FEDERAL NATIONAL MORTGAGE ASSOCIATION FANNIE MAE
Form 10-Q
November 07, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2012
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File No.: 0-50231
Federal National Mortgage Association
(Exact name of registrant as specified in its charter)
Fannie Mae

Federally chartered corporation	52-0883107
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3900 Wisconsin Avenue, NW Washington, DC	20016
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code:
(202) 752-7000
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer þ
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No þ
As of September 30, 2012, there were 1,158,077,970 shares of common stock of the registrant outstanding.

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PART I — FINANCIAL INFORMATION

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

We have been under conservatorship, with the Federal Housing Finance Agency ("FHFA") acting as conservator, since September 6, 2008. As conservator, FHFA succeeded to all rights, titles, powers and privileges of the company, and of any shareholder, officer or director of the company with respect to the company and its assets. The conservator has since delegated specified authorities to our Board of Directors and has delegated to management the authority to conduct our day-to-day operations. Our directors do not have fiduciary duties to any person or entity except to the conservator and, accordingly, are not obligated to consider the interests of the company, the holders of our equity or debt securities or the holders of Fannie Mae MBS unless specifically directed to do so by the conservator. We describe the rights and powers of the conservator, key provisions of our agreements with the U.S. Department of the Treasury ("Treasury"), and their impact on shareholders in our Annual Report on Form 10-K for the year ended December 31, 2011 ("2011 Form 10-K") in "Business—Conservatorship and Treasury Agreements" and in this report in "Executive Summary—Amendment to Senior Preferred Stock Purchase Agreement with Treasury."

You should read this Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") in conjunction with our unaudited condensed consolidated financial statements and related notes and the more detailed information in our 2011 Form 10-K.

This report contains forward-looking statements that are based on management's current expectations and are subject to significant uncertainties and changes in circumstances. Please review "Forward-Looking Statements" for more information on the forward-looking statements in this report. Our actual results may differ materially from those reflected in these forward-looking statements due to a variety of factors including, but not limited to, those described in "Risk Factors" and elsewhere in this report and in "Risk Factors" in our 2011 Form 10-K.

You can find a "Glossary of Terms Used in This Report" in the "MD&A" of our 2011 Form 10-K.

INTRODUCTION

Fannie Mae is a government-sponsored enterprise ("GSE") that was chartered by Congress in 1938. Our public mission is to support liquidity and stability in the secondary mortgage market, where existing mortgage-related assets are purchased and sold, and increase the supply of affordable housing. Our charter does not permit us to originate loans and lend money directly to consumers in the primary mortgage market. Our most significant activity is securitizing mortgage loans originated by lenders into Fannie Mae mortgage-backed securities that we guarantee, which we refer to as Fannie Mae MBS. We also purchase mortgage loans and mortgage-related securities for our mortgage portfolio. We use the term "acquire" in this report to refer to both our guarantees and our purchases of mortgage loans. We obtain funds to support our business activities by issuing a variety of debt securities in the domestic and international capital markets.

We are a corporation chartered by the U.S. Congress. Our conservator, FHFA, is a U.S. government agency. Treasury owns our senior preferred stock and a warrant to purchase 79.9% of our common stock. Moreover, Treasury has made a commitment under a senior preferred stock purchase agreement to provide us with funds under specified conditions and, after 2012, up to a maximum amount, to maintain a positive net worth. The U.S. government does not guarantee our securities or other obligations.

Our common stock is traded in the over-the-counter market and quoted on the OTC Bulletin Board under the symbol "FNMA." Our debt securities are actively traded in the over-the-counter market.

EXECUTIVE SUMMARY

The actions we have been taking since 2009 to provide liquidity and support to the market, grow a strong new book of business and minimize losses on loans we acquired prior to 2009 are having a positive impact on our business and our performance:

- Financial Results. We experienced significant improvement in our financial results for the third quarter and first nine months of 2012, as compared with the third quarter and first nine months of 2011, despite elevated levels of mortgage delinquencies and foreclosures compared with pre-housing crisis levels, as well as home prices that are significantly below their peak in 2006. As described below under "Summary of Our Financial Performance for the Third Quarter and First Nine Months of 2012," we had a positive net worth for the third quarter, paid Treasury its quarterly dividend and were not required to draw funds from Treasury for the quarter under the senior preferred stock purchase agreement. We expect to report net income for 2012, which would be the first time we have reported annual net income since 2006.
- Strong New Book of Business. Single-family loans we have acquired since the beginning of 2009 constituted 63% of our single-family guaranty book of business as of September 30, 2012, while the single-family loans we acquired prior to 2009 constituted 37% of our single-family book of business. We refer to the single-family loans we have acquired since the beginning of 2009 as our "new single-family book of business" and the single-family loans we acquired prior to 2009 as our "legacy book of business." Our new single-family book of business includes loans that are refinancings of loans that were in our legacy book of business. We provide information regarding the higher loan-to-value ("LTV") ratios of these loans in "Our Strong New Book of Business—Credit Risk Characteristics of Loans Acquired under Refi Plus and HARP." As described below in "Our Strong New Book of Business," we expect that our new single-family book of business will be profitable over its lifetime.
- Credit Performance. Our single-family serious delinquency rate has declined each quarter since the first quarter of 2010, and was 3.41% as of September 30, 2012, compared with 4.00% as of September 30, 2011. See "Credit Performance" below for additional information about the credit performance of the mortgage loans in our single-family guaranty book of business.
- Reducing Credit Losses and Helping Homeowners. We continued to execute on our strategies for reducing credit losses on our legacy book of business, which are described below under "Reducing Credit Losses on Our Legacy Book of Business." As part of our strategy to reduce defaults, we provided approximately 69,200 workouts to help homeowners stay in their homes or otherwise avoid foreclosure in the third quarter of 2012.
- Providing Liquidity and Support to the Mortgage Market. We continued to be a leading provider of liquidity to the mortgage market in the third quarter of 2012. As described below under "Providing Liquidity and Support to the Mortgage Market," we remained the largest single issuer of mortgage-related securities in the secondary mortgage market in the third quarter of 2012 and remained a constant source of liquidity in the multifamily market.
- Helping to Build a New Housing Finance System. We also continued our work during the third quarter of 2012 to help build a new housing finance system, including pursuing the three strategic goals identified by our conservator for the next phase of our conservatorship: build a new infrastructure for the secondary mortgage market; gradually contract our dominant presence in the marketplace while simplifying and shrinking our operations; and maintain foreclosure prevention activities and credit availability for new and refinanced mortgages. In March 2012, FHFA directed us to implement a set of corporate performance objectives and related targets and measures for 2012, referred to as the 2012 conservatorship scorecard, which provides the implementation roadmap for FHFA's strategic plan. For more information on our strategic goals, see "Business—Executive Summary—Our Business Objectives and Strategy" in our 2011 Form 10-K. For a description of the objectives and targets included in FHFA's 2012 conservatorship scorecard, see "Executive Compensation—Compensation Discussion and Analysis—2012 Executive Compensation Program—2012 Corporate Performance Objectives" in Amendment No. 1 on Form 10-K/A to our Annual Report on Form 10-K for the year ended December 31, 2011 (the "2011 Form 10-K/A").

Summary of Our Financial Performance for the Third Quarter and First Nine Months of 2012

We experienced significant improvement in our financial results for the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011. Over the past nine months, home prices have increased and we have experienced further improvement in the performance of our book of business, such as lower serious delinquency rates. As a result, our loan loss reserves and our provision for credit losses have decreased for the third quarter and first nine months of 2012.

Comprehensive Income (Loss)

Quarterly Results

We recognized comprehensive income of $2.6 billion in the third quarter of 2012, consisting of net income of $1.8 billion and other comprehensive income of $746 million. In comparison, we recognized a comprehensive loss of $5.3 billion in the third quarter of 2011, consisting of a net loss of $5.1 billion and other comprehensive loss of $197 million.

The significant improvement in our financial results for the third quarter of 2012 compared with the third quarter of 2011 was primarily due to a $2.1 billion decrease in our provision for credit losses and a $3.5 billion decrease in fair value losses. Our provision for credit losses declined from $4.2 billion in the third quarter of 2011 to $2.1 billion in the third quarter of 2012 primarily due to a decrease in our total loss reserves. This decrease was driven by an improvement in the profile of our single-family book of business resulting primarily from an increase in actual and expected home prices, including the sales prices of our real-estate owned ("REO") properties throughout 2012. Home prices increased by 1.5% in the third quarter of 2012 compared with a 0.9% decline in the third quarter of 2011 and increased by 4.8% in the first nine months of 2012 compared with a 1.7% decrease in the first nine months of 2011. Higher home prices decrease the likelihood that loans will default and reduce the amount of credit loss on loans that do default. In addition, sales prices on dispositions of our REO properties improved in the third quarter of 2012 as a result of strong demand compared to both the second quarter of 2012 and the prior year. We received net proceeds from our REO sales equal to 61% of the loans' unpaid principal balance in the third quarter of 2012, compared with 59% in the second quarter of 2012 and 54% in the third quarter of 2011. The increase in sales proceeds reduces the amount of credit loss at foreclosure and, accordingly, results in a lower provision for credit loss.

The positive impact of higher home prices and higher REO sales values on our provision for credit losses in the third quarter of 2012 was partially offset by a $3.5 billion increase in our provision for credit losses due to changes in our assumptions and data used in calculating our loss reserves. For additional information on the impact from changes in our assumptions used in calculating our loss reserves in the third quarter of 2012, see "Critical Accounting Policies and Estimates—Total Loss Reserves."

In addition, our provision for credit losses in the third quarter of 2012 was negatively impacted by a change in our accounting for loans to certain borrowers who have received bankruptcy relief. This change led to an increase in the number of loans we classify as troubled debt restructurings ("TDRs"), resulting in an increase in our provision for credit losses of approximately $1.1 billion in the third quarter of 2012. For additional information on this accounting change, see "Consolidated Results of Operations—Credit-Related Expenses—Provision for Credit Losses."

As discussed below in "Our Expectations Regarding Future Loss Reserves and Credit-Related Expenses," due to the large size of our guaranty book of business, even small changes in home prices, economic conditions and other variables can result in significant volatility in the amount of credit-related expenses we recognize from period to period.

Fair value losses declined from $4.5 billion in the third quarter of 2011 to $1.0 billion in the third quarter of 2012. The decrease in fair value losses was primarily due to lower risk management derivative losses as swap rates declined significantly in the third quarter of 2011 compared with a more modest decline in swap rates in the third quarter of 2012. Derivative instruments are an integral part of how we manage interest rate risk and an inherent part of the cost of funding and hedging our mortgage investments. We expect high levels of period-to-period volatility in our results because our derivatives are recorded at fair value in our financial statements while some of the instruments they hedge are not recorded at fair value in our financial statements.

In addition, we recognized other comprehensive income of $746 million in the third quarter of 2012 compared with other comprehensive loss of $197 million in the third quarter of 2011. The other comprehensive income recognized in the third quarter of 2012 was driven by a decrease in unrealized losses on non-agency available-for-sale securities primarily due to narrowing of credit spreads.

Year-to-Date Results

Our comprehensive income for the first nine months of 2012 was $11.1 billion, consisting of net income of $9.7 billion and other comprehensive income of $1.4 billion. In comparison, we recognized a comprehensive loss of $14.5 billion in the first nine months of 2011, primarily related to our net loss of $14.4 billion.

The significant improvement in our financial results in the first nine months of 2012 compared with the first nine months of 2011 was primarily due to a $20.2 billion decrease in our provision for credit losses and a $2.7 billion decline in our fair value losses. Our provision for credit losses declined from $21.2 billion in the first nine months of 2011 to $1.0 billion in the first nine months of 2012 primarily due to an increase in actual and expected home prices in 2012. Fair value losses declined from $5.9 billion in the first nine months of 2011 to $3.2 billion in the first nine months of 2012 due to lower losses on our risk management derivatives.

See "Consolidated Results of Operations" for more information on our results.

Net Worth

Our net worth of $2.4 billion as of September 30, 2012 reflects our comprehensive income of $11.1 billion offset by our payment to Treasury of $8.7 billion in senior preferred stock dividends during the first nine months of 2012.

As a result of our positive net worth as of September 30, 2012, we are not requesting a draw from Treasury under the senior preferred stock purchase agreement. The aggregate liquidation preference on the senior preferred stock remains at $117.1 billion, which requires a dividend payment of $2.9 billion for the fourth quarter of 2012. As of September 30, 2012, we have paid an aggregate of $28.5 billion to Treasury in dividends on the senior preferred stock. As described in "Amendment to Senior Preferred Stock Purchase Agreement with Treasury" below, our dividend obligations to Treasury will change beginning in 2013.

Table 1 below displays our Treasury draws and senior preferred stock dividend payments to Treasury since entering conservatorship on September 6, 2008.

Table 1: Treasury Draws and Senior Preferred Stock Dividend Payments

	2008	2009	2010	2011	2012 (first nine months)	Cumulative Total
	(Dollars in billions)					
Treasury draws[1][2]	$15.2	$60.0	$15.0	$25.9	$—	$116.1
Senior preferred stock dividends[3]	—	2.5	7.7	9.6	8.7	28.5
Treasury draws less senior preferred stock dividends	$15.2	$57.5	$7.3	$16.3	$(8.7)	$87.6
Cumulative percentage of senior preferred stock dividends to Treasury draws	0.2 %	3.3 %	11.3 %	17.1 %	24.5 %	24.5 %

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(1) Represents the total draws received from Treasury based on our quarterly net worth deficits for the periods presented. Draw requests are funded in the quarter following each quarterly net worth deficit.

(2) Treasury draws do not include the initial $1.0 billion liquidation preference of the senior preferred stock, for which we did not receive any cash proceeds.

(3) Represents total quarterly cash dividends paid to Treasury during the periods presented based on an annual rate of 10% per year on the aggregate liquidation preference of the senior preferred stock.

Total Loss Reserves

Our total loss reserves consist of (1) our allowance for loan losses, (2) our allowance for accrued interest receivable, (3) our allowance for preforeclosure property taxes and insurance receivables, and (4) our reserve for guaranty losses. Our total loss reserves, which reflect our estimate of the probable losses we have incurred in our guaranty book of business, including concessions we granted borrowers upon modification of their loans, decreased to $66.9 billion as of September 30, 2012 from $68.0 billion as of June 30, 2012 and $76.9 billion as of December 31, 2011. Our total loss reserve coverage to total nonperforming loans was 26% as of September 30, 2012, compared with 28% as of June 30, 2012 and 31% as of December 31, 2011.

Our Expectations Regarding Future Loss Reserves and Credit-Related Expenses

We expect the trends of stabilizing home prices and declining single-family serious delinquency rates to continue, although we expect serious delinquency rates to decline at a slower pace than in recent periods. As a result of these trends, we believe that our total loss reserves peaked as of December 31, 2011 and will not increase above $76.9 billion in the foreseeable future. Accordingly, we expect that our credit-related expenses will be significantly lower in 2012 than in 2011.

Although we expect these positive trends to continue, the amount of credit-related expenses we recognize in future periods could vary significantly from period to period and may be affected by many different factors, such as those described below. Moreover, although we believe that our total loss reserves peaked as of December 31, 2011, we expect our loss reserves will remain significantly elevated relative to historical levels for an extended period because

(1) we expect future defaults on loans that we acquired prior to 2009 and the resulting charge-offs will occur over a period of years and (2) a significant portion of our reserves represents concessions granted to borrowers upon modification of their loans and will remain in our reserves until the loans are fully repaid or default.

Our expectations regarding our future credit-related expenses and loss reserves are based on our current expectations and assumptions about many factors that are subject to change. Factors that could result in higher credit-related expenses and loss reserves than we currently expect include: a drop in actual or expected home prices; an increase in our serious delinquency rate; an increase in interest rates; an increase in unemployment rates; future legislative or regulatory requirements that have a significant impact on our business, such as a requirement that we implement a principal forgiveness program; future updates to our models relating to our loss reserves, including the assumptions used by these models; future changes to accounting policies relating to our loss reserves; significant changes in modification and foreclosure activity; changes in borrower behavior, such as an increasing number of underwater borrowers who strategically default on their mortgage loan; failures by our mortgage seller/servicers to fulfill their repurchase obligations in full; failures by our mortgage insurers to fulfill their obligations in full; natural or other disasters; and many other factors, including those discussed in "Outlook—Factors that Could Cause Actual Results to be Materially Different from Our Estimates and Expectations" in this report and in "Risk Factors" in both this report and in our 2011 Form 10-K. Due to the large size of our guaranty book of business, even small changes in these factors could have a significant impact on our financial results for a particular period.

We are currently assessing the financial impact on us from Hurricane Sandy. Our exposure to losses as a result of Hurricane Sandy arises primarily from our guaranty of principal and interest payments due to holders of Fannie Mae MBS secured by property in the affected areas, our portfolio holdings of mortgages and mortgage-related securities secured by property in the affected areas, and real estate that we own in the affected areas.

In addition, in April 2012, FHFA issued an Advisory Bulletin that could have an impact on the amount of our future credit-related expenses and loss reserves; however, we are still assessing the impact of the Advisory Bulletin. See "Legislative and Regulatory Developments—FHFA Advisory Bulletin Regarding Framework for Adversely Classifying Loans" in our quarterly report on Form 10-Q for the quarter ended June 30, 2012 ("Second Quarter 2012 Form 10-Q") for additional information.

Our Strong New Book of Business

Credit Risk Profile of Loans in our New Book of Business Compared with our Legacy Book of Business

Since 2009, we have seen the effect of actions we took, beginning in 2008, to significantly strengthen our underwriting and eligibility standards and change our pricing to promote sustainable homeownership and stability in the housing market. While it is too early to know how the single-family loans we have acquired since January 1, 2009 will ultimately perform, given their strong credit risk profile and based on their performance so far, we expect that these loans, in the aggregate, will be profitable over their lifetime, by which we mean that we expect our fee income on these loans to exceed our credit losses and administrative costs for them. In contrast, we expect that the single-family loans we acquired from 2005 through 2008, in the aggregate, will not be profitable over their lifetime. Loans we have acquired since the beginning of 2009 constituted 63% of our single-family guaranty book of business as of September 30, 2012. Our 2005 through 2008 acquisitions, which are becoming a smaller percentage of our single-family guaranty book of business, constituted only 24% of our single-family guaranty book of business as of September 30, 2012.

The 63% of our single-family guaranty book of business that represents our new single-family book of business includes loans that are refinancings of existing Fannie Mae loans under our Refi Plus™ initiative. Refi Plus loans constituted 15% of our single-family guaranty book of business as of September 30, 2012. Refi Plus loans include loans that are refinancings under the Administration's Home Affordable Refinance Program ("HARP"). Because HARP and Refi Plus are designed to expand refinancing opportunities for borrowers who may otherwise be unable to refinance their mortgage loans due to a decline in home values, many of the loans we acquire under HARP and some of the loans we acquire under Refi Plus have higher LTV ratios than we would otherwise permit, greater than 100% in some cases. The volume of loans with high LTV ratios that we acquired under Refi Plus and HARP increased in the third quarter of 2012. As a result, loans with LTV ratios greater than 100% constituted 11% of our acquisitions in the third quarter of 2012, compared with 3% in the third quarter of 2011, and the weighted average LTV ratio at origination of loans we acquired in the third quarter of 2012 increased to 77% from 71% in the third quarter of 2011.

Our expectations regarding the ultimate performance of our loans are based on numerous expectations and assumptions, including those relating to expected changes in regional and national home prices, borrower behavior,

public policy and other macroeconomic factors. If future conditions are more unfavorable than our expectations, the loans we acquired since the beginning of 2009 could become unprofitable. For example, home prices are a key factor affecting the profitability we expect. When home prices decline, the LTV ratios on our loans increase, and both the probability of default and the estimated severity of loss increase. If home prices decline significantly from September 2012 levels, the loans we acquired since the beginning of 2009 could become unprofitable. See "Outlook—Home Prices" for our current expectations regarding changes in home prices. Also see "Outlook—Factors that Could Cause Actual Results to be Materially Different from Our Estimates

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and Expectations" in this report and "Risk Factors" in both this report and our 2011 Form 10-K for a discussion of factors that could cause our expectations regarding the performance of the loans in our new single-family book of business to change.

Table 2 below displays information regarding the credit characteristics of the loans in our single-family conventional guaranty book of business as of September 30, 2012 by acquisition period, which illustrates the improvement in the credit risk profile of loans we acquired beginning in 2009 compared with loans we acquired in 2005 through 2008.

Table 2: Selected Credit Characteristics of Single-Family Conventional Loans Held, by Acquisition Period

	As of September 30, 2012							
	% of Single-Family Conventional Guaranty Book of Business[1]		Current Estimated Mark-to-Market LTV Ratio[1]		Current Mark-to-Market LTV Ratio >100%[1][2]		Serious Delinquency Rate[3]	
Year of Acquisition:								
New Single-Family Book of Business:								
2012	21	%	73	%	8	%	0.02	%
2011	16		67		3		0.19	
2010	14		69		4		0.49	
2009	12		70		5		0.85	
Total New Single-Family Book of Business	63		70		5		0.34	
Legacy Book of Business:								
2005-2008	24		99		42		9.62	
2004 and prior	13		58		7		3.49	
Total Single-Family Book of Business	100	%	76	%	14	%	3.41	%

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(1) Calculated based on the aggregate unpaid principal balance of single-family loans for each category divided by the aggregate unpaid principal balance of loans in our single-family conventional guaranty book of business as of September 30, 2012.

(2) The majority of loans in our new single-family book of business as of September 30, 2012 with mark-to-market LTV ratios over 100% were loans acquired under our Refi Plus initiative. See "Credit Risk Characteristics of Loans Acquired under Refi Plus and HARP" for more information on our recent acquisitions of loans with high LTV ratios.

(3) Some of the loans acquired in 2012 were originated so recently that they could not yet have become seriously delinquent. The serious delinquency rates for loans acquired in more recent years will be higher after the loans have aged, but we do not expect them to approach the levels of the September 30, 2012 serious delinquency rates of loans in our legacy book of business.

The single-family loans that we acquired in the first nine months of 2012 had a weighted average FICO® credit score at origination of 761 and an average original LTV ratio of 74%. Of the single-family loans we acquired in the first nine months of 2012, approximately 16% had an original LTV ratio greater than 90%, and approximately 1% had a FICO credit score at origination of less than 620. The average original LTV ratio of single-family loans we acquired in the first nine months of 2012, excluding HARP loans, was 69%, compared with 109% for HARP loans. See Table 2 in our 2011 Form 10-K for information regarding the credit risk profile of the single-family conventional loans we acquired during specified previous periods.

Credit Risk Characteristics of Loans Acquired under Refi Plus and HARP

Since 2009, our acquisitions have included a significant number of loans refinanced under HARP. We acquire HARP loans under Refi Plus, which provides expanded refinance opportunities for eligible Fannie Mae borrowers. HARP loans have LTV ratios at origination in excess of 80% and must be secured by the borrower's primary residence. In addition, a HARP loan cannot (1) be an adjustable-rate mortgage loan, or ARM, if the initial fixed period is less than

five years; (2) have an interest-only feature, which permits the payment of interest without a payment of principal; (3) be a balloon mortgage loan; or (4) have the potential for negative amortization. Under Refi Plus, we also acquire loans with LTV ratios at origination greater than 80% that do not meet the criteria for HARP because they are not secured by the borrower's primary residence, as well as loans that have LTV ratios at origination of less than 80%. Many of the loans we acquire under HARP and some of the loans we acquire under Refi Plus have higher LTV ratios than we would otherwise permit. Some borrowers for these loans also have lower FICO credit scores than we would otherwise require.

Loans we acquire under Refi Plus and HARP represent refinancings of loans that are already in our guaranty book of business. The credit risk associated with loans we acquire under Refi Plus and HARP essentially replaces the credit risk that we already held prior to the refinancing. Loans we acquire under Refi Plus and HARP have higher serious delinquency rates and may not perform as well as the other loans we have acquired since the beginning of 2009. However, we expect these loans will perform better than the loans they replace because Refi Plus and HARP loans should reduce the borrowers' monthly payments and/or provide more stable terms than the borrowers' old loans (for example, by refinancing into a mortgage with a fixed interest rate instead of an adjustable rate).

Loans we acquired under Refi Plus represented 24% of our new single-family book of business as of September 30, 2012 and had a serious delinquency rate of 0.60%, compared with a serious delinquency rate for our new single-family book of business overall of 0.34%. HARP loans, which are a subset of Refi Plus loans, represented 11% of our new single-family book of business as of September 30, 2012 and had a serious delinquency rate of 0.98%. See "Table 34: Selected Credit Characteristics of Single-Family Conventional Loans Acquired under HARP and Refi Plus" for more information on the serious delinquency rates and mark-to-market LTV ratios as of September 30, 2012 and the FICO credit scores at origination of loans in our new single-family book of business overall and of loans we acquired under Refi Plus and HARP.

The changes we implemented in the first half of 2012 to make the benefits of HARP available to more borrowers, combined with historically low interest rates in the third quarter, resulted in an increase in the volume of loans we acquired under HARP and Refi Plus in the third quarter of 2012, as compared with the first and second quarters of 2012. The approximately 164,000 loans we acquired under HARP in the third quarter of 2012 constituted 15% of our single-family acquisitions for the period, measured by unpaid principal balance, compared with 15% of single-family acquisitions in the second quarter of 2012 and 10% of single-family acquisitions in the first quarter of 2012. These loans were included in the approximately 312,000 loans we acquired under Refi Plus in the third quarter of 2012, which constituted 25% of our single-family acquisitions for the period, measured by unpaid principal balance, compared with 27% of single-family acquisitions in the second quarter of 2012 and 22% of single-family acquisitions in the first quarter of 2012.

As a result of changes to HARP, we expect that if interest rates remain low we will continue to acquire a high volume of refinancings under HARP until there is no longer a large population of borrowers with loans that have high LTV ratios who would benefit from refinancing. In particular, we expect to acquire many refinancings with LTV ratios greater than 125%, because borrowers were unable to refinance loans with LTV ratios greater than 125% in large numbers until changes to HARP were fully implemented in the second quarter of 2012. HARP is scheduled to end in December 2013.

Factors that May Affect the Credit Risk Profile and Performance of Loans in our New Book of Business in the Future

Whether the loans we acquire in the future will exhibit an overall credit profile similar to our more recent acquisitions will depend on a number of factors, including our future pricing and eligibility standards and those of mortgage insurers and the Federal Housing Administration ("FHA"), the percentage of loan originations representing refinancings, our future objectives, government policy, market and competitive conditions, and the volume and characteristics of loans we acquire under Refi Plus and HARP.

See "Business—Executive Summary—Our Strong New Book of Business and Expected Losses on Our Legacy Book of Business—Building a Strong New Single-Family Book of Business" in our 2011 Form 10-K for a more detailed discussion of the changes in the credit profile of our single-family acquisitions. In addition, see "MD&A—Risk Management—Credit Risk Management—Single-Family Mortgage Credit Risk Management" for more detail regarding the credit risk characteristics of our single-family guaranty book of business.

Credit Performance

Table 3 presents information for each of the last seven quarters about the credit performance of mortgage loans in our single-family guaranty book of business and our workouts. The term "workouts" refers to home retention solutions and foreclosure alternatives. The workout information in Table 3 does not reflect repayment plans and forbearances that have been initiated but not completed, nor does it reflect trial modifications that have not become permanent.

Table 3: Credit Statistics, Single-Family Guaranty Book of Business[1]

	2012 Q3 YTD	Q3	Q2	Q1	2011 Full Year	Q4	Q3	Q2
	(Dollars in millions)							
As of the end of each period:								
Serious delinquency rate[2]	3.41 %	3.41 %	3.53 %	3.67 %	3.91 %	3.91 %	4.00 %	4.08 %
Seriously delinquent loan count	599,430	599,430	622,052	650,918	690,911	690,911	708,847	729,772
Nonperforming loans[3]	$250,678	$250,678	$240,472	$243,981	$248,379	$248,379	$248,134	$245,848
Foreclosed property inventory:								
Number of properties[4]	107,225	107,225	109,266	114,157	118,528	118,528	122,616	135,719
Carrying value	$9,302	$9,302	$9,421	$9,721	$9,692	$9,692	$11,039	$12,480
Combined loss reserves[5]	$63,100	$63,100	$63,365	$69,633	$71,512	$71,512	$70,741	$68,887
Total loss reserves[6]	$65,685	$65,685	$66,694	$73,119	$75,264	$75,264	$73,973	$73,116
During the period:								
Foreclosed property (number of properties):								
Acquisitions[4]	133,367	41,884	43,783	47,700	199,696	47,256	45,194	53,697
Dispositions	(144,670)	(43,925)	(48,674)	(52,071)	(243,657)	(51,344)	(58,297)	(71,202)
Credit-related expenses (income)[7]	$1,500	$2,130	$(3,015)	$2,385	$27,218	$5,397	$4,782	$5,933
Credit losses[8]	$12,218	$3,485	$3,778	$4,955	$18,346	$4,548	$4,384	$3,810
REO net sales prices to UPB[9]	59 %	61 %	59 %	56 %	54 %	55 %	54 %	54 %
Loan workout activity (number of loans):								
Home retention loan workouts[10]	142,697	45,936	41,226	55,535	248,658	60,453	68,227	59,019
Short sales and deeds-in-lieu	69,548	23,322	24,013	22,213	79,833	22,231	19,306	21,176

of foreclosure								
Total loan workouts	212,245	69,258	65,239	77,748	328,491	82,684	87,533	80,195
Loan workouts as a percentage of delinquent loans in our guaranty book of business[11]	25.72 %	25.18 %	24.14 %	28.85 %	27.05 %	27.24 %	28.39 %	25.71 %

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(1) Our single-family guaranty book of business consists of (a) single-family mortgage loans held in our mortgage portfolio, (b) single-family mortgage loans underlying Fannie Mae MBS, and (c) other credit enhancements that we provide on single-family mortgage assets, such as long-term standby commitments. It excludes non-Fannie Mae mortgage-related securities held in our mortgage portfolio for which we do not provide a guaranty.

(2) Calculated based on the number of single-family conventional loans that are 90 days or more past due and loans that have been referred to foreclosure but not yet foreclosed upon, divided by the number of loans in our single-family conventional guaranty book of business. We include all of the single-family conventional loans that we own and those that back Fannie Mae MBS in the calculation of the single-family serious delinquency rate.

(3) Represents the total amount of nonperforming loans including troubled debt restructurings. A troubled debt restructuring is a restructuring of a mortgage loan in which a concession is granted to a borrower experiencing financial difficulty. We generally classify loans as nonperforming when the payment of principal or interest on the loan is 60 days or more past due. As of September 30, 2012, we classified $12.7 billion of loans on accrual status as TDRs where certain borrowers have received bankruptcy relief.

(4) Includes held for use properties, which are reported in our condensed consolidated balance sheets as a component of "Other assets" and acquisitions through deeds-in-lieu of foreclosure.

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(5) Consists of the allowance for loan losses for loans recognized in our condensed consolidated balance sheets and the reserve for guaranty losses related to both single-family loans backing Fannie Mae MBS that we do not consolidate in our condensed consolidated balance sheets and single-family loans that we have guaranteed under long-term standby commitments. For additional information on the change in our loss reserves see "Consolidated Results of Operations—Credit-Related Expenses—Provision for Credit Losses."

(6) Consists of (a) the combined loss reserves, (b) allowance for accrued interest receivable, and (c) allowance for preforeclosure property taxes and insurance receivables.

(7) Consists of (a) the provision for credit losses and (b) foreclosed property (income) expense.

(8) Consists of (a) charge-offs, net of recoveries and (b) foreclosed property (income) expense, adjusted to exclude the impact of fair value losses resulting from credit-impaired loans acquired from MBS trusts.

(9) Calculated as the amount of sale proceeds received on disposition of REO properties during the respective quarterly period, excluding those subject to repurchase requests made to our seller/servicers divided by the aggregate UPB of the related loans at the time of foreclosure. Net sales price represents the contract sale price less selling costs for the property and other charges paid by the seller at closing.

(10) Consists of (a) modifications, which do not include trial modifications or repayment plans or forbearances that have been initiated but not completed and (b) repayment plans and forbearances completed. See "Table 38: Statistics on Single-Family Loan Workouts" in "Risk Management—Credit Risk Management—Single-Family Mortgage Credit Risk Management—Problem Loan Management—Loan Workout Metrics" for additional information on our various types of loan workouts.

(11) Calculated based on annualized problem loan workouts during the period as a percentage of delinquent loans in our single-family guaranty book of business as of the end of the period.

Our single-family serious delinquency rate has decreased each quarter since the first quarter of 2010. The decrease in our serious delinquency rate is primarily the result of home retention solutions, foreclosure alternatives and completed foreclosures, as well as our acquisition of loans with stronger credit profiles since the beginning of 2009.

Although our single-family serious delinquency rate has decreased significantly since the first quarter of 2010, our serious delinquency rate and the period of time that loans remain seriously delinquent has been negatively affected in recent periods by the increase in the average number of days it is taking to complete a foreclosure. As described in "Business—Executive Summary—Reducing Credit Losses on Our Legacy Book of Business—Managing Timelines for Workouts and Foreclosures" in our 2011 Form 10-K, high levels of foreclosures, continuing issues in the servicer foreclosure process and changing legislative, regulatory and judicial requirements have lengthened the time it takes to foreclose on a mortgage loan in many states. We expect serious delinquency rates will continue to be affected in the future by home price changes, changes in other macroeconomic conditions, the length of the foreclosure process and the volume of loan modifications. We expect the number of our single-family loans that are seriously delinquent to remain well above pre-2008 levels for years. In addition, we anticipate that it will take a significant amount of time before our REO inventory is reduced to pre-2008 levels.

We provide additional information on our credit-related expenses in "Consolidated Results of Operations—Credit-Related Expenses" and on the credit performance of mortgage loans in our single-family book of business and our loan workouts in "Risk Management—Credit Risk Management—Single-Family Mortgage Credit Risk Management."

Reducing Credit Losses on Our Legacy Book of Business

To reduce the credit losses we ultimately incur on our legacy book of business, we have been focusing our efforts on the following strategies:

- Helping underwater and other eligible Fannie Mae borrowers with high LTV ratio loans refinance to more sustainable loans, including loans that significantly reduce their monthly payments, through HARP and our Refi Plus initiative;
- Reducing defaults by offering borrowers solutions that can significantly reduce their monthly payments and enable them to stay in their homes ("home retention solutions");
- Pursuing "foreclosure alternatives," which help borrowers avoid foreclosure and reduce the severity of the losses we incur overall;
- Efficiently managing timelines for home retention solutions, foreclosure alternatives and foreclosures;

- Improving servicing standards and servicers’ execution and consistency;
- Managing our REO inventory to minimize costs and maximize sales proceeds; and
- Pursuing contractual remedies from lenders, servicers and providers of credit enhancement.

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See “Business—Executive Summary—Reducing Credit Losses on our Legacy Book of Business” in our 2011 Form 10-K, as well as “Risk Management—Credit Risk Management—Single-Family Mortgage Credit Risk Management” in both this report and our 2011 Form 10-K, for more information on the strategies and actions we are taking to minimize our credit losses.

Providing Liquidity and Support to the Mortgage Market

Our Liquidity and Support Activities

We provide liquidity and support to the U.S. mortgage market in a number of important ways:

- We serve as a stable source of liquidity for purchases of homes and financing of multifamily rental housing, as well as for refinancing existing mortgages. We provided approximately $3.0 trillion in liquidity to the mortgage market from January 1, 2009 through September 30, 2012 through our purchases and guarantees of loans, which enabled borrowers to complete 8.9 million mortgage refinancings and 2.5 million home purchases, and provided financing for 1.5 million units of multifamily housing.
- We have strengthened our underwriting and eligibility standards to support sustainable homeownership. As a result, our new single-family book of business has a strong credit risk profile. Our support enables borrowers to have access to a variety of conforming mortgage products, including long-term, fixed-rate mortgages, such as the prepayable 30-year fixed-rate mortgage that protects homeowners from interest rate swings.
- We helped 1.2 million homeowners stay in their homes or otherwise avoid foreclosure from January 1, 2009 through September 30, 2012, which helped to support neighborhoods, home prices and the housing market.
- We helped borrowers refinance loans through Refi Plus. From April 1, 2009, the date we began accepting delivery of Refi Plus loans, through September 30, 2012, we have acquired approximately 2.5 million loans refinanced under our Refi Plus initiative. Refinancings delivered to us through Refi Plus in the third quarter of 2012 reduced borrowers’ monthly mortgage payments by an average of $221. Some borrowers’ monthly payments increased as they took advantage of the ability to refinance through Refi Plus to reduce the term of their loan, to switch from an adjustable-rate mortgage to a fixed-rate mortgage or to switch from an interest-only mortgage to a fully amortizing mortgage.
- We support affordability in the multifamily rental market. Over 85% of the multifamily units we financed from 2009 through 2011 were affordable to families earning at or below the median income in their area.
- In addition to purchasing and guaranteeing loans, we provide funds to the mortgage market through short-term financing and other activities. These activities are described in more detail in our 2011 Form 10-K in “Business—Business Segments—Capital Markets.”

2012 Acquisitions and Market Share

In the first nine months of 2012, we purchased or guaranteed approximately $668 billion in loans, measured by unpaid principal balance, which includes $35.9 billion in delinquent loans we purchased from our single-family MBS trusts. These activities enabled our lender customers to finance approximately 2.8 million single-family conventional loans and loans for approximately 371,000 units in multifamily properties during the first nine months of 2012.

We remained the largest single issuer of mortgage-related securities in the secondary market during the third quarter of 2012, with an estimated market share of new single-family mortgage-related securities issuances of 52%. Our estimated market share of new single-family mortgage-related securities issuances was 46% in the second quarter of 2012 and 43% in the third quarter of 2011. The volume of our loan acquisitions in the first nine months of 2012 was greater than the volume of our loan acquisitions for all of 2011, due to the implementation of changes to HARP and lower interest rates in 2012.

We remained a constant source of liquidity in the multifamily market. We owned or guaranteed approximately 22% of the outstanding debt on multifamily properties as of June 30, 2012 (the latest date for which information was available).

Amendment to Senior Preferred Stock Purchase Agreement with Treasury

On August 17, 2012, we, through FHFA acting on our behalf in its capacity as our conservator, and Treasury entered into an amendment to the senior preferred stock purchase agreement between us and Treasury. We describe the terms of this agreement and the related senior preferred stock, prior to the amendment described below, in our 2011 Form 10-K under the heading “Business—Conservatorship and Treasury Agreements—Treasury Agreements.” Unless the context

indicates otherwise, references in this report to the senior preferred stock purchase agreement refer to the agreement as amended on August 17, 2012.

The August 2012 amendment revised the terms of the senior preferred stock purchase agreement and the related senior preferred stock in the following ways:

- Dividends. Beginning in 2013, the method for calculating the amount of dividends we are required to pay Treasury on the senior preferred stock will change. The current method, which will remain in effect through December 31, 2012, is to apply an annual dividend rate of 10% to the aggregate liquidation preference of the senior preferred stock. Effective January 1, 2013, the amount of dividends payable on the senior preferred stock for a dividend period will be determined based on our net worth as of the end of the immediately preceding fiscal quarter. Our net worth as defined by the agreement is the amount, if any, by which our total assets (excluding Treasury's funding commitment and any unfunded amounts related to the commitment) exceed our total liabilities (excluding any obligation in respect of capital stock), in each case as reflected on our balance sheet prepared in accordance with generally accepted accounting principles ("GAAP"). For each dividend period from January 1, 2013 through and including December 31, 2017, the dividend amount will be the amount, if any, by which our net worth as of the end of the immediately preceding fiscal quarter exceeds an applicable capital reserve amount. The capital reserve amount will be $3.0 billion during 2013 and will be reduced by $600 million each year until it reaches zero on January 1, 2018. For each dividend period beginning in 2018, the dividend amount will be the entire amount of our net worth, if any, as of the end of the immediately preceding fiscal quarter.

As a result of these revised dividend payment provisions, beginning in 2013, when we have quarterly earnings that result in a net worth greater than the applicable capital reserve amount, we will pay dividends to Treasury in the next quarter; but if our net worth does not exceed the applicable capital reserve amount as of the end of a quarter, then we will not be required to accrue or pay any dividends in the next quarter. See "Risk Factors" for a discussion of the risks relating to our dividend obligations to Treasury on the senior preferred stock.

- Periodic Commitment Fee. Effective January 1, 2013, the periodic commitment fee provided for under the agreement is suspended, as long as the changes to the dividend payment provisions referenced above remain in effect. Although we had been scheduled to begin paying this commitment fee to Treasury beginning in 2011, Treasury waived the commitment fee for each quarter of 2011 and 2012 due to the continued fragility of the U.S. mortgage market and Treasury's belief that the imposition of the fee would not generate increased compensation for taxpayers.
- Transfer of Assets Covenant. The transfer of assets covenant contained in the agreement was amended to allow the company to dispose of assets and properties at fair market value, in one transaction or a series of related transactions, without requiring the prior written consent of Treasury, if such assets have a fair market value individually or in the aggregate of less than $250 million, regardless of whether or not the transaction is in the ordinary course of business.
- Mortgage Assets Covenant. The mortgage assets covenant contained in the agreement was amended to: (1) reduce the maximum allowable amount of mortgage assets we may own as of December 31, 2012 from $656.1 billion to $650 billion; and (2) require that, on December 31 of each year following December 31, 2012, we reduce our mortgage assets to 85% of the maximum allowable amount that we were permitted to own as of December 31 of the immediately preceding calendar year (rather than 90% as previously provided by the agreement), until the amount of our mortgage assets reaches $250 billion. This amendment to the mortgage assets covenant accelerates the reduction of our mortgage asset portfolio. As a result of this amendment, our mortgage asset cap will decrease to $250 billion by 2018, rather than by 2022.
- Annual Risk Management Plan Covenant. A new covenant was added requiring that we provide an annual risk management plan to Treasury not later than December 15 of each year we remain in conservatorship, beginning not later than December 15, 2012. Each annual risk management plan is required to set out our strategy for reducing our risk profile and to describe the actions we will take to reduce the financial and operational risk associated with each of our business segments. Each plan delivered after December 15, 2012 must include an assessment of our performance against the planned actions described in the prior year's plan.

In addition to the above-described amendments, the August 2012 amendment also required that we amend or replace the existing certificate of designation for the senior preferred stock to reflect the revised dividend payment provisions described above. In accordance with this requirement, on September 27, 2012, FHFA, acting on our behalf as our conservator, issued an amended and restated certificate of designation reflecting the revised terms.

In its August 17, 2012 announcement regarding the modifications to the senior preferred stock purchase agreement, Treasury stated that the modifications will help achieve several important objectives, including:

- making sure that every dollar of earnings that Fannie Mae and Freddie Mac generate will be used to benefit taxpayers for their investment in those firms;
- ending the circular practice of Treasury advancing funds to the GSEs simply to pay dividends back to Treasury;
- acting upon the commitment made in the Administration's 2011 White Paper that the GSEs will be wound down and will not be allowed to retain profits, rebuild capital, and return to the market in their prior form;
- supporting the continued flow of mortgage credit by providing borrowers, market participants, and taxpayers with additional confidence in the ability of the GSEs to meet their commitments while operating under conservatorship; and
- providing greater market certainty regarding the financial strength of the GSEs.

Housing and Mortgage Market and Economic Conditions

Economic growth accelerated in the third quarter of 2012 compared with the second quarter of 2012. The inflation-adjusted U.S. gross domestic product, or GDP, rose by 2.0% on an annualized basis in the third quarter of 2012, according to the Bureau of Economic Analysis advance estimate, compared with an increase of 1.3% in the second quarter of 2012. Growth in employment improved during the third quarter of 2012, as the overall economy gained an estimated 521,000 jobs, compared with 200,000 jobs in the second quarter, according to the U.S. Bureau of Labor Statistics. Over the past 12 months ending in September 2012, the economy created 1.9 million non-farm jobs. The unemployment rate was 7.8% in September 2012 compared with 8.2% in June 2012. In October 2012, non-farm payrolls strengthened, rising by 171,000 during the month, but the unemployment rate rose to 7.9%.

Housing activity improved during the third quarter of 2012. Total existing home sales averaged 4.7 million units annualized in the third quarter of 2012, a 3.2% increase from the second quarter of 2012, according to data available through October 2012 from the National Association of REALTORS®. Sales of foreclosed homes and preforeclosure, or "short," sales (together, "distressed sales") accounted for 24% of existing home sales in September 2012, compared with 25% in June 2012 and 30% in September 2011. New single-family home sales strengthened during the quarter, averaging an annualized rate of 377,000 units, a 4.0% increase from the prior quarter.

The overall mortgage market serious delinquency rate, which has trended down since peaking in the fourth quarter of 2009, remained high at 7.3% as of June 30, 2012, according to the Mortgage Bankers Association National Delinquency Survey. According to the National Association of REALTORS® October 2012 Existing Home Sales Report, the months' supply of existing unsold homes was 5.9 months as of September 30, 2012, compared with 6.5 months as of June 30, 2012 and 8.1 months as of September 30, 2011. While the high level of seriously delinquent mortgage loans has resulted in a high level of foreclosures, new home building has remained at a low level, which has brought the previously elevated level of housing supply down to a more market-balanced position over the past year. However, properties that are vacant and held off the market, combined with a portion of properties backing seriously delinquent mortgages not currently listed for sale, represent an elevated level of shadow inventory that could potentially put downward pressure on home prices.

After declining by an estimated 23.7% from their peak in the third quarter of 2006 to the first quarter of 2012, we estimate that home prices on a national basis increased by 3.5% in the second quarter of 2012 and by 1.5% in the third quarter of 2012. Our home price estimates are based on preliminary data and are subject to change as additional data become available. The decline in home prices over the past several years has left many homeowners with "negative equity" in their homes, which means their principal mortgage balance exceeds the current market value of their home. This increases the likelihood that borrowers will walk away from their mortgage obligations and that the loans will become delinquent and proceed to foreclosure. According to CoreLogic, approximately 11 million, or 22%, of all residential properties with mortgages were in a negative equity position at the end of the second quarter of 2012, the most recent date for which information is available. This potential supply also weighs on the supply/demand balance putting downward pressure on home prices. See "Risk Factors" in our 2011 Form 10-K for a description of risks to our business associated with the weak economy and housing market.

During the third quarter of 2012, the multifamily sector continued to experience growth in rental demand, but at a slightly slower rate. Preliminary third-party data suggest that the national vacancy rate for professionally managed, institutional investment-type apartment properties declined to an estimated 5.50% as of September 30, 2012, compared with an estimated 5.75% as of June 30, 2012 and an estimated 6.50% as of September 30, 2011. In addition,

preliminary third-party data suggest that asking rents experienced a modest increase in the third quarter of 2012, rising by an estimated 0.75% on a national basis. As indicated by data from Axiometrics, multifamily concession rates, the rental discount rate as a percentage of asking rents, continued its declining trend during the third quarter of 2012, declining to less than -2.0%, compared with -2.3% as of June 30, 2012 and -3.0% as of September 30, 2011. Estimated positive net absorption, or the net change in the number of occupied rental units after deducting new supply added, remained positive during the third quarter of 2012,

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although it slowed to approximately 23,000 units, according to preliminary data from Reis, Inc., compared with more than 31,000 units during the second quarter of 2012 and more than 36,000 units during the first quarter of 2012. Multifamily construction starts rose to an annualized rate of 260,000 units as of September 30, 2012, compared with 219,000 units as of September 30, 2011, based on data from the Census Bureau. We believe that the overall national rental market's supply will remain fairly stable over the longer term, based on expected construction completions, annualized obsolescence and anticipated household formation trends; however, there is a potential for over-supply in a limited number of local areas over the next 24 months.

Outlook

Credit-Related Expenses and Financial Results. We expect that our credit-related expenses for 2012 will be significantly lower than for 2011. As a result, we expect to report net income for 2012, which would be the first time we have reported annual net income since 2006. There is significant uncertainty in the current market environment, however, and any changes in the trends in macroeconomic factors that we currently anticipate, such as home prices and unemployment, may cause our future credit-related expenses and overall financial results to vary significantly from our current expectations. We further describe our outlook for credit-related expenses, including factors that could result in higher credit-related expenses than we currently expect, in "Summary of Our Financial Performance for the Third Quarter and First Nine Months of 2012—Our Expectations Regarding Future Loss Reserves and Credit-Related Expenses."

Credit Losses. Our credit losses, which include our charge-offs, net of recoveries, reflect our realization of losses on our loans. We realize losses on loans, through our charge-offs, when foreclosure sales are completed or when we accept short sales or deeds-in-lieu of foreclosure. We expect our credit losses to remain high in 2012 relative to pre-housing crisis levels. To the extent delays in foreclosures continue in 2012, our realization of some credit losses will be delayed. See "Consolidated Results of Operations—Credit-Related Expenses—Credit Loss Performance Metrics" for more information regarding our credit losses.

Overall Market Conditions. We expect mortgage loan delinquencies and foreclosures to continue to decline slowly while remaining at levels significantly higher than pre-housing crisis levels for the remainder of 2012 and through 2013. We expect that single-family default and severity rates will remain high for the remainder of 2012 compared to pre-housing crisis levels, but will be lower in 2012 overall than in 2011 overall. Despite multifamily sector improvement at the national level, we expect multifamily foreclosures in 2012 to remain generally commensurate with 2011 levels as certain local markets and properties continue to exhibit weak fundamentals. Conditions may worsen if the unemployment rate increases on either a national or regional basis.

As a result of the changes to HARP implemented this year and historically low interest rates, we acquired more refinancings in the first nine months of 2012 than we acquired in all of 2011. We expect that if interest rates remain low we will continue to acquire a high volume of refinancings under HARP until there is no longer a large population of borrowers with loans that have high LTV ratios who would benefit from refinancing. In particular, we expect to acquire many refinancings with LTV ratios greater than 125%, because borrowers were unable to refinance loans with LTV ratios greater than 125% in large numbers until changes to HARP were fully implemented in the second quarter of 2012. For a description of the changes to HARP, see "Business—Making Home Affordable Program—Changes to the Home Affordable Refinance Program" in our 2011 Form 10-K.

We estimate that total originations in the U.S. single-family mortgage market in 2012 will increase from 2011 levels by approximately 20% from an estimated $1.5 trillion to an estimated $1.8 trillion, and that the amount of originations in the U.S. single-family mortgage market that are refinancings will increase from approximately $980 billion in 2011 to approximately $1.3 trillion in 2012. Refinancings comprised approximately 79% of our single-family business volume in the first nine months of 2012, compared with approximately 76% for all of 2011.

Home Prices. After declining by an estimated 23.7% from their peak in the third quarter of 2006 to the first quarter of 2012, we estimate that home prices on a national basis increased by 3.5% in the second quarter of 2012 and by 1.5% in the third quarter of 2012. Although we believe home prices may decline again through early 2013, we expect that, if current market trends continue, home prices will not decline on a national basis below their first quarter 2012 levels. Future home price changes may be very different from our estimates as a result of significant inherent uncertainty in the current market environment, including uncertainty about the effect of actions the federal government has taken and

may take with respect to tax policies, spending cuts, mortgage finance programs and policies, and housing finance reform; the management of the Federal Reserve’s MBS holdings; the impact of those actions on and changes generally in unemployment and the general economic and interest rate environment; and the impact on the U.S. economy of the European debt crisis. Because of these uncertainties, the actual home price changes we experience may differ significantly from these estimates. We also expect significant regional variation in home price changes and the timing of home price stabilization. Our estimates of home price

changes are based on our home price index, which is calculated differently from the S&P/Case-Shiller U.S. National Home Price Index and therefore results in different percentages for comparable changes. Our estimated 23.7% peak-to-trough decline in home prices on a national basis corresponds to a 34.7% decline according to the S&P/Case-Shiller U.S. National Home Price Index.

Uncertainty Regarding our Future Status. There is significant uncertainty regarding the future of our company, including how long the company will continue to be in its current form, the extent of our role in the market, what form we will have, and what ownership interest, if any, our current common and preferred stockholders will hold in us after the conservatorship is terminated. We expect this uncertainty to continue. In February 2011, Treasury and the Department of Housing and Urban Development ("HUD") released a report to Congress on reforming America's housing finance market. The report states that the Administration will work with FHFA to determine the best way to responsibly wind down both Fannie Mae and Freddie Mac. The report emphasizes the importance of providing the necessary financial support to Fannie Mae and Freddie Mac during the transition period. In February 2012, Treasury Secretary Geithner stated that the Administration intended to release new details around approaches to housing finance reform, including winding down Fannie Mae and Freddie Mac, and to work with congressional leaders to explore options for legislation, but that he does not expect housing finance reform legislation to be enacted in 2012. We cannot predict the prospects for the enactment, timing or content of legislative proposals regarding long-term reform of the GSEs. See "Legislative and Regulatory Developments" in this report and "Business—Legislative and Regulatory Developments" in our 2011 Form 10-K for discussions of recent legislative reform of the financial services industry and proposals for GSE reform that could affect our business. See "Risk Factors" in our 2011 Form 10-K for a discussion of the risks to our business relating to the uncertain future of our company.

Treasury Draws and Dividend Payments. As a result of the revisions to the dividend payment provisions in our senior preferred stock purchase agreement with Treasury described in "Amendment to Senior Preferred Stock Purchase Agreement with Treasury," beginning in 2013, if our net worth does not exceed the applicable capital reserve amount as of the end of a fiscal quarter, then no dividend amount will accrue or be payable for the applicable dividend period. Accordingly, beginning in 2013, we will no longer be required to draw additional funds from Treasury under the senior preferred stock purchase agreement in order to meet our dividend obligations to Treasury on the senior preferred stock. However, in some future periods we could have a net worth deficit and in such case we would be required to obtain additional funding from Treasury pursuant to the senior preferred stock purchase agreement. See "Risk Factors" for a discussion of the risks relating to our dividend obligation to Treasury on the senior preferred stock.

Factors that Could Cause Actual Results to be Materially Different from Our Estimates and Expectations. We present a number of estimates and expectations in this executive summary, including estimates and expectations regarding our future financial results, the profitability of single-family loans we have acquired, our credit losses, our loss reserves, our credit-related expenses, and our draws from and dividends to Treasury. These estimates and expectations are forward-looking statements based on our current assumptions regarding numerous factors, including future home prices and the future performance of our loans. Our future estimates of our performance, as well as the actual amounts, may differ materially from our current estimates and expectations as a result of: the timing and level of, as well as regional variation in, home price changes; changes in interest rates, unemployment rates and other macroeconomic variables; government policy; the length of time it takes to complete foreclosures; changes in GAAP; credit availability; borrower behavior; the volume of loans we modify; the effectiveness of our loss mitigation strategies, management of our REO inventory and pursuit of contractual remedies; whether our counterparties meet their obligations in full; changes in the fair value of our assets and liabilities; impairments of our assets; natural or other disasters; and many other factors, including those discussed in "Risk Factors," "Forward-Looking Statements" and elsewhere in this report, and in "Risk Factors" in our 2011 Form 10-K. For example, if the economy were to enter a deep recession, we would expect actual outcomes to differ substantially from our current expectations.

LEGISLATIVE AND REGULATORY DEVELOPMENTS

The information in this section updates and supplements information regarding legislative and regulatory developments set forth in "Business—Legislative and Regulatory Developments" and "Business—Our Charter and Regulation of Our Activities" in our 2011 Form 10-K and in "MD&A—Legislative and Regulatory Developments" in both our quarterly report on Form 10-Q for the quarter ended March 31, 2012 ("First Quarter 2012 Form 10-Q") and our Second

Quarter 2012 Form 10-Q. Also see “Risk Factors” in this report and our 2011 Form 10-K for a discussion of risks relating to legislative and regulatory matters.

GSE Reform

Policymakers and others have focused significant attention in recent years on how to reform the nation's housing finance system, including what role, if any, the GSEs should play. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), which was signed into law in July 2010, calls for enactment of meaningful structural reforms of Fannie Mae and Freddie Mac. The Dodd-Frank Act also required the Treasury Secretary to submit a report to Congress with recommendations for ending the conservatorships of Fannie Mae and Freddie Mac. In February 2011, Treasury and HUD released their report to Congress on reforming America's housing finance market. The report provides that the Administration will work with FHFA to determine the best way to responsibly reduce Fannie Mae's and Freddie Mac's role in the market and ultimately wind down both institutions.

The report identifies a number of policy steps that could be used to wind down Fannie Mae and Freddie Mac, reduce the government's role in housing finance and help bring private capital back to the mortgage market. These steps include (1) increasing guaranty fees, (2) gradually increasing the level of required down payments so that any mortgages insured by Fannie Mae or Freddie Mac eventually have at least a 10% down payment, (3) reducing conforming loan limits to those established in the Federal Housing Finance Regulatory Reform Act of 2008 (the "2008 Reform Act"), (4) encouraging Fannie Mae and Freddie Mac to pursue additional credit loss protection and (5) reducing Fannie Mae's and Freddie Mac's portfolios, consistent with Treasury's senior preferred stock purchase agreements with the companies.

In addition, the report outlines three potential options for a new long-term structure for the housing finance system following the wind-down of Fannie Mae and Freddie Mac. The first option would privatize housing finance almost entirely. The second option would add a government guaranty mechanism that could scale up during times of crisis. The third option would involve the government offering catastrophic reinsurance behind private mortgage guarantors. Each of these options assumes the continued presence of programs operated by FHA, the Department of Agriculture and the Veterans Administration to assist targeted groups of borrowers. The report does not state whether or how the existing infrastructure or human capital of Fannie Mae may be used in the establishment of such a reformed system. The report emphasizes the importance of proceeding with a careful transition plan and providing the necessary financial support to Fannie Mae and Freddie Mac during the transition period. A copy of the report can be found on the Housing Finance Reform section of Treasury's Web site, www.Treasury.gov. We are providing Treasury's Web site address solely for your information, and information appearing on Treasury's Web site is not incorporated into this quarterly report on Form 10-Q.

In February 2012, Treasury Secretary Geithner stated that the Administration intended to release new details around approaches to housing finance reform, including winding down Fannie Mae and Freddie Mac, and to work with congressional leaders to explore options for legislation, but that he does not expect housing finance reform legislation to be enacted in 2012. As of the date of this filing, no further details have been released.

In the current congressional session, Congress has held hearings on the future status of Fannie Mae and Freddie Mac, and members of Congress have offered legislative proposals relating to the future status of the GSEs. We expect Congress to continue considering this issue in the next congressional session that begins in 2013. We expect additional hearings on GSE reform and additional legislation to be considered and proposals to be discussed, including proposals that could result in a substantial change to our business structure or that involve Fannie Mae's liquidation or dissolution. Several bills have been introduced in the current congressional session that would place the GSEs into receivership after a period of time and either grant federal charters to new entities to engage in activities similar to those currently engaged in by the GSEs or leave secondary mortgage market activities to entities in the private sector. For example, legislation has been introduced in both the House of Representatives and the Senate that would require FHFA to make a determination within two years of enactment regarding whether the GSEs were financially viable and, if the GSEs were determined not to be financially viable, to place them into receivership. As drafted, these bills may, upon enactment, impair our ability to issue securities in the capital markets and therefore our ability to conduct our business, absent the federal government providing an explicit guarantee of our existing and future liabilities.

In addition to bills that seek to resolve the status of the GSEs, numerous bills have been introduced and considered in the current congressional session that could constrain the current operations of the GSEs or alter the existing authority that FHFA or Treasury has over the enterprises. For example, the Subcommittee on Capital Markets and Government

Sponsored Enterprises of the House Financial Services Committee has approved bills that would or could:

- suspend current compensation packages and apply a government pay scale for GSE employees;
- require the GSEs to increase guaranty fees;
- subject GSE loans to the risk retention standards in the Dodd-Frank Act;
- require a quicker reduction of GSE portfolios than required under the senior preferred stock purchase agreement;

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- require Treasury to pre-approve all GSE debt issuances;
- repeal the GSEs' affordable housing goals;
- provide additional authority to FHFA's Inspector General;
- prohibit FHFA from approving any new GSE products during conservatorship or receivership, with certain exceptions;
- prevent Treasury from amending the senior preferred stock purchase agreement to reduce the dividend rate on our senior preferred stock;
- abolish the Affordable Housing Trust Fund that the GSEs are required to fund except when such contributions have been temporarily suspended by FHFA;
- require FHFA to identify mission critical assets of the GSEs and require the GSEs to dispose of non-mission critical assets;
- cap the maximum aggregate amount of funds Treasury or any other agency or entity of the federal government can provide to the GSEs subject to certain qualifications;
- grant FHFA the authority to revoke the enterprises' charters following receivership under certain circumstances; and
- subject the GSEs to the Freedom of Information Act.

Of these bills that passed at a subcommittee level, the only one that has passed the full committee is the bill that would put GSE employees on a government pay scale. Unless these bills are enacted by the end of 2012, they would need to be reintroduced in the next congressional session that convenes in January 2013 in order to be considered again. We expect additional legislation relating to the GSEs to be introduced and considered by Congress. We cannot predict the prospects for the enactment, timing or content of legislative proposals concerning the future status of the GSEs, their regulation or operations.

In sum, there continues to be uncertainty regarding the future of our company, including how long the company will continue to exist in its current form, the extent of our role in the market, what form we will have, and what ownership interest, if any, our current common and preferred stockholders will hold in us after the conservatorship is terminated. See "Risk Factors" in our 2011 Form 10-K for a discussion of the risks to our business relating to the uncertain future of our company. Also see "Risk Factors" in this report for a discussion of how the uncertain future of our company may adversely affect our ability to retain and recruit well-qualified employees, including senior management.

The Dodd-Frank Act: Regulation of Swap Transactions

The Commodity Futures Trading Commission (the "CFTC") and the SEC issued a joint final rule in May 2012 that, among other items, established the definitions of "swap dealer," "security-based swap dealer," "major swap participant" and "major security-based swap participant" under the Dodd-Frank Act. Institutions that meet one of these definitions are required to register with either the CFTC or the SEC, as applicable, and are subject to significant additional regulations. In addition, in August 2012, the CFTC and SEC issued a joint final rule that, among other items, defines "swap" and "security-based swap."

We have reviewed these rules and determined that we are not a swap dealer, security-based swap dealer, major swap participant or major security-based swap participant for purposes of the Dodd-Frank Act. Accordingly, we do not need to register with the CFTC or the SEC. Although we do not need to register with the CFTC or the SEC, because we are a user of interest rate swaps, the Dodd-Frank Act requires us, among other items, to submit new swap transactions for clearing to a derivatives clearing organization. Additionally, the Federal Reserve Board, the Federal Deposit Insurance Corporation, FHFA, the Farm Credit Administration and the Office of the Comptroller of the Currency have proposed rules under the Dodd-Frank Act governing margin and capital requirements applicable to entities that are subject to their oversight. These proposed rules would require that, for all trades that have not been submitted to a derivatives clearing organization, we collect from our counterparties and provide to our counterparties collateral in excess of the amounts we have historically collected or provided.

Increase in Single-Family Guaranty Fee Pricing

In August 2012, FHFA directed us and Freddie Mac to increase our single-family guaranty fee prices by an average of 10 basis points. This increase was effective on November 1, 2012 for whole loan commitments and will be effective on December 1, 2012 for loans exchanged for Fannie Mae MBS. These changes to guaranty fee pricing represent a step toward encouraging greater participation in the mortgage market by private firms, which is one of the goals set

forth in FHFA’s strategic plan for the next phase of Fannie Mae’s and Freddie Mac’s conservatorships.

In addition to the fee increase described above, in September 2012, FHFA published a notice presenting an approach to adjust the guaranty fees that we and Freddie Mac charge on single-family mortgages in states where costs related to foreclosure practices are significantly higher than the national average. The approach outlined in FHFA's notice would be to charge a one-time upfront payment of between 15 and 30 basis points on each loan acquired in the following five states that have significantly higher default-related costs than the national average: Connecticut, Florida, Illinois, New Jersey and New York. FHFA's notice requests public input on this approach and potential future approaches to setting and adjusting state-level guaranty fees. FHFA's notice indicates that, after reviewing public input and determining a final state-level guaranty fee pricing method, it expects to direct us and Freddie Mac to implement these pricing adjustments in 2013.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expenses in the condensed consolidated financial statements. Understanding our accounting policies and the extent to which we use management judgment and estimates in applying these policies is integral to understanding our financial statements. We describe our most significant accounting policies in "Note 1, Summary of Significant Accounting Policies" in this report and in our 2011 Form 10-K.

We evaluate our critical accounting estimates and judgments required by our policies on an ongoing basis and update them as necessary based on changing conditions. Management has discussed any significant changes in judgments and assumptions in applying our critical accounting policies with the Audit Committee of our Board of Directors. We have identified three of our accounting policies as critical because they involve significant judgments and assumptions about highly complex and inherently uncertain matters, and the use of reasonably different estimates and assumptions could have a material impact on our reported results of operations or financial condition. These critical accounting policies and estimates are as follows:

- Fair Value Measurement
- Total Loss Reserves
- Other-Than-Temporary Impairment of Investment Securities

See "MD&A—Critical Accounting Policies and Estimates" in our 2011 Form 10-K for a detailed discussion of these critical accounting policies and estimates. We provide below information about our Level 3 assets and liabilities as of September 30, 2012 as compared with December 31, 2011. We also describe any significant changes in the judgments and assumptions we made during the first nine months of 2012 in applying our critical accounting policies and significant changes to critical estimates.

Fair Value Measurement

The use of fair value to measure our assets and liabilities is fundamental to our financial statements and our fair value measurement is a critical accounting estimate because we account for and record a portion of our assets and liabilities at fair value. In determining fair value, we use various valuation techniques. We describe the valuation techniques and inputs used to determine the fair value of our assets and liabilities and disclose their carrying value and fair value in "Note 12, Fair Value."

Fair Value Hierarchy—Level 3 Assets and Liabilities

The assets and liabilities that we have classified as Level 3 consist primarily of financial instruments for which there is limited market activity and therefore little or no price transparency. As a result, the valuation techniques that we use to estimate the fair value of Level 3 instruments involve significant unobservable inputs, which generally are more subjective and involve a high degree of management judgment and assumptions. Our Level 3 assets and liabilities consist of certain mortgage-backed securities and residual interests, certain mortgage loans, certain acquired property, certain long-term debt arrangements and certain highly structured, complex derivative instruments.

Table 4 presents a comparison of the amount of financial assets carried in our condensed consolidated balance sheets at fair value on a recurring basis ("recurring assets") that were classified as Level 3 as of September 30, 2012 and December 31, 2011. The availability of observable market inputs to measure fair value varies based on changes in market conditions, such as liquidity. As a result, we expect the amount of financial instruments carried at fair value on a recurring basis and classified as Level 3 to vary each period.

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Table 4: Level 3 Recurring Financial Assets at Fair Value

	As of September 30, 2012	December 31, 2011
	(Dollars in millions)	
Trading securities	$2,573	$4,238
Available-for-sale securities	25,840	29,492
Mortgage loans	2,416	2,319
Other assets	197	238
Level 3 recurring assets	$31,026	$36,287
Total assets	$3,226,250	$3,211,484
Total recurring assets measured at fair value	$120,617	$156,552
Level 3 recurring assets as a percentage of total assets	1 %	1 %
Level 3 recurring assets as a percentage of total recurring assets measured at fair value	26 %	23 %
Total recurring assets measured at fair value as a percentage of total assets	4 %	5 %

Assets measured at fair value on a nonrecurring basis and classified as Level 3, which are not presented in the table above, primarily include mortgage loans and acquired property. The fair value of Level 3 nonrecurring assets totaled $30.4 billion as of September 30, 2012.

Financial liabilities measured at fair value on a recurring basis and classified as Level 3 consisted of long-term debt with a fair value of $1.9 billion as of September 30, 2012 and $1.2 billion as of December 31, 2011, and other liabilities with a fair value of $167 million as of September 30, 2012 and $173 million as of December 31, 2011.

We updated our assumptions for prepayment speeds, severities and default rates during the third quarter of 2012, which resulted in an increase in the fair value of our loans of approximately $23 billion. These updates resulted in lower expectations of losses on certain loans, primarily performing loans with high LTV ratios.

Total Loss Reserves

Our total loss reserves consist of the following components:

- Allowance for loan losses;
- Allowance for accrued interest receivable;
- Reserve for guaranty losses; and
- Allowance for preforeclosure property tax and insurance receivable.

These components can be further divided into our single-family and multifamily loss reserves.

We continually monitor delinquency and default trends and periodically make changes in our historically developed assumptions to better reflect present conditions. In the third quarter of 2012, as described below, we enhanced our collective single-family loss reserve model and our model that calculates loss reserves for individually impaired loans. The combined impact from these changes resulted in an approximately $3.5 billion increase to our allowance for loan losses and provision for credit losses.

We enhanced our loan loss models for loans in our collective single-family loss reserve to reflect more recent experience of default expectations, including incorporating current credit bureau data, which provides additional information about the borrower’s ability to pay. The impact of this change had the most pronounced effect on loans with higher mark-to-market LTV ratios, where we have observed better than anticipated payment performance. The change resulted in an approximately $1.5 billion decrease to our allowance for loan losses and provision for credit losses.

We also enhanced our single-family loan loss models for individually impaired loans based on current observable trends of payment behavior on our modified loans to reflect slower prepayment and lower default expectations for these loans, which significantly extended the expected average life of our modified loans. Since a loan modification changes the contractual terms of a loan such that a concession is granted to the borrower, an extension of the average life of a modified loan increases the charge we record related to the concession. Therefore, while our expectations of credit loss decreased due to better performance of our modified loans, this decrease was more than offset by an

increase in the present value of the concession granted to the borrower by the modification. The change resulted in an approximately $5.0 billion increase to our allowance for loan losses and provision for credit losses.

Other-Than-Temporary Impairment of Investment Securities

We evaluate available-for-sale securities in an unrealized loss position as of the end of each quarter for other-than-temporary impairment. Our evaluation requires significant management judgment and consideration of various factors to determine if we will receive the amortized cost basis of our investment securities. We evaluate a debt security for other-than-temporary impairment using an econometric model that estimates the present value of cash flows given multiple factors. These factors include: the severity and duration of the impairment; recent events specific to the issuer and/or industry to which the issuer belongs; the payment structure of the security; external credit ratings and the failure of the issuer to make scheduled interest or principal payments. We rely on expected future cash flow projections to determine if we will recover the amortized cost basis of our available-for-sale securities.

In the second quarter of 2012, we updated our assumptions used to project cash flow estimates on our Alt-A and subprime private-label securities to incorporate observable market trends, which included extending the time it takes to liquidate loans underlying these securities and increasing severity rates for loans where the servicer stopped advancing payments. These updates resulted in lower net present value of cash flow projections on our Alt-A and subprime securities and increased our other-than-temporary impairment expense by approximately $500 million. We provide more detailed information on our accounting for other-than-temporary impairment in "Note 5, Investments in Securities."

CONSOLIDATED RESULTS OF OPERATIONS

This section provides a discussion of our condensed consolidated results of operations for the periods indicated and should be read together with our condensed consolidated financial statements, including the accompanying notes. Table 5 displays a summary of our condensed consolidated results of operations for the periods indicated.

Table 5: Summary of Condensed Consolidated Results of Operations

	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2012	2011	Variance	2012	2011	Variance
	(Dollars in millions)					
Net interest income	$5,317	$5,186	$131	$15,942	$15,118	$824
Fee and other income	378	291	87	1,148	793	355
Net revenues	$5,695	$5,477	$218	$17,090	$15,911	$1,179
Investment gains, net	134	73	61	381	319	62
Net other-than-temporary impairments	(38)	(262)	224	(701)	(362)	(339)
Fair value losses, net	(1,020)	(4,525)	3,505	(3,186)	(5,870)	2,684
Administrative expenses	(588)	(591)	3	(1,719)	(1,765)	46
Credit-related expenses						
Provision for credit losses	(2,079)	(4,151)	2,072	(1,038)	(21,242)	20,204
Foreclosed property income (expense)	48	(733)	781	(221)	(743)	522
Total credit-related expenses	(2,031)	(4,884)	2,853	(1,259)	(21,985)	20,726
Other non-interest expenses[1]	(339)	(373)	34	(956)	(787)	(169)
Income (loss) before federal income taxes	1,813	(5,085)	6,898	9,650	(14,539)	24,189
Benefit for federal income taxes	—	—	—	—	91	(91)
Net income (loss)	1,813	(5,085)	6,898	9,650	(14,448)	24,098
Less: Net loss (income) attributable to the noncontrolling interest	8	—	8	4	(1)	5
Net income (loss) attributable to Fannie Mae	$1,821	$(5,085)	$6,906	$9,654	$(14,449)	$24,103
Total comprehensive income (loss) attributable to Fannie Mae	$2,567	$(5,282)	$7,849	$11,090	$(14,463)	$25,553

[1] Consists of debt extinguishment losses, net and other expenses.

Net Interest Income

Table 6 displays an analysis of our net interest income, average balances, and related yields earned on assets and incurred on liabilities for the periods indicated. For most components of the average balances, we use a daily weighted average of amortized cost. When daily average balance information is not available, such as for mortgage loans, we use monthly averages. Table 7 displays the change in our net interest income between periods and the extent to which that variance is attributable to: (1) changes in the volume of our interest-earning assets and interest-bearing liabilities or (2) changes in the interest rates of these assets and liabilities.

Table 6: Analysis of Net Interest Income and Yield

	For the Three Months Ended September 30,					
	2012			2011		
	Average Balance	Interest Income/ Expense	Average Rates Earned/Paid	Average Balance	Interest Income/ Expense	Average Rates Earned/Paid
	(Dollars in millions)					
Interest-earning assets:						
Mortgage loans of Fannie Mae	$366,836	$3,536	3.86 %	$386,067	$3,701	3.83 %
Mortgage loans of consolidated trusts	2,627,408	27,057	4.12	2,598,264	30,633	4.72
Total mortgage loans	2,994,244	30,593	4.09	2,984,331	34,334	4.60
Mortgage-related securities	263,333	3,085	4.69	312,482	3,930	5.03
Elimination of Fannie Mae MBS held in portfolio	(171,205)	(2,075)	4.85	(199,691)	(2,520)	5.05
Total mortgage-related securities, net	92,128	1,010	4.39	112,791	1,410	5.00
Non-mortgage securities[1]	42,922	13	0.12	72,333	24	0.13
Federal funds sold and securities purchased under agreements to resell or similar arrangements	40,565	19	0.18	27,217	7	0.10
Advances to lenders	7,178	34	1.85	3,417	19	2.18
Total interest-earning assets	$3,177,037	$31,669	3.99 %	$3,200,089	$35,794	4.47 %
Interest-bearing liabilities:						
Short-term debt[2]	$93,186	$37	0.16 %	$181,495	$63	0.14 %
Long-term debt	559,968	2,919	2.09	552,191	3,385	2.45
Total short-term and long-term funding debt	653,154	2,956	1.81	733,686	3,448	1.88
Debt securities of consolidated trusts	2,707,451	25,471	3.76	2,650,256	29,680	4.48
Elimination of Fannie Mae MBS held in portfolio	(171,205)	(2,075)	4.85	(199,691)	(2,520)	5.05
Total debt securities of consolidated trusts held by third parties	2,536,246	23,396	3.69	2,450,565	27,160	4.43
Total interest-bearing liabilities	$3,189,400	$26,352	3.30 %	$3,184,251	$30,608	3.84 %
Net interest income/net interest yield		$5,317	0.67 %		$5,186	0.65 %
Net interest income/net interest yield of consolidated trusts[3]		$1,586	0.24 %		$953	0.15 %

	For the Nine Months Ended September 30,							
	2012				2011			
	Average Balance	Interest Income/ Expense	Average Rates Earned/Paid		Average Balance	Interest Income/ Expense	Average Rates Earned/Paid	
	(Dollars in millions)							
Interest-earning assets:								
Mortgage loans of Fannie Mae	$372,916	$10,704	3.83	%	$395,686	$11,146	3.76	%
Mortgage loans of consolidated trusts	2,613,196	84,482	4.31		2,601,710	94,111	4.82	
Total mortgage loans	2,986,112	95,186	4.25		2,997,396	105,257	4.68	
Mortgage-related securities	275,456	9,809	4.75		321,979	12,204	5.05	
Elimination of Fannie Mae MBS held in portfolio	(178,218)	(6,558)	4.91		(206,176)	(7,956)	5.15	
Total mortgage-related securities, net	97,238	3,251	4.46		115,803	4,248	4.89	
Non-mortgage securities[1]	55,391	56	0.13		76,266	99	0.17	
Federal funds sold and securities purchased under agreements to resell or similar arrangements	33,349	42	0.17		20,980	20	0.13	
Advances to lenders	5,959	89	1.96		3,548	59	2.19	
Total interest-earning assets	$3,178,049	$98,624	4.14	%	$3,213,993	$109,683	4.55	%
Interest-bearing liabilities:								
Short-term debt[2]	$105,393	$108	0.13	%	$160,961	$246	0.20	%
Long-term debt	569,112	9,101	2.13		591,126	11,383	2.57	
Total short-term and long-term funding debt	674,505	9,209	1.82		752,087	11,629	2.06	
Debt securities of consolidated trusts	2,685,408	80,031	3.97		2,652,057	90,892	4.57	
Elimination of Fannie Mae MBS held in portfolio	(178,218)	(6,558)	4.91		(206,176)	(7,956)	5.15	
Total debt securities of consolidated trusts held by third parties	2,507,190	73,473	3.91		2,445,881	82,936	4.52	
Total interest-bearing liabilities	$3,181,695	$82,682	3.46	%	$3,197,968	$94,565	3.94	%
Net interest income/net interest yield		$15,942	0.67	%		$15,118	0.63	%
Net interest income/net interest yield of consolidated trusts[3]		$4,451	0.23	%		$3,219	0.16	%

	As of September 30,			
	2012		2011	
Selected benchmark interest rates[4]				
3-month LIBOR	0.36	%	0.37	%
2-year swap rate	0.37		0.58	
5-year swap rate	0.76		1.26	
30-year Fannie Mae MBS par coupon rate	1.84		2.96	

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(1) Includes cash equivalents.

(2) Includes federal funds purchased and securities sold under agreements to repurchase.

(3) Net interest income of consolidated trusts represents interest income from mortgage loans of consolidated trusts less interest expense from debt securities of consolidated trusts. Net interest yield is calculated based on net interest income from consolidated trusts divided by average balance of mortgage loans of consolidated trusts.

(4) Data from British Bankers' Association, Thomson Reuters Indices and Bloomberg L.P.

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Table 7: Rate/Volume Analysis of Changes in Net Interest Income

	For the Three Months Ended September 30, 2012 vs. 2011			For the Nine Months Ended September 30, 2012 vs. 2011		
	Total	Variance Due to:[1]		Total	Variance Due to:[1]	
	Variance	Volume	Rate	Variance	Volume	Rate
	(Dollars in millions)					
Interest income:						
Mortgage loans of Fannie Mae	$(165)	$(185)	$20	$(442)	$(651)	$209
Mortgage loans of consolidated trusts	(3,576)	340	(3,916)	(9,629)	414	(10,043)
Total mortgage loans	(3,741)	155	(3,896)	(10,071)	(237)	(9,834)
Mortgage-related securities	(845)	(589)	(256)	(2,395)	(1,688)	(707)
Elimination of Fannie Mae MBS held in portfolio	445	348	97	1,398	1,042	356
Total mortgage-related securities, net	(400)	(241)	(159)	(997)	(646)	(351)
Non-mortgage securities[2]	(11)	(9)	(2)	(43)	(24)	(19)
Federal funds sold and securities purchased under agreements to resell or similar arrangements	12	4	8	22	14	8
Advances to lenders	15	18	(3)	30	37	(7)
Total interest income	(4,125)	(73)	(4,052)	(11,059)	(856)	(10,203)
Interest expense:						
Short-term debt [3]	(26)	(34)	8	(138)	(71)	(67)
Long-term debt	(466)	47	(513)	(2,282)	(411)	(1,871)
Total short-term and long-term funding debt	(492)	13	(505)	(2,420)	(482)	(1,938)
Debt securities of consolidated trusts	(4,209)	628	(4,837)	(10,861)	1,130	(11,991)
Elimination of Fannie Mae MBS held in portfolio	445	348	97	1,398	1,042	356
Total debt securities of consolidated trusts held by third parties	(3,764)	976	(4,740)	(9,463)	2,172	(11,635)
Total interest expense	(4,256)	989	(5,245)	(11,883)	1,690	(13,573)
Net interest income	$131	$(1,062)	$1,193	$824	$(2,546)	$3,370

[1] Combined rate/volume variances are allocated to both rate and volume based on the relative size of each variance.
[2] Includes cash equivalents.
[3] Includes federal funds purchased and securities sold under agreements to repurchase.

Although our portfolio balance declined, net interest income increased in the third quarter and first nine months of 2012, compared with the third quarter and first nine months of 2011, primarily due to lower interest expense on funding debt, a reduction in the amount of interest income not recognized for nonaccrual mortgage loans and accelerated net amortization income on loans and debt of consolidated trusts. These factors were partially offset by lower interest income on Fannie Mae mortgage loans and securities. The primary drivers of these changes were:

- lower interest expense on funding debt due to lower borrowing rates and lower funding needs, which allowed us to continue to replace higher-cost debt with lower-cost debt;
- higher coupon interest income recognized on mortgage loans due to a reduction in the amount of interest income not recognized for nonaccrual mortgage loans. The balance of nonaccrual loans in our condensed consolidated balance sheet declined as we continued to complete a high number of loan workouts and foreclosures, and fewer loans became seriously delinquent;
- accelerated net amortization income related to mortgage loans and debt of consolidated trusts driven by a high volume of prepayments due to declining interest rates;
-

lower interest income on Fannie Mae mortgage loans due to a decrease in average balance and new business acquisitions which continued to replace higher-yielding loans with loans issued at lower mortgage rates; and

- lower interest income on mortgage securities due to lower interest rates and a decrease in the balance of our mortgage securities, as we continue to manage our portfolio requirements of the senior preferred stock purchase agreement.

Additionally, our net interest income and net interest yield were higher than they would have otherwise been because our debt funding needs were lower than would otherwise have been required because of the funds we have received from Treasury to date under the senior preferred stock purchase agreement and because dividends paid to Treasury are not recognized as interest expense.

Table 8 displays the interest income not recognized for loans on nonaccrual status and the resulting reduction in our net interest yield on total interest earning assets for the periods indicated.

Table 8: Impact of Nonaccrual Loans on Net Interest Income

	For the Three Months Ended September 30,				For the Nine Months Ended September 30,			
	2012		2011		2012		2011	
	Interest Income not Recognized for Nonaccrual Loans[1]	Reduction in Net Interest Yield[2]	Interest Income not Recognized for Nonaccrual Loans[1]	Reduction in Net Interest Yield[2]	Interest Income not Recognized for Nonaccrual Loans[1]	Reduction in Net Interest Yield[2]	Interest Income not Recognized for Nonaccrual Loans[1]	Reduction in Net Interest Yield[2]
	(Dollars in millions)							
Mortgage loans of Fannie Mae	$ (856)		$ (1,078)		$ (2,734)		$ (3,623)	
Mortgage loans of consolidated trusts	(137)		(212)		(464)		(690)	
Total mortgage loans	$ (993)	(12) bp	$ (1,290)	(16) bp	$ (3,198)	(13) bp	$ (4,313)	(18) bp

(1) Amount includes cash received for loans on nonaccrual status.

(2) Calculated based on annualized interest income not recognized divided by total interest-earning assets, expressed in basis points.

For a discussion of the interest income from the assets we have purchased and the interest expense from the debt we have issued, see the discussion of our Capital Markets group's net interest income in "Business Segment Results."

Other-Than-Temporary Impairment of Investment Securities

Net other-than-temporary impairments for the third quarter of 2012 decreased compared with the third quarter of 2011, primarily due to an increase in the net present value of projected cash flows on our Alt-A and subprime private-label securities resulting from improved home prices, as well as a tightening of credit spreads.

The increase in net other-than-temporary impairments for the first nine months of 2012 compared with the first nine months of 2011 was primarily driven by an update to the assumptions used to project cash flow estimates on our Alt-A and subprime securities in the second quarter of 2012. For additional information, see "Critical Accounting Policies and Estimates—Other-Than-Temporary Impairment of Investment Securities."

Fair Value Losses, Net

Table 9 displays the components of our fair value gains and losses.

Table 9: Fair Value Losses, Net

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
	(Dollars in millions)			
Risk management derivatives fair value losses attributable to:				
Net contractual interest expense accruals on interest rate swaps	$(369)	$(497)	$(1,134)	$(1,790)
Net change in fair value during the period	(139)	(3,570)	(1,016)	(3,777)
Total risk management derivatives fair value losses, net	(508)	(4,067)	(2,150)	(5,567)
Mortgage commitment derivatives fair value losses, net	(816)	(188)	(1,583)	(226)
Total derivatives fair value losses, net	(1,324)	(4,255)	(3,733)	(5,793)
Trading securities gains (losses), net	406	(214)	676	146
Other, net[1]	(102)	(56)	(129)	(223)
Fair value losses, net	$(1,020)	$(4,525)	$(3,186)	$(5,870)

	2012	2011
5-year swap rate:		
As of January 1	1.22 %	2.18 %
As of March 31	1.27	2.47
As of June 30	0.97	2.03
As of September 30	0.76	1.26

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(1) Consists of debt fair value gains (losses), net; debt foreign exchange gains (losses), net; and mortgage loans fair value gains (losses), net.

We can expect high levels of period-to-period volatility in our results of operations and financial condition due to changes in market conditions that result in periodic fluctuations in the estimated fair value of financial instruments that we mark to market through our earnings. These instruments include trading securities and derivatives. The estimated fair value of our trading securities and derivatives may fluctuate substantially from period to period because of changes in interest rates, credit spreads and interest rate volatility, as well as activity related to these financial instruments. While the estimated fair value of our derivatives may fluctuate, some of the financial instruments that the derivatives hedge are not recorded at fair value in our condensed consolidated financial statements.

Risk Management Derivatives Fair Value Losses, Net

Risk management derivative instruments are an integral part of our interest rate risk management strategy. We supplement our issuance of debt securities with derivative instruments to further reduce duration risk, which includes prepayment risk. We recognized risk management derivative fair value losses in the third quarter and first nine months of 2012 and 2011 primarily as a result of a decrease in the fair value of our pay-fixed derivatives due to a decline in swap rates during these periods. Risk management derivative fair value losses in the third quarter and first nine months of 2011 were greater than the losses in the third quarter and first nine months of 2012, primarily due to a significant decline in swap rates in the third quarter and first nine months of 2011 compared with a more modest decline in swap rates in the third quarter and first nine months of 2012.

We present, by derivative instrument type, the fair value gains and losses on our derivatives for the three and nine months ended September 30, 2012 and 2011 in "Note 9, Derivative Instruments."

Mortgage Commitment Derivatives Fair Value Losses, Net

We recognized fair value losses on our mortgage commitments in the third quarter and first nine months of 2012 and 2011 primarily due to losses on commitments to sell mortgage-related securities as a result of an increase in prices as interest rates decreased during the commitment period. Mortgage commitment derivative fair value losses in the third quarter and first nine months of 2012 were greater than the losses in the third quarter and first nine months of 2011,

primarily as a result of (1) a higher volume of net commitments to sell mortgage-related securities in the third quarter and first nine months of 2012, and

(2) a further increase in prices driven by the Federal Reserve's announcement that it would increase its MBS purchases from financial institutions beginning in September 2012.

Trading Securities Gains (Losses), Net

Gains from our trading securities in the third quarter and first nine months of 2012 were primarily driven by the narrowing of credit spreads on commercial mortgage-backed securities ("CMBS").

Losses from our trading securities in the third quarter of 2011 were primarily driven by the widening of credit spreads on CMBS. However, these credit spreads narrowed over the first nine months of 2011, which primarily drove gains on trading securities for the nine-month period.

Credit-Related Expenses

We refer to our provision for loan losses and guaranty losses collectively as our "provision for credit losses." Credit-related expenses consist of our provision for credit losses and foreclosed property (income) expense.

Provision for Credit Losses

Our total loss reserves provide for an estimate of credit losses incurred in our guaranty book of business, including concessions we granted borrowers upon modification of their loans, as of each balance sheet date. We establish our loss reserves through our provision for credit losses for losses that we believe have been incurred and will eventually be reflected over time in our charge-offs. When we determine that a loan is uncollectible, typically upon foreclosure, we record a charge-off against our loss reserves. We record recoveries of previously charged-off amounts as a reduction to charge-offs.

Table 10 displays the components of our total loss reserves and our total fair value losses previously recognized on loans purchased out of unconsolidated MBS trusts reflected in our condensed consolidated balance sheets. Because these fair value losses lowered our recorded loan balances, we have fewer inherent losses in our guaranty book of business and consequently require lower total loss reserves. For these reasons, we consider these fair value losses as an "effective reserve," apart from our total loss reserves, to the extent that we expect to realize these amounts as credit losses on the acquired loans in the future. As of September 30, 2012, we estimate that nearly two-thirds of this amount represents credit losses we expect to realize in the future and over one-third will eventually be recovered, either through net interest income for loans that cure or through foreclosed property income for loans where the sale of the collateral exceeds our recorded investment in the loan. We exclude these fair value losses from our credit loss calculation as described in "Credit Loss Performance Metrics."

Table 10: Total Loss Reserves

	As of September 30, 2012	December 31, 2011
	(Dollars in millions)	
Allowance for loan losses	$63,012	$72,156
Reserve for guaranty losses[1]	1,295	994
Combined loss reserves	64,307	73,150
Allowance for accrued interest receivable	1,832	2,496
Allowance for preforeclosure property taxes and insurance receivable[2]	769	1,292
Total loss reserves	66,908	76,938
Fair value losses previously recognized on acquired credit-impaired loans[3]	14,304	16,273
Total loss reserves and fair value losses previously recognized on acquired credit-impaired loans	$81,212	$93,211

(1) Amount included in "Other liabilities" in our condensed consolidated balance sheets.

(2) Amount included in "Other assets" in our condensed consolidated balance sheets.

(3) Represents the fair value losses on loans purchased out of unconsolidated MBS trusts reflected in our condensed consolidated balance sheets.

The following table displays changes in the total allowance for loan losses, reserve for guaranty losses and the total combined loss reserves for the three and nine months ended September 30, 2012 and 2011.

Table 11: Allowance for Loan Losses and Reserve for Guaranty Losses (Combined Loss Reserves)

	For the Three Months Ended September 30,					
	2012			2011		
	Of Fannie Mae	Of Consolidated Trusts	Total	Of Fannie Mae	Of Consolidated Trusts	Total
	(Dollars in millions)					
Changes in combined loss reserves:						
Allowance for loan losses:						
Beginning balance	$52,082	$11,293	$63,375	$55,966	$13,540	$69,506
Provision (benefit) for loan losses	3,029	(946)	2,083	(196)	4,355	4,159
Charge-offs[1][2]	(3,309)	(232)	(3,541)	(3,853)	(260)	(4,113)
Recoveries	323	27	350	848	35	883
Transfers[3]	1,378	(1,378)	—	1,770	(1,770)	—
Other[4]	711	34	745	863	137	1,000
Ending balance[5]	$54,214	$8,798	$63,012	$55,398	$16,037	$71,435
Reserve for guaranty losses:						
Beginning balance	$1,320	$—	$1,320	$960	$—	$960
Benefit for guaranty losses	(4)	—	(4)	(8)	—	(8)
Charge-offs	(32)	—	(32)	(38)	—	(38)
Recoveries	11	—	11	2	—	2
Ending balance	$1,295	$—	$1,295	$916	$—	$916
Combined loss reserves:						
Beginning balance	$53,402	$11,293	$64,695	$56,926	$13,540	$70,466
Total provision (benefit) for credit losses	3,025	(946)	2,079	(204)	4,355	4,151
Charge-offs[1][2]	(3,341)	(232)	(3,573)	(3,891)	(260)	(4,151)
Recoveries	334	27	361	850	35	885
Transfers[3]	1,378	(1,378)	—	1,770	(1,770)	—
Other[4]	711	34	745	863	137	1,000
Ending balance[5]	$55,509	$8,798	$64,307	$56,314	$16,037	$72,351

	For the Nine Months Ended September 30,					
	2012			2011		
	Of Fannie Mae	Of Consolidated Trusts	Total	Of Fannie Mae	Of Consolidated Trusts	Total
	(Dollars in millions)					
Changes in combined loss reserves:						
Allowance for loan losses:						
Beginning balance	$57,309	$ 14,847	$72,156	$48,530	$13,026	$61,556
Provision (benefit) for loan losses	1,083	(407)	676	10,003	10,545	20,548
Charge-offs[1][2]	(11,625)	(703)	(12,328)	(15,018)	(1,466)	(16,484)
Recoveries	1,185	136	1,321	3,197	1,537	4,734
Transfers[3]	5,195	(5,195)	—	7,739	(7,739)	—
Other[4]	1,067	120	1,187	947	134	1,081
Ending balance[5]	$54,214	$ 8,798	$63,012	$55,398	$16,037	$71,435
Reserve for guaranty losses:						
Beginning balance	$994	$—	$994	$323	$—	$323
Provision for guaranty losses	362	—	362	694	—	694
Charge-offs	(132)	—	(132)	(106)	—	(106)
Recoveries	71	—	71	5	—	5
Ending balance	$1,295	$—	$1,295	$916	$—	$916
Combined loss reserves:						
Beginning balance	$58,303	$ 14,847	$73,150	$48,853	$13,026	$61,879
Total provision (benefit) for credit losses	1,445	(407)	1,038	10,697	10,545	21,242
Charge-offs[1][2]	(11,757)	(703)	(12,460)	(15,124)	(1,466)	(16,590)
Recoveries	1,256	136	1,392	3,202	1,537	4,739
Transfers[3]	5,195	(5,195)	—	7,739	(7,739)	—
Other[4]	1,067	120	1,187	947	134	1,081
Ending balance[5]	$55,509	$ 8,798	$64,307	$56,314	$16,037	$72,351

	As of September 30, 2012	December 31, 2011
Allocation of combined loss reserves:		
Balance at end of each period attributable to:		
Single-family	$63,100	$71,512
Multifamily	1,207	1,638
Total	$64,307	$73,150
Single-family and multifamily combined loss reserves as a percentage of applicable guaranty book of business:		
Single-family	2.22 %	2.52 %
Multifamily	0.60	0.84
Combined loss reserves as a percentage of:		
Total guaranty book of business	2.11 %	2.41 %
Recorded investment in nonperforming loans	25.38	29.03

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(1) Includes accrued interest of $198 million and $289 million for the three months ended September 30, 2012 and 2011, respectively, and $709 million and $1.1 billion for the nine months ended September 30, 2012 and 2011, respectively.

(2) While we purchase the substantial majority of loans that are four or more months delinquent from our MBS trusts, we do not exercise this option to purchase loans during a forbearance period. Accordingly, charge-offs of consolidated trusts generally represent loans that remained in our consolidated trusts at the time of default.

(3) Includes transfers from trusts for delinquent loan purchases.

(4) Amounts represent the net activity recorded in our allowances for accrued interest receivable and preforeclosure property taxes and insurance receivable from borrowers. The provision for credit losses, charge-offs, recoveries and transfer activity included in this table reflects all changes for both the allowance for loan losses and the valuation allowances for accrued interest and preforeclosure property taxes and insurance receivable that relate to the mortgage loans.

(5) Includes $376 million and $334 million as of September 30, 2012 and 2011, respectively, for acquired credit-impaired loans.

Our provision for credit losses continues to be a key driver of our results for each period presented. The amount of our provision for credit losses varies from period to period based on changes in actual and expected home prices, borrower payment behavior, the types and volumes of loss mitigation activities and foreclosures completed, and actual and estimated recoveries from our lender and mortgage insurer counterparties. See "Risk Management—Credit Risk Management—Institutional Counterparty Credit Risk Management" for information on mortgage insurers and outstanding mortgage seller/servicer repurchase obligations. In addition, our provision for credit losses and our loss reserves can be impacted by updates to our allowance for loan loss models that we use to estimate our loss reserves.

The decrease in our provision for credit losses in the third quarter of 2012 compared with the third quarter of 2011 was primarily due to a decrease in our total loss reserves driven by an improvement in the profile of our single-family book of business resulting primarily from an increase in actual and expected home prices, including the sales prices of our REO properties throughout 2012. Home prices increased by 1.5% in the third quarter of 2012 compared with a 0.9% decline in the third quarter of 2011 and increased by 4.8% in the first nine months of 2012 compared with a 1.7% decrease in the first nine months of 2011. Higher home prices decrease the likelihood that loans will default and reduce the amount of credit loss on loans that do default. In addition, sales prices on dispositions of our REO properties improved in the third quarter of 2012 as a result of strong demand compared to both the second quarter of 2012 and the prior year. We received net proceeds from our REO sales equal to 61% of the loans' unpaid principal balance in the third quarter of 2012, compared with 59% in the second quarter of 2012 and 54% in the third quarter of 2011. The increase in sales proceeds reduces the amount of credit loss at foreclosure and, accordingly, results in a lower provision for credit loss.

The positive impact of higher home prices and higher REO sales values on our provision for credit losses in the third quarter of 2012 was partially offset by a $3.5 billion increase in our provision for credit losses due to changes in our assumptions and data used in calculating our loss reserves. For additional information on the impact from changes in our assumptions used in calculating our loss reserves in the third quarter of 2012, see "Critical Accounting Policies and Estimates—Total Loss Reserves."

In addition, our provision for credit losses in the third quarter of 2012 was negatively impacted by a change in our accounting for loans to certain borrowers who have received bankruptcy relief, which led to an increase in the number of loans we classify as TDRs. A TDR is a loan restructuring that grants a concession to a borrower experiencing financial difficulties. In the third quarter of 2012, we began classifying loans as TDRs where the borrower used the bankruptcy process to receive a discharge of the mortgage debt or to cure a mortgage delinquency over time. We determined that the discharge of mortgage debt in bankruptcy was a concession in cases in which the discharge effectively resulted in us losing our ability to hold the borrower personally liable for deficiencies under state law, although we continue to be able to foreclose on the collateral. We also determined that curing a mortgage delinquency over time through bankruptcy resulted in a concession similar to other long-term repayment plans. The increase in TDRs as a result of this change resulted in an increase in our provision for credit losses of approximately

$1.1 billion.

We continue to experience high volumes of loan modifications involving concessions to borrowers, which are considered TDRs. Individual impairment for a TDR is based on the restructured loan's expected cash flows over the life of the loan, taking into account the effect of any concessions granted to the borrower, discounted at the loan's original effective interest rate. If we expect to recover our recorded investment in an individually impaired loan through probable foreclosure of the underlying collateral, we measure the impairment based on the fair value of the collateral, less selling cost. The allowance calculated for an individually impaired loan has generally been greater than the allowance that would be calculated under the collective reserve.

The significant decrease in our provision for credit losses in the first nine months of 2012 compared with the first nine months of 2011 was primarily due to an increase in actual and expected home prices in 2012.

In April 2012, FHFA issued an Advisory Bulletin that could have an impact on our provision for credit losses in the future; however, we are still assessing the impact of the Advisory Bulletin. See "Legislative and Regulatory Developments—FHFA Advisory Bulletin Regarding Framework for Adversely Classifying Loans" in our Second Quarter 2012 Form 10-Q for additional information.

We discuss our expectations regarding our future credit-related expenses and loss reserves in "Executive Summary—Summary of Our Financial Performance for the Third Quarter and First Nine Months of 2012—Our Expectations Regarding Future Loss Reserves and Credit-Related Expenses."

Nonperforming Loans

Our balance of nonperforming single-family loans remained high as of September 30, 2012 due to both high levels of delinquencies and an increase in TDRs. The increase in TDRs as of September 30, 2012 compared with December 31, 2011 resulted from our classification, beginning in the third quarter of 2012, of loans to certain borrowers who have received bankruptcy relief as TDRs.

When a TDR occurs, the loan may return to a current status, but it will continue to be classified as a nonperforming loan as the loan is not performing in accordance with its original terms. Table 12 displays the composition of our nonperforming loans, which includes our single-family and multifamily held-for-investment and held-for-sale mortgage loans. For information on the impact of TDRs and other individually impaired loans on our allowance for loan losses, see "Note 3, Mortgage Loans."

Table 12: Nonperforming Single-Family and Multifamily Loans

	As of	
	September 30, 2012	December 31, 2011
	(Dollars in millions)	
On-balance sheet nonperforming loans including loans in consolidated Fannie Mae MBS trusts:		
Nonaccrual loans	$ 122,602	$ 142,998
Troubled debt restructurings on accrual status[1][2]	130,760	108,797
Total on-balance sheet nonperforming loans	253,362	251,795
Off-balance sheet nonperforming loans in unconsolidated Fannie Mae MBS trusts[3]	72	154
Total nonperforming loans	253,434	251,949
Allowance for loan losses and allowance for accrued interest receivable related to individually impaired on-balance sheet nonperforming loans	(49,385)	(47,711)
Total nonperforming loans, net of allowance	$ 204,049	$ 204,238
Accruing on-balance sheet loans past due 90 days or more[4]	$ 831	$ 768

	For the Nine Months Ended	
	September 30,	
	2012	2011
	(Dollars in millions)	
Interest related to on-balance sheet nonperforming loans:		
Interest income forgone[5]	$ 6,108	$ 6,475
Interest income recognized for the period[6]	4,659	4,760

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(1) Includes HomeSaver Advance first-lien loans on accrual status.

(2) As of September 30, 2012, we classified $12.7 billion of loans on accrual status as TDRs where certain borrowers have received bankruptcy relief.

(3) Represents loans that would meet our criteria for nonaccrual status if the loans had been on-balance sheet.

(4) Recorded investment in loans that, as of the end of each period, are 90 days or more past due and continuing to accrue interest. The majority of this amount consists of loans insured or guaranteed by the U.S. government and loans for which we have recourse against the seller in the event of a default.

(5) Represents the amount of interest income we did not record but would have recorded during the period for on-balance sheet nonperforming loans as of the end of each period had the loans performed according to their original contractual terms.

(6) Represents interest income recognized during the period for on-balance sheet loans classified as nonperforming as of the end of each period. Includes primarily amounts accrued while the loans were performing and cash payments received on nonaccrual loans.

Foreclosed Property (Income) Expense

The decrease in foreclosed property expense in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 was primarily due to improved sales prices on dispositions of our REO properties, resulting from strong demand in markets with limited REO supply. In addition, foreclosed property expense in the third quarter and first nine months of 2011 was negatively impacted by a decrease in the estimated recovery amount due to us from mortgage insurers.

Credit Loss Performance Metrics

Our credit-related expenses should be considered in conjunction with our credit loss performance metrics. Our credit loss performance metrics, however, are not defined terms within GAAP and may not be calculated in the same manner as similarly titled measures reported by other companies. Because management does not view changes in the fair value of our mortgage loans as credit losses, we adjust our credit loss performance metrics for the impact associated with our acquisition of credit-impaired loans from unconsolidated MBS trusts. We also exclude interest forgone on nonperforming loans in our mortgage portfolio, other-than-temporary impairment losses resulting from deterioration in the credit quality of our mortgage-related securities and accretion of interest income on acquired credit-impaired loans from credit losses. We believe that credit loss performance metrics may be useful to investors as the losses are presented as a percentage of our book of business and have historically been used by analysts, investors and other companies within the financial services industry. Moreover, by presenting credit losses with and without the effect of fair value losses associated with the acquisition of credit-impaired loans, investors are able to evaluate our credit performance on a more consistent basis among periods. Table 13 displays the components of our credit loss performance metrics as well as our average single-family and multifamily default rates and initial charge-off severity rates.

Table 13: Credit Loss Performance Metrics

	For the Three Months Ended September 30,				For the Nine Months Ended September 30,			
	2012		2011		2012		2011	
	Amount	Ratio[1]	Amount	Ratio[1]	Amount	Ratio[1]	Amount	Ratio[1]
	(Dollars in millions)							
Charge-offs, net of recoveries	$3,212	42.2 bp	$3,266	42.8 bp	$11,068	48.5 bp	$11,851	51.6 bp
Foreclosed property (income) expense	(48)	(0.6)	733	9.6	221	1.0	743	3.2
Credit losses including the effect of fair value losses on acquired credit-impaired loans	3,164	41.6	3,999	52.4	11,289	49.5	12,594	54.8
Plus: Impact of acquired credit-impaired loans on charge-offs and foreclosed property expense[2]	348	4.6	461	6.1	1,142	5.0	1,484	6.5
Credit losses and credit loss ratio	$3,512	46.2 bp	$4,460	58.5 bp	$12,431	54.5 bp	$14,078	61.3 bp
Credit losses attributable to:								
Single-family	$3,485		$4,384		$12,218		$13,798	
Multifamily	27		76		213		280	
Total	$3,512		$4,460		$12,431		$14,078	
Single-family default rate		0.38 %		0.44 %		1.20 %		1.34 %
Single-family initial charge-off severity rate [3]		29.83 %		34.20 %		31.36 %		35.00 %
Average multifamily default rate		0.05 %		0.08 %		0.30 %		0.38 %
Average multifamily initial charge-off severity rate [3]		28.31 %		32.49 %		37.03 %		35.40 %

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(1) Basis points are based on the annualized amount for each line item presented divided by the average guaranty book of business during the period.

(2) Includes fair value losses from acquired credit-impaired loans.

(3) Single-family and multifamily rates exclude fair value losses on credit-impaired loans acquired from MBS trusts and any costs, gains or losses associated with REO after initial acquisition through final disposition; single-family rate excludes charge-offs from short sales.

Credit losses decreased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 primarily due to: (1) improved actual home prices and sales prices of our REO properties resulting from strong demand in markets with limited REO supply; and (2) lower volume of REO acquisitions due to the slow pace of foreclosures. The decrease in credit losses was partially offset by a decrease in amounts collected by us as a result of repurchase requests in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011.We expect our credit losses to remain high in 2012 relative to pre-housing crisis levels. We expect delays in foreclosures to continue for the remainder of 2012, which delays our realization of credit losses.

Our new single-family book of business accounted for approximately 6% of our single-family credit losses for the third quarter of 2012 and 4% of these losses for the first nine months of 2012. Credit losses on mortgage loans typically do not peak until the third through sixth years following origination; however, this range can vary based on many factors, including changes in macroeconomic conditions and foreclosure timelines. We provide more detailed credit performance information, including serious delinquency rates by geographic region and foreclosure activity, in “Risk Management—Credit Risk Management—Mortgage Credit Risk Management.”

Regulatory Hypothetical Stress Test Scenario

Under a September 2005 agreement with FHFA’s predecessor, the Office of Federal Housing Enterprise Oversight, we are required to disclose on a quarterly basis the present value of the change in future expected credit losses from our existing single-family guaranty book of business from an immediate 5% decline in single-family home prices for the entire United States followed by a return to the average of the possible growth rate paths used in our internal credit pricing models. The sensitivity results represent the difference between future expected credit losses under our base case scenario, which is derived from our internal home price path forecast, and a scenario that assumes an instantaneous nationwide 5% decline in home prices.

Table 14 displays the credit loss sensitivities as of the dates indicated for first-lien single-family loans that are in our portfolio or underlying Fannie Mae MBS, before and after consideration of projected credit risk sharing proceeds, such as private mortgage insurance claims and other credit enhancements.

Table 14: Single-Family Credit Loss Sensitivity[1]

	As of	
	September 30, 2012	December 31, 2011
	(Dollars in millions)	
Gross single-family credit loss sensitivity	$14,201	$21,922
Less: Projected credit risk sharing proceeds	(1,137)	(1,690)
Net single-family credit loss sensitivity	$13,064	$20,232
Single-family loans in our portfolio and loans underlying Fannie Mae MBS	$2,774,803	$2,769,454
Single-family net credit loss sensitivity as a percentage of outstanding single-family loans in our portfolio and Fannie Mae MBS	0.47 %	0.73 %

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(1) Represents total economic credit losses, which consist of credit losses and forgone interest. Calculations are based on 98% and 97% of our total single-family guaranty book of business as of September 30, 2012 and December 31, 2011, respectively. The mortgage loans and mortgage-related securities that are included in these estimates consist of: (a) single-family Fannie Mae MBS (whether held in our mortgage portfolio or held by third parties), excluding certain whole loan REMICs and private-label wraps; (b) single-family mortgage loans, excluding mortgages secured only by second liens, subprime mortgages, manufactured housing chattel loans and reverse mortgages; and (c) long-term standby commitments. We expect the inclusion in our estimates of the excluded products may impact the estimated sensitivities set forth in this table.

Because these sensitivities represent hypothetical scenarios, they should be used with caution. Our regulatory stress test scenario is limited in that it assumes an instantaneous uniform 5% nationwide decline in home prices, which is not representative of the historical pattern of changes in home prices. Changes in home prices generally vary on a regional, as well as a local, basis. In addition, these stress test scenarios are calculated independently without considering changes in other interrelated assumptions, such as unemployment rates or other economic factors, which are likely to have a significant impact on our future expected credit losses.

BUSINESS SEGMENT RESULTS

Results of our three business segments are intended to reflect each segment as if it were a stand-alone business. Under our segment reporting structure, the sum of the results for our three business segments does not equal our condensed consolidated results of operations as we separate the activity related to our consolidated trusts from the results generated by our three segments. In addition, because we apply accounting methods that differ from our condensed consolidated results for segment reporting purposes, we include an eliminations/adjustments category to reconcile our business segment results and the activity related to our consolidated trusts to our condensed consolidated results of operations. We describe the management reporting and allocation process used to generate our segment results in our 2011 Form 10-K in "Notes to Consolidated Financial Statements—Note 14, Segment Reporting." We are working on reorganizing our company by function rather than by business in order to improve our operational efficiencies and effectiveness. In future periods, we may change some of our management reporting and how we report our business segment results.

In this section, we summarize our segment results for the third quarter and first nine months of 2012 and 2011 in the tables below and provide a comparative discussion of these results. This section should be read together with our comparative discussion of our condensed consolidated results of operations in "Consolidated Results of Operations." See "Note 10, Segment Reporting" for a reconciliation of our segment results to our condensed consolidated results.

Single-Family Business Results

Table 15 displays the financial results of our Single-Family business for the periods indicated. For a discussion on Single-Family credit risk management, including information on serious delinquency rates and loan workouts, see "Risk Management—Credit Risk Management—Single-Family Mortgage Credit Risk Management." The primary source of revenue for our Single-Family business is guaranty fee income. Expenses and other items that impact income or loss primarily include credit-related expenses, net interest loss and administrative expenses.

Table 15: Single-Family Business Results

	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2012	2011	Variance	2012	2011	Variance
	(Dollars in millions)					
Net interest loss[1]	$(192)	$(374)	$182	$(786)	$(1,952)	$1,166
Guaranty fee income[2][3]	2,014	1,867	147	5,895	5,618	277
Credit-related expenses[4]	(2,130)	(4,782)	2,652	(1,500)	(21,821)	20,321
Other expenses[3][5]	(502)	(456)	(46)	(1,333)	(1,414)	81
(Loss) income before federal income taxes	(810)	(3,745)	2,935	2,276	(19,569)	21,845
(Provision) benefit for federal income taxes	(12)	(1)	(11)	(12)	106	(118)
Net (loss) income attributable to Fannie Mae	$(822)	$(3,746)	$2,924	$2,264	$(19,463)	$21,727
Single-family effective guaranty fee rate (in basis points)[3][6]	28.3	26.1		27.6	26.1	
Single-family average charged guaranty fee on new acquisitions (in basis points)[3][7]	41.8	31.1		37.1	29.0	
Average single-family guaranty book of business[8]	$2,842,649	$2,859,814		$2,846,328	$2,870,557	
Single-family Fannie Mae MBS issuances[9]	$229,671	$111,808		$601,469	$381,135	

(1) Primarily includes: (1) the cost to reimburse the Capital Markets group for interest income not recognized for loans in our mortgage portfolio on nonaccrual status; (2) the cost to reimburse MBS trusts for interest income not recognized for loans in consolidated trusts on nonaccrual status; and (3) income from cash payments received on loans that have been placed on nonaccrual status.

(2) Guaranty fee income is included in fee and other income in our condensed consolidated statements of operations and comprehensive income (loss).

(3) Pursuant to the TCCA, effective April 1, 2012, we increased the guaranty fee on all single-family residential mortgages delivered to us on or after that date for securitization by 10 basis points, and the incremental revenue must be remitted to Treasury. The resulting revenue is included in guaranty fee income and the expense is included in other expenses. This increase in guaranty fee is also included in the single-family charged guaranty fee.

(4) Consists of the provision for credit losses and foreclosed property income (expense).

(5) Consists of investment gains (losses), net, fair value losses, net, fee and other income, administrative expenses and other expenses.

(6) Calculated based on annualized Single-Family segment guaranty fee income divided by the average single-family guaranty book of business, expressed in basis points.

(7) Calculated based on the average contractual fee rate for our single-family guaranty arrangements entered into during the period plus the recognition of any upfront cash payments ratably over an estimated average life, expressed in basis points.

(8) Consists of single-family mortgage loans held in our mortgage portfolio, single-family mortgage loans held by consolidated trusts, single-family Fannie Mae MBS issued from unconsolidated trusts held by either third parties or within our retained portfolio, and other credit enhancements that we provide on single-family mortgage assets. Excludes non-Fannie Mae mortgage-related securities held in our investment portfolio for which we do not provide a guaranty.

(9) Reflects unpaid principal balance of Fannie Mae MBS issued and guaranteed by the Single-Family segment during the period.

Single-family business results reflected a decrease in net loss in the third quarter of 2012 compared with the third quarter of 2011, and net income in the first nine months of 2012 compared with a net loss in the first nine months of 2011, primarily due to a decrease in credit-related expenses. In addition, net interest loss decreased and guaranty fee income increased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011.

Single-family credit-related expenses represent the substantial majority of our consolidated activity. We provide a discussion of our credit-related expenses and credit losses in "Consolidated Results of Operations—Credit-Related Expenses."

The decrease in net interest loss in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 was primarily due to a reduction in the amount of interest income not recognized for nonaccrual mortgage loans in our condensed consolidated balance sheet as we continued to complete a high number of loan workouts and foreclosures. In addition, as loans with stronger credit profiles become a larger portion of our single-family guaranty book of business, a smaller percentage of our loans are becoming seriously delinquent.

Guaranty fee income increased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 due to an increase in the amortization of risk-based fees. Additionally, as described in "Business—Legislative and Regulatory Developments—Changes to Our Single-Family Guaranty Fee Pricing" in our 2011 Form 10-K, in December 2011, Congress enacted the TCCA which, among other provisions, requires that we increase our single-family guaranty fees by at least 10 basis points and remit this increase to Treasury, rather than retaining the incremental revenue. Effective April 1, 2012, the guaranty fee on all single-family residential mortgages delivered to Fannie Mae and Freddie Mac on or after that date for securitization was increased by 10 basis points; accordingly, the Single-Family average charged guaranty fee increased. The resulting revenue is included in guaranty fee income, and the expense is included in other expenses. We recorded other expenses of $78 million for the third quarter of 2012 and $104 million for the first nine months of 2012 for this obligation due to Treasury.

Our estimated market share of new single-family mortgage-related securities issuances, which excludes previously securitized mortgages, remained high at 52% for the third quarter of 2012 and 50% for the first nine months of 2012. Despite our continued high market share, our average single-family guaranty book of business was flat in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011, primarily due to the decline in U.S. residential mortgage debt outstanding.

Multifamily Business Results

Multifamily business results primarily reflect our multifamily guaranty business. Our multifamily business results also include activity relating to our low-income housing tax credit ("LIHTC") and equity investments. Although we are no longer making new LIHTC or equity investments, we continue to make contractually required contributions for our legacy investments. Activity from multifamily products is also reflected in the Capital Markets group results, which include net interest income related to multifamily loans and securities, gains and losses from the sale of multifamily Fannie Mae MBS and re-securitizations, and other miscellaneous income. Estimated net interest income earned on multifamily mortgage loans and multifamily Fannie Mae MBS in the Capital Markets group results was $212 million for the third quarter of 2012 compared with $210 million for the third quarter of 2011 and $631 million for the first nine months of 2012 compared with $662 million for the first nine months of 2011.

Table 16 displays the financial results of our Multifamily business for the periods indicated. The primary sources of revenue for our multifamily business are guaranty fee income and fee and other income. Expenses and other items that impact income or loss primarily include credit-related income (expenses) and administrative expenses.

Table 16: Multifamily Business Results

	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2012	2011	Variance	2012	2011	Variance
	(Dollars in millions)					
Guaranty fee income[1]	$265	$226	$39	$760	$651	$109
Fee and other income	55	51	4	151	166	(15)
Gains (losses) from partnership investments[2]	43	(30)	73	72	(8)	80
Credit-related income (expenses)[3]	99	(102)	201	241	(164)	405
Other expenses[4]	(67)	(73)	6	(192)	(178)	(14)
Income before federal income taxes	395	72	323	1,032	467	565
Benefit (provision) for federal income taxes	32	—	32	32	(61)	93
Net income attributable to Fannie Mae	$427	$72	$355	$1,064	$406	$658
Multifamily effective guaranty fee rate (in basis points)[5]	52.9	47.0		51.1	45.4	
Multifamily credit loss performance ratio (in basis points)[6]	5.4	15.8		14.3	19.5	
Average multifamily guaranty book of business[7]	$200,384	$192,357		$198,201	$191,185	
Multifamily new business volumes[8]	$8,965	$6,500		$22,862	$16,963	
Multifamily units financed from new business volumes	135,000	110,000		371,000	289,000	
Multifamily Fannie Mae MBS issuances[9]	$9,576	$7,756		$25,969	$24,466	
Multifamily Fannie Mae structured securities issuances (issued by Capital Markets group)[10]	$4,038	$1,495		$7,462	$4,517	
Additional net interest income earned on Fannie Mae multifamily mortgage loans and MBS (included in Capital Markets Group's results)[11]	$212	$210		$631	$662	
Average Fannie Mae multifamily mortgage loans and MBS in Capital Markets Group's portfolio[12]	$97,186	$109,608		$100,636	$112,092	

	As of September 30, 2012	December 31, 2011
	(Dollars in millions)	
Multifamily serious delinquency rate	0.28 %	0.59 %
Percentage of multifamily guaranty book of business with credit enhancement	90 %	90 %
Fannie Mae percentage of total multifamily mortgage debt outstanding[13]	21.5 %	21.1 %
Multifamily Fannie Mae MBS outstanding[14]	$120,171	$101,574

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(1) Guaranty fee income is included in fee and other income in our condensed consolidated statements of operations and comprehensive income (loss).

(2) Gains (losses) from partnership investments are included in other expenses in our condensed consolidated statements of operations and comprehensive income (loss). Gains (losses) from partnership investments are reported using the equity method of accounting. As a result, net income attributable to noncontrolling interest from partnership investments is not included in income for the Multifamily segment.

(3) Consists of the benefit (provision) for credit losses and foreclosed property income (expense).

(4) Consists of net interest loss, investment gains, administrative expenses, and other (expenses) income.

(5) Calculated based on annualized Multifamily segment guaranty fee income divided by the average multifamily guaranty book of business, expressed in basis points.

(6) Calculated based on the annualized Multifamily credit losses divided by the average multifamily guaranty book of business, expressed in basis points.

(7) Consists of multifamily mortgage loans held in our mortgage portfolio, multifamily mortgage loans held by consolidated trusts, multifamily Fannie Mae MBS issued from unconsolidated trusts held by either third parties or within our retained portfolio, and other credit enhancements that we provide on multifamily mortgage assets. Excludes non-Fannie Mae mortgage-related securities held in our investment portfolio for which we do not provide a guaranty.

(8) Reflects unpaid principal balance of multifamily Fannie Mae MBS issued (excluding portfolio securitizations) and multifamily loans purchased during the period.

(9) Reflects unpaid principal balance of multifamily Fannie Mae MBS issued during the period. Includes: (a) issuances of new MBS, (b) Fannie Mae portfolio securitization transactions of $1.1 billion and $1.3 billion for the three months ended September 30, 2012 and 2011, respectively, and $3.4 billion and $7.6 billion for the nine months ended September 30, 2012 and 2011, respectively, and (c) conversions of adjustable-rate loans to fixed-rate loans and discount MBS ("DMBS") to MBS of $18 million and $69 million for the three months ended September 30, 2012 and 2011, respectively, and $208 million and $188 million for the nine months ended September 30, 2012 and 2011, respectively.

(10) Reflects original unpaid principal balance of out-of-portfolio multifamily structured securities issuances by our Capital Markets Group.

(11) Interest expense estimate is based on allocated duration-matched funding costs. Net interest income was reduced by guaranty fees allocated to Multifamily from the Capital Markets Group on multifamily loans in Fannie Mae's portfolio.

(12) Based on unpaid principal balance.

(13) Includes mortgage loans and Fannie Mae MBS issued and guaranteed by the Multifamily segment. Information labeled as of September 30, 2012 is as of June 30, 2012 and is based on the Federal Reserve's June 2012 mortgage debt outstanding release, the latest date for which the Federal Reserve has estimated mortgage debt outstanding for multifamily residences. Prior period amounts have been changed to reflect revised historical data from the Federal Reserve.

(14) Includes $27.4 billion and $28.3 billion of Fannie Mae multifamily MBS held in the mortgage portfolio, the vast majority of which have been consolidated to loans in our condensed consolidated balance sheets, as of September 30, 2012 and December 31, 2011, respectively, and $1.3 billion and $1.4 billion of bonds issued by state and local housing finance agencies as of September 30, 2012 and December 31, 2011, respectively.

Multifamily business results reflected an increase in net income in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011, primarily due to credit-related income in the third quarter and first nine months of 2012 compared with credit-related expenses in the third quarter and first nine months of 2011. Credit-related income in the third quarter and first nine months of 2012 was primarily due to reductions to our total loss reserves resulting from an improvement in national multifamily market fundamentals. In comparison, multifamily credit-related expenses in the third quarter and first nine months of 2011 were primarily due to underperformance of certain local markets and properties due to localized economic conditions. Multifamily credit losses, which consist of net charge-offs and foreclosed property expense, were $27 million for the third quarter of 2012 compared with $76 million for the third quarter of 2011, and $213 million for the first nine months of 2012 compared with $280 million for the first nine months of 2011.

Guaranty fee income increased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 as we continue to acquire loans with higher guaranty fees. Our acquisitions of loans with higher guaranty fees have become a larger part of our multifamily guaranty book of business, while loans with lower guaranty fees continue to liquidate.

We recognized gains from partnership investments in the third quarter and first nine months of 2012 compared with losses from partnership investments in the third quarter and first nine months of 2011 as stronger national multifamily market fundamentals resulted in improved property-level operating performance and increased gains on the sale of investments.

A benefit for federal income taxes of $32 million in the third quarter and first nine months of 2012 was driven by the utilization of tax credits related to LIHTC investments to offset our alternative minimum tax liability resulting from

our projected 2012 taxable income. In comparison, a provision for federal income taxes was recognized in the second quarter of 2011, resulting from an effective settlement of issues with the Internal Revenue Service relating to tax years 2007 and 2008, which reduced our total corporate tax liability. However, the reduction in our tax liability also reduced the tax credits we were able to use, resulting in a provision for federal income taxes for the Multifamily segment in the first nine months of 2011. There was no provision for federal income taxes recognized in the third quarter of 2011.

Capital Markets Group Results

Table 17 displays the financial results of our Capital Markets group for the periods indicated. Following the table we discuss the Capital Markets group's financial results and describe the Capital Markets group's mortgage portfolio. For a discussion of the debt issued by the Capital Markets group to fund its investment activities, see "Liquidity and Capital Management." For a discussion of the derivative instruments that the Capital Markets group uses to manage interest rate risk, see "Consolidated Balance Sheet Analysis—Derivative Instruments" and "Risk Management—Market Risk Management, Including Interest Rate Risk Management—Derivative Instruments" in our 2011 Form 10-K and "Notes to Consolidated Financial Statements—Note 9, Derivative Instruments" in both this report and our 2011 Form 10-K. The primary sources of revenue for our Capital Markets group are net interest income and fee and other income. Expenses and other items that impact income or loss primarily include fair value gains and losses, investment gains and losses, other-than-temporary impairments, allocated guaranty fee expense and administrative expenses.

Table 17: Capital Markets Group Results

	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2012	2011	Variance	2012	2011	Variance
	(Dollars in millions)					
Net interest income [1]	$3,247	$3,904	$(657)	$10,231	$11,481	$(1,250)
Investment gains, net[2]	2,201	801	1,400	4,666	2,589	2,077
Net other-than-temporary impairments	(38)	(262)	224	(699)	(361)	(338)
Fair value losses, net[3]	(961)	(4,670)	3,709	(3,252)	(5,959)	2,707
Fee and other income	185	125	60	551	309	242
Other expenses[4]	(492)	(610)	118	(1,578)	(1,723)	145
Income (loss) before federal income taxes	4,142	(712)	4,854	9,919	6,336	3,583
(Provision) benefit for federal income taxes	(20)	1	(21)	(20)	46	(66)
Net income (loss) attributable to Fannie Mae	$4,122	$(711)	$4,833	$9,899	$6,382	$3,517

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(1) Includes contractual interest income, excluding recoveries, on nonaccrual loans received from the Single-Family segment of $1.3 billion and $1.6 billion for the three months ended September 30, 2012 and 2011, respectively, and $4.0 billion and $5.1 billion for the nine months ended September 30, 2012 and 2011, respectively. The Capital Markets group's net interest income is reported based on the mortgage-related assets held in the segment's portfolio and excludes interest income on mortgage-related assets held by consolidated MBS trusts that are owned by third parties and the interest expense on the corresponding debt of such trusts.

(2) We include the securities that we own regardless of whether the trust has been consolidated in reporting of gains and losses on securitizations and sales of available-for-sale securities.

(3) Includes fair value gains or losses on derivatives and trading securities that we own, regardless of whether the trust has been consolidated.

(4) Includes allocated guaranty fee expense, debt extinguishment losses, net, administrative expenses, and other expenses. Gains or losses related to the extinguishment of debt issued by consolidated trusts are excluded from the Capital Markets group's results because purchases of securities are recognized as such.

The Capital Markets group's results reflected net income in the third quarter of 2012 compared with a net loss in the third quarter of 2011, primarily due to a decrease in fair value losses and net-other-than-temporary impairments and an increase in investment gains, partially offset by a decrease in net interest income. The Capital Markets group's results reflected an increase in net income in the first nine months of 2012 compared with the first nine months of 2011, primarily due to a decrease in fair value losses and an increase in investment gains, partially offset by a decrease in net interest income and an increase in net other-than-temporary impairments.

Fair value losses decreased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 primarily due to a decrease in risk management derivatives fair value losses. The derivatives fair value losses that are reported for the Capital Markets group are consistent with the losses reported in our condensed consolidated statement of operations and comprehensive income (loss). We discuss our derivatives fair value losses in "Consolidated Results of Operations—Fair Value Losses, Net."

The net other-than-temporary impairments recognized by the Capital Markets group during the third quarter and first nine months of 2012 are consistent with our condensed consolidated statement of operations and comprehensive income (loss) as described in "Consolidated Results of Operations—Other-Than-Temporary Impairment of Investment Securities." In addition, see "Note 5, Investments in Securities" for information on our other-than-temporary impairments by major security type and primary drivers for other-than-temporary impairments recorded in the third quarter and first nine months of 2012.

Net interest income decreased in the third quarter and first nine months of 2012 primarily due to a decrease in the balance of mortgage-related securities and lower interest rates on loans in our mortgage portfolio. This decrease in interest income on our interest-earning assets was partially offset by a decline in interest expense due to lower funding needs and lower borrowing rates, which allowed us to continue to replace higher-cost debt with lower-cost debt.

Our net interest income and net interest yield were higher than they would have otherwise been because our debt funding needs were lower than would otherwise have been required because of the funds we have received from Treasury to date under the senior preferred stock purchase agreement and because dividends paid to Treasury are not recognized as interest expense.

We supplement our issuance of debt securities with derivative instruments to further reduce duration risk, which includes prepayment risk. The effect of these derivatives, in particular the periodic net interest expense accruals on interest rate swaps, is not reflected in the Capital Markets group's net interest income but is included in our results as a component of "Fair value losses, net" and is displayed in "Table 9: Fair Value Losses, Net." If we had included the economic impact of adding the net contractual interest accruals on our interest rate swaps in our Capital Markets group's interest expense, the Capital Markets group's net interest income would have decreased by $369 million in the third quarter of 2012 compared with a decrease of $497 million in the third quarter of 2011, and would have decreased by $1.1 billion for the first nine months of 2012 compared with a decrease of $1.8 billion for the first nine months of 2011.

Investment gains increased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011 due to a higher volume of securitizations.

The Capital Markets Group's Mortgage Portfolio

The Capital Markets group's mortgage portfolio consists of mortgage loans and mortgage-related securities that we own. Mortgage-related securities held by the Capital Markets group include Fannie Mae MBS and non-Fannie Mae mortgage-related securities. The Fannie Mae MBS that we own are maintained as securities on the Capital Markets group's balance sheet. Mortgage-related assets held by consolidated MBS trusts are not included in the Capital Markets group's mortgage portfolio.

The amount of mortgage assets that we may own is restricted by our senior preferred stock purchase agreement with Treasury. Under the agreement, the maximum allowable amount of mortgage assets we may own as of December 31, 2012 is $650 billion. Beginning in 2013, by December 31 of each year, we are required to reduce our mortgage assets to 85% of the maximum allowable amount that we were permitted to own as of December 31 of the immediately preceding calendar year, until the amount of our mortgage assets reaches $250 billion. As of September 30, 2012, we owned $654.3 billion in mortgage assets, compared with $708.4 billion as of December 31, 2011. The terms of the senior preferred stock purchase agreement were amended on August 17, 2012 and the amended terms are described in "Executive Summary—Amendment to Senior Preferred Stock Purchase Agreement with Treasury."

Table 18 displays our Capital Markets group's mortgage portfolio activity for the periods indicated.

Table 18: Capital Markets Group's Mortgage Portfolio Activity[1]

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
	(Dollars in millions)			
Mortgage loans:				
Beginning balance	$386,804	$405,417	$398,271	$427,074
Purchases	71,946	36,169	181,631	102,533
Securitizations [2]	(59,661)	(18,420)	(142,554)	(64,962)
Liquidations [3]	(19,493)	(19,361)	(57,752)	(60,840)
Mortgage loans, ending balance	379,596	403,805	379,596	403,805
Mortgage securities:				
Beginning balance	285,982	326,384	310,143	361,697
Purchases [4]	6,959	5,964	17,450	15,587
Securitizations [2]	59,661	18,420	142,554	64,962
Sales	(61,836)	(17,936)	(148,331)	(74,997)
Liquidations [3]	(16,093)	(14,479)	(47,143)	(48,896)
Mortgage securities, ending balance	274,673	318,353	274,673	318,353
Total Capital Markets mortgage portfolio	$654,269	$722,158	$654,269	$722,158

[1] Based on unpaid principal balance.
[2] Includes portfolio securitization transactions that do not qualify for sale treatment under GAAP.
[3] Includes scheduled repayments, prepayments, foreclosures and lender repurchases.
[4] Includes purchases of Fannie Mae MBS issued by consolidated trusts.

Table 19 displays the composition of the Capital Markets group's mortgage portfolio as of September 30, 2012 and December 31, 2011.

Table 19: Capital Markets Group's Mortgage Portfolio Composition[1]

	As of September 30, 2012	December 31, 2011
	(Dollars in millions)	
Capital Markets group's mortgage loans:		
Single-family loans:		
Government insured or guaranteed	$41,066	$41,555
Conventional:		
Long-term, fixed-rate	242,887	245,810
Intermediate-term, fixed-rate	10,630	10,289
Adjustable-rate	19,230	23,490
Total single-family conventional	272,747	279,589
Total single-family loans	313,813	321,144
Multifamily loans:		
Government insured or guaranteed	324	362
Conventional:		
Long-term, fixed-rate	3,423	3,629
Intermediate-term, fixed-rate	49,890	58,885
Adjustable-rate	12,146	14,251
Total multifamily conventional	65,459	76,765
Total multifamily loans	65,783	77,127
Total Capital Markets group's mortgage loans	379,596	398,271
Capital Markets group's mortgage-related securities:		
Fannie Mae	194,252	220,061
Freddie Mac	12,020	14,509
Ginnie Mae	931	1,043
Alt-A private-label securities	17,740	19,670
Subprime private-label securities	15,437	16,538
CMBS	21,055	23,226
Mortgage revenue bonds	9,319	10,899
Other mortgage-related securities	3,919	4,197
Total Capital Markets group's mortgage-related securities[2]	274,673	310,143
Total Capital Markets group's mortgage portfolio	$654,269	$708,414

(1) Based on unpaid principal balance.

(2) The fair value of these mortgage-related securities was $284.1 billion and $316.5 billion as of September 30, 2012 and December 31, 2011, respectively.

The Capital Markets group's mortgage portfolio decreased as of September 30, 2012 compared with December 31, 2011 primarily due to liquidations, partially offset by purchases of delinquent loans from MBS trusts. The total unpaid principal balance of nonperforming loans in the Capital Markets group's mortgage portfolio was $232.8 billion as of September 30, 2012 and $236.2 billion as of December 31, 2011. This population includes loans that have been modified and have been classified as TDRs, as well as unmodified delinquent loans that are on nonaccrual status in our condensed consolidated financial statements.

We expect to continue to purchase loans from MBS trusts as they become four or more consecutive monthly payments delinquent subject to market conditions, economic benefit, servicer capacity, and other factors including the limit on the mortgage assets that we may own pursuant to the senior preferred stock purchase agreement. We purchased approximately 215,600 delinquent loans with an unpaid principal balance of $35.9 billion from our single-family MBS trusts in the first nine months of 2012. As of September 30, 2012, the total unpaid principal balance of all loans in single-family MBS trusts that were delinquent for four or more consecutive monthly payments was $3.9 billion.

CONSOLIDATED BALANCE SHEET ANALYSIS

This section provides a discussion of our condensed consolidated balance sheets as of the dates indicated and should be read together with our condensed consolidated financial statements, including the accompanying notes.

Table 20 displays a summary of our condensed consolidated balance sheets as of September 30, 2012 and December 31, 2011.

Table 20: Summary of Condensed Consolidated Balance Sheets

	As of September 30, 2012	December 31, 2011	Variance
	(Dollars in millions)		
Assets			
Cash and cash equivalents and federal funds sold and securities purchased under agreements to resell or similar arrangements	$66,174	$63,539	$2,635
Restricted cash	59,944	50,797	9,147
Investments in securities[1]	108,874	151,780	(42,906)
Mortgage loans:			
Of Fannie Mae	363,459	380,379	(16,920)
Of consolidated trusts	2,642,449	2,590,398	52,051
Allowance for loan losses	(63,012)	(72,156)	9,144
Mortgage loans, net of allowance for loan losses	2,942,896	2,898,621	44,275
Other assets[2]	48,362	46,747	1,615
Total assets	$3,226,250	$3,211,484	$14,766
Liabilities and equity (deficit)			
Debt:			
Of Fannie Mae	$652,971	$732,444	$(79,473)
Of consolidated trusts	2,543,739	2,457,428	86,311
Other liabilities[3]	27,128	26,183	945
Total liabilities	3,223,838	3,216,055	7,783
Senior preferred stock	117,149	112,578	4,571
Other deficit[4]	(114,737)	(117,149)	2,412
Total equity (deficit)	2,412	(4,571)	6,983
Total liabilities and equity (deficit)	$3,226,250	$3,211,484	$14,766

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(1) Includes $19.9 billion as of September 30, 2012 and $49.8 billion as of December 31, 2011 of non-mortgage-related securities that are included in our other investments portfolio, which we present in "Table 30: Cash and Other Investments Portfolio."

(2) Consists of accrued interest receivable, net; acquired property, net; and other assets.

(3) Consists of accrued interest payable and other liabilities.

(4) Consists of preferred stock, common stock, accumulated deficit, accumulated other comprehensive income (loss), treasury stock, and noncontrolling interest.

Cash and Other Investments Portfolio

Our cash and other investments portfolio consists of cash and cash equivalents, federal funds sold and securities purchased under agreements to resell or similar arrangements, and investments in non-mortgage-related securities. See "Liquidity and Capital Management—Liquidity Management—Cash and Other Investments Portfolio" for additional information on our cash and other investments portfolio.

Restricted Cash

Restricted cash primarily includes unscheduled borrower payments received by the servicer or consolidated trusts due to be remitted to the MBS certificateholders in the subsequent month. Our restricted cash increased as of September 30, 2012 compared with the balance as of December 31, 2011 primarily due to an increase in refinance activity, resulting in an increase in unscheduled payments received.

Investments in Mortgage-Related Securities

Our investments in mortgage-related securities are classified in our condensed consolidated balance sheets as either trading or available-for-sale and are measured at fair value. Unrealized and realized gains and losses on trading securities are included as a component of "Fair value losses, net" and unrealized gains and losses on available-for-sale securities are included in "Other comprehensive income (loss)" in our condensed consolidated statements of operations and comprehensive income (loss). Realized gains and losses on available-for-sale securities are recognized when securities are sold in "Investment gains, net" in our condensed consolidated statements of operations and comprehensive income (loss). See "Note 5, Investments in Securities" for additional information on our investments in mortgage-related securities, including the composition of our trading and available-for-sale securities at amortized cost and fair value and the gross unrealized gains and losses related to our available-for-sale securities as of September 30, 2012 and December 31, 2011.

Table 21 displays the fair value of our investments in mortgage-related securities, including trading and available-for-sale securities, as of the dates indicated.

Table 21: Summary of Mortgage-Related Securities at Fair Value

	As of September 30, 2012	As of December 31, 2011
	(Dollars in millions)	
Mortgage-related securities:		
Fannie Mae	$17,815	$24,274
Freddie Mac	13,030	15,555
Ginnie Mae	1,072	1,189
Alt-A private-label securities	12,504	13,032
Subprime private-label securities	8,637	8,866
CMBS	23,241	24,437
Mortgage revenue bonds	9,354	10,978
Other mortgage-related securities	3,324	3,601
Total	$88,977	$101,932

Investments in Private-Label Mortgage-Related Securities

We classify private-label securities as Alt-A, subprime, multifamily or manufactured housing if the securities were labeled as such when issued. We have also invested in private-label subprime mortgage-related securities that we have resecuritized to include our guaranty ("wraps").

Although the current economic environment has started to show signs of improvement, weakness in the housing market and high unemployment over the past several years have adversely affected the performance of our Alt-A and subprime private-label securities. The unpaid principal balance of our investments in Alt-A and subprime securities was $33.2 billion as of September 30, 2012, of which $29.1 billion was rated below investment grade. Table 22 displays the unpaid principal balance and the fair value of our investments in Alt-A and subprime private-label securities along with an analysis of the cumulative losses on these investments as of September 30, 2012. We realized actual cumulative principal shortfalls of approximately 8% as of September 30, 2012 and 6% as of December 31, 2011 of the total cumulative credit losses reported in this table and reflected in our condensed consolidated financial statements.

Table 22: Analysis of Losses on Alt-A and Subprime Private-Label Mortgage-Related Securities

	As of September 30, 2012				
	Unpaid Principal Balance	Fair Value	Total Cumulative Losses[1]	Noncredit Component[2]	Credit Component[3]
	(Dollars in millions)				
Trading securities:[4]					
Alt-A private-label securities	$2,420	$1,276	$(1,105)	$66	$(1,171)
Subprime private-label securities	2,477	1,265	(1,213)	(305)	(908)
Total	4,897	2,541	(2,318)	(239)	(2,079)
Available-for-sale securities:[4]					
Alt-A private-label securities	15,320	11,228	(4,829)	(540)	(4,289)
Subprime private-label securities	12,960	7,372	(5,627)	(1,030)	(4,597)
Total	28,280	18,600	(10,456)	(1,570)	(8,886)
Grand Total	$33,177	$21,141	$(12,774)	$(1,809)	$(10,965)

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(1) Amounts reflect the difference between the fair value and unpaid principal balance net of unamortized premiums, discounts and certain other cost basis adjustments.

(2) We have calculated the credit component based on the difference between the amortized cost basis of the securities and the present value of expected future cash flows. The remaining difference between the fair value and the present value of expected future cash flows is classified as a noncredit component of any change in fair value.

(3) For securities classified as trading, amounts reflect the estimated portion of the total cumulative losses that is credit-related. For securities classified as available-for-sale, amounts reflect the estimated portion of total cumulative other-than-temporary credit impairment losses, net of accretion, that are recognized in our condensed consolidated statements of operations and comprehensive income (loss).

(4) Excludes resecuritizations, or wraps, of private-label securities backed by subprime loans that we have guaranteed and hold in our mortgage portfolio as Fannie Mae securities.

Table 23 displays the 60 days or more delinquency rates and average loss severities for the loans underlying our Alt-A and subprime private-label mortgage-related securities for the most recent remittance period of the current reporting quarter. The delinquency rates and average loss severities are based on available data provided by Intex Solutions, Inc. ("Intex") and CoreLogic, LoanPerformance ("CoreLogic"). We also present the average credit enhancement and monoline financial guaranteed amount for these securities as of September 30, 2012. Based on the stressed condition of our non-governmental financial guarantors, we believe that all but one of these counterparties may not be able to fully meet their obligations to us in the future. See "Risk Management—Credit Risk Management—Institutional Counterparty Credit Risk Management—Financial Guarantors" in this report and in our 2011 Form 10-K for additional information on our financial guarantor exposure and the counterparty risk associated with our financial guarantors.

Table 23: Credit Statistics of Loans Underlying Alt-A and Subprime Private-Label Mortgage-Related Securities (Including Wraps)

	As of September 30, 2012						
	Unpaid Principal Balance				Average		Monoline Financial Guaranteed
		Available-		≥ 60 Days	Loss	Average Credit	
	Trading	for-Sale	Wraps[1]	Delinquent[2][3]	Severity[3][4]	Enhancement[3][5]	Amount[6]
	(Dollars in millions)						
Private-label mortgage-related securities backed by: [7]							
Alt-A mortgage loans:							
Option ARM Alt-A mortgage loans:							
2004 and prior	$—	$448	$—	28.6 %	49.5 %	12.5 %	$—
2005	—	1,203	—	37.8	61.2	33.8	216
2006	—	1,038	—	39.6	68.7	19.0	58
2007	1,659	—	—	42.7	65.3	48.6	492
Other Alt-A mortgage loans:							
2004 and prior	—	5,445	—	10.0	58.2	12.2	11
2005	78	3,664	101	20.6	60.3	4.7	—
2006	53	3,417	—	24.3	59.7	0.3	—
2007	630	—	143	37.5	85.1	32.7	247
2008	—	105	—	24.9	74.8	23.2	—
Total Alt-A mortgage loans	2,420	15,320	244				1,024
Subprime mortgage loans:							
2004 and prior	—	1,459	899	21.5	77.2	61.0	559
2005	—	145	1,117	38.1	81.1	56.0	217
2006	—	10,781	—	44.2	79.1	14.4	52
2007	2,477	575	5,102	44.2	78.0	18.4	162
Total subprime mortgage loans	2,477	12,960	7,118				990
Total Alt-A and subprime mortgage loans	$4,897	$28,280	$7,362				$2,014

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(1) Represents our exposure to private-label Alt-A and subprime mortgage-related securities that have been resecuritized (or wrapped) to include our guarantee.

(2) Delinquency data provided by Intex, where available, for loans backing Alt-A and subprime private-label mortgage-related securities that we own or guarantee. The reported Intex delinquency data reflect information from September 2012 remittances for August 2012 payments. For consistency purposes, we have adjusted the Intex delinquency data, where appropriate, to include all foreclosures, all REO and loans that were in bankruptcy and 60 or more days delinquent.

(3) The average delinquency, severity and credit enhancement metrics are calculated for each loan pool associated with securities where Fannie Mae has exposure and are weighted based on the unpaid principal balance of those securities.

(4) Severity data obtained from CoreLogic, where available, for loans backing Alt-A and subprime private-label mortgage-related securities that we own or guarantee. The CoreLogic severity data reflect information from

September 2012 remittances for August 2012 payments. For consistency purposes, we have adjusted the severity data, where appropriate.

(5) Average credit enhancement percentage reflects both subordination and financial guarantees. Reflects the ratio of the current amount of the securities that will incur losses in the securitization structure before any losses are allocated to securities that we own or guarantee. Percentage generally calculated based on the quotient of the total unpaid principal balance of all credit enhancements in the form of subordination or financial guarantee of the security divided by the total unpaid principal balance of all of the tranches of collateral pools from which credit support is drawn for the security that we own or guarantee. Beginning in March 2012, in calculating the weighted average credit enhancement percentage for bonds in the population that show negative credit enhancement in Intex due to under-collateralization, the negative credit enhancement amounts have been replaced with zero values.

(6) Reflects amount of unpaid principal balance supported by financial guarantees from monoline financial guarantors.

(7) Vintages are based on series date and not loan origination date.

Mortgage Loans

The increase in mortgage loans, net of the allowance for loan losses, in the first nine months of 2012 was primarily driven by securitization activity from our lender swap and portfolio securitization programs. For additional information on our mortgage loans, see “Note 3, Mortgage Loans.” For additional information on the mortgage loan purchase and sale activities reported by our Capital Markets group, see “Business Segment Results—Capital Markets Group Results.”

Debt

Debt of Fannie Mae is the primary means of funding our mortgage investments. We provide a summary of the activity of the debt of Fannie Mae and a comparison of the mix between our outstanding short-term and long-term debt in “Liquidity and Capital Management—Liquidity Management—Debt Funding.” Also see “Note 8, Short-Term Borrowings and Long-Term Debt” for additional information on our outstanding debt.

Debt of consolidated trusts represents the amount of Fannie Mae MBS issued from consolidated trusts and held by third-party certificateholders. The increase in debt of consolidated trusts in the first nine months of 2012 was primarily driven by securitization activity from our lender swap and portfolio securitization programs.

SUPPLEMENTAL NON-GAAP INFORMATION—FAIR VALUE BALANCE SHEETS

As part of our disclosure requirements with FHFA, we disclose on a quarterly basis supplemental non-GAAP consolidated fair value balance sheets, which reflect our assets and liabilities at estimated fair value.

Table 24 summarizes changes in our stockholders’ equity (deficit) reported in our GAAP condensed consolidated balance sheets and in the estimated fair value of our net assets in our non-GAAP consolidated fair value balance sheets for the nine months ended September 30, 2012. The estimated fair value of our net assets is calculated based on the difference between the fair value of our assets and the fair value of our liabilities, adjusted for noncontrolling interests. We use various valuation techniques to estimate fair value, some of which incorporate internal assumptions that are subjective and involve a high degree of management judgment. We describe the specific valuation techniques used to determine fair value and disclose the carrying value and fair value of our financial assets and liabilities in “Note 12, Fair Value.”

Table 24: Comparative Measures—GAAP Change in Stockholders’ Equity (Deficit) and Non-GAAP Change in Fair Value of Net Assets (Net of Tax Effect)

	For the Nine Months Ended September 30, 2012
	(Dollars in millions)
GAAP consolidated balance sheets:	
Fannie Mae stockholders’ deficit as of December 31, 2011[1]	$(4,624)
Total comprehensive income	11,086
Capital transactions:[2]	
Funds received from Treasury under the senior preferred stock purchase agreement	4,571
Senior preferred stock dividends	(8,679)
Capital transactions, net	(4,108)
Other	5
Fannie Mae stockholders’ equity as of September 30, 2012[1]	$2,359
Non-GAAP consolidated fair value balance sheets:	
Estimated fair value of net assets as of December 31, 2011	$(127,848)
Capital transactions, net	(4,108)
Change in estimated fair value of net assets, excluding capital transactions	46,353
Increase in estimated fair value of net assets, net	42,245
Estimated fair value of net assets as of September 30, 2012	$(85,603)

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(1) Our net worth, as defined under the senior preferred stock purchase agreement, is equivalent to the "Total equity (deficit)" amount reported in our condensed consolidated balance sheets, which consists of "Total Fannie Mae's stockholders' equity (deficit)" and "Noncontrolling interest."

(2) Represents capital transactions, which are reported in our condensed consolidated financial statements.

During the first nine months of 2012, the estimated fair value of our net assets, excluding capital transactions, increased by $46.4 billion. This increase was primarily driven by an improvement in credit-related items due to higher actual and expected home prices experienced in the second and third quarters of 2012, which lowered the expected losses on our guaranty book of business. We estimate that home prices increased by 3.5% in the second quarter of 2012 and 1.5% in the third quarter of 2012. Even a small change in home prices may cause volatility in our fair value measurements due to the large size of our guaranty book of business.

We updated our assumptions for prepayment speeds, severities and default rates during the third quarter of 2012, which resulted in an increase in the fair value of our loans of approximately $23 billion. These updates resulted in lower expectations of losses on certain loans, primarily performing loans with high LTV ratios.

The increase in fair value from higher actual and expected home prices and updated expectations for prepayment speeds, severities and default rates was partially offset by a decrease in fair value of $17 billion due to a change in the definition of principal market for certain of our loans and a change in fair value estimation for HARP loans as a result of the adoption of ASU 2011-04, Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRS, during the first nine months of 2012.

Cautionary Language Relating to Supplemental Non-GAAP Financial Measures

In reviewing our non-GAAP consolidated fair value balance sheets, there are a number of important factors and limitations to consider. The estimated fair value of our net assets is calculated as of a particular point in time based on our existing assets and liabilities. It does not incorporate other factors that may have a significant impact on our long-term fair value, including revenues generated from future business activities in which we expect to engage, the value from our foreclosure and loss mitigation efforts or the impact that legislation or potential regulatory actions may have on us. As a result, the estimated fair value of our net assets presented in our non-GAAP consolidated fair value balance sheets does not represent an estimate of our net realizable value, liquidation value or our market value as a whole. Amounts we ultimately realize from the disposition of assets or settlement of liabilities may vary materially from the estimated fair values presented in our non-GAAP consolidated fair value balance sheets.

In addition, the fair value of our net assets attributable to common stockholders presented in our fair value balance sheet does not represent an estimate of the value we expect to realize from operating the company or what we expect to draw from Treasury under the terms of our senior preferred stock purchase agreement, primarily because:

- The estimated fair value of our credit exposures significantly exceeds our projected credit losses as fair value takes into account certain assumptions about liquidity and required rates of return that a market participant may demand in assuming a credit obligation. Because we do not generally intend to have other parties assume the credit risk inherent in our book of business, and therefore would not be obligated to pay a market premium for its assumption, we do not expect the current market premium portion of our current estimate of fair value to impact future Treasury draws, and
- The fair value of our net assets reflects a point in time estimate of the fair value of our existing assets and liabilities, and does not incorporate the value associated with new business that may be added in the future.

The fair value of our net assets is not a measure defined within GAAP and may not be comparable to similarly titled measures reported by other companies.

Supplemental Non-GAAP Consolidated Fair Value Balance Sheets

We display our non-GAAP fair value balance sheets as of the dates indicated in Table 25.

Table 25: Supplemental Non-GAAP Consolidated Fair Value Balance Sheets

	As of September 30, 2012				As of December 31, 2011			
	GAAP Carrying Value	Fair Value Adjustment[1]	Estimated Fair Value		GAAP Carrying Value	Fair Value Adjustment[1]	Estimated Fair Value	
	(Dollars in millions)							
Assets:								
Cash and cash equivalents	$80,618	$—	$80,618		$68,336	$—	$68,336	
Federal funds sold and securities purchased under agreements to resell or similar arrangements	45,500	—	45,500		46,000	—	46,000	
Trading securities	42,522	—	42,522		74,198	—	74,198	
Available-for-sale securities	66,352	—	66,352		77,582	—	77,582	
Mortgage loans:								
Mortgage loans held for sale	490	13	503		311	14	325	
Mortgage loans held for investment, net of allowance for loan losses:								
Of Fannie Mae	308,850	(39,955)	268,895		322,825	(27,829)	294,996	
Of consolidated trusts	2,633,556	138,481 (2)	2,772,037	(3)	2,575,485	76,540 (2)	2,652,025	(3)
Total mortgage loans	2,942,896	98,539	3,041,435	(4)	2,898,621	48,725	2,947,346	(4)
Advances to lenders	6,367	(113)	6,254	(5)(6)	5,538	(118)	5,420	(5)(6)
Derivative assets at fair value	1,328	—	1,328	(5)(6)	561	—	561	(5)(6)
Guaranty assets and buy-ups, net	378	351	729	(5)(6)	503	398	901	(5)(6)
Total financial assets	3,185,961	98,777	3,284,738	(7)	3,171,339	49,005	3,220,344	(7)
Credit enhancements	456	987	1,443	(5)(6)	455	2,550	3,005	(5)(6)
Other assets	39,833	(234)	39,599	(5)(6)	39,690	(258)	39,432	(5)(6)
Total assets	$3,226,250	$99,530	$3,325,780		$3,211,484	$51,297	$3,262,781	
Liabilities:								
Short-term debt:								
Of Fannie Mae	$105,062	$17	$105,079		$146,752	$30	$146,782	
Of consolidated trusts	3,806	—	3,806		4,973	—	4,973	
Long-term debt:								
Of Fannie Mae	547,909 (8)	27,269	575,178		585,692 (8)	28,291	613,983	

Of consolidated trusts	2,539,933	(8)	157,783	(2)	2,697,716		2,452,455	(8)	144,202	(2)	2,596,657	
Derivative liabilities at fair value	2,033		—		2,033	(9)(10)	916		—		916	(9)(10)
Guaranty obligations	644		2,549		3,193	(9)(10)	811		3,133		3,944	(9)(10)
Total financial liabilities	3,199,387		187,618		3,387,005	(7)	3,191,599		175,656		3,367,255	(7)
Other liabilities	24,451		(126)		24,325	(9)(10)	24,456		(1,135)		23,321	(9)(10)
Total liabilities	3,223,838		187,492		3,411,330		3,216,055		174,521		3,390,576	
Equity (deficit):												
Fannie Mae stockholders' equity (deficit):												
Senior preferred[11]	117,149		—		117,149		112,578		—		112,578	
Preferred	19,130		(18,551)		579		19,130		(18,163)		967	
Common	(133,920)		(69,411)		(203,331)		(136,332)		(105,061)		(241,393)	
Total Fannie Mae stockholders' equity (deficit)/non-GAAP fair value of net assets	$2,359		$(87,962)		$(85,603)		$(4,624)		$(123,224)		$(127,848)	
Noncontrolling interest	53		—		53		53		—		53	
Total equity (deficit)	2,412		(87,962)		(85,550)		(4,571)		(123,224)		(127,795)	
Total liabilities and equity (deficit)	$3,226,250		$99,530		$3,325,780		$3,211,484		$51,297		$3,262,781	

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Explanation and Reconciliation of Non-GAAP Measures to GAAP Measures

(1) Each of the amounts listed as a "fair value adjustment" represents the difference between the carrying value included in our GAAP condensed consolidated balance sheets and our best judgment of the estimated fair value of the listed item.

(2) Fair value of consolidated loans is impacted by credit risk, which has no corresponding impact on the consolidated debt.

(3) Includes certain mortgage loans that we elected to report at fair value in our GAAP condensed consolidated balance sheets of $7.8 billion and $3.6 billion as of September 30, 2012 and December 31, 2011, respectively.

(4) Performing loans had a fair value of $2.9 trillion and an unpaid principal balance of $2.8 trillion as of September 30, 2012 compared with a fair value of $2.8 trillion and an unpaid principal balance of $2.7 trillion as of December 31, 2011. Nonperforming loans, which for the purposes of our non-GAAP fair value balance sheets consists of loans that are delinquent by one or more payments, had a fair value of $107.0 billion and an unpaid principal balance of $194.1 billion as of September 30, 2012 compared with a fair value of $128.9 billion and an unpaid principal balance of $226.5 billion as of December 31, 2011. See "Note 12, Fair Value" for additional information on valuation techniques for performing and nonperforming loans.

(5) The following line items: (a) Advances to lenders; (b) Derivative assets at fair value; (c) Guaranty assets and buy-ups, net; (d) Credit enhancements; and (e) Other assets, together consist of the following assets presented in our GAAP condensed consolidated balance sheets: (a) Accrued interest receivable, net; (b) Acquired property, net; and (c) Other assets.

(6) "Other assets" include the following GAAP condensed consolidated balance sheets line items: (a) Accrued interest receivable, net and (b) Acquired property, net. The carrying value of these items in our GAAP condensed consolidated balance sheets totaled $20.2 billion and $21.4 billion as of September 30, 2012 and December 31, 2011, respectively. "Other assets" in our GAAP condensed consolidated balance sheets include the following: (a) Advances to lenders; (b) Derivative assets at fair value; (c) Guaranty assets and buy-ups, net; and (d) Credit enhancements. The carrying value of these items totaled $8.5 billion and $7.1 billion as of September 30, 2012 and December 31, 2011, respectively.

(7) We estimated the fair value of these financial instruments in accordance with the fair value accounting guidance as described in "Note 12, Fair Value."

(8) Includes certain long-term debt instruments that we elected to report at fair value in our GAAP condensed consolidated balance sheets of $8.2 billion and $4.8 billion as of September 30, 2012 and December 31, 2011, respectively.

(9) The following line items: (a) Derivative liabilities at fair value; (b) Guaranty obligations; and (c) Other liabilities, consist of the following liabilities presented in our GAAP condensed consolidated balance sheets: (a) Accrued interest payable and (b) Other liabilities.

(10) "Other liabilities" include Accrued interest payable in our GAAP condensed consolidated balance sheets. The carrying value of this item in our GAAP condensed consolidated balance sheets totaled $11.7 billion and $12.6 billion as of September 30, 2012 and December 31, 2011, respectively. We assume that certain other liabilities, such as deferred revenues, have no fair value. Although we report the "Reserve for guaranty losses" as part of "Other liabilities" in our GAAP condensed consolidated balance sheets, it is incorporated into and reported as part of the fair value of our guaranty obligations in our non-GAAP supplemental consolidated fair value balance sheets. "Other liabilities" in our GAAP condensed consolidated balance sheets include the following: (a) Derivative liabilities at fair value and (b) Guaranty obligations. The carrying value of these items totaled $2.7 billion and $1.7 billion as of September 30, 2012 and December 31, 2011, respectively.

(11) The amount included in "estimated fair value" of the senior preferred stock is the liquidation preference, which is the same as the GAAP carrying value, and does not reflect fair value.

LIQUIDITY AND CAPITAL MANAGEMENT

Liquidity Management

Our business activities require that we maintain adequate liquidity to fund our operations. Our liquidity risk management policy is designed to address our liquidity risk. Liquidity risk is the risk that we will not be able to meet our funding obligations in a timely manner. Liquidity risk management involves forecasting funding requirements, maintaining sufficient capacity to meet our needs based on our ongoing assessment of financial market liquidity and adhering to our regulatory requirements.

Our treasury function resides within the Capital Markets group and is responsible for implementing our liquidity and contingency planning strategies. We conduct liquidity contingency planning to prepare for an event in which our access to the unsecured debt markets becomes limited. We plan for alternative sources of liquidity that are designed to allow us to meet our cash obligations without relying upon the issuance of unsecured debt. While our liquidity contingency planning attempts to address stressed market conditions and our status under conservatorship and Treasury support arrangements, we believe that our liquidity contingency plan may be difficult or impossible to execute for a company of our size in our circumstances.

See “Liquidity and Capital Management—Liquidity Management—Liquidity Risk Management Practices and Contingency Planning” in our 2011 Form 10-K for a discussion of our liquidity contingency plans. Also see “Risk Factors” in our 2011 Form 10-K for a description of the risks associated with our liquidity risk and liquidity contingency planning.

One of our liquidity management policies requires that we maintain a minimum threshold of Treasury securities and/or cash deposits with the Federal Reserve Bank of New York. Effective August 2012, this minimum threshold represents 50% of our average projected 30-day cash needs over the previous three months. Prior to this change, this minimum threshold was 50% of the average of the previous three month-end balances of our cash and other investments portfolio.

Our liquidity position could be adversely affected by many factors, both internal and external to our business, including: actions taken by our conservator, the Federal Reserve, U.S. Treasury or other government agencies; legislation relating to us or our business; a U.S. government payment default on its debt obligations; a downgrade in the credit ratings of our senior unsecured debt or the U.S government’s debt from the major ratings organizations; a systemic event leading to the withdrawal of liquidity from the market; an extreme market-wide widening of credit spreads; public statements by key policy makers; a significant decline in our net worth; potential investor concerns about the adequacy of funding available to us under the senior preferred stock purchase agreement after 2012; loss of demand for our debt, or certain types of our debt, from a major group of investors; a significant credit event involving one of our major institutional counterparties; a sudden catastrophic operational failure in the financial sector; or elimination of our GSE status.

Debt Funding

We fund our business primarily through the issuance of short-term and long-term debt securities in the domestic and international capital markets. Because debt issuance is our primary funding source, we are subject to “roll-over,” or refinancing, risk on our outstanding debt.

We have a diversified funding base of domestic and international investors. Purchasers of our debt securities are geographically diversified and include fund managers, commercial banks, pension funds, insurance companies, foreign central banks, corporations, state and local governments, and other municipal authorities.

Although our funding needs may vary from quarter to quarter depending on market conditions, we currently expect our debt funding needs will decline in future periods as we reduce the size of our mortgage portfolio in compliance with the requirement of the senior preferred stock purchase agreement that we reduce our mortgage portfolio to $650 billion by December 31, 2012 and, by December 31 of each year thereafter, to 85% of the maximum allowable amount that we were permitted to own as of December 31 of the immediately preceding calendar year, until the amount of our mortgage assets reaches $250 billion.

Fannie Mae Debt Funding Activity

Table 26 displays the activity in debt of Fannie Mae for the periods indicated. This activity excludes the debt of consolidated trusts and intraday loans. The reported amounts of debt issued and paid off during the period represent the face amount of the debt at issuance and redemption, respectively. Activity for short-term debt of Fannie Mae relates to borrowings with an original contractual maturity of one year or less while activity for long-term debt of Fannie Mae relates to borrowings with an original contractual maturity of greater than one year.

Table 26: Activity in Debt of Fannie Mae

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
	(Dollars in millions)			
Issued during the period:				
Short-term:				
Amount	$81,621	$134,500	$181,226	$362,752
Weighted-average interest rate	0.12 %	0.12 %	0.12 %	0.12 %
Long-term:				
Amount	$66,205	$81,284	$191,150	$162,708
Weighted-average interest rate	1.10 %	1.39 %	1.26 %	1.81 %
Total issued:				
Amount	$147,826	$215,784	$372,376	$525,460
Weighted-average interest rate	0.56 %	0.60 %	0.70 %	0.65 %
Paid off during the period:[1]				
Short-term:				
Amount	$69,619	$102,760	$222,937	$320,962
Weighted-average interest rate	0.10 %	0.16 %	0.11 %	0.21 %
Long-term:				
Amount	$86,116	$93,274	$232,351	$242,852
Weighted-average interest rate	1.57 %	1.96 %	2.19 %	2.49 %
Total paid off:				
Amount	$155,735	$196,034	$455,288	$563,814
Weighted-average interest rate	0.91 %	1.01 %	1.17 %	1.19 %

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(1) Consists of all payments on debt, including regularly scheduled principal payments, payments at maturity, payments resulting from calls and payments for any other repurchases. Calls and repurchases of zero-coupon debt are reported at original face value, which does not equal the amount of actual cash payment.

Overall debt funding activity decreased in the third quarter and first nine months of 2012 compared with the third quarter and first nine months of 2011. This decrease was primarily due to fewer short-term debt issuances during the third quarter of 2012 compared to the third quarter of 2011 due to lower funding needs as the size of our mortgage portfolio decreases. Short-term debt funding activity decreased during the first nine months of 2012 as we redeemed more short-term debt than we issued. As interest rates declined in the third quarter and first nine months of 2012, we issued long-term debt with lower interest rates to replace redemptions of long-term debt with higher interest rates.
We believe that continued federal government support of our business and the financial markets, as well as our status as a GSE, are essential to maintaining our access to debt funding. Changes or perceived changes in the government's support could materially adversely affect our ability to refinance our debt as it becomes due, which could have a material adverse impact on our liquidity, financial condition and results of operations. In February 2011, Treasury and HUD released a report to Congress on reforming America's housing finance market. The report provides that the Administration will work with FHFA to determine the best way to responsibly wind down both Fannie Mae and Freddie Mac. The report emphasizes the importance of proceeding with a careful transition plan and providing the necessary financial support to Fannie Mae and Freddie Mac during the transition period. For more information on GSE reform, see "Legislative and Regulatory Developments—GSE Reform" in this report and in our 2011 Form 10-K.

In addition, due to our reliance on the U.S. government's support, our access to debt funding or the cost of our debt funding could be materially adversely affected by a change or perceived change in the creditworthiness of the U.S. government. A downgrade in our credit ratings could reduce demand for our debt securities and increase our borrowing costs. See our discussion of credit ratings in "Risk Factors" for information about factors that may lead to the U.S. government's long-term debt rating being lowered, and "Credit Ratings" for further discussion of our dependence on our credit ratings.

Future changes or disruptions in the financial markets could significantly change the amount, mix and cost of funds we obtain, which also could increase our liquidity and roll-over risk and have a material adverse impact on our liquidity, financial condition and results of operations. See "Risk Factors" in our 2011 Form 10-K for a discussion of the risks we face relating to (1) the uncertain future of our company; (2) our reliance on the issuance of debt securities to obtain funds for our operations and the relative cost to obtain these funds; and (3) our liquidity contingency plans.

Outstanding Debt

Total outstanding debt of Fannie Mae includes short-term and long-term debt, excluding debt of consolidated trusts.

As of September 30, 2012, our outstanding short-term debt, based on its original contractual maturity, as a percentage of our total outstanding debt decreased to 16% from 20% as of December 31, 2011. For information on our outstanding debt maturing within one year, including the current portion of our long-term debt, as a percentage of our total debt, see "Maturity Profile of Outstanding Debt of Fannie Mae." In addition, the weighted-average interest rate on our long-term debt, based on its original contractual maturity, decreased to 2.16% as of September 30, 2012 from 2.42% as of December 31, 2011.

Pursuant to the terms of the senior preferred stock purchase agreement, we are prohibited from issuing debt without the prior consent of Treasury if it would result in our aggregate indebtedness exceeding our outstanding debt limit, which is 120% of the amount of mortgage assets we were allowed to own on December 31 of the immediately preceding calendar year. Our debt limit under the senior preferred stock purchase agreement was reduced to $874.8 billion in 2012. As of September 30, 2012, our aggregate indebtedness totaled $659.3 billion, which was $215.5 billion below our debt limit. The calculation of our indebtedness for purposes of complying with our debt limit reflects the unpaid principal balance and excludes debt basis adjustments and debt of consolidated trusts. Because of our debt limit, we may be restricted in the amount of debt we issue to fund our operations.

Table 27 displays information as of the dates indicated on our outstanding short-term and long-term debt based on its original contractual terms.

Table 27: Outstanding Short-Term Borrowings and Long-Term Debt[1]

	As of September 30, 2012				December 31, 2011			
	Maturities	Outstanding	Weighted-Average Interest Rate		Maturities	Outstanding	Weighted-Average Interest Rate	
	(Dollars in millions)							
Short-term debt:								
Fixed-rate:								
Discount notes	—	$104,547	0.15	%	—	$146,301	0.13	%
Foreign exchange discount notes	—	515	1.71		—	371	1.88	
Other[2]	—	—	—		—	80	0.04	
Total short-term debt of Fannie Mae[3]		105,062	0.16			146,752	0.13	
Debt of consolidated trusts	—	3,806	0.15		—	4,973	0.09	
Total short-term debt		$108,868	0.16	%		$151,725	0.13	%
Long-term debt:								
Senior fixed:								
Benchmark notes and bonds	2012 - 2030	$260,774	2.58	%	2012 - 2030	$277,146	2.81	%
Medium-term notes[4]	2012 - 2022	174,867	1.31		2012 - 2021	176,886	1.61	
Foreign exchange notes and bonds	2021 - 2028	689	5.30		2021 - 2028	662	5.44	
Other[5][6]	2012 - 2038	41,654	5.11		2012 - 2040	50,912	5.29	
Total senior fixed		477,984	2.34			505,606	2.64	
Senior floating:								
Medium-term notes[4]	2012 - 2019	63,516	0.29		2012 - 2016	71,855	0.32	
Other[5][6]	2020 - 2037	396	7.46		2020 - 2037	420	8.01	
Total senior floating		63,912	0.33			72,275	0.35	
Subordinated fixed:								
Qualifying subordinated[7]	2013 - 2014	2,522	5.00		2012 - 2014	4,894	5.08	
Subordinated debentures	2019	3,124	9.92		2019	2,917	9.91	
Total subordinated fixed		5,646	7.72			7,811	6.88	
Secured borrowings[8]	2021 - 2022	367	1.87		—	—	—	
Total long-term debt of Fannie Mae[9]		547,909	2.16			585,692	2.42	
Debt of consolidated trusts[6]	2012 - 2052	2,539,933	3.58		2012 - 2051	2,452,455	4.18	
Total long-term debt		$3,087,842	3.32	%		$3,038,147	3.84	%
Outstanding callable debt of Fannie Mae[10]		$177,233	1.67	%		$187,937	2.17	%

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(1) Outstanding debt amounts and weighted-average interest rates reported in this table include the effect of unamortized discounts, premiums and other cost basis adjustments. Reported amounts include fair value gains and losses associated with debt that we elected to carry at fair value. The unpaid principal balance of outstanding debt of Fannie Mae, which excludes unamortized discounts, premiums and other cost basis adjustments, and debt of consolidated trusts, totaled $658.7 billion and $741.6 billion as of September 30, 2012 and December 31, 2011, respectively.

(2) Includes foreign exchange discount notes denominated in U.S. dollars.

(3) Short-term debt of Fannie Mae consists of borrowings with an original contractual maturity of one year or less and, therefore, does not include the current portion of long-term debt. Reported amounts include a net discount and other cost basis adjustments of $40 million and $53 million as of September 30, 2012 and December 31, 2011,

respectively.

(4) Includes long-term debt with an original contractual maturity of greater than 1 year and up to 10 years, excluding zero-coupon debt.

(5) Includes long-term debt that is not included in other debt categories.

(6) Includes a portion of structured debt instruments that is reported at fair value.

(7) Consists of subordinated debt with an interest deferral feature.

(8) Represents remaining liability for transfer of financial assets from our condensed consolidated balance sheets that did not qualify as a sale.

(9) Long-term debt of Fannie Mae consists of borrowings with an original contractual maturity of greater than one year. Reported amounts include the current portion of long-term debt that is due within one year, which totaled $123.7 billion and $134.3 billion as of September 30, 2012 and December 31, 2011, respectively. Reported amounts also include unamortized discounts, premiums and other cost basis adjustments of $6.2 billion and $9.2 billion as of September 30, 2012 and December 31, 2011, respectively. The unpaid principal balance of long-term debt of Fannie Mae, which excludes unamortized discounts, premiums, fair value adjustments and other cost basis adjustments and amounts related to debt of consolidated trusts, totaled $554.0 billion and $594.8 billion as of September 30, 2012 and December 31, 2011, respectively.

(10) Consists of long-term callable debt of Fannie Mae that can be paid off in whole or in part at our option or the option of the investor at any time on or after a specified date. Includes the unpaid principal balance, and excludes unamortized discounts, premiums and other cost basis adjustments.

Maturity Profile of Outstanding Debt of Fannie Mae

Table 28 displays the maturity profile, as of September 30, 2012, of our outstanding debt maturing within one year, by month, including amounts we have announced for early redemption. Our outstanding debt maturing within one year, including the current portion of our long-term debt, decreased as a percentage of our total outstanding debt, excluding debt of consolidated trusts, to 35% as of September 30, 2012, compared with 38% as of December 31, 2011. The weighted-average maturity of our outstanding debt that is maturing within one year was 127 days as of September 30, 2012, compared with 158 days as of December 31, 2011.

Table 28: Maturity Profile of Outstanding Debt of Fannie Mae Maturing Within One Year[1]

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(1) Includes unamortized discounts, premiums and other cost basis adjustments of $74 million as of September 30, 2012. Excludes debt of consolidated trusts maturing within one year of $6.6 billion as of September 30, 2012.

Table 29 displays the maturity profile, as of September 30, 2012, of the portion of our long-term debt that matures in more than one year, on a quarterly basis for one year and on an annual basis thereafter, excluding amounts we have announced for early redemption within one year. The weighted-average maturity of our outstanding debt maturing in more than one year was approximately 57 months as of September 30, 2012 and approximately 59 months as of December 31, 2011.

Table 29: Maturity Profile of Outstanding Debt of Fannie Mae Maturing in More Than One Year[1]

(1) Includes unamortized discounts, premiums and other cost basis adjustments of $6.2 billion as of September 30, 2012. Excludes debt of consolidated trusts of $2.5 trillion as of September 30, 2012.

We intend to repay our short-term and long-term debt obligations as they become due primarily through proceeds from the issuance of additional debt securities.

Cash and Other Investments Portfolio

Table 30 displays information on the composition of our cash and other investments portfolio as of the dates indicated.

Table 30: Cash and Other Investments Portfolio

	As of September 30, 2012	December 31, 2011
	(Dollars in millions)	
Cash and cash equivalents	$20,674	$17,539
Federal funds sold and securities purchased under agreements to resell or similar arrangements	45,500	46,000
Non-mortgage-related securities:		
U.S. Treasury securities [1]	19,897	47,737
Asset-backed securities	—	2,111
Total non-mortgage-related securities	19,897	49,848
Total cash and other investments	$86,071	$113,387

(1) Excludes $2.6 billion and $600 million of U.S. Treasury securities which are a component of cash equivalents as of September 30, 2012 and December 31, 2011, respectively, as these securities had a maturity at the date of acquisition of three months or less.

Our cash and other investments portfolio decreased from December 31, 2011 to September 30, 2012. The balance of our cash and other investments portfolio fluctuates based on changes in our cash flows, overall liquidity in the fixed income markets and our liquidity risk management policies and practices. See “Risk Management—Credit Risk Management—Institutional Counterparty Credit Risk Management—Issuers of Investments Held in our Cash and Other Investments Portfolio” for additional information on the risks associated with the assets in our cash and other investments portfolio.

Credit Ratings

Our credit ratings from the major credit ratings organizations, as well as the credit ratings of the U.S. government, are primary factors that could affect our ability to access the capital markets and our cost of funds. In addition, our credit ratings are important when we seek to engage in certain long-term transactions, such as derivative transactions.

Standard & Poor’s

Ratings Services (“S&P”), Moody’s Investors Service (“Moody’s”) and Fitch Ratings Limited (“Fitch”) have all indicated that, if they were to lower the sovereign credit ratings on the U.S, they would likely lower their ratings on the debt of Fannie Mae and certain other government-related entities. We cannot predict whether one or more of these ratings agencies will lower our debt ratings in the future. See “Risk Factors” for a discussion of the possibility of further downgrades and the risks to our business relating to a decrease in our credit ratings, which could include an increase in our borrowing costs, limits on our ability to issue debt, and additional collateral requirements under our derivatives contracts.

Table 31 displays the credit ratings issued by the three major credit rating agencies as of November 1, 2012.

Table 31: Fannie Mae Credit Ratings

	As of November 1, 2012		
	S&P	Moody’s	Fitch
Long-term senior debt	AA+	Aaa	AAA
Short-term senior debt	A-1+	P-1	F1+
Qualifying subordinated debt	A	Aa2	AA-
Preferred stock	C	Ca	C/RR6
Bank financial strength rating	—	E+	—
Outlook	Negative (for Long Term Senior Debt and Qualifying Subordinated Debt)	Negative (for Long Term Senior Debt and Qualifying Subordinated Debt)	Negative (for AAA rated Long Term Issuer Default Rating)

Cash Flows

Nine Months Ended September 30, 2012. Cash and cash equivalents increased from December 31, 2011 by $3.1 billion to $20.7 billion as of September 30, 2012. Net cash generated from investing activities totaled $386.4 billion, resulting primarily from proceeds received from repayments of loans held for investment. Net cash from operating activities totaled $32.3 billion. These net cash inflows were partially offset by net cash used in financing activities of $415.5 billion primarily attributable to a significant amount of debt redemptions in excess of proceeds received from the issuances of debt.

Nine Months Ended September 30, 2011. Cash and cash equivalents increased from December 31, 2010 by $7.0 billion to $24.3 billion as of September 30, 2011. Net cash generated from investing activities totaled $327.8 billion, resulting primarily from proceeds received from repayments of loans held for investment. These net cash inflows were offset by net cash used in operating activities of $6.7 billion and net cash used in financing activities of $314.1 billion primarily attributable to a significant amount of debt redemptions in excess of proceeds received from the issuances of debt as well as proceeds received from Treasury under the senior preferred stock purchase agreement.

Capital Management

Regulatory Capital

FHFA has announced that, during the conservatorship, our existing statutory and FHFA-directed regulatory capital requirements will not be binding and that FHFA will not issue quarterly capital classifications. We submit capital reports to FHFA and FHFA monitors our capital levels. The deficit of core capital over statutory minimum capital was $146.4 billion as of September 30, 2012 and $148.4 billion as of December 31, 2011.

Senior Preferred Stock Purchase Agreement

As a result of the covenants under the senior preferred stock purchase agreement, Treasury’s ownership of the warrant to purchase up to 79.9% of the total shares of our common stock outstanding and the uncertainty regarding our future, we effectively no longer have access to equity funding except through draws under the senior preferred stock purchase agreement.

Under the senior preferred stock purchase agreement, Treasury made a commitment to provide funding, under certain conditions, to eliminate deficits in our net worth. We have received a total of $116.1 billion from Treasury pursuant to the senior preferred stock purchase agreement as of September 30, 2012. The aggregate liquidation preference of the senior preferred stock, including the initial aggregate liquidation preference of $1.0 billion, remains at $117.1 billion.

While we had a positive net worth as of September 30, 2012, in some future periods we could have a net worth deficit and in such case would be required to obtain additional funding from Treasury pursuant to the senior preferred stock purchase agreement.

The senior preferred stock purchase agreement provides that the $200 billion maximum amount of the commitment from Treasury will increase as necessary to accommodate any net worth deficiencies attributable to periods during 2010, 2011 and 2012. If we do not have a positive net worth as of December 31, 2012, then the amount of funding available under the senior preferred stock purchase agreement after 2012 will be $124.8 billion ($200 billion less $75.2 billion in cumulative draws for net worth deficiencies through December 31, 2009).

In the event we have a positive net worth as of December 31, 2012, then the amount of funding available after 2012 under the senior preferred stock purchase agreement will depend on the size of that positive net worth relative to the cumulative draws for net worth deficiencies attributable to periods during 2010, 2011 and 2012, as follows:

- If our positive net worth as of December 31, 2012 is less than the cumulative draws for net worth deficiencies attributable to periods during 2010, 2011 and 2012, then the amount of available funding will be $124.8 billion less our positive net worth as of December 31, 2012.
- If our positive net worth as of December 31, 2012 is greater than the cumulative draws for net worth deficiencies attributable to periods during 2010, 2011 and 2012, then the amount of available funding will be $124.8 billion less the cumulative draws attributable to periods during 2010, 2011 and 2012.

Treasury has waived the quarterly commitment fee under the senior preferred stock purchase agreement for each quarter of 2011 and 2012 due to the continued fragility of the U.S. mortgage market and Treasury's belief that imposing the commitment fee would not generate increased compensation for taxpayers. In addition, pursuant to the amendment to the senior preferred stock purchase agreement described in "Executive Summary—Amendment to Senior Preferred Stock Purchase Agreement with Treasury," the periodic commitment fee under the agreement will be suspended effective January 1, 2013.

We are not permitted to redeem the senior preferred stock prior to the termination of Treasury's funding commitment under the senior preferred stock purchase agreement. Moreover, we are not permitted to pay down the liquidation preference of the outstanding shares of senior preferred stock except to the extent of (1) accrued and unpaid dividends previously added to the liquidation preference and not previously paid down; and (2) quarterly commitment fees previously added to the liquidation preference and not previously paid down. In addition, if we issue any shares of capital stock for cash while the senior preferred stock is outstanding, the net proceeds of the issuance must be used to pay down the liquidation preference of the senior preferred stock; however, the liquidation preference of each share of senior preferred stock may not be paid down below $1,000 per share prior to the termination of Treasury's funding commitment. Following the termination of Treasury's funding commitment, we may pay down the liquidation preference of all outstanding shares of senior preferred stock at any time, in whole or in part. The limited circumstances under which Treasury's funding commitment will terminate are described in "Business— Conservatorship and Treasury Agreements" in our 2011 Form 10-K.

Dividends

Our third quarter dividend of $2.9 billion was declared by the conservator and paid by us on September 28, 2012. The current annualized dividend on the senior preferred stock remains at $11.7 billion based on the 10% dividend rate. Pursuant to the August 2012 amendment to the senior preferred stock purchase agreement, beginning in 2013, the method for calculating the amount of dividends payable on the senior preferred stock will no longer be based on applying an annual dividend rate of 10% to the aggregate liquidation preference of the senior preferred stock. Effective January 1, 2013, the amount of dividends payable on the senior preferred stock for a dividend period will be based on our net worth as of the end of the immediately preceding fiscal quarter. For each dividend period from January 1, 2013 through and including December 31, 2017, the dividend amount will be the amount, if any, by which our net worth as of the end of the immediately preceding fiscal quarter exceeds an applicable capital reserve amount. The applicable capital reserve amount will be $3.0 billion for 2013 and will be reduced by $600 million each year until it reaches zero on January 1, 2018. For each dividend period beginning in 2018, the dividend amount will be the entire amount of our net worth, if any, as of the end of the immediately preceding fiscal quarter. See "Risk Factors" for a discussion of the risks relating to our dividend obligations to Treasury on the senior preferred stock.

OFF-BALANCE SHEET ARRANGEMENTS

Our maximum potential exposure to credit losses relating to our outstanding and unconsolidated Fannie Mae MBS and other financial guarantees is primarily represented by the unpaid principal balance of the mortgage loans underlying outstanding and unconsolidated Fannie Mae MBS and other financial guarantees of $56.2 billion as of September 30, 2012 and $62.0 billion as of December 31, 2011.

We also provide assistance to housing finance agencies under the temporary credit and liquidity facilities programs in which Treasury has purchased participation interests. For a description of these programs, see "MD&A—Off-Balance Sheet Arrangements—Treasury Housing Finance Agency Initiative" in our 2011 Form 10-K.

RISK MANAGEMENT

Our business activities expose us to the following three major categories of financial risk: credit risk, market risk (including interest rate and liquidity risk) and operational risk. We seek to actively monitor and manage these risks by using an established risk management framework. Our risk management framework is intended to provide the basis for the principles that govern our risk management activities. In addition to these financial risks, there is significant uncertainty regarding the future of our company, including how long we will continue to be in existence, which we discuss in more detail in "Legislative and Regulatory Developments—GSE Reform" in this report and in "Risk Factors" in our 2011 Form 10-K. We are also subject to a number of other risks that could adversely impact our business, financial condition, earnings and cash flow, including model, legal and reputational risks that may arise due to a failure to comply with laws, regulations or ethical standards and codes of conduct applicable to our business activities and functions.

In this section we provide an update on our management of our major risk categories. For a more complete discussion of the financial risks we face and how we manage credit risk, market risk and operational risk, see "MD&A—Risk Management" in our 2011 Form 10-K and "Risk Factors" in our 2011 Form 10-K and in this report.

Credit Risk Management

We are generally subject to two types of credit risk: mortgage credit risk and institutional counterparty credit risk. Mortgage credit risk is the risk that a borrower will fail to make required mortgage payments. Institutional counterparty credit risk is the risk that our institutional counterparties may fail to fulfill their contractual obligations to us, including seller/servicers who are obligated to repurchase loans from us or reimburse us for losses in certain circumstances.

Mortgage Credit Risk Management

We are exposed to credit risk on our mortgage credit book of business because we either hold mortgage assets, have issued a guaranty in connection with the creation of Fannie Mae MBS backed by mortgage assets or provided other credit enhancements on mortgage assets. While our mortgage credit book of business includes all of our mortgage-related assets, both on- and off-balance sheet, our guaranty book of business excludes non-Fannie Mae mortgage-related securities held in our portfolio for which we do not provide a guaranty. We provide information on the performance of non-Fannie Mae mortgage-related securities held in our portfolio, including the impairment that we have recognized on these securities, in "Consolidated Balance Sheet Analysis—Investments in Mortgage-Related Securities—Investments in Private-Label Mortgage-Related Securities."

Mortgage Credit Book of Business

Table 32 displays the composition of our mortgage credit book of business as of the dates indicated. Our total single-family mortgage credit book of business accounted for 93% of our total mortgage credit book of business as of September 30, 2012 and December 31, 2011.

Table 32: Composition of Mortgage Credit Book of Business[1]

	As of September 30, 2012			As of December 31, 2011		
	Single-Family	Multifamily	Total	Single-Family	Multifamily	Total
	(Dollars in millions)					
Mortgage loans and Fannie Mae MBS[2]	$2,806,813	$184,279	$2,991,092	$2,798,633	$176,898	$2,975,531
Unconsolidated Fannie Mae MBS, held by third parties[3]	16,163	1,569	17,732	17,910	1,702	19,612
Other credit guarantees[4]	22,075	16,392	38,467	25,824	16,582	42,406
Guaranty book of business	$2,845,051	$202,240	$3,047,291	$2,842,367	$195,182	$3,037,549
Agency mortgage-related securities[5]	12,924	32	12,956	15,522	33	15,555
Other mortgage-related securities[6]	38,882	28,588	67,470	43,019	31,511	74,530
Mortgage credit book of business	$2,896,857	$230,860	$3,127,717	$2,900,908	$226,726	$3,127,634
Guaranty Book of Business Detail:						
Conventional Guaranty Book of Business[7]	$2,775,323	$200,077	$2,975,400	$2,769,919	$192,797	$2,962,716
Government Guaranty Book of Business[8]	$69,728	$2,163	$71,891	$72,448	$2,385	$74,833

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(1) Based on unpaid principal balance.

(2) Consists of mortgage loans and Fannie Mae MBS recognized in our condensed consolidated balance sheets. The principal balance of resecuritized Fannie Mae MBS is included only once in the reported amount.

(3) Reflects unpaid principal balance of unconsolidated Fannie Mae MBS, held by third-party investors. The principal balance of resecuritized Fannie Mae MBS is included only once in the reported amount.

(4) Includes single-family and multifamily credit enhancements that we have provided and that are not otherwise reflected in the table.

(5) Consists of mortgage-related securities issued by Freddie Mac and Ginnie Mae.

(6) Consists primarily of mortgage revenue bonds, Alt-A and subprime private-label securities and CMBS.

(7) Refers to mortgage loans and mortgage-related securities that are not guaranteed or insured, in whole or in part, by the U.S. government or one of its agencies.

(8) Refers to mortgage loans and mortgage-related securities guaranteed or insured, in whole or in part, by the U.S. government or one of its agencies.

In the following sections, we discuss the mortgage credit risk of the single-family and multifamily loans in our guaranty book of business. The credit statistics reported below, unless otherwise noted, pertain generally to the portion of our guaranty book of business for which we have access to detailed loan-level information, which constituted approximately 99% of each of our single-family conventional guaranty book of business and our multifamily guaranty book of business, excluding defeased loans, as of September 30, 2012 and December 31, 2011. We typically obtain this data from the sellers or servicers of the mortgage loans in our guaranty book of business and receive representations and warranties from them as to the accuracy of the information. While we perform various quality assurance checks by sampling loans to assess compliance with our underwriting and eligibility criteria, we do not independently verify all reported information and we rely on lender representations regarding the accuracy of the characteristics of loans in our guaranty book of business. See "Risk Factors" in our 2011 Form 10-K for a discussion of the risk that we could experience mortgage fraud as a result of this reliance on lender representations.

Single-Family Mortgage Credit Risk Management

Our strategy in managing single-family mortgage credit risk consists of four primary components: (1) our acquisition and servicing policies along with our underwriting and servicing standards, including the use of credit enhancements; (2) portfolio diversification and monitoring; (3) management of problem loans; and (4) REO management. These strategies may increase our expenses and may not be effective in reducing our credit-related expenses or credit losses.

We provide information on our credit-related expenses and credit losses in “Consolidated Results of Operations—Credit-Related Expenses.”

In evaluating our single-family mortgage credit risk, we closely monitor changes in housing and economic conditions and the impact of those changes on the credit risk profile of our single-family mortgage credit book of business. We regularly review and provide updates to our underwriting standards and eligibility guidelines that take into consideration changing market

conditions. The credit risk profile of our single-family mortgage credit book of business is influenced by, among other things, the credit profile of the borrower, features of the loan, loan product type, the type of property securing the loan and the housing market and general economy. We focus more on loans that we believe pose a higher risk of default, which typically have been loans associated with higher mark-to-market LTV ratios, loans to borrowers with lower FICO credit scores and certain higher risk loan product categories, such as Alt-A loans. These and other factors affect both the amount of expected credit loss on a given loan and the sensitivity of that loss to changes in the economic environment.

In September 2012, we and Freddie Mac announced a new representation and warranty framework for conventional loans acquired by us on or after January 1, 2013. This new framework, which is part of FHFA's seller-servicer contract harmonization initiative, seeks to provide lenders a higher degree of certainty and clarity regarding their repurchase exposure and liability on future deliveries, as well as consistency around repurchase timelines and remedies. Under the new framework, lenders will be relieved of certain repurchase obligations for loans that meet specific payment history requirements and other eligibility requirements. For example, a lender would not be required to repurchase a mortgage loan in breach of certain underwriting and eligibility representations and warranties if the borrower has made timely payments for 36 months following the acquisition date (or, for Refi Plus loans, for 12 months following the acquisition date), and the loan meets other specified eligibility requirements. As a result of this new framework, we will make changes in our quality control process that will move the primary focus of our quality control reviews from the time a loan defaults to shortly after the time the loan is delivered to us. These changes will include augmenting the random sampling approach we currently use in selecting new mortgage loan deliveries for review with more targeted, discretionary loan selections.

Because we believe we have limited credit exposure on our government loans, the single-family credit statistics we focus on and report in the sections below generally relate to our single-family conventional guaranty book of business, which represents the substantial majority of our total single-family guaranty book of business.

Table 33 displays our single-family conventional business volumes and our single-family conventional guaranty book of business for the periods indicated, based on certain key risk characteristics that we use to evaluate the risk profile and credit quality of our single-family loans.

Table 33: Risk Characteristics of Single-Family Conventional Business Volume and Guaranty Book of Business[1]

	Percent of Single-Family Conventional Business Volume[2]				Percent of Single-Family Conventional Guaranty Book of Business[3][4]	
	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		As of	
	2012	2011	2012	2011	September 30, 2012	December 31, 2011
Original LTV ratio:[5]						
<= 60%	24 %	26 %	26 %	28 %	23 %	24 %
60.01% to 70%	14	14	14	15	15	16
70.01% to 80%	34	38	35	38	40	40
80.01% to 90%[6]	9	10	9	9	10	10
90.01% to 100%[6]	8	9	8	7	9	9
100.01% to 125%[6]	6	3	5	3	2	1
Greater than 125%[6]	5	—	3	—	1	—
Total	100 %	100 %	100 %	100 %	100 %	100 %
Weighted average	77 %	71 %	74 %	70 %	72 %	71 %
Average loan amount	$216,658	$202,476	$214,047	$205,186	$157,291	$156,194
Estimated mark-to-market LTV ratio:[7]						
<= 60%					28 %	26 %
60.01% to 70%					14	12
70.01% to 80%					22	18
80.01% to 90%					13	16
90.01% to 100%					9	10
100.01% to 125%					8	11
Greater than 125%					6	7
Total					100 %	100 %
Weighted average					76 %	79 %
Product type:						
Fixed-rate:[8]						