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, 1992. 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, 1992. 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. At the close of business on January 31, 1993, 274,180,485 shares of the Corporation's common stock (without par value) were outstanding.

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.

February 16, 1993

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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"), mortgage loans guaranteed by the Farmers Home Administration, 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 1992, approximately 47 percent were from mortgage banking companies, 18 percent were from savings and loan associations, 20 percent were from commercial and mutual savings banks, and 15 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 $203,150, except for loans secured by

properties in Alaska, Hawaii and the Virgin Islands. 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 Federal Housing Finance Board. On January 1, 1993, the limitation for one-family dwellings was increased from $202,300 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 (2% of the portfolio at December 31, 1992) 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 5 percent of its portfolio loan purchases in 1992.

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 for its portfolio 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,				
	1992	**1991**	**1990**	**1989**	**1988**
Unpaid Principal Balances ("UPB") at End of Period					
Single-family: Government insured or guaranteed	$ 9,025	$ 9,900	$ 11,204	$ 11,857	$ 12,235
Conventional: Long-term fixed-rate	66,949	57,643	50,846	47,768	43,060
Intermediate-term fixed-rate	43,943	26,534	21,409	19,036	17,937
Adjustable-rate	23,278	20,941	20,737	22,020	21,040
Second	1,356	2,069	1,885	1,614	1,561
Multifamily	13,568	11,896	10,547	8,426	7,180
Total UPB	$158,119	$128,983	$116,628	$110,721	$103,013
Average yield	8.68%	9.54%	9.94%	10.03%	9.84%

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 property 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 enter into a mandatory delivery portfolio commitment with the yield established upon execution of the portfolio commitment.

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. 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 housing needs. Under this initiative, the Corporation is creating new products and expanding the use of existing ones to help meet the needs of such families. As of December 31, 1992, the Corporation had deliveries of $6.5 billion under this effort.

As part of its affordable housing initiative, the Corporation is expanding its outreach efforts to lenders and other potential partners in this business, including state and local housing finance agencies and nonprofit entities. Among other things, the Corporation is offering commitments to purchase a variety of new products. One new initiative is FannieNeighbors℠, a nationwide effort created by Fannie Mae to increase homeownership and promote revitalization in minority and low- and moderate-income urban areas across America. Single-family homes that fall within specially designated low- and moderate-income and/or minority census tracts, or areas designated by housing finance agencies as targeted areas for neighborhood revitalization, are eligible for community lending underwriting flexibilities.

Under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, the Corporation will have certain goals to promote affordable housing for low- and very low-income families and to serve the housing needs of those in underserved areas such as central cities. 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 properties acquired through foreclosure. 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, FHA/VA or Farmers Home Administration-guaranteed 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 ("Ginnie Mae certificates"). REMICs represent beneficial interests in a trust having multiple classes of certificates entitled to different cash flows from the underlying mortgage loans, MBS, SMBS or Ginnie Mae 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 MBS, mortgage loans or Ginnie Mae certificates, 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, 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 cash 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. The focus of competition between the Corporation and Freddie Mac shifted in the last quarter of 1990 when Freddie Mac began issuing a mortgage-backed security called the "Gold PC." Under the Gold PC, the pass-through or coupon rate is passed through to investors faster than under the MBS program, giving the Gold PC a higher economic value (price). In order to support the price of the Gold PC and further develop the market for this security, Freddie Mac has been increasing its REMIC activity. The level of competition between the Corporation and Freddie Mac for loans to be purchased for cash has increased during the same period, both as a consequence of increased REMIC activity and because mortgage lenders have experienced record levels of originations. Traditionally the execution choice of smaller customers, sales for cash have become a common method for mortgage lenders of all sizes.

In 1992, Freddie Mac also began issuing REMICs backed by Ginnie Mae certificates. The Government National Mortgage Association has announced its intention to do so on several occasions, but has not yet done so.

The Corporation competes primarily on the basis of price, products, and services offered. Competition based on advances in technology-related services continues to increase as do the types and nature of the products offered by the Corporation and Freddie Mac.

Under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, the Secretary of HUD must approve any new Fannie Mae or Freddie Mac program that is significantly different from those previously approved or engaged in. The ability of Fannie Mae and Freddie Mac to compete with private issuers possibly could be affected by this requirement. See "Government Regulation and Charter Act" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments."

Facilities

The Corporation owns its principal office, which is located at 3900 Wisconsin Avenue, NW, Washington, DC. The Corporation also owns an office at 3939 Wisconsin Avenue that is being prepared for occupancy later this year and leases approximately 389,000 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, 1992 the Corporation employed approximately 3,000 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 residential mortgages, (2) respond appropriately to the private capital market by developing new finance and mortgage products, (3) provide ongoing assistance to the secondary market for residential mortgages (including activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities) and (4) promote access to mortgage credit throughout the nation (including central cities, rural areas and underserved areas) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing.

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. In addition, the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the "1992 Act") established an independent Office of Federal Housing Enterprise Oversight (the "Office") within HUD under the management of a Director (the "Director") who is responsible for ensuring that the Corporation is adequately capitalized and operating safely in accordance with the 1992 Act. The 1992 Act established risk-based capital, minimum capital and critical capital levels for the Corporation. If the Corporation fails to meet one or more of these capital standards, the Director is required to take certain remedial measures and may take others, depending on the standards the Corporation fails to meet. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments." The Director is given enforcement powers that include the power to impose temporary and final cease-and-desist orders and civil penalties on the Corporation and on a director or executive officer of the Corporation. Prior approval of the Director is required for the Corporation to pay a dividend if the dividend would decrease the Corporation's capital below risk-based capital or minimum capital levels established under the 1992 Act. See "Common Stock." The Director is authorized to levy annual assessments on Fannie Mae and Freddie Mac to cover reasonable expenses of the Office.

The 1992 Act also gives the Director the authority to conduct annually an on-site examination of the Corporation for purposes of ensuring the Corporation's financial safety and soundness. The Director also has the discretion to conduct more frequent examinations if deemed necessary for safety and soundness. In addition, the Corporation is required to submit annual and quarterly reports of the financial condition and operations of the Corporation to the Director. Moreover, the Charter Act, as amended by the 1992 Act, authorizes the General Accounting Office ("GAO") to audit the programs, activities, receipts, expenditures and financial transactions of the Corporation. The Corporation also is required to submit an annual report to the House and Senate Banking Committees and the Secretary of HUD regarding the Corporation's performance in meeting housing goals relating to the purchase of mortgages on housing for low- and moderate-income families, mortgages on rental and owner-occupied housing for low-income families in low-income areas or for very-low-income families, and mortgages on housing located in central cities, rural areas and other underserved areas.

Under the 1992 Act, the Secretary of HUD retains general regulatory authority to promulgate rules and regulations to carry out the purposes of the Charter Act, but the Secretary has no regulatory authority over matters specifically granted to the Director in the 1992 Act or over any other matters relating to the safety and soundness of the Corporation. The Secretary of HUD also must approve any new conventional mortgage program that is significantly different from those previously approved or engaged in. The Secretary is required to approve any new program unless it is not authorized by the Charter Act of the Corporation or the Secretary finds that it is not in the public interest. However, until one year after the final regulations establishing the risk-based capital test are in effect, the Secretary must disapprove a new program if the Director determines that the program would risk significant deterioration of the financial condition of the Corporation.

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. The appointed directors must include one person from the home building industry, one person from the mortgage lending industry, and one person from the real estate industry. Under the 1992 Act, one appointed director also must be from an organization that has represented consumer or community interests for not less than two years or a person who has demonstrated a career commitment to the provision of housing for low-income households. Any member of the Board of Directors that is appointed by the President of the United States may be removed by the President for good cause.

In addition to placing the Corporation under federal regulation, the Charter Act also grants to the Corporation certain privileges. 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. (However, in issuing such securities, the Corporation must clearly indicate that the securities, and the interest thereon, are not guaranteed by the United States and do not constitute a debt or obligation of 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, in 1992 the SEC, the Department of the Treasury and the Board of Governors of the Federal Reserve System 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 qualifications 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.

The 1992 Act requires a number of studies, including studies by the Comptroller General of the United States, the Secretary of HUD, the Secretary of the Treasury and the Director of Congressional Budget Office (CBO Director) of the effect of fully privatizing Fannie Mae and Freddie Mac. The privatization studies are to be submitted to Congress by October 1994. The Federal Housing Finance Board, the Comptroller General, the CBO Director, and the Secretary of HUD also are required to study, among other things, the competitive effects of Fannie Mae's and Freddie Mac's mortgage activities on federally insured depository institutions, and the cost of such activities to such institutions, the Savings Association Insurance Fund and the Resolution Trust Corporation. They are required to submit these studies to Congress by April 1993. Management cannot predict the impact, if any, of such studies on the corporation. Privatization of the corporation would require legislation.

Management expects that the Secretary of HUD and the Director will adopt new regulations to implement certain provisions of the 1992 Act.

RECENT LEGISLATIVE AND REGULATORY DEVELOPMENTS

In 1992, legislation was enacted that establishes capital standards for Fannie Mae and Freddie Mac, creates an independent office within HUD to oversee regulatory and capital requirements, and makes other changes affecting the Corporation. This legislation is described in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Balance Sheet Analysis—Regulatory Developments" and in "Government Regulation and Charter Act."

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.

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 was held in April 1992 and legal briefs were filed in July and September 1992. A decision in the case is expected in early 1993. Additional information regarding this case, as well as hedging issues in a later IRS audit and the possible impact on the Corporation if the IRS hedging position is sustained, is presented in Notes to Financial Statements, "Income Taxes."

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 that is appointed by the President of the United States may be removed by the President 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 if the Corporation fails to meet certain minimum capital standards, the Director of the Federal Housing Enterprise Oversight Office (the "Director") could require that the Director approve the Corporation's issuance of stock or securities convertible into stock. At January 31, 1993, there were outstanding approximately 274 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. However, no dividend may be paid without the prior approval of the Director if the dividend would decrease the Corporation's capital below risk-based capital or minimum capital levels established under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992. 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 59 for quarterly dividends paid during 1991 and 1992.

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 Chemical Bank, 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.*

	1992		1991	
Quarter	**High**	**Low**	**High**	**Low**
1st	$71.63	$60.75	$48.50	$32.38
2nd	68.25	55.12	51.75	42.63
3rd	68.38	60.63	65.13	49.00
4th	77.25	61.50	69.63	54.00

On February 12, 1993, the closing price of the Corporation's common stock as so reported was $79.38.

SELECTED FINANCIAL DATA

The following selected financial data for the years 1988 through 1992 (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:	**1992**	**1991**	**1990**	**1989**	**1988**
Interest income	$ 13,534	$ 12,593	$ 12,069	$ 11,080	$ 10,226
Interest expense	11,476	10,815	10,476	9,889	9,389
Net interest income	2,058	1,778	1,593	1,191	837
Guaranty fees	834	675	536	408	328
Income from tax settlement	—	239	—	—	—
Gain (loss) on sales of mortgages, net	23	(28)	7	9	12
Miscellaneous income, net	168	106	107	60	69
Provision for losses	(320)	(370)	(310)	(310)	(365)
Administrative expenses	(381)	(319)	(286)	(254)	(218)
Income before federal income taxes and extraordinary item	2,382	2,081	1,647	1,104	663
Provision for federal income taxes	(733)	(626)	(474)	(297)	(156)
Income before extraordinary item	1,649	1,455	1,173	807	507
Extraordinary loss	(26)	(92)	—	—	—
Net income	$ 1,623	$ 1,363	$ 1,173	$ 807	$ 507
Per share:					
Earnings before extraordinary item:					
Primary	$ 6.01	$ 5.33	$ 4.50	$ 3.14	$ 2.14
Fully diluted	6.00	5.31	4.49	3.10	2.11
Net earnings:					
Primary	5.92	4.99	4.50	3.14	2.14
Fully diluted	5.91	4.98	4.49	3.10	2.11
Cash dividends	1.38	1.04	0.72	0.43	0.24

	December 31,				
Balance Sheet Data:	**1992**	**1991**	**1990**	**1989**	**1988**
Mortgage portfolio, net	$156,021	$126,486	$113,875	$107,756	$ 99,867
Total assets	180,978	147,072	133,113	124,315	112,258
Borrowings:					
Due within one year	56,404	34,608	38,453	36,346	36,599
Due after one year	109,896	99,329	84,950	79,718	68,860
Total liabilities	174,204	141,525	129,172	121,324	109,998
Stockholders' equity	6,774	5,547	3,941	2,991	2,260

Other Data:	**1992**	**1991**	**1990**	**1989**	**1988**
Net interest margin	1.37%	1.42%	1.39%	1.16%	0.89%
Return on average equity	26.5	27.7	33.7	31.1	25.2
Return on average assets	1.0	1.0	.9	.7	.5
Ratio of earnings to fixed charges(1)	1.20:1	1.19:1	1.15:1	1.11:1	1.07:1
Dividend payout ratio	23.2%	20.7%	14.7%	12.8%	11.2%
Equity to assets ratio	3.8	3.6	2.7	2.2	1.8
Mortgage purchases	$ 75,905	$ 37,202	$ 23,959	$ 22,518	$ 23,110
MBS issued	194,037	112,903	96,695	69,764	54,878
MBS outstanding at year-end	444,979	371,984	299,833	228,232	178,250

(1) 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 1992, Fannie Mae reported record earnings, business volumes, and capital levels. Net income increased to $1.623 billion, 19 percent higher than the $1.363 billion earned in 1991, while earnings per share increased to $5.91 in 1992 from $4.98 in 1991.

The higher level of earnings in 1992 in part reflected a record amount of mortgage originations, spurred by refinance activity. The Corporation's total business volume was $257 billion in 1992, compared with $139 billion in 1991. This led to significant growth in the mortgage portfolio and in Mortgage-Backed Securities ("MBS") outstanding. The net mortgage portfolio was $156 billion at December 31, 1992, up 23 percent from the 1991 year-end level compared with growth rates of 11 percent in 1991 and 6 percent in 1990. At year-end 1992, MBS outstanding, net of MBS held in portfolio, were $424 billion, or 19 percent higher than the $355 billion outstanding at year-end 1991.

The record earnings, coupled with growth in the allowance for losses, enabled the Corporation to increase its capital base by $1.3 billion, bringing total capital to $7.6 billion at December 31, 1992.

Acquisitions of single-family properties through foreclosure rose from 7,450 in 1991 to 9,646 in 1992, while total charge-offs increased $39 million to $244 million. These increases reflected the significant growth in outstanding MBS and portfolio balances in recent years, as well as the weak economies in California and New England. Charge-offs as a percentage of average portfolio and MBS outstanding were five basis points in both 1992 and 1991. Management expects higher acquisitions of foreclosed properties in 1993, primarily as a result of growth in business volumes.

A summary comparison of the Corporation's 1992 performance versus 1991 follows:

- Net interest income was $2.058 billion, an increase of $280 million or 16 percent from the $1.778 billion earned in 1991. This increase was due primarily to an 18 percent increase in the average investment portfolio, offset in part by a five basis point decline in net interest margin to 1.37 percent in 1992.

- MBS guaranty fee income was $834 million in 1992, a 24 percent increase over 1991, resulting from the significant growth in MBS outstanding.

- The provision for losses in 1992 was $320 million, down from $370 million in 1991, while the allowance for losses increased by $76 million to $780 million at December 31, 1992. The Corporation's loss provision was lower in 1992 than in 1991 in anticipation of the effect of the adoption of a new accounting standard relating to foreclosed assets. Under this new standard, foreclosure, holding, disposition, and interest carrying costs, which previously were charged against the loss allowance, will be recorded in the income statement either as foreclosed property expense or as a reduction in net interest income. Management believes that credit-related expenses on the income statement under the new standard in 1993 will not differ significantly from the level of the 1992 provision for losses.

- Miscellaneous income was up $62 million to $168 million in 1992. Fee income from the issuance of Real Estate Mortgage Investment Conduit ("REMIC") securities, which is included in miscellaneous income, increased to a record $87 million in 1992 from $59 million in 1991.

- Administrative expenses rose from $319 million in 1991 to $381 million in 1992 as the Corporation increased its technology-related expenditures. The ratio of total administrative expenses to the average mortgage portfolio plus average MBS outstanding declined to .072 percent from .073 percent in 1991 and .079 percent in 1990.

The remainder of Management's Discussion and Analysis 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 related costs. The following table presents an analysis of net interest income for 1992, 1991, and 1990.

Net Interest Income and Average Balances

(Dollars in millions)

	1992	1991	1990
Interest income:			
Mortgage portfolio	$ 12,650	$ 11,603	$ 10,958
Investments and cash equivalents	884	990	1,111
Total interest income	13,534	12,593	12,069
Interest expense	11,476	10,815	10,476
Net interest income	2,058	1,778	1,593
Tax equivalent adjustment (1)	118	125	130
Net interest income tax equivalent basis	$ 2,176	$ 1,903	$ 1,723
Average balances:			
Interest-earning assets (2):			
Mortgage portfolio, net	$139,004	$119,637	$110,385
Investments and cash equivalents	20,153	14,845	13,252
Total interest-earning assets	$159,157	$134,482	$123,637
Interest-bearing liabilities	$146,287	$126,069	$117,551
Interest-free funds	12,870	8,413	6,086
Total interest-bearing liabilities and interest-free funds	$159,157	$134,482	$123,637
Average interest rates (1):			
Interest-earning assets:			
Mortgage portfolio, net	9.13%	9.76%	9.98%
Investments and cash equivalents	4.44	6.79	8.62
Total interest-earning assets	8.54	9.43	9.84
Interest-bearing liabilities	7.77	8.56	8.91
Investment spread (3)	.77	.87	.93
Interest-free return (4)	.63	.54	.44
Miscellaneous	(.03)	.01	.02
Net interest margin (5)	1.37%	1.42%	1.39%

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

(2) Includes average balance of nonperforming loans of $ 1.1 billion, $0.9 billion, and $0.7 billion in 1992, 1991, and 1990, respectively.

(3) The difference between the yield on interest-earning assets, adjusted for tax benefits of nontaxable income, and the effective cost of funds on interest-bearing liabilities.

(4) The return on that portion of the investment portfolio funded by equity and non-interest-bearing liabilities.

(5) Net interest income, on a tax equivalent basis, as a percentage of the average investment portfolio.

The growth in net interest income in 1992 was largely a result of an 18 percent increase in the average investment portfolio and higher levels of interest-free funds. These positive factors were partially offset by a decline in investment spread, which was caused primarily by a volume of mortgage liquidations that exceeded the amount of debt maturing or eligible for call.

Net interest income was higher in 1991 when compared with 1990 due to both a 9 percent increase in the average investment portfolio and growth in the interest-free return.

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 1992 and 1991.

Rate/Volume Analysis

(Dollars in millions)

	Increase (Decrease)	Attributable to changes in (1)	
		Volume	Rate
1992 vs. 1991			
Interest income:			
Mortgage portfolio	$1,047	$1,795	$ (748)
Investments and cash equivalents	(106)	292	(398)
Total interest income	941	2,087	(1,146)
Interest expense	661	1,639	(978)
Net interest income	$ 280	$ 448	$ (168)
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)

(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 $1.2 billion at the end of 1992, compared with $1.1 billion at December 31, 1991, and $0.7 billion at December 31, 1990. If nonperforming assets had been fully performing, they would have contributed an additional $88 million to net interest income in 1992, $77 million in 1991, and $49 million in 1990.

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

Guaranty Fee Income

As a result of significant growth in MBS outstanding, guaranty fee income continued to increase. These fees compensate the Corporation for its guarantee 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 1992, 1991, and 1990.

Guaranty Fee Income

(Dollars in millions)

	1992	1991	1990
Guaranty fee income	$ 834	$ 675	$ 536
Average balance of MBS outstanding (1)	394,126	321,092	254,703
Effective guaranty fee rate	.212%	.210%	.211%

(1) Excludes $18.7 billion, $13.9 billion, and $11.9 billion in 1992, 1991, and 1990, respectively, which represented the average balances of Fannie Mae MBS held in the mortgage portfolio.

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 Notes to Financial Statements, "Income Taxes."

Gain (Loss) on Sales of Mortgages

Gain on sales of mortgages totaled $23 million in 1992, compared with a loss of $28 million in 1991 and a gain of $7 million in 1990. The gain in 1992 resulted from the sale of higher coupon mortgages, principally to facilitate structured transactions. The loss in 1991 was largely due to the sale of low-coupon mortgages.

Miscellaneous Income

Miscellaneous income during 1992 rose sharply, primarily as a result of a 47 percent increase in REMIC fee income. This increase in REMIC fees was attributable to the issuance of $154.8 billion of REMICs in 1992 versus $101.8 billion in 1991.

Miscellaneous income during 1991 did not change significantly compared with 1990 as growth in REMIC issuances was offset by a decline in average fee rates in response to competitive pressures.

The following table presents REMIC issuances and fees for 1992, 1991, and 1990.

REMIC Issuances and Fees

				% Change	
	1992	1991	1990	1992 vs. 1991	1991 vs. 1990
Issuances (in billions)	$155	$102	$61	52%	67%
Gross fee income (in millions)	134	115	97	17	19
Net fee income (in millions)	87	59	62	47	(5)

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 included in miscellaneous income.

Management anticipates that REMIC fee income will decrease in 1993 due to an expected decline in the volume of MBS issuances and increased competition for REMICs backed by Government National Mortgage Association ("Ginnie Mae") certificates.

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

Provision for Losses

In 1992, the Corporation's provision for losses declined to $320 million from $370 million in 1991, and was slightly higher than the $310 million recorded in 1990. Management provides for losses to maintain an adequate reserve to cover expected foreclosure losses. Information on how the Corporation manages credit risk is included under "Management of Interest Rate and Credit Risk."

Administrative Expenses

Administrative expenses were $381 million in 1992, compared with $319 million and $286 million in 1991 and 1990, respectively. Compensation expense was $209 million or 55 percent of administrative expenses in 1992, compared with $187 million (59 percent) in 1991 and $172 million (60 percent) in 1990. The ratio of administrative expenses to the average mortgage portfolio plus average MBS outstanding continued to improve. In 1992, the ratio was .072 percent, down from .073 percent in 1991 and .079 percent in 1990. The ratio of administrative expenses to revenues (net interest income, guaranty fees, and miscellaneous income) was 12.5 percent in 1992 and 1991, and 12.8 percent in 1990.

Income Taxes

The total provision for federal income taxes was $719 million in 1992, compared with $578 million and $474 million in 1991 and 1990, respectively. The effective federal income tax rate in 1992 was 31 percent, an increase from 30 percent in 1991 and 29 percent in 1990. The effective tax rate increased in both 1992 and 1991 primarily due to the growth in taxable income without a proportionate increase in income from tax-advantaged investments.

As discussed in the Notes to Financial Statements, "Income Taxes," the Internal Revenue Service has challenged the characterization of certain deductions relating to hedging transactions.

Extraordinary Loss

The Corporation had an extraordinary loss of $40 million ($26 million after tax) from the early extinguishment of $8.3 billion of debt in 1992. The repurchase or call of $2.2 billion of high-coupon debt resulted in an extraordinary loss of $140 million ($92 million after tax) in 1991. The repurchase of high-coupon debt favorably affects 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 to absorb future losses.

Management of Interest Rate Risk

The sensitivity of earnings to a given change in interest rates can be measured, to some degree, by the duration gap, or the difference between the estimated durations of mortgage assets and those of

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 1990 through 1992 has been under six 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 noncallable liabilities, however, stay approximately the same. The resulting duration mismatch could increase earnings volatility. One way the Corporation has reduced the volatility in the projected duration gap that can result when interest rates change significantly is by issuing callable debt that better matches the optional prepayment characteristics of the mortgages it funds. A related financing strategy employed by the Corporation has been to enter into callable swaps that effectively convert noncallable debt to callable debt. At December 31, 1992, callable instruments equaled 47 percent of total outstanding long-term debt, up from 36 percent at the end of 1991 and 22 percent at the end of 1990. In 1992, 75 percent of long-term debt issued was callable, compared with 63 percent in 1991 and 66 percent in 1990. Management believes the early redemption feature of callable instruments makes them desirable for managing the interest rate risk associated with mortgage loan prepayments and expects to continue to issue a high percentage of callable debt in 1993.

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, lenders, or mortgage insurers on its mortgage portfolio loans or on loans backing its MBS. The Corporation has a credit quality program structured to monitor and manage actively 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, underwriting standards, and levels of mortgage insurance, and requiring credit enhancements on higher risk business. Credit enhancements, which partially or fully offset the Corporation's default risk, include recourse, pledged collateral, letters of credit, and pool insurance. At December 31, 1992, 14 percent of the total conventional single-family mortgage portfolio and MBS were supported by credit enhancements, compared with 21 percent at December 31, 1991.

The Corporation manages its institutional risk by monitoring the financial strength and performance of lenders and mortgage insurance companies, which provide loss coverage in the event of default on high loan-to-value ("LTV") loans, and by conducting reviews of lenders' operations.

The Corporation mitigates market risk primarily through geographic diversification of the mortgage portfolio and MBS and risk sharing on its higher risk business. Fannie Mae also analyzes market conditions, home price movements, 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 that 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.

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, 1992, 77 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 (38 percent not higher than 70 percent); the average original LTV ratio was 72 percent. The average LTV ratio on new mortgage purchases and MBS issues has declined in each of the past four years; however, due to an anticipated decline in refinancings and return to longer term fixed-rate products, LTVs on new business are expected to increase in 1993. The average original LTV ratio on loans from both California and New England was 68 percent at the end of 1992.

The table below presents certain risk characteristics of conventional loan purchases and MBS issuances in the years 1990—1992 and conventional product outstanding at December 31, 1992.

Risk Characteristics of Conventional Single-Family Purchases and MBS Issuances

	Percentage of Business Volumes			Outstanding at
	1992	1991	1990	December 31, 1992
Product:				
Long-term fixed-rate	55%	63%	70%	60%
Intermediate-term fixed-rate (1)	37	25	18	27
ARM	8	12	12	13
Total	100%	100%	100%	100%
Occupancy:				
Owner-occupied	97%	96%	97%	96%
Investor	2	2	1	2
Other	1	2	2	2
Total	100%	100%	100%	100%
Number of units:				
1 unit	98%	97%	96%	96%
2 to 4 units	2	3	4	4
Total	100%	100%	100%	100%
Average loan amount (Maximum $202,300 in 1992)	$95,800	$91,000	$89,800	$76,100

(1) Contractual maturities of 20 years or less at purchase for portfolio loans and 15 years or less at issue date for MBS issuances.

The primary concentration of the Corporation's mortgages is in fixed-rate product, which is generally less risky than adjustable-rate mort gages ("ARMs"). In addition, intermediate-term fixed-rate product has represented an increasingly higher percentage of total business. As shown in the table, the percentage of total conventional mortgage purchases and MBS issuances related to intermediate-term fixed-rate product rose from 25 percent in 1991 to 37 percent in 1992, primarily as a result of the high level of refinancings. Intermediate-term products generally have lower LTV ratios than long-term mortgages and better credit performance. The table also highlights other factors that limit product risk, such as the small percentage of investor loans and loans on two- to four-unit properties, both of which are considered riskier products. The Corporation's loan limits and the low average loan size of mortgages in portfolio and underlying MBS reduce credit risk exposure when compared with nonconforming mortgage loans, which have an original balance in excess of the Corporation's statutory loan limits.

A second performance measure of credit risk is the rate of serious delinquencies (90 or more days delinquent). At 1992 year-end, serious delinquencies were 0.63 percent, down slightly from the level at the end of the previous year despite the sluggish economy. The level of serious delinquencies reflects a significant decline from December 1986, when it was 1.38 percent. This improvement was due, in large part, to 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, 1992, 1991, and 1990.

Single-Family Serious Delinquencies (1)

	December 31,		
	1992	1991	1990
Northeast	1.04%	1.00%	.74%
Southeast	.56	.65	.63
Midwest	.35	.41	.42
Southwest	.55	.76	.96
West	.57	.40	.30
Total	.63%	.64%	.58%

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

California and New England are two areas of the country where the weak economy has had a particularly severe impact. As shown in the table, the serious delinquency rate in the Western region rose in 1992 and 1991, and is expected to rise further in 1993. The Northeast region has, and is expected to continue to have, a serious delinquency rate significantly above the average rate for the Corporation.

The third performance measure relates to acquisitions of foreclosed properties and charge-offs. 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	1992	1991	1990
Acquired:			
Northeast	2,526	1,069	548
Southeast	2,366	1,939	1,729
Midwest	815	747	739
Southwest	2,450	3,097	4,288
West	1,489	598	702
Total	9,646	7,450	8,006
In inventory at year-end	4,413	3,295	3,585
Aggregate carrying value, net	$295,000	$164,000	$146,000
Average carrying value per case	$ 67	$ 50	$ 41

A major reason for the increase in properties acquired through foreclosure is the substantial growth in business volumes in recent years, as well as the weak economies in California and New England. Because foreclosures generally occur in the third to fifth year of the life of a mortgage, the large volume of mortgages acquired and MBS securitized in the late 1980s would be expected to result in increased foreclosures. Due to the high volume of loans outstanding entering their peak foreclosure years, management expects an increase in the number of properties acquired through foreclosure in 1993.

Net charge-offs and the ratio of net charge-offs to average principal balances outstanding for single-family loans in portfolio and backing MBS are shown in the following table.

Single-Family Charge-Offs

(Dollars in millions)

	Year Ended December 31,		
	1992	**1991**	**1990**
Net charge-offs	$202	$143	$190
Net loss charge-off ratio	.04%	.03%	.05%

Net charge-offs rose in 1992 because of the increase in foreclosures. However, due to a new accounting standard, the level of charge-offs is expected to decline in 1993, despite an anticipated increase in foreclosures. See Notes to Financial Statements, "Summary of Significant Accounting Policies—Acquired Property" for additional information.

Multifamily

For the majority of multifamily loans, either held in portfolio or backing MBS, the Corporation has full or partial recourse to the lender or third parties, pledged collateral, or FHA insurance. Fannie Mae also has a delegated underwriting and servicing ("DUS") program under which the lender is responsible for the first five 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, 1992 was 49 percent, compared with 44 percent and 40 percent at December 31, 1991 and 1990, respectively. Of the total multifamily portfolio and MBS, 30 percent, 24 percent, and 19 percent in 1992, 1991, and 1990, 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.

Multifamily serious delinquencies at December 31, 1992, 1991, and 1990 were 2.7 percent, 3.6 percent and 1.7 percent, respectively. Multifamily serious delinquencies are those loans for which the Corporation has primary risk of loss that are two months or more delinquent. Delinquency percentages are based on the dollar amount of such loans in portfolio and underlying MBS.

The level of serious delinquencies for multifamily loans has declined significantly from its peak of 6.6 percent in 1988, primarily as a result of better underwriting in recent years, improvements in the multifamily market, and the foreclosure and disposition of problem loans.

The following table summarizes the number of multifamily properties acquired through foreclosure during the year and carried at year-end, including their carrying value.

Multifamily Real Estate Owned (REO)

(Dollars in thousands)

Number of Properties	1992	1991	1990
Acquired:			
Northeast	6	—	—
Southeast	9	6	1
Midwest	4	4	1
Southwest	4	15	20
West	3	2	3
Total	26	27	25
In inventory at year-end	37	28	32
Aggregate carrying value, net	$136,700	$98,900	$111,000
Average carrying value per case	$ 3,700	$ 3,500	$ 3,500

Multifamily foreclosure activity in 1992 was stable despite prevailing economic conditions. Management does not expect a significant change in 1993 in property acquisitions through foreclosure.

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,		
	1992	1991	1990
Net charge-offs	$42	$62	$44
Net loss charge-off ratio	.19%	.32%	.25%

Allowance for 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.

The level of future charge-offs is expected to be lower under the new accounting standard because only the expected loss of principal now will be charged to the allowance for losses. Previously, real estate owned expenses and carrying costs also were charged to the allowance for losses. Because the size of the current allowance had been set to accommodate expected future charge-offs under the old standard, management does not expect the allowance to increase significantly for the next two or three years. Credit-related expenses on the income statement in 1993 under the new standard are not expected to differ significantly from the level of the 1992 provision for losses.

The following table summarizes changes in the allowance for losses from 1988 through 1992 for loans in portfolio and backing MBS.

Allowance for Losses

(Dollars in millions)

	Total
Balance, January 1, 1988	$ 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
Provision for loan losses	320
Net loan charge-offs:	
Conventional:	
Single-family	(200)
Multifamily	(42)
Government	(2)
Balance, December 31, 1992	$ 780

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 are discussions of recent regulatory developments and the role of liquidity management in meeting the Corporation's business requirements.

Mortgage Portfolio

As of December 31, 1992, the net mortgage portfolio totaled $156.0 billion. In comparison, the portfolio totaled $126.5 billion and $113.9 billion at December 31, 1991 and 1990, respectively. The yield on the net mortgage portfolio (before deducting the allowance for losses) was 8.68 percent as of

December 31, 1992, compared with 9.54 percent as of December 31, 1991 and 9.94 percent as of December 31, 1990. The decreases in yield in the last two years were due primarily to increased prepayments of higher coupon mortgages, a decline in conventional mortgage purchase yields and ARM adjustments as interest rates declined, and an increase in the proportion of intermediate-term fixed-rate mortgages in portfolio, which generally have a lower yield relative to long-term fixed-rate mortgages.

The following table summarizes mortgage purchases and repayments for the years 1990 through 1992:

Mortgage Purchases and Repayments

(Dollars in millions)

	Purchases			Repayments (1)		
	1992	1991	1990	1992	1991	1990
Mortgage type:						
Single-family mortgages:						
Government insured or guaranteed	$ 951	$ 1,164	$ 698	$ 1,825	$ 1,306	$ 1,240
Conventional:						
Long-term fixed-rate	32,846	19,111	12,245	18,897	7,238	4,090
Intermediate-term fixed-rate	30,775	9,541	5,044	10,389	3,928	2,482
Adjustable-rate	9,091	4,892	2,826	5,573	4,253	3,651
Second	136	705	654	849	521	383
Total single-family	73,799	35,413	21,467	37,533	17,246	11,846
Multifamily	2,106	1,789	2,492	434	442	374
Total	$75,905	$37,202	$23,959	$37,967	$17,688	$12,220
Average net yield	7.77%	8.89%	9.82%	9.22%	9.53%	10.20%

(1) Includes mortgage loan prepayments, scheduled amortization, and foreclosures.

The increase in mortgage purchases in 1992 and 1991 compared with prior years was due primarily to the high level of refinancing activity because of a sustained decline in mortgage interest rates. This, in turn, resulted in a large increase in both the number of mortgages prepaying and the number of new mortgages offered for sale in the secondary market.

Mortgage sales from portfolio totaled $8.8 billion in 1992, compared with $7.2 billion in 1991 and $5.8 billion in 1990. The higher sales level in 1992 compared with 1991 and 1990 primarily reflects the Corporation's increased buy/sell activities. Buy/sell 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 providing 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 invest in mortgages. Sales in connection with buy/sell activities were $7.5 billion, $5.3 billion, and $5.5 billion in 1992, 1991, and 1990, respectively. Buy/sell activity does not materially affect net interest margin nor does it generate significant gains or losses. In 1991, the Corporation also sold $800 million of low-coupon mortgages and incurred a loss of $59 million on the sale.

Financing Activities

Debt Issued and Outstanding

The average cost of debt outstanding at December 31, 1992 was 7.21 percent, compared with 8.25 percent and 8.81 percent at December 31, 1991 and 1990, 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)

	1992	1991	1990
Issued during the year:			
Short-term (1):			
Amount	$203,230	$151,223	$ 94,407
Average cost	3.43%	5.60%	7.83%
Long-term (1):			
Amount	$ 30,599	$ 30,234	$ 19,581
Average cost	6.24%	7.73%	8.93%
Total debt:			
Amount	$233,829	$181,457	$113,988
Average cost (2)	3.81%	5.96%	8.03%
Repaid during the year:			
Amount	$200,762	$171,311	$106,974
Average cost (2)	4.13%	6.29%	8.27%
Outstanding at year end:			
Due within one year:			
Net amount	$ 56,404	$ 34,608	$ 38,453
Average cost	4.56%	6.59%	8.05%
Due after one year:			
Net amount	$109,896	$ 99,329	$ 84,950
Average cost	8.06%	8.67%	9.07%
Total debt:			
Net amount	$166,300	$133,937	$123,403
Average cost (2)	7.21%	8.25%	8.81%

(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 issuance costs and hedging results, and the effect of currency, debt, and interest rate swaps.

The following table presents the amount of callable debt and the notional amount of callable swaps issued and outstanding for each year.

Callable Debt and Swaps

(Dollars in billions)

	1992	1991	1990
Issued during the year	$30.7	$20.1	$13.3
Percentage of total long-term debt issued (1)	75%	63%	66%
Outstanding at year-end	$63.2	$41.2	$22.3
Percentage of total long-term debt outstanding (1)	47%	36%	22%

(1) Includes the notional amount of callable swaps.

Capital Resources

At December 31, 1992, the Corporation's capital base (stockholders' equity plus allowance for losses) had grown to $7.6 billion, compared with $6.3 billion and $4.5 billion at the end of 1991 and 1990, respectively. At December 31, 1992, 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 1992, the Board voted increases in the quarterly cash dividend totaling ten cents per share. The dividend paid in the fourth quarter of 1992 was 40 cents per share.

As discussed under "Regulatory Developments," the Corporation, effective October 28, 1992, is subject to revised capital standards. As of December 31, 1992, the Corporation met the applicable standards, although the precise level of capital required cannot be definitively determined until regulations relating to off-balance-sheet obligations other than MBS are published. Management expects that continued growth in retained earnings will ensure continued compliance with the applicable standards.

Regulatory Developments

In October 1992, the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 ("Act") was enacted. The Act modifies the regulatory oversight of Fannie Mae and the Federal Home Loan Mortgage Corporation ("Freddie Mac") by the Department of Housing and Urban Development ("HUD"). The Act provides for the creation of a substantially independent office within HUD, the Office of Federal Housing Enterprise Oversight ("the Office"), to oversee Fannie Mae's and Freddie Mac's capital adequacy and to ensure that the companies operate safely. In addition, the Act increases the HUD Secretary's oversight of Fannie Mae's housing and program activities.

The Act also establishes capital standards to be applied equally to Fannie Mae and Freddie Mac. Three separate capital standards apply: a minimum capital standard, a critical capital standard, and a risk-based standard. Until April 1994, to meet the minimum standard, Fannie Mae core capital must equal the sum of: (1) 2.25 percent of on-balance-sheet assets; (2) 0.40 percent of outstanding MBS; and (3) 0.40 percent of other off-balance-sheet obligations. Core capital is defined as the sum of: (1) the par value of outstanding common and perpetual noncumulative preferred stock, (2) paid-in capital, and (3) retained earnings. Beginning in April 1994, the applicable percentages for determining compliance with the minimum standard are 2.50, 0.45, and 0.45 percent, respectively. The Corporation also is subject to a critical capital standard. To meet the critical capital standard Fannie Mae core capital must equal the sum of (1) 1.25 percent of on-balance-sheet assets; (2) 0.25 percent of outstanding MBS; and (3) 0.25 percent of other off-balance-sheet obligations. For purposes of the minimum and critical capital standards, the Director of the Office ("Director") may adjust the

percentages applicable to other off-balance-sheet obligations, and certain mortgage purchase commitments are excluded.

The Director is required to develop, consistent with parameters specified in the Act, a risk-based capital standard. The risk-based standard includes credit and interest rate components along with an additional amount of capital for management and operations risk. To meet the standard, the Corporation must hold capital equal to (1) the level of capital necessary to meet the combined occurrence of highly stressful credit and interest rate conditions for a ten-year period, and (2) 30 percent of such level of capital for management and operations risk. Capital is defined as the sum of core capital (as defined above) and a general loan loss allowance. The risk-based standard will not be applicable until approximately three years from enactment of the Act.

The Act requires the Director to classify Fannie Mae within one of four capital levels. The Corporation will be deemed to be "adequately capitalized" if it meets the risk-based and minimum capital standards. If the Corporation fails to meet the risk-based standard but meets the minimum standard it will be classified as "undercapitalized." If Fannie Mae fails to meet the minimum standard, the Corporation is deemed to be "significantly undercapitalized" and if the Corporation is below the critical standard it will be classified as "critically undercapitalized." If the Corporation is not "adequately capitalized," the Director is required to take certain remedial measures, and may take others, depending on the Corporation's capital classification. These measures can include restrictions on dividends and other capital distributions. If the Corporation were "significantly undercapitalized," the Director also could impose limitations on growth and activities and require the Corporation to raise capital in a form and amount determined by the Director. If the Corporation were classified as "critically undercapitalized," appointment of a conservator generally would be required.

The Director can reclassify the Corporation's capital status to a lower level if the Director determines that the Corporation is engaging in an activity that the Director has not approved that could result in rapid depletion of core capital, or if the value of the properties securing the Corporation's mortgage assets or underlying MBS has decreased significantly.

The Act establishes a series of housing goals and targets for 1993 and 1994 and authorizes the Secretary of HUD to alter those goals and targets, pursuant to stated standards involving both housing need and corporate financial strength, for the years after 1994. Interim targets are established in the statute that require that 30 percent of the Corporation's business in each year, measured by units, serve families with incomes at or below the median income in the area in which they live, and 30 percent of the company's business each year, again counted by units, finance housing in central cities. Units meeting both tests count against both goals. The Secretary of HUD is authorized to establish actual goals for each year related to the targets, but has not yet done so. Finally, during 1993 and 1994, combined, the Corporation must purchase a total of $2 billion of mortgages financing housing for low- and very-low income families. Half the purchases, by dollars, must be multifamily housing and half one- to four-family properties. The Secretary can enforce the housing goals after a process that includes development by the Corporation of a "housing plan" for meeting the goals and consideration of whether meeting the goals was or is feasible. Fannie Mae is committed to meeting the housing goals, and anticipates being able to do so.

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

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 its 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 the needed volume of funds at relatively favorable rates.

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, 1992, Fannie Mae had a portfolio of cash equivalents and shorter term investments totaling $19.7 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, 1992, the Corporation had mandatory delivery commitments and lender option commitments outstanding to purchase $4.7 billion and $9.2 billion of mortgage loans, respectively, compared with $4.7 billion and $5.6 billion, respectively, outstanding at December 31, 1991.

Mortgage-Backed Securities

MBS outstanding grew to a record $445.0 billion at December 31, 1992, compared with $372.0 billion at December 31, 1991, and $299.8 billion at December 31, 1990. 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. SMBS and REMICs represent interests in a trust having multiple classes that entitle investors to different cash flows from the underlying mortgage loans.

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 payment of principal and interest to investors. The issuance of MBS creates guaranty fee income with Fannie Mae assuming credit risk, but without 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, 1992, 1991, and 1990.

MBS Issued and Outstanding

(Dollars in millions)

	Issued				Outstanding (1)		
	Lender Originated (1)						
	Lender Risk	Fannie Mae Risk	Fannie Mae Originated	Total	Lender Risk (2)	Fannie Mae Risk (3)	Total (4)
1992	$12,344	$168,396	$13,297	$194,037	$79,809	$365,170	$444,979
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

(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 $39.7 billion, $43.3 billion, and $35.9 billion at December 31, 1992, 1991, and 1990, respectively, on which the lender or a third party agreed to bear default risk limited to a certain portion or percentage of the loans delivered and, in some cases, the lender has pledged collateral to secure that obligation.

(3) Included are $8.0 billion at December 31, 1992 and $9.3 billion at December 31, 1991 and 1990, which are backed by government insured or guaranteed mortgages.

(4) Included are $20.5 billion, $16.7 billion, and $11.8 billion at December 31, 1992, 1991, and 1990, respectively, of Fannie Mae MBS in portfolio.

Fannie Mae issued more MBS in 1992 than it had issued in any prior year. This was primarily due to an increase in the volume of fixed-rate mortgages originated and available in the secondary market to create MBS as a result of the high level of refinancings brought about by substantially lower interest rates during the year.

In 1992, REMIC issuances totaled $154.8 billion, compared with $101.8 billion in 1991, and $60.9 billion in 1990. The increase in REMIC issuances reflects continued demand for investments with a variety of average life and prepayment characteristics and greater availability of the underlying MBS.

Fannie Mae has issued REMICs backed by both Fannie Mae and Ginnie Mae certificates. The issuance of REMICs backed by Ginnie Mae certificates provides an additional source of fee income that does not subject the Corporation to added credit risk. The outstanding balance of REMICs as of December 31, 1992 was $276.9 billion, compared with $193.3 billion and $104.3 billion as of December 31, 1991 and 1990, respectively.

As the level of refinancings declines, management expects a decrease in the volume of MBS and REMIC issuances in 1993. Ginnie Mae-backed REMIC issuances by Fannie Mae also are expected to decline with the addition of new entrants, including Freddie Mac and possibly Ginnie Mae, to that market.

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, 1992 and 1991, 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, 1992. 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, 1992 and 1991, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 1992, in conformity with generally accepted accounting principles.

We also have audited in accordance with generally accepted auditing standards the supplemental fair value balance sheet of Federal National Mortgage Association as of December 31, 1992 included in Note 10 to the financial statements. The supplemental fair value balance sheet has been prepared by management to present relevant financial information that is not provided by the financial statements and is not intended to be a presentation in conformity with generally accepted accounting principles. In addition, the supplemental fair value balance sheet does not purport to present the net realizable, liquidation, or market value of the Corporation as a whole. Furthermore, amounts ultimately realized by the Corporation from the disposal of assets may vary from the fair values presented. In our opinion, the supplemental fair value balance sheet included in Note 10 presents fairly, in all material respects, the information set forth therein on the basis of accounting described in Note 10.

KPMG PEAT MARWICK

Washington, DC
January 11, 1993

FEDERAL NATIONAL MORTGAGE ASSOCIATION

STATEMENTS OF INCOME

	Year Ended December 31,		
	1992	1991	1990
	(Dollars in millions, except per share amounts)		
Interest income:			
Mortgage portfolio	$12,650	$11,603	$10,958
Investments and cash equivalents	884	990	1,111
Total interest income	13,534	12,593	12,069
Interest expense	11,476	10,815	10,476
Net interest income	2,058	1,778	1,593
Other income:			
Guaranty fees	834	675	536
Income from tax settlement	—	239	—
Gain (loss) on sales of mortgages, net	23	(28)	7
Miscellaneous, net	168	106	107
Total other income	1,025	992	650
Other expenses:			
Provision for losses	320	370	310
Administrative	381	319	286
Total other expenses	701	689	596
Income before federal income taxes and extraordinary item	2,382	2,081	1,647
Provision for federal income taxes	733	626	474
Income before extraordinary item	1,649	1,455	1,173
Extraordinary loss: early extinguishment of debt (net of tax effect of $14 million and $48 million in 1992 and 1991, respectively)	26	92	—
Net income	$ 1,623	$ 1,363	$ 1,173
Per share:			
Earnings before extraordinary item:			
Primary	$ 6.01	$ 5.33	$ 4.50
Fully diluted	6.00	5.31	4.49
Net earnings:			
Primary	5.92	4.99	4.50
Fully diluted	5.91	4.98	4.49
Cash dividends	1.38	1.04	.72
Average shares used to compute fully diluted earnings per share (in millions)	275	274	261

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

BALANCE SHEETS

Assets

	December 31, 1992	December 31, 1991
	(Dollars in millions)	
Mortgage portfolio, net	$156,021	$126,486
Investments	14,786	9,836
Cash and cash equivalents	5,193	4,357
Accrued interest receivable	1,123	1,048
Receivable from currency swaps	1,008	3,202
Acquired property and foreclosure claims, net	524	348
Other	2,323	1,795
Total assets	$180,978	$147,072

Liabilities and Stockholders' Equity

	1992	1991
Liabilities:		
Debentures, notes, and bonds, net:		
Due within one year	$ 56,404	$ 34,608
Due after one year	109,896	99,329
	166,300	133,937
Accrued interest payable	2,548	2,514
Payable from currency swaps	870	2,385
Other	4,486	2,689
Total liabilities	174,204	141,525
Stockholders' Equity:		
Common stock, $2.10 stated value, no maximum authorization, issued 282,175,863 shares (1992) and 282,167,915 shares (1991)	593	593
Additional paid-in capital	1,277	1,245
Retained earnings	5,099	3,853
	6,969	5,691
Less: treasury stock, at cost, 8,887,584 shares (1992) and 9,179,664 shares (1991)	195	144
Total stockholders' equity	6,774	5,547
Total liabilities and stockholders' equity	$180,978	$147,072

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

STATEMENTS 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, 1990	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
Net income	—	—	—	1,623	—	1,623
Dividends	—	—	—	(377)	—	(377)
Shares repurchased	(1)	—	—	—	(76)	(76)
Treasury stock issued for stock options and benefit plans	1	—	32	—	25	57
Balance, December 31, 1992	273	$593	$1,277	$5,099	$(195)	$6,774

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION

STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	1992	1991	1990
	(Dollars in millions)		
Cash flows from operating activities:			
Net income	$ 1,623	$ 1,363	$ 1,173
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for losses	320	370	310
Loss on early extinguishment of debt	40	140	—
Other increases, net	1,507	1,453	842
Net cash provided by operating activities	3,490	3,326	2,325
Cash flows from investing activities:			
Purchases of mortgages	(75,995)	(37,117)	(23,743)
Proceeds from sales of mortgages	8,866	7,128	5,817
Mortgage principal repayments	37,195	17,043	11,604
Net proceeds from disposition of foreclosed properties	673	457	464
Net increase in investments	(4,950)	(243)	(2,485)
Net cash used in investing activities	(34,211)	(12,732)	(8,343)
Cash flows from financing activities:			
Proceeds from issuance of debentures	30,643	30,306	19,666
Payments to redeem debentures	(21,534)	(17,937)	(12,249)
Proceeds from issuance of short-term debt	202,105	150,174	93,245
Payments to redeem short-term debt	(179,254)	(153,466)	(94,724)
Net proceeds (payments) for stock activities	(403)	233	(229)
Net cash provided by financing activities	31,557	9,310	5,709
Net increase (decrease) in cash and cash equivalents	836	(96)	(309)
Cash and cash equivalents at beginning of year	4,357	4,453	4,762
Cash and cash equivalents at end of year	$ 5,193	$ 4,357	$ 4,453
Supplemental disclosures of cash flow information:			
Cash paid during the year for:			
Interest	$ 11,231	$ 10,476	$ 10,372
Income taxes	927	597	547

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, i.e., mortgages that are not federally insured or guaranteed, is discontinued when the mortgages become 90 days or more 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 for future 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

In 1992, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants issued Statement of Position No. 92-3, "Accounting for Foreclosed Assets" ("SOP 92-3"). The new SOP, which the Corporation adopted at December 31, 1992, requires foreclosed assets to be recorded at the lower of cost or fair value. The difference between fair value at foreclosure and the principal owed will be recorded as a charge-off. Foreclosure, holding and disposition costs will be charged directly against earnings as incurred. Interest carrying costs, currently recorded as a charge-off, will be reported as a reduction of net interest income.

Prior to adoption of SOP 92-3, real estate acquired and held for sale as a result of foreclosure was carried at the lower of the investment in the property or its estimated net realizable value. The difference between estimated net realizable value, which takes into consideration foreclosure, holding, and disposition costs, and the principal owed was recorded as a charge-off.

The carrying amount of acquired property at December 31, 1992 approximated fair value.

Gain/Loss on Sales of Mortgages

When the Corporation places mortgages from portfolio 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, after considering estimated prepayments of the MBS, 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.

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 certain borrowings 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.

Cash and Cash Equivalents

The Corporation considers 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 at December 31.

	1992	1991
	(Dollars in millions)	
Single-family mortgages:		
Government insured or guaranteed	$ 9,025	$ 9,900
Conventional:		
Long-term fixed-rate(1)	66,949	57,643
Intermediate-term fixed-rate(1)	43,943	26,534
Adjustable-rate	23,278	20,941
Second	1,356	2,069
	144,551	117,087
Multifamily mortgages:		
Government insured	3,974	4,090
Conventional	9,594	7,806
	13,568	11,896
Total unpaid principal balance	158,119	128,983
Less:		
Unamortized discount and deferred loan fees, net	1,859	2,304
Allowance for losses	239	193
	$156,021	$126,486

(1) Long-term mortgages have contractual maturities at the date of purchase greater than 20 years. Intermediate-term mortgages have contractual maturities at purchase equal to or less than 20 years.

Included in the mortgage portfolio are $23.3 billion of MBS and other mortgage-related securities with an estimated market value at December 31, 1992 of $24.6 billion, compared with $19.4 billion of MBS and other mortgage-related securities at December 31, 1991 with an estimated market value of

$20.6 billion. The estimated market values reflect gross unrealized gains of $1.3 billion and $1.2 billion at December 31, 1992 and 1991, respectively. Contractual maturity of MBS is not a reliable indicator of expected life because borrowers have the right to prepay their obligations at any time.

3. Allowance for Losses

Changes in the allowance for the years 1990 to 1992 are summarized below.

	Total
	(Dollars in millions)
Balance, January 1, 1990	$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
Provision	320
Net foreclosure losses charged off	(244)
Balance, December 31, 1992	$780

At December 31, 1992, $239 million of the allowance for losses is included in the Balance Sheet under "Mortgage portfolio, net," which represents the allocation for portfolio loan losses; $536 million is included under "Other liabilities" for estimated losses on MBS; and the remainder, or $5 million, which relates to unrecoverable losses on FHA loans, is included in "Acquired property and foreclosure claims, net." The corresponding amounts at December 31, 1991 were $193 million, $503 million, and $8 million, respectively. The total allowance for losses is available to absorb losses related to either the loan portfolio or loans underlying MBS.

4. Investments

Presented below are the amortized cost and estimated market value of non-mortgage investments at December 31, 1992 and 1991.

	1992				1991			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
	(Dollars in millions)							
Federal funds	$ 3,625	$—	$—	$ 3,625	$2,954	$—	—	$2,954
Asset-backed securities	4,124	60	12	4,172	2,416	79	—	2,495
Repurchase agreements	3,189	—	—	3,189	2,195	—	—	2,195
Other	3,848	6	9	3,845	2,271	12		2,283
Total	$14,786	$66	$21	$14,831	$9,836	$91	—	$9,927

The following table shows non-mortgage investments at December 31, 1992 and 1991 by remaining maturity with the amortized cost, estimated market value, and yield.

	1992			1991		
	Amortized Cost	Estimated Market Value	Yield	Amortized Cost	Estimated Market Value	Yield
	(Dollars in millions)					
Remaining maturity at December 31:						
Due within one year	$10,328	$10,324	3.92%	$7,272	$7,277	5.50%
Due after one year through five years	310	311	5.07	92	97	8.81
Due after five years	24	24	5.80	56	58	8.07
	10,662	10,659	3.96	7,420	7,432	5.56
Asset-backed securities (1)	4,124	4,172	6.55	2,416	2,495	8.30
Total	$14,786	$14,831	4.68%	$9,836	$9,927	6.23%

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

Sales of non-mortgage investments were not significant in 1992, 1991, or 1990.

5. Debentures, Notes, and Bonds, Net

The average cost of all debt outstanding at December 31, 1992 and 1991 was 7.21 percent and 8.25 percent, respectively. The average effective maturity of all debt outstanding at December 31, 1992 and 1991 was 54 months and 56 months, respectively, including the effect of interest rate swaps.

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.

Borrowings Due Within One Year

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

	1992					1991				
	Outstanding at December 31		Average Outstanding During Year		Maximum Outstanding At Any Month End	Outstanding at December 31		Average Outstanding During Year		Maximum Outstanding At Any Month End
	Amount	Cost (1)	Amount	Cost (1)		Amount	Cost (1)	Amount	Cost (1)	
	(Dollars in millions)									
Short-term notes	$40,644	3.59%	$25,639	4.10%	$40,644	$17,516	5.17%	$18,531	6.30%	$20,795
Other short-term debt	3,603	3.51	2,344	3.77	3,603	2,713	4.00	3,440	6.55	5,652
Current portion of borrowings due after one year (2):										
Debentures	8,942	8.86				11,653	9.14			
Other	3,215	5.92				2,726	7.23			
Total due within one year	$56,404	4.56%				$34,608	6.59%			

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

(2) 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.

Borrowings Due After One Year

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

		1992		1991	
	Maturity Date	Amount Outstanding	Average Cost (1)	Amount Outstanding	Average Cost (1)
		(Dollars in millions)			
Investment agreements	1993-2012	$ 1,512	8.91%	$ 2,149	8.04%
Long-term—other, net of $62 million of discount for 1992 ($65 million for 1991)	1993-2018	429	8.53	612	8.32
Debentures, net of $32 million of discount and premium for 1992 ($39 million for 1991)	1993-2022	85,106	8.42	82,404	8.80
Medium-term notes, includes $81 million of premium for 1992 ($120 million for 1991) (2)	1993-2021	20,939	6.34	11,233	7.61
Zero coupon securities, net of $5,473 million of discount for 1992 ($5,551 million for 1991)	1993-2014	595	11.25	672	10.67
Zero coupon subordinated capital debentures, net of $6,281 million of discount for 1992 ($6,326 million for 1991)	2019	468	10.22	424	10.22
Subordinated capital debentures, net of $12 million of discount for 1991	1996-2019	722	9.41	1,039	9.12
		109,771	8.06%	98,533	8.67%
Adjustment for foreign currency translation	—	125		796	
		$109,896		$99,329	

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

(2) 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 at December 31, 1992 included $47.5 billion of callable debt, which generally is redeemable in whole or in part (and, in certain cases, at a specified premium), at the option of the Corporation any time on or after a specified date, and $2.4 billion of Indexed Sinking Fund Debentures ("ISFDs"), which are subject to mandatory redemptions tied to certain Treasury rates after an initial non-redemption period. The final maturity of callable debt and average life of ISFDs are used to compute average effective maturity data.

The following table summarizes the amounts and call periods of callable debt and 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 are also included in the table.

Call Date	Year of Maturity	Amount Outstanding	Average Cost
		(Dollars in millions)	
Callable Debt and Callable Swaps (notional amount)			
Currently	1995-1996	$ 175	5.72%
1993	1995-2013	11,829	7.64
1994	1996-2019	12,826	8.34
1995	1997-2020	17,200	6.19
1996	1999-2021	9,705	6.41
1997	2002-2021	7,375	6.33
1998	2022	500	8.40
1999	2007	200	7.84
		59,810	
ISFDs and ISFD Swaps (notional amount)	1993-2000	3,427	6.85
Total		$63,237	

Principal amounts at December 31, 1992 of total debt payable in the years 1994-1998 assuming callable debt is paid at maturity and assuming callable debt is redeemed at the initial call date are as follows:

	Total Debt by Year of Maturity	Assuming Callable Debt Redeemed at Initial Call Date
	(Dollars in billions)	
1994	$10.8	$23.0
1995	14.6	22.8
1996	18.2	18.8
1997	21.5	14.4
1998	7.8	5.3

In 1992 and 1991, the Corporation repurchased or called $8.3 billion of debt with an average cost of 8.09 percent and $2.2 billion with an average cost of 9.88 percent, respectively. The Corporation recorded extraordinary losses of $40 million ($26 million after tax) in 1992 and $140 million ($92 million after tax) in 1991 on the early extinguishment of debt.

6. Income Taxes

Components of the provision for federal income taxes for the years ended December 31, 1992, 1991, and 1990 were as follows.

	1992	1991	1990
	(Dollars in millions)		
Current	$ 852	$ 811	$523
Deferred	(119)	(185)	(49)
	733	626	474
Tax benefit of extraordinary loss	(14)	(48)	—
Net federal income tax provision	$ 719	$ 578	$474

Deferred federal income tax expense (benefit) relating to timing differences consisted of the following:

	1992	1991	1990
	(Dollars in millions)		
Deferred commitment fees	$ (86)	$ (22)	$ 2
Amortization of purchase discount	(46)	(18)	(35)
Losses (gains) on disposition of mortgages	11	(99)	10
Provision for losses	(26)	(58)	(60)
Benefits from tax-advantaged investments	29	29	29
Other items, net	(1)	(17)	5
Total deferred federal income tax benefit	$(119)	$(185)	$(49)

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

	1992	1991	1990
Statutory corporate rate	34%	34%	34%
Tax exempt interest and dividends received deductions	(3)	(4)	(5)
Effective rate	31%	30%	29%

The Corporation is exempt from state and local taxes, except for real estate taxes.

Resolution of Tax Case

At December 31, 1990, the Corporation had a case pending 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 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 in 1991.

IRS Examinations

The IRS, in its audit report of the Corporation's 1983 through 1985 tax returns, proposed certain deficiencies relating to hedging transactions. The IRS has indicated that hedging gains and losses reported as ordinary income or deductions should be recharacterized as capital gains and losses. This issue is in litigation and a ruling is expected in early 1993.

The IRS has audited the Corporation's tax returns for 1986 and 1987 and has proposed additional deficiencies related to certain hedging transactions that it indicates also should be recharacterized as capital gains and losses.

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 taxable income for 1988 through 1992 includes similar deductions that may be challenged in future IRS audits. If the IRS' position on hedging losses is sustained for all outstanding tax years, the Corporation's current net income would be reduced by approximately $300 million, which includes cumulative interest (net of tax effect) of $90 million.

New Accounting Standard

In 1992, the FASB issued Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("FAS 109"). The new standard requires the Corporation to adopt new accounting and disclosure rules for income taxes beginning January 1, 1993. Under FAS 109, deferred income taxes arising from temporary differences between tax and financial income will be measured using the current marginal tax rate. In addition, FAS 109 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. Adoption of the standard will not have a material effect on the earnings or financial condition of the Corporation.

7. 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 1993-1995, 1992-1994, and 1991-1993 award periods were 65,495; 79,770; and 167,243 performance shares, respectively.

Stock options also may be granted to key employees under this plan. The options do not become exercisable until at least 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 value of the

stock on the date the option is granted. The following table summarizes stock option activity for the years 1990-1992.

	1992		1991		1990	
	Number of Options	Option Price	Number of Options	Option Price	Number of Options	Option Price
Balance, January 1	2,263,487	$ 5.38-$59.25	1,831,910	$ 5.38-$40.56	1,522,031	$ 5.38-$40.56
Granted	853,740	64.25- 73.44	852,910	43.00- 59.25	544,000	32.00- 34.50
Exercised	(362,681)	5.38- 55.75	(333,950)	5.38- 40.56	(193,631)	5.38- 15.75
Terminated	(49,308)	15.75- 55.75	(87,383)	9.44- 40.56	(40,490)	9.44- 40.56
Balance, December 31	2,705,238	$ 5.38-$73.44	2,263,487	$ 5.38-$59.25	1,831,910	$ 5.38-$40.56

At December 31, 1992 and 1991, stock options on 781,676 shares and 764,107 shares, respectively, were exercisable.

In 1992, 16,005 shares of restricted stock (78,023 in 1991) were awarded, issued, and placed in escrow under the Stock Compensation Plan and the Restricted Stock Plan for Directors; and 33,448 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 issuanc of up to nine million shares of common stock to qualified employees at a price equal to 85 percent of its fair market value on the first day of the period in which employees can elect to purchase the stock. In 1992, the Corporation granted each qualified employee, excluding certain officers, the right to purchase in January 1993 up to 300 shares of stock. Under the 1992 offering, 743,600 shares were purchased at $54.61 per share compared with 945,110 shares purchased in 1992 at $35.43 per share under the plan's 1991 offering.

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 1992, 1991, and 1990.

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 1992, 1991, and 1990.

Postretirement Benefit Plans

All regular, full-time employees of the Corporation are covered by a non-contributory retirement plan or by the contributory Civil Service Retirement Law. Benefits payable under the corporate plan

are based on years of service and compensation using the average pay during three consecutive highest paid years of employment. The Corporation's policy is to fund the pension expense accrued each year, up to the contribution that would be tax deductible for the year. Contributions to the plan reflect benefits attributed to employees' service to date as well as services expected to be rendered in the future. Plan assets consist primarily of listed stocks, fixed-income securities, cash, and other liquid assets. No contributions have been made to the retirement plan in recent years because the plan is overfunded.

The following table sets forth the corporate retirement plan's funded status and amounts recognized in the Corporation's financial statements at December 31, 1992 and 1991:

	1992	1991
	(Dollars in millions)	
Actuarial present value of benefit obligations:		
Accumulated benefit obligation, including vested benefits of $40.1 million ($34.2 million in 1991)	$(43.4)	$(37.7)
Projected benefit obligation for services rendered to date	$(74.8)	$(64.8)
Plan assets at fair value	88.1	83.5
Excess of plan assets over the projected benefit obligation	13.3	18.7
Unrecognized net gain from past experience different from that assumed and effects of changes in assumptions	(13.7)	(16.5)
Unrecognized prior service costs	1.7	2.2
Unrecognized net transition asset recognized over 18.25 years	(13.5)	(14.7)
Pension liability included in other liabilities	$(12.2)	$(10.3)
Net pension cost included the following components:		
Service cost - benefits earned during the period	$ 5.4	$ 5.2
Interest cost on projected benefit obligation	5.9	5.3
Actual return on plan assets	(5.9)	(12.9)
Net amortization and deferral	(3.5)	4.7
Net periodic pension cost	$ 1.9	$ 2.3

For 1992 and 1991, the weighted-average discount rate used in determining the actuarial present value of the projected benefit obligation was 8.5 percent, the average rate of increase in future compensation levels used in the calculation was 6.5 percent, and the expected long-term rate of return on assets was 9.5 percent. The Corporation uses the straight-line method of amortization for prior service costs.

The Corporation also has an Executive Pension Plan, which supplements for key senior officers the benefits payable under the retirement plan. Estimated benefits under the supplementary plan are accrued as an expense over the period of employment. Accrued benefits are funded through a trust.

As of January 1, 1993, Fannie Mae will adopt Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" ("FAS 106"). FAS 106 requires that the cost of retiree medical and other benefits be accrued over employees'

working lives. Most firms, including Fannie Mae, currently record the cost of nonpension retiree benefits as they are paid.

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 had an accumulated unfunded postretirement benefit obligation of approximately $40 million at December 31, 1992. The Corporation estimates the annual cost for providing these postretirement benefits will be approximately $8 million, which includes the amortization of the obligation over approximately 20 years. Cash payments expensed in 1990-1992 were less than $2 million in each year.

8. Financial Instruments with Off-Balance-Sheet Risk

The Corporation is a party to transactions involving financial instruments with off-balance-sheet risk. The Corporation uses these instruments to fulfill its statutory purpose of meeting the financing needs of the secondary mortgage market and to reduce its own 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 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.

Commitments

The Corporation will enter into a master delivery commitment with a lender on either a mandatory or optional basis. Under a mandatory master commitment, a lender must either deliver loans under an MBS contract at a specified guaranty fee rate or enter into a mandatory portfolio commitment with the yield established upon executing the portfolio commitment.

The Corporation also will accept mandatory or lender option delivery commitments not issued pursuant to a master commitment. These commitments may be for portfolio or MBS. For most lender option commitments, the yield or guaranty fee rate 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 risk relating to loans purchased pursuant to those commitments is largely mitigated.

Hedge Instruments

The Corporation typically uses interest rate swaps, interest rate futures contracts, short sales of Treasury securities, and deferred rate setting agreements 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 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 and by requiring collateral in certain circumstances.

Interest rate swaps are contractual agreements between two parties 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 debt obligations.

The Corporation also has interest rate swap agreements that are linked to specific debt issues (debt swaps) or specific investments (asset swaps). These swaps achieve a specific financing or investment objective at a desired cost or yield. The costs and terms of the specific debt issues and yield of the specific investments, as presented in the financial statements, include the effects of the swaps.

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 to the entity holding the offsetting futures position. Accordingly, the amount at risk due to nonperformance of counterparties is minimal.

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. This risk is controlled through evaluation of the creditworthiness of counterparties and continuous monitoring of hedge positions.

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 was $85 million at December 31, 1992 and $11 million at December 31, 1991.

The following table presents the contract or notional amount of off-balance-sheet financial instruments at December 31, 1992 and 1991.

	1992	1991
	(Dollars in billions)	
MBS Outstanding (1)	$444.4	$371.5
MBS Outstanding with Lender or Third Party Recourse	(79.8)	(96.2)
Net MBS Outstanding with Fannie Mae Risk (1)	364.6	275.3
Master Commitments:		
Mandatory	75.4	50.7
Optional	9.4	2.1
Portfolio Commitments:		
Mandatory	4.7	4.7
Optional	7.4	4.8
MBS Commitments:		
Mandatory	0.7	4.3
Optional	6.6	4.5
Interest Rate Swaps (2)	14.3	4.7
Debt Swaps	9.3	4.3
Interest Rate Futures and Short Sales of Treasury Securities	1.4	1.1
Asset Swaps (3)	0.6	0.1

(1) Net of allowance for losses.

(2) The weighted-average interest rate being received under these swaps was 3.78 percent and the weighted-average interest rate being paid was 7.53 percent at December 31, 1992, compared with 6.12 percent and 9.24 percent, respectively, at December 31, 1991.

(3) The weighted-average interest rate being received under these swaps was 3.74 percent and the weighted-average interest rate being paid was 8.82 percent at December 31, 1992, compared with 5.18 percent and 6.87 percent, respectively, at December 31, 1991.

9. Concentrations of Credit Risk

Concentrations of credit risk exist when a significant number of counterparties (borrowers, lenders, mortgage insurers) engage in similar activities or are susceptible to similar changes in economic conditions that could affect their ability to meet contractual obligations.

The following table presents unpaid principal balances ("UPB") by primary default risk and the general geographic distribution of properties underlying mortgages in the portfolio and MBS outstanding as of December 31, 1992 and 1991.

1992	Gross UPB (Dollars in millions)	Geographic Distribution: Northeast	Southeast	Midwest	Southwest	West	Total
Fannie Mae risk	$491,825	22%	20%	16%	13%	29%	100%
Lender risk	90,738	34	17	13	8	28	100
Total	$582,563	24%	20%	15%	12%	29%	100%

1991	Gross UPB (Dollars in millions)	Geographic Distribution: 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%

No significant concentration exists at the state level except for California, where, at December 31, 1992, 23 percent of total mortgages in portfolio and backing MBS were located, compared with 24 percent at December 31, 1991.

To minimize credit risk, the Corporation generally requires mortgage insurance or other credit protection if the original loan-to-value ("LTV") ratio (unpaid principal amount of the conventional mortgage loan to the value of the mortgaged property) is 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, 1992 and 1991.

1992	UPB Gross (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	$464,224	23%	16%	15%	23%	16%	7%	100%
Lender risk	77,682	19	14	16	29	18	4	100
Total	$541,906	22%	16%	15%	24%	16%	7%	100%

1991	UPB Gross (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%

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

10. Disclosures of Fair Value of Financial Instruments

In December 1991, the FASB issued Statement of Financial Accounting Standards No. 107, "Disclosures about Fair Value of Financial Instruments" ("FAS 107"). FAS 107 requires disclosure of information about fair value for all financial instruments, assets and liabilities, both recognized and those not recognized in the balance sheet.

The fair value estimates are based on pertinent information available to management as of December 31, 1992. The basic assumptions used and the estimates disclosed in the Fair Value Balance Sheet represent management's best judgment of appropriate valuation methods. The assumptions and estimates are based upon management's evaluation of economic conditions as of December 31, 1992. In certain cases, fair values are not subject to precise quantification or verification and may change as economic and market factors, and management's evaluation of those factors, change.

Although management uses its best judgment in estimating the fair value of these financial instruments, there are inherent limitations in any estimation technique. Therefore, these fair value estimates are not necessarily indicative of the amounts that the Corporation would realize in a market transaction. The accompanying Fair Value Balance Sheet does not represent an estimate of the overall market value of the Corporation as a going concern and that takes into account future business opportunities.

Fair Value Balance Sheet

Assets

	December 31, 1992	
	Cost	Fair Value
	(Dollars in millions)	
Mortgage loan portfolio	$156,021	$164,675
Investments	14,786	14,831
Cash and cash equivalents	5,193	5,193
Other assets	4,978	3,655
	180,978	188,354
Off-balance-sheet items:		
Guaranty fee income, net	—	1,722
Other	—	48
Total assets	$180,978	$190,124

Liabilities and Net Equity

	Cost	Fair Value
Liabilities:		
Noncallable debt:		
Due within one year	$ 54,886	$ 55,034
Due after one year	61,527	66,756
Callable debt:		
Due within one year	1,518	1,562
Due after one year	48,369	49,914
	166,300	173,266
Other liabilities	7,904	7,379
Off-balance-sheet items:		
Swap obligations	—	383
Total liabilities	174,204	181,028
Equity, net of tax effect	6,774	9,096
Total liabilities and net equity	$180,978	$190,124

See accompanying Notes to Fair Value Balance Sheet.

Notes to Fair Value Balance Sheet

The following discussion summarizes the significant methodologies and assumptions used in estimating the fair values presented in the accompanying Fair Value Balance Sheet.

Mortgage Portfolio

The fair value calculations of the Corporation's mortgage portfolio take into consideration such variables as interest rates, credit quality, and loan collateral. Because an active market does not exist for a large portion of mortgage loans in the portfolio, the portfolio's unsecuritized mortgages were aggregated into pools by product type, coupon, and maturity. These pools were then converted into notional MBS by subtracting the normal guaranty fee that Fannie Mae's securitization business would charge for a pool of loans with similar characteristics from the weighted-average interest rate less servicing fees. The method for estimating this guaranty fee and the credit risk associated with the mortgage portfolio is described under "Guaranty Fee Income, Net."

The Corporation then employed an option-adjusted spread ("OAS") approach to estimate fair values for both notional MBS (the mortgage loan portfolio) and for MBS held in portfolio. The OAS represents the risk premium or incremental interest spread over Treasury rates that is included in a security's yield to compensate an investor for the uncertain effects of embedded prepayment options on mortgages. The OAS is calculated using quoted market values for selected benchmark securities and provides a generally applicable return measure that considers the effect of prepayment risk and interest rate volatility.

Investments

Fair values of the Corporation's investment portfolio were based on actual quoted prices or prices quoted for similar financial instruments.

Cash and Cash Equivalents

The carrying amount of cash and cash equivalents was used as a reasonable estimate of their fair value.

Other Assets

Other assets include accrued interest receivable, currency swap receivables, and several other smaller asset categories. The fair value of other assets approximates their carrying amount. Currency swap receivables, which are included in the total at cost, and reclassified as a component of the fair value of the related foreign-denominated debt.

Guaranty Fee Income, Net

MBS are not assets owned by the Corporation, except when acquired for investment purposes, nor are the related outstanding securities recorded as liabilities of the Corporation. On MBS outstanding, the Corporation receives a guaranty fee equal to the spread between the net yield remitted to Fannie Mae and the pass-through rate paid to the owner of the securities. The guaranty fee represents a future income stream for the Corporation. Under generally accepted accounting principles, this guaranty fee is recognized as income over the life of the securities. The Fair Value Balance Sheet reflects the present value of guaranty fees, net of estimated future administrative costs and credit losses, and taking into account estimated prepayments, as an asset.

The Corporation estimates the credit loss exposure attached to the notional MBS, MBS held in portfolio, and off-balance-sheet MBS, where Fannie Mae has the primary risk of default. The Corporation deducts credit risk premiums from the contractual guaranty fee to arrive at the net guaranty fee. The credit risk premiums are calculated using an internal forecasting model that estimates future credit losses based on actual historical loss experience for the Corporation. The net guaranty fee cash flows are then valued using an OAS method similar to that described under "Mortgage Portfolio."

Other Off-Balance-Sheet Items

The Corporation issues mandatory delivery commitments to purchase mortgages or issue MBS. Under mandatory portfolio delivery commitments, lenders are obligated to sell mortgages to the Corporation at the commitment yield. Mandatory commitments to purchase mortgages have been valued based on the yield differential between required yields at December 31, 1992 and actual commitment yields, discounted over the estimated life of the assets to be delivered, plus the estimated value of the expected guaranty fee, calculated as described under "Mortgage Portfolio." Mandatory commitments to issue MBS have been valued based on the expected guaranty fee stream, as described above.

In certain instances, the Corporation enters into MBS sales commitments related to the commitments to purchase mortgages. MBS sales commitments have been valued based on the differential between market prices at December 31, 1992 and the prices on MBS sales commitments. The Fair Value Balance Sheet reflects mandatory commitments to purchase mortgage loans or issue MBS net of MBS sales commitments.

The Corporation also issues master commitments and certain lender option commitments not attached to master commitments. No value has been ascribed to these types of commitments because it is not known with certainty what products will be delivered pursuant to these commitments and, in some cases, no benchmark yield or guaranty fee has been established at the date of the Fair Value Balance Sheet.

Other Liabilities

Other liabilities include accrued interest payable, amounts payable to MBS holders, estimated losses on MBS, currency swap payables, and several other smaller liability categories. The fair value of other liabilities approximates their carrying amount, except for currency swap payables, which are included as a component of the fair value of the related foreign-denominated debt, and credit loss exposure for MBS, which is included as a component of the net MBS guaranty fee.

The fair value amount also includes the estimated effect on deferred income taxes of providing for federal income taxes, at the statutory corporate tax rate of 34 percent, on the difference between equity at fair value ($10,293 million) and at cost ($6,774 million).

Noncallable and Callable Debt

The fair value of the Corporation's noncallable debt was estimated using quotes for selected Fannie Mae benchmark debt securities with similar terms. Similar to the valuation of the mortgage portfolio, the fair value of callable debt was estimated using an OAS model.

Interest Rate Swap Obligations

The Corporation enters into interest rate swaps, including callable swaps, that, in general, effectively extend the maturity of short-term debt obligations. Under these swaps, the Corporation generally pays a fixed rate and receives a floating rate based on a notional principal amount. The fair value of noncallable interest rate swaps is estimated based on either expected cash flows or quoted market values of these instruments.

The Corporation also enters into interest rate swaps that are linked to specific debt issues (debt swaps) or bond investments (asset swaps). In valuing the related debt or investment, the Corporation has included the effect of the debt swap or asset swap on the expected cash flows for the integrated transaction.

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.

	1992 Quarter Ended			
	December	September	June	March
	(Dollars in millions, except per share amounts)			
Interest income	$3,521	$3,390	$3,389	$3,234
Interest expense	2,977	2,883	2,871	2,745
Net interest income	544	507	518	489
Guaranty fees	222	215	204	193
Gain (loss) on sales of mortgages, net	(2)	14	4	7
Miscellaneous income, net	36	51	45	36
Provision for losses	(80)	(80)	(80)	(80)
Administrative expenses	(103)	(97)	(95)	(86)
Income before income taxes and extraordinary item	617	610	596	559
Provision for federal income taxes	(189)	(188)	(185)	(171)
Income before extraordinary item	428	422	411	388
Extraordinary loss: early extinguishment of debt (net of tax effect)	(2)	(9)	(9)	(6)
Net income	$ 426	$ 413	$ 402	$ 382
Per share:				
Earnings before extraordinary item (fully diluted) (1)	$ 1.56	$ 1.54	$ 1.50	$ 1.41
Net earnings (fully diluted) (1)	1.55	1.51	1.47	1.39
Cash dividends	0.40	0.34	0.34	0.30

	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: early extinguishment of debt (net of tax effect)	(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

(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 January 25, 1993, 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, 62	President and Chief Operating Officer of the Corporation, November 1987 until his retirement in January 1992; Tequesta, Florida	1985	New Jersey Resources Corporation; Penske Transportation
Salvador Bonilla-Mathé (2), 38	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, 59	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), 52	President, George L. Clark, Inc., a real estate company, September 1987 to present; Brooklyn, New York	1989(3)	
Christine M. Diemer(2), 40	Executive Director, Building Industry Association of Southern California, Orange County Region, a building association, July 1989 to present; California Department of Housing and Community Development, a state housing department, Director, January 1987 to June 1989; Corona del Mar, California	1989	
J. Brian Gaffney (2), 59	Principal, 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, 51	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.
James A. Johnson, 49	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; Washington, D.C.	1990	

Name and Age	Principal Occupation, Business Experience, and Residence	First Became Director	Other Directorships (1)
Vincent A. Mai, 52	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, 44	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, 44	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, 65	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, 51	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; Salt Lake City, Utah	1985	
Gloria E.A. Toote (2), 61	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, 53	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, 48	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.

The term of each director will end on the date of the May 1993 annual meeting of stockholders, except that the President of the United States may remove any director that the President appointed for good cause.

Executive Officers

The age and business experience, as of January 25, 1993, of each of the executive officers of the Corporation, are as follows:

James A. Johnson, 49, 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.

Lawrence M. Small, 51, 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, 44, 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, 59, has been Executive Vice President since February 1982, General Counsel since May 1981 and Secretary since July 1981.

J. Timothy Howard, 44, 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, and Executive Vice President—Economics, Strategic Planning, and Financial Analysis from September 1987 to December 1987.

William E. Kelvie, 45, has been Executive Vice President and Chief Information Officer since November 1992. Mr. Kelvie was Senior Vice President and Chief Information Officer from November 1990 to November 1992. Prior to his employment with the Corporation, Mr. Kelvie was a managing principal with Nolan, Norton & Co. from March 1987 to November 1990.

Robert J. Levin, 37, 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, and Senior Vice President—Mortgage-Backed Securities from February 1987 to February 1988.

Ann D. Logan, 38, has been Executive Vice President and Chief Credit Officer—Designate since January 1993. Ms. Logan was Senior Vice President—Northeastern Regional Office from June 1989 to January 1993, Vice President for Regional Activities from May 1989 to June 1989, and Vice President for Mortgage Operations from November 1987 to May 1989.

Michael A. Smilow, 55, 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.

Glenn T. Austin, Jr., 44, has been Senior Vice President—Southeastern Regional Office since May 1985.

Douglas M. Bibby, 46, 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, 30, 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, and Transactions Manager from December 1987 to March 1988.

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.

Judith Dedmon, 42, has been Senior Vice President—Southwestern Regional Office since July 1987.

John H. Fulford, III, 43, has been Senior Vice President—Western Regional Office since November 1985.

John R. Hayes, 54, has been Senior Vice President—Midwestern Regional Office since November 1985.

Lynda C. Horvath, 40, has been Senior Vice President—Mortgage Operations since February 1991. Ms. Horvath was Acting Senior Vice President—Mortgage Operations from November 1990 to February 1991, Vice President for Product Acquisition and Development from January 1989 to November 1990, and Vice President for MBS Financial Analysis from September 1985 to January 1989.

Thomas A. Lawler, 39, has been Senior Vice President—Portfolio Management since November 1989. Mr. Lawler was Vice President for Portfolio Management from January 1989 to November 1989, and Vice President and Senior Economist from February 1986 to December 1988.

William R. Maloni, 48, has been Senior Vice President—Policy and Public Affairs since March 1989. Mr. Maloni was Senior Vice President—Government Relations from April 1987 to March 1989.

Gary L. Perlin, 41, has been Senior Vice President—Finance and Treasurer since November 1985.

Michael A. Quinn, 38, has been Senior Vice President and Controller since March 1991. Prior to his employment with the Corporation, Mr. Quinn was Vice President and Assistant Controller with Chemical Bank from September 1987 to March 1991.

Ellen S. Seidman, 44, has been Senior Vice President—Regulation, Research, and Economics since November 1991. Ms. Seidman was Vice President for Strategic Planning and Critical Issues from February 1991 to November 1991, Vice President and Assistant to the Chairman from November 1988 to February 1991, and Director of Strategic Planning from November 1987 to November 1988.

Jayne J. Shontell, 38, has been Senior Vice President—Financial and Information Services since November 1992. Ms. Shontell was Vice President for Financial Services and Information Group from August 1992 to November 1992, Vice President for Business Development from September 1991 to August 1992, and Vice President for Critical Issues from January 1991 to September 1991. Ms. Shontell was Vice President for Business and Product Development from August 1990 to January 1991, Vice President for Financial Institution Restructuring from October 1989 to August 1990, Vice President for MBS Capital Market Transactions from May 1988 to October 1989 and Vice President for MBS Marketing and Sales from September 1985 to May 1988.

In January 1993, Caryl S. Bernstein, Executive Vice President, General Counsel and Secretary of Fannie Mae announced her retirement from the Corporation effective at the end of June 1993. In June 1992, Michael A. Smilow, Executive Vice President and Chief Credit Officer of Fannie Mae, announced his retirement from the Corporation effective at the end of January 1993. In January 1993, Mr. Smilow delayed his retirement until later in the year. In January 1993, Gary L. Perlin, Senior Vice President—Finance and Treasurer of Fannie Mae, announced his resignation from the Corporation effective March 1, 1993.

Additional Information

For information concerning executive compensation, stock ownership of management and directors, certain transactions of executive officers, and any person or group owning more than five percent of the voting stock of the Corporation, reference is made to the Corporation's proxy statement, dated March 27, 1992, for the Corporation's 1992 annual meeting of stockholders and any later proxy statement published prior to the Corporation's publication of a new Information Statement, which are incorporated herein by this reference.

The Corporation will provide without charge a copy of the Corporation's most recent proxy statement to each person to whom this Information Statement has been delivered, upon the written or oral request of such person. Requests for such copies should be directed to the individual specified on page 2 of this Information Statement.

ACCOUNTANTS

The financial statements of the Corporation as of December 31, 1992 and 1991 and for each of the years in the three-year period ended December 31, 1992, included herein, have been included in reliance upon the report of KPMG Peat Marwick, independent certified public accountants, and upon the authority of that firm as experts in accounting and auditing.

FannieMae