prior to his employment with the Corporation, Mr. Buckley was a Senior Vice President with Robinson, Lake, Lerer and Montgomery from November 1989 to November 1991. Mr. Buckley was Director of Communications with the National Republican Congressional Committee from February 1989 to October 1989 and was a Political Consultant to CBS News from June 1988 to January 1989. Mr. Buckley was Press Secretary to United States Congressman Jack Kemp from February 1985 to May 1988.

Donna M. Callejon, 29, has been Senior Vice President—Marketing and Mortgage-Backed Securities since November 1991. Ms. Callejon was Vice President for Product Acquisition from November 1990 to November 1991, Co-Head of MBS Transactions from June 1989 to November 1990, Director of Negotiated Transactions from March 1988 to June 1989, Transactions Manager from December 1987 to March 1988, and Senior Market Analyst from December 1986 to December 1987.

Larry H. Dale, 46, has been Executive Director—National Housing Impact since October 1991. Mr. Dale was Senior Vice President—Marketing and MBS from June 1990 to October 1991, Senior Vice President—Multifamily Finance and Housing Initiatives from May 1989 to June 1990 and Senior Vice President—Multifamily Activities from June 1987 to May 1989. Prior to his employment with the Corporation, Mr. Dale was Vice President of Newman and Associates from 1984 to June 1987.

Judith Dedmon, 41, has been Senior Vice President—Southwestern Regional Office since July 1987. Ms. Dedmon was Senior Vice President—Quality Standards from April 1987 to July 1987, and Vice President for Quality Standards from July 1985 to April 1987.

John H. Fulford, III, 42, has been Senior Vice President—Western Regional Office since November 1985.

John R. Hayes, 53, has been Senior Vice President—Midwestern Regional Office since November 1985.