FEDERAL NATIONAL MORTGAGE ASSOCIATION FANNIE MAE
Form 10-Q
August 08, 2008

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 June 30, 2008

OR

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

For the transition period from to

Commission File 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 o

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. (Check one):

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

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

As of June 30, 2008, there were 1,076,594,797 shares of common stock outstanding.

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PART I FINANCIAL INFORMATION

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

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 contained in our Annual Report on Form 10-K for the year ended December 31, 2007 (2007 Form 10-K). The results of operations presented in our interim financial statements and discussed in MD&A are not necessarily indicative of the results that may be expected for the full year. Please refer to Glossary of Terms Used in This Report in our 2007 Form 10-K for an explanation of key terms used throughout this discussion.

INTRODUCTION

Fannie Mae is a government-sponsored enterprise (GSE), owned by private shareholders (NYSE: FNM) and chartered by Congress to support liquidity and stability in the secondary mortgage market. Our business includes three integrated business segments Single-Family Credit Guaranty (Single-Family), Housing and Community Development (HCD), and Capital Markets that work together to provide services, products and solutions to our lender customers and a broad range of housing partners. Together, our business segments contribute to our chartered mission objectives, helping to increase the total amount of funds available to finance housing in the United States and to make homeownership more available and affordable for low-, moderate- and middle-income Americans. We also work with our customers and partners to increase the availability and affordability of rental housing. Although we are a corporation chartered by the U.S. Congress, the U.S. government does not guarantee, directly or indirectly, our securities or other obligations. Our business is self-sustaining and funded exclusively with private capital.

Our Single-Family business works with our lender customers to securitize single-family mortgage loans into Fannie Mae mortgage-backed securities (Fannie Mae MBS) and to facilitate the purchase of single-family mortgage loans for our mortgage portfolio. Our HCD business works with our lender customers to securitize multifamily mortgage loans into Fannie Mae MBS and to facilitate the purchase of multifamily mortgage loans for our mortgage portfolio. Our HCD business also makes debt and equity investments to increase the supply of affordable housing. Our Capital Markets group manages our investment activity in mortgage loans, mortgage-related securities and other investments, our debt financing activity, and our liquidity and capital positions. We fund our investments primarily through proceeds from our issuance of debt securities in the domestic and international capital markets.

SELECTED FINANCIAL DATA

The selected financial data presented below is summarized from our condensed consolidated results of operations for the three and six months ended June 30, 2008 and 2007, as well as from selected condensed consolidated balance sheet data as of June 30, 2008 and December 31, 2007. This data should be read in conjunction with this MD&A, as well as with the unaudited condensed consolidated financial statements and related notes included in this report and with our audited consolidated financial statements and related notes included in our 2007 Form 10-K.

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007[1]	2008	2007[1]
	(In millions, except per share amounts)			
Statement of operations data:				
Net interest income	$ 2,057	$ 1,193	$ 3,747	$ 2,387
Guaranty fee income	1,608	1,120	3,360	2,218
Losses on certain guaranty contracts		(461)		(744)
Trust management income	75	150	182	314
Fair value gains (losses), net[2]	517	1,424	(3,860)	858
Other income (expenses), net[3]	(889)	(3)	(1,059)	397
Credit-related expenses[4]	(5,349)	(518)	(8,592)	(839)
Net income (loss)	(2,300)	1,947	(4,486)	2,908
Preferred stock dividends and issuance costs at redemption	(303)	(118)	(625)	(253)
Net income (loss) available to common stockholders	(2,603)	1,829	(5,111)	2,655
Per common share data:				
Earnings (loss) per share:				
Basic	$ (2.54)	$ 1.88	$ (5.11)	$ 2.73
Diluted	(2.54)	1.86	(5.11)	2.72
Weighted-average common shares outstanding:				
Basic	1,025	973	1,000	973
Diluted	1,025	1,001	1,000	1,001
Cash dividends declared per common share	$ 0.35	$ 0.50	$ 0.70	$ 0.90
New business acquisition data:				
Fannie Mae MBS issues acquired by third parties[5]	$ 137,731	$ 134,440	$ 293,433	$ 259,642
Mortgage portfolio purchases[6]	61,347	48,676	97,670	84,833
New business acquisitions	$ 199,078	$ 183,116	$ 391,103	$ 344,475

	As of	
	June 30, 2008	December 31, 2007[1]
	(Dollars in millions)	
Balance sheet data:		
Investments in securities:		
Trading	$ 99,562	$ 63,956
Available-for-sale	245,226	293,557
Mortgage loans:		
Loans held for sale	6,931	7,008
Loans held for investment, net of allowance	411,300	396,516
Total assets	885,918	879,389
Short-term debt	240,223	234,160
Long-term debt	559,279	562,139
Total liabilities	844,528	835,271
Preferred stock	21,725	16,913
Total stockholders equity	41,226	44,011
Regulatory capital data:		
Core capital[7]	$ 46,964	$ 45,373
Total capital[8]	55,568	48,658
Book of business data:		
Mortgage portfolio[9]	$ 754,116	$ 727,903
Fannie Mae MBS held by third parties[10]	2,252,282	2,118,909
Other guarantees[11]	31,812	41,588
Mortgage credit book of business	$ 3,038,210	$ 2,888,400
Guaranty book of business[12]	$ 2,898,207	$ 2,744,237

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007[1]	2008	2007[1]
Ratios:				
Return on assets ratio[13]*	(1.20)%	0.86%	(1.16)%	0.62%
Return on equity ratio[14]*	(50.3)	22.6	(43.9)	16.6
Equity to assets ratio[15]*	4.6	4.8	4.8	4.8
Dividend payout ratio[16]	N/A	26.8	N/A	33.1
Average effective guaranty fee rate (in basis points)[17]	26.3bp	21.5bp	27.9bp	21.6bp
Credit loss ratio (in basis points)[18]	17.5bp	4.0bp	15.1bp	3.7bp

(1) Certain prior period amounts have been reclassified to conform to the current period presentation.

(2) Consists of the following: (a) derivatives fair value gains (losses), net; (b) trading securities gains (losses), net; (c) hedged mortgage assets gains (losses), net; (d) debt foreign exchange gains (losses), net; and (e) debt fair value gains (losses), net.

(3) Consists of the following: (a) investment gains (losses), net; (b) debt extinguishment gains (losses), net; (c) losses from partnership investments; and (d) fee and other income.

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

(5) Unpaid principal balance of Fannie Mae MBS issued and guaranteed by us during the reporting period less: (a) securitizations of mortgage loans held in our portfolio during the reporting period and (b) Fannie Mae MBS purchased for our investment portfolio during the reporting period.

(6) Unpaid principal balance of mortgage loans and mortgage-related securities we purchased for our investment portfolio during the reporting period. Includes mortgage-related securities acquired through the extinguishment of debt and capitalized interest.

(7) The sum of (a) the stated value of outstanding common stock (common stock less treasury stock); (b) the stated value of outstanding non-cumulative perpetual preferred stock; (c) paid-in capital; and (d) our retained earnings. Core capital excludes accumulated other comprehensive income (loss).

(8) The sum of (a) core capital and (b) the total allowance for loan losses and reserve for guaranty losses, less (c) the specific loss allowance (that is, the allowance required on individually impaired loans).

(9) Unpaid principal balance of mortgage loans and mortgage-related securities held in our portfolio.

(10) Unpaid principal balance of Fannie Mae MBS held by third-party investors. The principal balance of resecuritized Fannie Mae MBS is included only once in the reported amount.

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

(12) Unpaid principal balance of: mortgage loans held in our mortgage portfolio; Fannie Mae MBS (whether held in our mortgage portfolio or held by third parties); and other credit enhancements that we provide on mortgage assets. Excludes non-Fannie Mae mortgage-related securities held in our investment portfolio for which we do not provide a guaranty. The principal balance of resecuritized Fannie Mae MBS is included only once in the reported amount.

(13) Annualized net income (loss) available to common stockholders divided by average total assets during the period.

(14) Annualized net income (loss) available to common stockholders divided by average outstanding common equity during the period.

(15) Average stockholders equity divided by average total assets during the period.

(16) Common dividends declared during the period divided by net income (loss) available to common stockholders for the period.

(17) Annualized guaranty fee income as a percentage of average outstanding Fannie Mae MBS and other guarantees during the period.

(18) Annualized (a) charge-offs, net of recoveries and (b) foreclosed property expense, as a percentage of the average guaranty book of business during the period. We exclude from our credit loss ratio any initial losses recorded on delinquent loans purchased from MBS trusts pursuant to Statement of Position No. 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer* (SOP 03-3), when the purchase price of seriously delinquent loans that we purchase from Fannie Mae MBS trusts exceeds the fair value of the loans at the time of purchase. Also excludes the difference between the unpaid principal balance of HomeSaver Advance™ loans at origination and the estimated fair value of these loans. Our credit loss ratio including the effect of these initial losses recorded pursuant to SOP 03-3 and related to HomeSaver Advance loans was 22.6 basis points and 4.7 basis points for the three months ended June 30, 2008 and 2007, respectively, and 21.7 basis points and 4.4 basis

points for the six months ended June 30, 2008 and 2007, respectively. We previously calculated our credit loss ratio based on credit losses as a percentage of our mortgage credit book of business, which includes non-Fannie Mae mortgage-related securities held in our mortgage investment portfolio that we do not guarantee. Because losses related to non-Fannie Mae mortgage-related securities are not reflected in our credit losses, we revised the calculation of our credit loss ratio to reflect credit losses as a percentage of our guaranty book of business. Our credit loss ratio calculated based on our mortgage credit book of business would have been 16.7 basis points and 3.8 basis points for the three months ended June 30, 2008 and 2007, respectively, and 14.3 basis points and 3.5 basis points for the six months ended June 30, 2008 and 2007, respectively.

Note:

* Average balances for purposes of the ratio calculations are based on beginning and end of period balances.

EXECUTIVE SUMMARY

Our Executive Summary presents a high-level overview of the most significant factors focused on by our management in currently evaluating our business and financial position and prospects.

Conditions in the Housing and Mortgage Markets

The housing and mortgage markets have experienced unprecedented challenges during 2008 and those challenges have driven our financial results. The housing market downturn that began in 2006 continued through 2007 and has further deteriorated in 2008. The market continues to experience declines in new and existing home sales, mortgage originations and home prices, as well as increases in inventories of unsold homes, mortgage delinquencies, defaults and foreclosures. Growth in U.S. residential mortgage debt outstanding slowed to an estimated annual rate of 2.9% based on the first three months of 2008, compared with an estimated annual rate of 8.0% based on the first three months of 2007. We estimate that home prices declined by 0.6% on a national basis during the second quarter of 2008, which translates to an 8% total national decline since the beginning of the downturn in the second quarter of 2006. We have seen more severe declines in certain states, such as California, Florida, Nevada and Arizona, which have experienced home price declines of 24% or more since their 2006 peaks. While we continue to expect home price declines in 2008 to be within our estimated 7% to 9% range, and peak-to-trough home price declines to be within our estimated 15% to 19% range, we see the trend moving toward the high end of those ranges, driven in particular by higher home price declines in certain regions.

Summary of Our Financial Results for the Second Quarter of 2008

The challenges experienced in the housing and mortgage markets during 2008 have impacted our financial results. For the second quarter of 2008, we recorded a net loss of $2.3 billion and a diluted loss per share of $2.54, compared with a net loss of $2.2 billion and a diluted loss per share of $2.57 for the first quarter of 2008. We recorded net income of $1.9 billion and diluted earnings per share of $1.86 for the second quarter of 2007. The $114 million increase in our net loss for the second quarter of 2008 compared with the first quarter of 2008 was driven principally by credit-related expenses. During the quarter, net deferred tax assets increased by $2.8 billion from $17.8 billion at March 31, 2008 to $20.6 billion at June 30, 2008, due primarily to the increase in our combined loan loss reserves. As we have continued to serve the market, we have seen growth in our book of business and market share since December 31, 2007. Our mortgage credit book of business increased to $3.0 trillion as of June 30, 2008, up from $2.9 trillion as of December 31, 2007. Our estimated market share of new single-family mortgage-related securities issuances remains high at approximately 45.4% for the second quarter of 2008, compared with an estimated 50.1% in the first quarter, and an estimated 27.9% for the second quarter of 2007.

We provide a more detailed discussion of key factors affecting changes in our results of operations and financial condition in Consolidated Results of Operations, Business Segment Results, Consolidated Balance Sheet Analysis, Supplemental Non-GAAP Information Fair Value Balance Sheets, and Risk Management Credit Risk Management Mortgage Credit Risk Management Mortgage Credit Book of Business.

Market Events of July 2008

In mid-July, following the close of the second quarter, liquidity and trading levels in the capital markets became extremely volatile, and the functioning of the markets was disrupted. The market value of our common stock dropped rapidly, to its lowest level since October 1990, and we experienced reduced demand for our unsecured debt and MBS products. This market disruption caused a significant increase in our cost of funding and a substantial increase in

mark-to-market losses on our trading securities arising from a significant widening of credit spreads. In addition, during July, credit performance continued to deteriorate, and we recorded charge-offs and foreclosed property expenses that were higher than we had experienced in any month during the second quarter and higher than we expected, driven by higher defaults and higher loan loss

severities in markets most affected by the steep home price declines. Greater credit losses in July not only reduce our July net income through our actual realized losses, but also affect us as we expect that we will need to make further increases to our combined loss reserves in the second half of 2008 to incorporate our experience in July.

Credit

As noted above, the housing and mortgage market downturn negatively impacted us in the second quarter. Our quarterly default rate increased from 12 basis points in the first quarter of 2008 to 14 basis points in the second quarter of 2008, with particular acceleration in defaults from states, such as California, Arizona, Nevada and Florida, and certain vintages (2006 and 2007) that carry a higher than average unpaid principal balance. Average initial charge-off severity has also increased, with our average initial charge-off severity rate increasing from 19% in the first quarter of 2008 to 23% in the second quarter of 2008. Increases in our default and initial charge-off severity rates are both driven primarily by losses on our Alt-A loans in markets most affected by the steep home price declines. The deterioration in the credit performance of our higher risk loans is especially pronounced in our Alt-A mortgage book, with particular pressure on loans with layered risk, such as loans with subordinate financing and interest-only payment terms. As of June 30, 2008, our Alt-A mortgage loans represented approximately 11% of our total single-family mortgage credit book of business, and accounted for 49% of our credit losses for the second quarter of 2008.

Because we use our most recent actual experience to make projections, we are incorporating the July events described above into our current forecasts. In light of our experience during the second quarter and our credit performance in July, we are increasing our forecast for our credit loss ratio (which excludes SOP 03-3 and HomeSaver Advance™ fair value losses) to 23 to 26 basis points for 2008, as compared with our previous guidance of 13 to 17 basis points. We continue to anticipate that our credit loss ratio will increase further in 2009 compared with 2008. We also expect significant additions to our combined loss reserves through the remainder of 2008. Finally, while we expect that 2008 will be our peak year for credit-related expenses as we build our combined loss reserves in anticipation of charge-offs we expect to incur in 2009 and 2010, the total amount of credit-related expenses will be significant in 2009.

One significant offset to credit-related expenses is the revenue we earn. We have two main sources of revenue: the guaranty fee income we generate over time from our existing guaranty book of business and from new guaranty business, and the net interest income we earn on the assets we hold in our portfolio. We generated $7.7 billion of revenue in the first half of 2008 and expect to generate revenues in the second half of the year similar to those generated in the first half of the year.

In light of continued deterioration in credit performance, we have been, and are continuing, to take steps designed to mitigate our credit losses. During the second quarter, we took a variety of steps to address credit losses using a variety of tools.

Underwriting Changes. We have continued to review and revise our underwriting standards through eligibility changes, including those implemented through our most recent release of DesktopUnderwriter®, which tightens existing standards. These revisions have resulted in a significant reduction in the volume of the types of loans that currently represent a majority of our credit losses. Effective January 1, 2009, we are discontinuing the purchase of newly originated lender-channel Alt-A loans. In addition, we will continue to review our underwriting standards and may in the future make additional changes as necessary to reflect future changes in the market.

Workout Rates of Delinquent Loans. We have increased our workout rate from approximately 50% of problem loans in 2007 to 56% in the first half of the year. We are targeting a workout ratio goal of 60% by the end of the year, reflecting a substantial expansion of our loss mitigation activities, personnel and initiatives.

Review of Defaulted Loans. We have increased efforts to pursue recoveries from lenders, focusing especially on our Alt-A book, by expanding loan reviews in cases where we incurred a loss or

could incur a loss due to fraud or improper lending practices. We expect this effort is likely to increase our recoveries in 2008 and 2009.

REO Inventory Management. As our foreclosure rates have increased, our inventory of REO properties has increased. We are enhancing our REO inventory management capabilities by opening offices in the hardest hit regions, such as California and Florida, and increasing our local resources devoted to property management and sales efforts. We have expanded our network of firms to assist in property disposition to ensure we have adequate capacity to sell the additional properties we expect to acquire through foreclosure. Finally, we are evaluating various proposals we have received from third parties involving the sale of properties in bulk transactions.

In addition to these specific activities, we are continuing to develop strategies designed to mitigate the increase in our credit losses. We have formed a multi-disciplinary team in credit risk, operations and financial management devoted to supporting loss mitigation and foreclosure prevention and have significantly increased the level of internal management and staff resources engaged in that effort.

For a further description of our credit risk management, refer to Consolidated Results of Operations Credit-Related Expenses and Risk Management Credit Risk Management Mortgage Credit Risk Management.

Capital

As noted above, the market conditions that we experienced during the second quarter were more negative than we anticipated, and that trend accelerated in July. Our core capital as of June 30, 2008 was $47.0 billion, $14.3 billion above our statutory minimum capital requirement and $9.4 billion above our regulator-directed 15% surplus requirement. We currently expect that we will remain above our regulatory capital requirement for the remainder of 2008. (Our regulatory capital requirement is equal to our statutory minimum capital requirement plus any additional surplus above that statutory minimum that we expect our regulator will require us to hold.) Due to the volatile market conditions, we now have less visibility into our capital position in 2009. We currently have internally prepared scenarios, derived from our own statistical models and management s judgment, that indicate that we will remain above our regulatory capital requirement through 2009, and others that show that we may not. There are a variety of current uncertainties that make estimates for 2009 challenging, including:

- the credit performance of the loans in our mortgage credit book of business;
- the pace at which we realize credit losses;
- the impact of the recently passed housing legislation, and the timing of that impact;
- the amount and pace of home price declines;
- the impact of other factors, such as unemployment rates and energy prices, on overall economic conditions and borrower behavior;
- the amount of impairments we are required to take on our securities;
- the impact of credit spreads on mark-to-market values;
- changes in state laws and judicial actions with respect to foreclosure;
- the cost of our funding;

the amount of mortgage insurance claims that are paid;

the ability to recover our deferred tax asset;

the amount of revenue we generate; and

the inter-relationship among and between these factors in the current mortgage market.

For more information regarding risks to our business that may impact performance and capital levels, refer to Part II Item 1A Risk Factors.

Our capital position, and whether we are classified as adequately capitalized for regulatory purposes, also depends on the level of capital we are required to hold by our regulator. In May 2008, the Office of Federal Housing Enterprise Oversight (OFHEO) indicated its intention to reduce our capital surplus requirement by five percentage points to a 10% surplus requirement in September 2008, based upon our continued maintenance of excess capital well above OFHEO s regulatory requirement and no material adverse change to our ongoing regulatory compliance. Under the recently enacted Federal Housing Finance Regulatory Reform Act of 2008 (the Regulatory Reform Act), our new regulator, the Federal Housing Finance Authority (FHFA), has new authority to increase our regulatory capital requirement pursuant to a formal rulemaking process and consultation with the Chairman of the Board of Governors of the Federal Reserve System, but we do not yet know what those capital levels will be. In addition, OFHEO has recently finalized rules modifying our regulatory risk-based capital stress test which will be applied beginning with the third quarter of 2008. The uncertainties that make 2009 estimates challenging also impact the calculation of this requirement, adding additional uncertainty to the regulatory requirements for capital. We are in ongoing dialogue with our regulator regarding our capital position. For more information regarding our regulatory capital requirements, including the newly finalized risk-based capital requirements, refer to Liquidity and Capital Management Capital Management Regulatory Capital Requirements.

In light of volatile market conditions, it is critical that we manage our capital levels to maintain a capital cushion well in excess of our regulatory capital requirement. To that end, we use strategies designed to preserve and protect our capital. In addition, we may, from time to time, raise capital opportunistically. Management continues to carefully monitor our capital and dividend positions and the trends impacting those positions and, if necessary, intends to take actions designed to help mitigate the impacts of a worsening environment on those positions. In this environment, conditions that negatively impact capital can develop rapidly and are based on a variety of factors. Therefore, we may need to take action quickly to respond.

We have already begun to take some of those actions. Today, the Board of Directors announced that the company is decreasing the dividend on our common stock to five cents per share. On August 4, 2008, we announced an increase in our guaranty fee pricing on new acquisitions commensurate with the risks in the current market. We are also prudently managing the size of our balance sheet. Finally, we are evaluating our costs and expenses and expect to reduce ongoing operating costs by 10% by year end 2009. Additional steps we could take include: reducing or eliminating our dividends; slowing growth; decreasing the size of the balance sheet; further raising guaranty fees; and raising additional capital (which could be dilutive). Some of these actions could have negative consequences, including decreased revenue due to growth limitations, or increased mark-to-market charges associated with the decreased liquidity for mortgage assets that could arise from a reduction in our market activity. If our capital fails to meet standards set by our regulator, our regulator could require us to enter into a capital restoration plan or take other actions. As discussed below, the U.S. Treasury is authorized to buy Fannie Mae s debt, equity and other securities, subject to our agreement.

For more information regarding our capital management, including our recent capital raises, refer to Liquidity and Capital Management Capital Management Capital Activity Capital Management Actions. For more information regarding our capital measures, refer to Notes to the Condensed Consolidated Financial Statements Note 15, Regulatory Capital Requirements.

Legislative and Regulatory Actions

On July 30, 2008, President Bush signed into law the Housing and Economic Recovery Act of 2008 that included GSE regulatory reform legislation. The legislation, which is described in more detail in Legislation Relating to Our

Regulatory Framework, establishes FHFA as our new safety, soundness and mission regulator, replacing OFHEO and the U.S. Department of Housing and Urban Development (HUD) for this purpose.

In general, the legislation strengthens the existing safety and soundness oversight of the GSEs, providing FHFA with safety and soundness authority that is comparable to and in some respects broader than that of the

federal bank regulatory agencies. For example, FHFA will have enhanced powers to raise capital levels above statutory minimum levels, to regulate the size and content of our portfolio, and to approve new mortgage products. The legislation also increases the financial and administrative cost of our affordable housing mission.

In addition, the legislation includes provisions that were initially proposed by Treasury Secretary Henry Paulson, Jr. on July 13, 2008. These provisions:

Authorize U.S. Treasury to buy Fannie Mae s debt, equity and other securities, subject to our agreement; and

Give the Chairman of the Board of Governors of the Federal Reserve System a consultative role in our regulator s process for setting capital requirements and other safety and soundness standards.

Both provisions lapse at the end of 2009.

For a further description of the new legislation, including a discussion of its potential impact on us, refer to Legislation Relating To Our Regulatory Framework and Part II Item 1A Risk Factors.

LEGISLATION RELATING TO OUR REGULATORY FRAMEWORK

The Regulatory Reform Act was signed into law by President Bush on July 30, 2008, and became effective immediately. The legislation establishes FHFA as an independent agency with general supervisory and regulatory authority over Fannie Mae, Freddie Mac, and the 12 Federal Home Loan Banks. FHFA assumes the duties of our former regulators, OFHEO and HUD, with respect to safety, soundness and mission oversight of Fannie Mae and Freddie Mac. We expect that our new regulator will implement the various provisions of the legislation over the next several months, generally though rulemaking. In general, we remain subject to existing regulations, orders and determinations until new ones are issued or made. Refer to Item 1. Business Our Charter and Regulation of Our Activities in our 2007 Form 10-K for a description of our regulation prior to enactment of this legislation.

Safety and Soundness Provisions

Capital. The legislation provides significant new authority to FHFA with respect to our risk-based and minimum capital requirements. FHFA has broad authority to establish risk-based capital standards for us and Freddie Mac to ensure that we operate in a safe and sound manner and maintain sufficient capital and reserves. FHFA also has broad authority to increase the level of our required minimum capital and to establish capital or reserve requirements for specific products and activities, so as to ensure that we operate in a safe and sound manner.

Portfolio. The legislation requires FHFA to establish standards governing our portfolio holdings, to ensure that they are backed by sufficient capital and consistent with our mission and safe and sound operations. The legislation further requires FHFA to monitor our portfolio and, in some circumstances, authorizes FHFA to require us to dispose of or acquire assets.

Prudential Standards. The legislation requires FHFA to establish prudential management and operations standards, including standards for internal controls, risk management, and investments and acquisitions.

Prompt Corrective Action. The legislation strengthens FHFA s prompt corrective action authority, including its discretionary authority to change our capital classification under certain circumstances and to restrict our growth and activities if we are not adequately capitalized.

Conservatorship and Receivership. The legislation provides FHFA new authority to place us into receivership, and enhanced authority to place us into conservatorship, based on certain specified grounds. Further, FHFA must place us into receivership if it determines that our debts have exceeded our assets for 60 days, or we have not been paying our debts as they become due for 60 days.

Enforcement Powers. The legislation provides FHFA with enhanced enforcement powers, including greater cease-and-desist authority and increased civil monetary penalties, and new authority to suspend or remove directors and management.

Mission Provisions

Products and Activities. The legislation requires us, with some exceptions, to obtain the approval of FHFA before we initially offer a product. The process for obtaining FHFA s approval includes a 30-day public notice and comment period relating to the product. A product may be approved only if it is authorized by our charter, in the public interest, and consistent with the safety and soundness of the enterprise and the mortgage finance system. We must provide written notice to FHFA before commencing any new activity.

Affordable Housing Allocations. The legislation requires us and Freddie Mac to make annual allocations to fund government affordable housing programs, based on the dollar amount of our total new business purchases, at the rate of 4.2 basis points per dollar. If this requirement had been in effect in 2007, our contribution for that year would have been approximately $300 million. For the first three years, a diminishing portion (100%, 50%, 25%) of our allocation will be used to pay for the Federal Housing Administration s (FHA) HOPE for Homeowners Program. The legislation requires FHFA to temporarily suspend our allocation upon finding that it: is contributing or would contribute to our financial instability; is causing or would cause us to be classified as undercapitalized; or is preventing or would prevent us from successfully completing a capital restoration plan. FHFA must issue regulations prohibiting us from redirecting the cost of our allocations, through increased charges or fees, or decreased premiums, or in any other manner, to the originators of mortgages that we purchase or securitize.

Affordable Housing Goals and Duty to Serve. The legislation restructures our affordable housing goals and creates a new duty for us and Freddie Mac to serve three underserved markets manufactured housing, affordable housing preservation, and rural housing. With respect to these markets, we are required to provide leadership to the market in developing loan products and flexible underwriting guidelines to facilitate a secondary market for mortgages for very low-, low-, and moderate-income families. Both the restructured goals and the new duty to serve take effect in 2010. The legislation provides that the housing goals established by HUD for 2008 will remain in effect for 2009, except that by April 2009, FHFA must review the 2009 goals to determine their feasibility given the market conditions current at such time and, after seeking public comment for up to 30 days, FHFA may make appropriate adjustments to the 2009 goals consistent with such market conditions.

Temporary Provisions

Enhanced Authority of U.S. Treasury to Purchase GSE Securities. The Secretary of the Treasury has long had authority to purchase up to $2.25 billion in our obligations. The legislation provides the Secretary of the Treasury with additional temporary authority to purchase our obligations and other securities on terms that the Secretary may determine, subject to our agreement. This expanded authority expires on December 31, 2009. To exercise this authority, the Secretary must determine that such a purchase is necessary to provide stability to the financial markets, prevent disruptions in the availability of mortgage finance, and protect taxpayers. In connection with exercising this authority, the Secretary must consider: the need for preferences or priorities regarding payments to the government; limits on maturity or disposition of obligations or securities to be purchased; the company s plan for orderly resumption of private market funding or capital market access; the probability of our fulfilling the terms of the obligations or other securities, including repayment; the need to maintain our status as a private shareholder-owned company; and restrictions on the use of our resources, including limitations on the payment of dividends and executive compensation.

Consultation with the Federal Reserve. Until December 31, 2009, our regulator must consult with the Chairman of the Board of Governors of the Federal Reserve on risks posed by the GSEs to the financial system before taking certain regulatory actions such as issuance of regulations regarding capital or portfolio, or appointment of a conservator or receiver.

Other Provisions

Conforming Loan Limits. The legislation permanently increases our conforming loan limit in high cost areas, to the lower of 115% of the median home price for comparable properties in the area, or 150% of the otherwise applicable loan limit (currently $625,500). This provision takes effect on January 1, 2009, upon expiration of the loan limit provisions contained in the Economic Stimulus Act of 2008.

SEC Registration. The legislation provides that no class of equity securities of Fannie Mae or Freddie Mac shall be treated as exempted securities for purposes of section 12, 13, 14, or 16 of the Securities Exchange Act of 1934. (Fannie Mae voluntarily registered its common stock with the U.S. Securities and Exchange Commission (SEC) on March 31, 2003. We registered our preferred stock on July 29, 2008, in accordance with the legislation.)

Executive Compensation. FHFA may at any time review the reasonableness of executive compensation, and may prohibit payment to the officer during such review. In addition, FHFA is authorized to prohibit or limit certain golden parachute and indemnification payments to directors, officers, and certain other parties. Until December 31, 2009, FHFA shall have the power to approve, disapprove or modify executive compensation.

Board of Directors. The legislation eliminates the five presidential appointees from our board of directors, and provides that our board shall consist of 13 persons elected by the shareholders, or such other number as the Director of FHFA determines appropriate. The legislation leaves in place the requirement that our board shall at all times have as members at least one person from the homebuilding, mortgage lending, and real estate industries, and at least one person from an organization representing consumer or community interests or one person who has demonstrated a career commitment to the provision of housing for low-income households.

For a description of how this GSE regulatory reform legislation could materially adversely affect our business and earnings, see Part II Item 1A Risk Factors of this report.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with generally accepted accounting principles (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 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 have identified the following as our most critical accounting policies and estimates:

Fair Value of Financial Instruments

Other-than-temporary Impairment of Investment Securities

Allowance for Loan Losses and Reserve for Guaranty Losses

Deferred Tax Assets

We describe below significant changes in the judgments and assumptions we made during the first six months of 2008 in applying our critical accounting policies and estimates. Also see Part II Item 7 MD&A Critical Accounting Policies and Estimates of our 2007 Form 10-K for additional information about our critical accounting policies and estimates.

Fair Value of Financial Instruments

We adopted SFAS No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes a framework for measuring fair value and outlines a fair value hierarchy based on the inputs to valuation techniques used to measure fair value, effective January 1, 2008. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (also referred to as an exit price). SFAS 157 categorizes fair value measurements into a three-level hierarchy based on the extent to which the measurement relies on observable

market inputs in measuring fair value. Level 1, which is the highest priority in the fair value hierarchy, is based on unadjusted quoted prices in active markets for identical assets or liabilities. Level 2 is based on observable market-based inputs, other than quoted prices, in active markets for identical assets or liabilities. Level 3, which is the lowest priority in the fair value hierarchy, is based on unobservable inputs. Assets and liabilities are classified within this hierarchy in their entirety based on the lowest level of any input that is significant to the fair value measurement.

The use of fair value to measure our financial instruments is fundamental to our financial statements and is a critical accounting estimate because a substantial portion of our assets and liabilities are recorded at estimated fair value. The majority of our financial instruments carried at fair value fall within the level 2 category and are valued primarily utilizing inputs and assumptions that are observable in the marketplace, can be derived from observable market data or corroborated by observable levels at which transactions are executed in the marketplace. Because items classified as level 3 are generally based on unobservable inputs, the process to determine fair value is generally more subjective and involves a high degree of management judgment and assumptions. These assumptions may have a significant effect on our estimates of fair value, and the use of different assumptions as well as changes in market conditions could have a material effect on our results of operations or financial condition. We provide additional information regarding our level 3 assets below.

Fair Value Hierarchy Level 3 Assets

Level 3 is primarily comprised of financial instruments whose fair value is estimated based on valuation methodologies utilizing significant inputs and assumptions that are generally less observable because of limited market activity or little or no price transparency. We typically classify financial instruments as level 3 if the valuation is based on inputs from a single source, such as a dealer quotation, where we are not able to corroborate the inputs and assumptions with other available, relevant market information. Our level 3 financial instruments include certain mortgage- and asset-backed securities and residual interests, certain performing residential mortgage loans, non-performing mortgage-related assets, our guaranty assets and buy-ups, our master servicing assets and certain highly structured, complex derivative instruments.

Some of our financial instruments, such as our trading and available-for-sale (AFS) securities and our derivatives, are measured at fair value on a recurring basis in periods subsequent to initial recognition. We measure some of our other financial instruments at fair value on a non-recurring basis in periods subsequent to initial recognition, such as held-for-sale mortgage loans. Table 1 presents, by balance sheet category, the amount of financial assets carried in our condensed consolidated balance sheets at fair value on a recurring basis and classified as level 3 as of June 30, 2008. We also identify the types of financial instruments within each asset category that are based on level 3 measurements and describe the valuation techniques used for determining the fair value of these financial instruments. 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 financial instruments carried at fair value on a recurring basis and classified as level 3 to vary each period.

Table 1: Level 3 Recurring Assets at Fair Value

	As of June 30, 2008	
Balance Sheet Category	**Estimated Fair Value (Dollars in millions)**	**Description and Valuation Technique**
Trading securities	$ 14,325	Primarily consists of mortgage-related securities backed by Alt-A loans and subprime loans. We generally have estimated the fair value based on the use of average prices obtained from multiple pricing services. In the absence of such information or if we are not able to corroborate these prices by other available, relevant market information, we estimate the fair value based on broker or dealer quotations or using internal calculations that incorporate inputs that are implied by market prices for similar securities and structure types. These inputs may be adjusted for various factors, such as prepayment speeds and credit spreads.
AFS securities	40,033	Primarily consists of mortgage-related securities backed by Alt-A loans and subprime loans and mortgage revenue bonds. The valuation techniques are the same as those noted above for trading securities.
Derivatives assets	270	Primarily consists of a limited population of certain highly structured, complex interest rate risk management derivatives. Examples include certain swaps with embedded caps and floors that reference non-standard indexes. We determine the fair value of these derivative instruments using indicative market prices obtained from large, experienced dealers. Indicative market prices from a single source that cannot be corroborated are classified as level 3.
Guaranty assets and buy-ups	1,947	Represents the present value of the estimated compensation we expect to receive for providing our guaranty related to portfolio securitization transactions. We generally estimate the fair value based on internal models that calculate the present value of expected cash flows. Key model inputs and assumptions include prepayment speeds, forward yield curves and discount rates that are commensurate with the level of

estimated risk.

Level 3 recurring assets	$ 56,575
Total assets	$ 885,918
Total recurring assets measured at fair value	$ 347,748
Level 3 recurring assets as a percentage of total assets	6%
Level 3 recurring assets as a percentage of total recurring assets measured at fair value	16%
Total recurring assets measured at fair value as a percentage of total assets	39%

Level 3 recurring assets totaled $56.6 billion, or 6% of our total assets, as of June 30, 2008, compared with 7% of our total assets as of March 31, 2008. The balance of level 3 recurring assets increased by $451 million and $15.3 billion for the second quarter and first six months of 2008, respectively. These level 3 balance increases were principally driven by an increase in the portion of mortgage assets for which there is a lack of market liquidity and limited availability of external pricing data, resulting in transfers of these assets from level 2 to level 3. These transfers reflect the ongoing effects of the significant disruption in the mortgage market and severe reduction in market liquidity for certain mortgage products, such as private-label mortgage-related securities backed by Alt-A loans or subprime loans. Because of the reduction in recently executed transactions and market price quotations for these instruments, the market inputs for these instruments are less observable.

Financial assets measured at fair value on a non-recurring basis and classified as level 3, which are not presented in the table above, include held-for-sale (HFS) loans that are measured at lower of cost or market and that were written down to fair value as of the end of the period. The fair value of these loans totaled $812 million as of June 30, 2008. In addition, certain financial assets measured at cost that have been written down to fair value during the period due to impairment are classified as non-recurring. The fair value of these level 3 non-recurring financial assets, which primarily consisted of certain guaranty assets and acquired property, totaled $8.2 billion as of June 30, 2008. Financial liabilities measured at fair value on a recurring basis and classified as level 3 as of June 30, 2008 consisted of long-term debt with a fair value of $3.3 billion and derivatives liabilities with a fair value of $107 million. See Notes to Condensed Consolidated Financial Statements Note 17, Fair Value of Financial Instruments for further information regarding SFAS 157, including the classification within the three-level hierarchy of all of our assets and liabilities carried in our condensed consolidated balance sheet at fair value as of June 30, 2008.

Fair Value Control Processes

We employ control processes to validate the fair value of our financial instruments. These control processes are designed to ensure that the values used for financial reporting are based on observable inputs wherever possible. If observable market-based inputs are not available, the control processes are designed to ensure that the valuation approach used is appropriate and consistently applied and that the assumptions are reasonable. Our control processes provide for segregation of duties and oversight of our fair value methodologies and valuations by our Valuation Oversight Committee. Valuations are performed by personnel independent of our business units. A price verification group reviews selected valuations and compares the valuations to alternative external market data (*e.g.,* quoted market prices, broker or dealer quotations, pricing services, recent trading activity and comparative analyses to similar instruments) for reasonableness. The price verification group also performs independent reviews of the assumptions used in determining the fair value of products with material estimation risk for which observable market-based inputs do not exist. Valuation models are regularly reviewed and approved for use for specific products by the Chief Risk Office, which also is independent from our business units. Any changes to the valuation methodology or pricing are reviewed by the Valuation Oversight Committee to confirm the changes are appropriate.

We continue to refine our valuation methodologies as markets and products develop and the pricing for certain products becomes more or less transparent. While we believe our valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a materially different estimate of fair value as of the reporting date.

Change in Measuring the Fair Value of Guaranty Obligations

Beginning January 1, 2008, as part of the implementation of SFAS 157, we changed our approach to measuring the fair value of our guaranty obligations. Specifically, we adopted a measurement approach that is based upon an estimate of the compensation that we would require to issue the same guaranty in a standalone arm s-length transaction with an unrelated party. When we initially recognize a guaranty issued in a lender swap transaction after December 31, 2007, we measure the fair value of the guaranty obligation based on the fair value of the total compensation we receive, which primarily consists of the guaranty fee, credit enhancements, buy-downs, risk-based price adjustments and our right to receive interest income during the float period in excess of the amount required to compensate us for master servicing. Because the fair value of those guaranty obligations now equals the fair value of the total compensation we receive, we do not recognize losses or record deferred profit in our financial statements at inception of those guaranty contracts issued after December 31, 2007.

We also changed how we measure the fair value of our existing guaranty obligations, as disclosed in Supplemental Non-GAAP Information Fair Value Balance Sheets and in Notes to Condensed Consolidated Financial Statements, to be consistent with our new approach for measuring guaranty obligations at initial recognition. The fair value of all

guaranty obligations measured after their initial recognition represents our estimate of a hypothetical transaction price we would receive if we were to issue

our guarantees to an unrelated party in a standalone arm s-length transaction at the measurement date. To measure this fair value, we continue to use the models and inputs that we used prior to our adoption of SFAS 157 and calibrate those models to our current market pricing.

Prior to January 1, 2008, we measured the fair value of the guaranty obligations that we recorded when we issued Fannie Mae MBS based on market information obtained from spot transaction prices. In the absence of spot transaction data, which was the case for the substantial majority of our guarantees, we used internal models to estimate the fair value of our guaranty obligations. We reviewed the reasonableness of the results of our models by comparing those results with available market information. Key inputs and assumptions used in our models included the amount of compensation required to cover estimated default costs, including estimated unrecoverable principal and interest that we expected to incur over the life of the underlying mortgage loans backing our Fannie Mae MBS, estimated foreclosure-related costs, estimated administrative and other costs related to our guaranty, and an estimated market risk premium, or profit, that a market participant of similar credit standing would require to assume the obligation. If our modeled estimate of the fair value of the guaranty obligation was more or less than the fair value of the total compensation received, we recognized a loss or recorded deferred profit, respectively, at inception of the guaranty contract. See Part II Item 7 MD&A Critical Accounting Policies and Estimates Fair Value of Guaranty Assets and Guaranty Obligations Effect on Losses on Certain Guaranty Contracts of our 2007 Form 10-K for additional information.

The accounting for our guarantees in our condensed consolidated financial statements is unchanged with our adoption of SFAS 157. Accordingly, the guaranty obligation amounts recorded in our condensed consolidated balance sheets attributable to guarantees issued prior to January 1, 2008 will continue to be amortized in accordance with our established accounting policy. This change, however, affects how we determine the fair value of our existing guaranty obligations as of each balance sheet date. See Supplemental Non-GAAP Information Fair Value Balance Sheets and Notes to Condensed Consolidated Financial Statements for additional information regarding the impact of this change.

Deferred Tax Assets

We recognize deferred tax assets and liabilities for the future tax consequences related to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and for tax credits. Our net deferred tax assets totaled $20.6 billion and $13.0 billion as of June 30, 2008 and December 31, 2007, respectively. We evaluate our deferred tax assets for recoverability based on available evidence, including assumptions about future profitability. We are required to establish a valuation allowance for deferred tax assets and record a charge to income if we determine, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets will not be realized. Such a charge likely would have a material adverse effect on our results of operations, financial condition and capital position. In evaluating the need for a valuation allowance, we estimate future taxable income based on management approved business plans and ongoing tax planning strategies. This process involves significant management judgment about assumptions that are subject to change from period to period based on changes in tax laws or variances between our future projected operating performance and our actual results. Accordingly, we have included the assessment of a deferred tax asset valuation allowance as a critical accounting policy.

We are in a cumulative book taxable loss position as of the three-year period ended June 30, 2008. The realization of our deferred tax assets is dependent upon the generation of sufficient future taxable income. For purposes of establishing a deferred tax valuation allowance, this cumulative book taxable loss position is considered significant, objective evidence that we may not be able to realize some portion of our deferred tax assets in the future. In assessing the nature of our cumulative book taxable loss position, we evaluated the factors contributing to these losses and analyzed whether these factors were temporary or indicative of a permanent decline in our earnings. We determined that our current cumulative book taxable loss position was caused primarily by an increase in our credit losses due to

the current housing and credit market conditions. Prior to 2007, we had generated pre-tax book income for over 20 consecutive years. Based on our forecasts of future taxable income, which include assumptions about the depth and severity of home price depreciation and credit losses, we anticipate that it is more likely than not that our results of future operations will generate sufficient taxable income to allow us to realize our deferred tax assets. Therefore, we did not record a valuation allowance against our net deferred tax assets as of June 30, 2008 or December 31, 2007.

Although current market conditions have created significant volatility in our pre-tax book income, our current forecasts of future taxable income reflect sufficient taxable income in future periods to realize our deferred tax assets based on the nature of our book-to-tax differences and the stability of our core business model. Included in our forecasts are credit assumptions regarding our estimate of future expected credit losses, which we believe is the most variable component of our current forecasts of future taxable income. If future events differ from our current forecasts, a valuation allowance may need to be established, which likely would have a material adverse effect on our results of operations, financial condition and capital position. We will continue to update our assumptions and forecasts of future taxable income and assess the need for a valuation allowance.

We provide additional detail on the components of our deferred tax assets and deferred tax liabilities as of December 31, 2007 in our 2007 Form 10-K in Notes to Consolidated Financial Statements Note 11, Income Taxes and we provide information on the increase in our deferred tax assets since December 31, 2007 in Notes to Condensed Consolidated Financial Statements Note 10, Income Taxes of this report.

CONSOLIDATED RESULTS OF OPERATIONS

The following discussion of our condensed consolidated results of operations is based on a comparison of our results between the three and six months ended June 30, 2008 and the three and six months ended June 30, 2007. Table 2 presents a summary of our unaudited condensed consolidated results of operations for each of these periods.

Table 2: Summary of Condensed Consolidated Results of Operations

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		Quarterly Variance		Year-to-Date Variance	
	2008	2007	2008	2007	$	%	$	%
	(Dollars in millions, except per share amounts)							
Net interest income	$ 2,057	$ 1,193	$ 3,747	$ 2,387	$ 864	72%	$ 1,360	57%
Guaranty fee income	1,608	1,120	3,360	2,218	488	44	1,142	51
Trust management income	75	150	182	314	(75)	(50)	(132)	(42)
Fee and other income[1]	225	257	452	534	(32)	(12)	(82)	(15)
Net revenues	**3,965**	**2,720**	**7,741**	**5,453**	**1,245**	**46**	**2,288**	**42**
Losses on certain guaranty contracts		(461)		(744)	461	100	744	100
Investment gains (losses), net[1]	(883)	(93)	(994)	202	(790)	(849)	(1,196)	(592)
Fair value gains (losses), net[1]	517	1,424	(3,860)	858	(907)	(64)	(4,718)	(550)
Losses from partnership investments	(195)	(215)	(336)	(380)	20	9	44	12
Administrative expenses	(512)	(660)	(1,024)	(1,358)	148	22	334	25
Credit-related expenses[2]	(5,349)	(518)	(8,592)	(839)	(4,831)	(933)	(7,753)	(924)
Other non-interest expenses[1][3]	(286)	(60)	(791)	(164)	(226)	(377)	(627)	(382)

Income (loss) before federal income taxes and extraordinary losses	(2,743)	2,137	(7,856)	3,028	(4,880)	(228)	(10,884)	(359)
Benefit (provision) for federal income taxes	476	(187)	3,404	(114)	663	355	3,518	3,086
Extraordinary losses, net of tax effect	(33)	(3)	(34)	(6)	(30)	(1,000)	(28)	(467)
Net income (loss)	**$ (2,300)**	**$ 1,947**	**$ (4,486)**	**$ 2,908**	**$ (4,247)**	**(218)%**	**$ (7,394)**	**(254)%**
Diluted earnings (loss) per common share	**$ (2.54)**	**$ 1.86**	**$ (5.11)**	**$ 2.72**	**$ (4.40)**	**(237)%**	**$ (7.83)**	**(288)%**

(1) Certain prior period amounts have been reclassified to conform with the current period presentation in our condensed consolidated statements of operations.

(2) Consists of provision for credit losses and foreclosed property expense.

(3) Consists of debt extinguishment gains (losses), net, minority interest in earnings of consolidated subsidiaries and other expenses.

Our business generates revenues from four principal sources: net interest income, guaranty fee income, trust management income, and fee and other income. Other significant factors affecting our results of operations include: fair value gains and losses; the timing and size of investment gains and losses; credit-related expenses; losses from partnership investments; administrative expenses and our effective tax rate. We provide a comparative discussion of the effect of our principal revenue sources and other significant items on our condensed consolidated results of operations for the three and six months ended June 30, 2008 and 2007 below.

Net Interest Income

Table 3 presents an analysis of our net interest income and net interest yield for the three and six months ended June 30, 2008 and 2007.

Table 3: Analysis of Net Interest Income and Yield

	For the Three Months Ended June 30,					
	2008			2007		
	Average Balance[1]	Interest Income/ Expense	Average Rates Earned/Paid	Average Balance[1]	Interest Income/ Expense	Average Rates Earned/Paid
	(Dollars in millions)					
Interest-earning assets:						
Mortgage loans[2]	$ 418,504	$ 5,769	5.51%	$ 390,034	$ 5,625	5.77%
Mortgage securities	318,396	4,063	5.10	325,303	4,460	5.48
Non-mortgage securities[3]	57,504	400	2.75	68,515	928	5.36
Federal funds sold and securities purchased under agreements to resell	26,869	186	2.74	15,301	205	5.31
Advances to lenders	3,332	46	5.46	6,056	48	3.12
Total interest-earning assets	$ 824,605	$ 10,464	5.07%	$ 805,209	$ 11,266	5.59%
Interest-bearing liabilities:						
Short-term debt	$ 242,453	$ 1,685	2.75%	$ 159,817	$ 2,193	5.43%
Long-term debt	550,940	6,720	4.88	611,777	7,879	5.15
Federal funds purchased and securities sold under agreements to repurchase	303	2	2.61	37	1	4.58
Total interest-bearing liabilities	$ 793,696	$ 8,407	4.23%	$ 771,631	$ 10,073	5.21%
Impact of net non-interest bearing funding	$ 30,909		0.16%	$ 33,578		0.22%
Net interest income/net interest yield[4]		$ 2,057	1.00%		$ 1,193	0.60%
Taxable-equivalent adjustment on tax-exempt investments[5]		82	0.04%		90	0.04%

Taxable-equivalent net interest income/taxable-equivalent net interest yield[6]	$ 2,139	1.04%	$ 1,283	0.64%

	For the Six Months Ended June 30,					
	2008			2007		
	Average Balance[1]	Interest Income/ Expense	Average Rates Earned/Paid	Average Balance[1]	Interest Income/ Expense	Average Rates Earned/Paid
	(Dollars in millions)					
Interest-earning assets:						
Mortgage loans[2]	$ 414,163	$ 11,431	5.52%	$ 388,095	$ 11,010	5.67%
Mortgage securities	317,107	8,207	5.18	328,288	9,027	5.50
Non-mortgage securities[3]	62,067	1,078	3.44	65,355	1,764	5.37
Federal funds sold and securities purchased under agreements to resell	31,551	579	3.63	14,484	387	5.31
Advances to lenders	3,780	111	5.81	5,159	84	3.24
Total interest-earning assets	$ 828,668	$ 21,406	5.16%	$ 801,381	$ 22,272	5.56%
Interest-bearing liabilities:						
Short-term debt	$ 249,949	$ 4,243	3.36%	$ 161,022	$ 4,406	5.44%
Long-term debt	548,244	13,411	4.89	607,399	15,475	5.10
Federal funds purchased and securities sold under agreements to repurchase	371	5	2.67	123	4	5.22
Total interest-bearing liabilities	$ 798,564	$ 17,659	4.41%	$ 768,544	$ 19,885	5.17%
Impact of net non-interest bearing funding	$ 30,104		0.16%	$ 32,837		0.21%
Net interest income/net interest yield[4]		$ 3,747	0.91%		$ 2,387	0.60%
Taxable-equivalent adjustment on tax-exempt investments[5]		165	0.04%		182	0.04%
Taxable-equivalent net interest income/taxable-equivalent net interest yield[6]		$ 3,912	0.95%		$ 2,569	0.64%

(1) For mortgage loans, average balances have been calculated based on the average of the amortized cost amounts at the beginning of the year and at the end of each month in the period. For all other categories, average balances have been calculated based on a daily average. The average balance for the three and six months ended June 30, 2008 for advances to lenders also has been calculated based on a daily average.

(2) Average balance amounts include nonaccrual loans with an average balance totaling $8.4 billion and $5.7 billion for the three months ended June 30, 2008 and 2007, respectively, and $8.3 billion and $5.9 billion for the six months ended June 30, 2008 and 2007, respectively. Interest income amounts include interest income related to

SOP 03-3 loans returned to accrual status of $168 million and $115 million for the three months ended June 30, 2008 and 2007, respectively, and of $313 million and $219 million for the six months ended June 30, 2008 and 2007, respectively. Of these amounts recognized into interest income, $53 million and $15 million for the three months ended June 30, 2008 and 2007, respectively, and $88 million and $22 million for the six months ended June 30, 2008 and 2007, respectively, related to the accretion of the fair value loss recorded upon purchase of SOP 03-3 loans.

(3) Includes cash equivalents.

(4) Net interest yield computed by dividing annualized net interest income for the period by the average balance of total interest-earning assets during the period.

(5) Represents adjustment to permit comparison of yields on tax-exempt and taxable assets calculated using a 35% marginal tax rate for each of the periods presented.

(6) Taxable-equivalent net interest yield is computed by dividing annualized taxable-equivalent net interest income for the period by the average balance of total interest-earning assets during the period.

Table 4 presents the total variance, or change, in our taxable-equivalent net interest income between the three and six months ended June 30, 2008 and 2007, 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 4: Rate/Volume Analysis of Net Interest Income

	For the Three Months Ended June 30, 2008 vs. 2007			For the Six Months Ended June 30, 2008 vs. 2007		
	Total	Variance Due to:[1]		Total	Variance Due to:[1]	
	Variance	Volume	Rate	Variance	Volume	Rate
	(Dollars in millions)					
Interest income:						
Mortgage loans[2]	$ 144	$ 399	$ (255)	$ 421	$ 725	$ (304)
Mortgage securities	(397)	(93)	(304)	(820)	(301)	(519)
Non-mortgage securities[3]	(528)	(131)	(397)	(686)	(85)	(601)
Federal funds sold and securities purchased under agreements to resell	(19)	109	(128)	192	343	(151)
Advances to lenders	(2)	(28)	26	27	(27)	54
Total interest income	(802)	256	(1,058)	(866)	655	(1,521)
Interest expense:						
Short-term debt	(508)	848	(1,356)	(163)	1,886	(2,049)
Long-term debt	(1,159)	(756)	(403)	(2,064)	(1,464)	(600)
Federal funds purchased and securities sold under agreements to repurchase	1	1		1	4	(3)
Total interest expense	(1,666)	93	(1,759)	(2,226)	426	(2,652)
Net interest income	864	$ 163	$ 701	1,360	$ 229	$ 1,131
Taxable-equivalent adjustment on tax-exempt investments[3]	(8)			(17)		
Taxable-equivalent net interest income	$ 856			$ 1,343		

(1) Combined rate/volume variances are allocated to both rate and volume based on the relative size of each variance.

(2) Refer to footnote 2 in Table 3.

(3) Represents adjustment to permit comparison of yields on tax-exempt and taxable assets calculated using a 35% marginal tax rate for each of the periods presented.

Taxable-equivalent net interest income of $2.1 billion for the second quarter of 2008 increased by 67% from the second quarter of 2007, driven by a 63% (40 basis points) expansion of our taxable-equivalent net interest yield to 1.04% and a 2% increase in our average interest-earning assets. Taxable-equivalent net interest income of $3.9 billion for the first six months of 2008 increased by 52% from the first six months of 2007, driven by a 48% (31 basis points) expansion of our taxable-equivalent net interest yield to 0.95% and a 3% increase in our average interest-earning assets.

The increase in our taxable-equivalent net interest income and net interest yield for the second quarter and first six months of 2008 was mainly driven by the reduction in short-term borrowing rates, which reduced the average cost of our debt, and wider mortgage-to-debt spreads on acquisitions. Also contributing to the lower cost of funds was the redemption of step-rate debt securities, which provided an annualized benefit to our net interest yield of approximately 4 basis points and 11 basis points for the second quarter and first six months of 2008, respectively. Instead of having a fixed coupon for the life of the security, step-rate debt securities allow for the interest rate to increase at predetermined rates according to a specified schedule, resulting in increased interest payments. However, the interest expense on step-rate debt securities is recognized at a constant effective rate over the term of the security. Because we redeemed these securities prior to maturity, we reversed a portion of the interest expense that we had previously accrued.

The increase in our average interest-earning assets for the second quarter and first six months of 2008 was attributable to an increase in our portfolio purchases during the first six months of 2008, particularly in the second quarter of 2008, as mortgage-to-debt spreads reached historic highs. OFHEO s reduction in our capital surplus requirement provided us with more flexibility to take advantage of opportunities to purchase mortgage assets at attractive prices and spreads.

Although we consider the periodic net contractual interest accruals on our interest rate swaps to be part of the cost of funding our mortgage investments, these amounts are not reflected in our taxable-equivalent net interest income and net interest yield. Instead, the net contractual interest accruals on our interest rate swaps are reflected in our condensed consolidated statements of operations as a component of Fair value gains (losses), net. As indicated in Table 8 below, we recorded net contractual interest expense on our interest rate swaps totaling $304 million and $330 million for the three and six months ended June 30, 2008, respectively, which had the economic effect of increasing our funding costs by approximately 15 basis points and 8 basis points for the three and six months ended June 30, 2008, respectively. We recorded net contractual interest income on our interest rate swaps of $64 million and $98 million for the three and six months ended June 30, 2007, respectively, which had the economic effect of reducing our funding costs by approximately 3 basis points for each period.

During July 2008, our cost of short-term funding as compared with the London Interbank Offered Rate (LIBOR) was less favorable than it was during the second quarter of 2008, which could result in a taxable equivalent net interest yield that is flat or lower for the remainder of 2008 depending on future market conditions. Our taxable-equivalent net interest yield may be offset, as it was during the second quarter of 2008, by accrual of higher payments on our net pay-fixed swap positions due to low short-term LIBOR rates.

Guaranty Fee Income

Table 5 shows the components of our guaranty fee income, our average effective guaranty fee rate, and Fannie Mae MBS activity for the three and six months ended June 30, 2008 and 2007.

Table 5: Guaranty Fee Income and Average Effective Guaranty Fee Rate[1]

	For the Three Months Ended June 30,				
	2008		2007		Amount
	Amount	Rate[2]	Amount	Rate[2]	Variance
	(Dollars in millions)				
Guaranty fee income/average effective guaranty fee rate, excluding certain fair value adjustments and buy-up impairment	$ 1,458	23.8bp	$ 1,104	21.2bp	32%
Net change in fair value of buy-ups and guaranty assets	152	2.5	17	0.3	794
Buy-up impairment	(2)		(1)		100
Guaranty fee income/average effective guaranty fee rate[3]	$ 1,608	26.3bp	$ 1,120	21.5bp	44%
Average outstanding Fannie Mae MBS and other guarantees[4]	$ 2,442,886		$ 2,080,676		17%
Fannie Mae MBS issues[5]	177,763		149,879		19

	For the Six Months Ended June 30,				
	2008		2007		Amount
	Amount	Rate[2]	Amount	Rate[2]	Variance
	(Dollars in millions)				
Guaranty fee income/average effective guaranty fee rate, excluding certain fair value adjustments and buy-up impairment	$ 3,177	26.4bp	$ 2,204	21.5bp	44%
Net change in fair value of buy-ups and guaranty assets	214	1.8	19	0.1	1,026
Buy-up impairment	(31)	(0.3)	(5)		520
Guaranty fee income/average effective guaranty fee rate[3]	$ 3,360	27.9bp	$ 2,218	21.6bp	51%
Average outstanding Fannie Mae MBS and other guarantees[4]	$ 2,407,296		$ 2,050,797		17%
Fannie Mae MBS issues[5]	346,355		282,302		23

(1)

Guaranty fee income primarily consists of contractual guaranty fees related to Fannie Mae MBS held in our portfolio and held by third-party investors, adjusted for (1) the amortization of upfront fees and impairment of guaranty assets, net of a proportionate reduction in the related guaranty obligation and deferred profit, and (2) impairment of buy-ups. The average effective guaranty fee rate reflects our average contractual guaranty fee rate adjusted for the impact of amortization of deferred amounts and buy-up impairment. Losses recognized at inception on certain guaranty contracts for periods prior to January 1, 2008 are excluded from guaranty fee income and the average effective guaranty fee rate; however, as described in footnote 3 below, the accretion of these losses into income over time is included in our guaranty fee income and average effective guaranty fee rate.

(2) Presented in basis points and calculated based on annualized amounts of our guaranty fee income components divided by average outstanding Fannie Mae MBS and other guarantees for each respective period.

(3) Losses recognized at inception on certain guaranty contracts for periods prior to January 1, 2008, which are excluded from guaranty fee income, are recorded as a component of our guaranty obligation. We accrete a portion of our guaranty obligation, which includes these losses, into income each period in proportion to the reduction in the guaranty asset for payments received. This accretion increases our guaranty fee income and reduces the related guaranty obligation. Effective January 1, 2008, we no longer recognize losses at inception of our guaranty contracts due to a change in our method for measuring the fair value of our guaranty obligations. Although we will no longer recognize losses at inception of our guaranty contracts, we will continue to accrete previously recognized losses into our guaranty fee income over the remaining life of the mortgage loans underlying the Fannie Mae MBS.

(4) Other guarantees includes $31.8 billion and $41.6 billion as of June 30, 2008 and December 31, 2007, respectively, and $35.3 billion and $19.7 billion as of June 30, 2007 and December 31, 2006, respectively, related to long-term standby commitments we have issued and credit enhancements we have provided.

(5) Reflects unpaid principal balance of Fannie Mae MBS issued and guaranteed by us, including mortgage loans held in our portfolio that we securitized during the period and Fannie Mae MBS issued during the period that we acquired for our portfolio.

The 44% increase in guaranty fee income for the second quarter of 2008 over the second quarter of 2007 resulted from a 17% increase in average outstanding Fannie Mae MBS and other guarantees, and a 22% increase in the average effective guaranty fee rate to 26.3 basis points from 21.5 basis points. The 51% increase in guaranty fee income for the first six months of 2008 over the first six months of 2007 resulted from a 17% increase in average outstanding Fannie Mae MBS and other guarantees, and a 29% increase in the average effective guaranty fee rate to 27.9 basis points from 21.6 basis points.

The increase in average outstanding Fannie Mae MBS and other guarantees for the second quarter and first six months of 2008 reflected the significant growth in our market share of mortgage-related securities issuances, due in large part to the disruption in the credit and mortgage markets and dramatic shift in market dynamics, including a significant reduction in the issuances of private-label mortgage-related securities.

The increase in our average effective guaranty fee rate in the second quarter and first six months of 2008 was driven primarily by the accelerated recognition of deferred amounts into income as interest rates were lower in the second quarter and first six months of 2008, relative to the level of interest rates during the comparable prior year periods. Our guaranty fee income also includes accretion of deferred amounts on guaranty contracts where we recognized losses at the inception of the contract, which totaled an estimated $127 million and $424 million for the three and six months ended June 30, 2008, compared with $91 million and $183 million for the three and six months ended June 30, 2007. See Part II Item 7 MD&A Critical Accounting Policies and Estimates of our 2007 Form 10-K for additional information on our accounting for these losses and the impact on our financial statements.

The increase in our average effective guaranty fee rate was also affected by guaranty fee pricing changes that we believe enable us to more accurately price for the current risks in the housing market. These pricing changes include an adverse market delivery charge of 25 basis points for all loans delivered to us, which became effective March 1, 2008. The impact of our guaranty fee pricing changes was partially offset by a shift in the composition of our guaranty book of business to a greater proportion of higher-quality, lower risk and lower guaranty fee mortgages, as we reduced our acquisitions of higher risk, higher fee product categories, such as Alt-A loans. Our average charged guaranty fee on new single-family business was 28.0 basis points and 26.9 basis points for the second quarter and first six months of 2008, respectively, compared with 28.2 basis points and 27.1 basis points for the second quarter and first six months of 2007, respectively. The average charged guaranty fee on our new single-family business represents the average contractual fee rate for our single-family guaranty arrangements and the recognition of any upfront cash payments ratably over an estimated life of four years.

We expect the changes in our risk assessment and eligibility criteria to continue to enhance the risk profile of our new business. We also believe that our single-family guaranty book of business will continue to grow in 2008 and 2009 at a faster rate than the overall growth in U.S. single-family mortgage debt outstanding. We recently announced new pricing changes for loans delivered to us effective October 1, 2008. The new pricing changes increase our adverse market delivery charge to 50 basis points from 25 basis points and update our standard pricing adjustments for mortgage loans with certain risk characteristics. We believe that our guaranty fee income will grow in 2008 compared with 2007 due to an increase in our guaranty business volumes and prices in 2008 compared with 2007.

Trust Management Income

Trust management income decreased to $75 million and $182 million for the second quarter and first six months of 2008, respectively, from $150 million and $314 million for the second quarter and first six months of 2007, respectively. The decrease during each period was attributable to significantly lower short-term interest rates during the first six months of 2008 relative to the first six months of 2007, which reduced the amount of float income derived from the cash flows between the date of remittance of mortgage and other payments to us by servicers and the date of

distribution of these payments to MBS certificateholders.

Fee and Other Income

Fee and other income decreased to $225 million and $452 million for the second quarter and first six months of 2008, respectively, from $257 million and $534 million for the second quarter and first six months of 2007, respectively. The decrease during each period was primarily attributable to lower multifamily fees due to a reduction in multifamily loan liquidations for the first six months of 2008.

Losses on Certain Guaranty Contracts

Effective January 1, 2008 with our adoption of SFAS 157, we no longer recognize losses or record deferred profit in our consolidated financial statements at inception of our guaranty contracts for MBS issued subsequent to December 31, 2007 because the estimated fair value of the guaranty obligation at inception now equals the estimated fair value of the total compensation received. For further discussion of this change, see Critical Accounting Policies and Estimates Fair Value of Financial Instruments Change in Measuring the Fair Value of Guaranty Obligations and Notes to Condensed Consolidated Financial Statements Note 1, Summary of Significant Accounting Policies. We recorded losses on certain guaranty contracts totaling $461 million and $744 million for the three and six months ended June 30, 2007, respectively. These losses reflected the increase in the estimated market risk premium that a market participant would require to assume our guaranty obligations due to the decline in home prices and deterioration in credit conditions.

Investment Gains (Losses), Net

We summarize the components of investment gains (losses), net for the three and six months ended June 30, 2008 and 2007 below in Table 6 and discuss significant changes in these components between periods.

Table 6: Investment Gains (Losses), Net

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Other-than-temporary impairment on AFS securities[1]	$ (507)	$	$ (562)	$ (3)
Lower-of-cost-or-market adjustments on HFS loans	(240)	(115)	(311)	(118)
Gains (losses) on Fannie Mae portfolio securitizations, net	(67)	(11)	(25)	38
Gains (losses) on sale of AFS securities, net	(20)	55	13	326
Other investment losses, net	(49)	(22)	(109)	(41)
Investment gains (losses), net	$ (883)	$ (93)	$ (994)	$ 202

(1) Excludes other-than-temporary impairment on guaranty assets and buy-ups as these amounts are recognized as a component of guaranty fee income. Refer to Table 5: Guaranty Fee Income and Average Effective Guaranty Fee Rate.

The increase in investment losses for the second quarter and first six months of 2008 over the second quarter and first six months of 2007 was primarily attributable to the following:

A significant increase in other-than-temporary impairment on AFS securities, principally for Alt-A and subprime private-label securities, reflecting a reduction in expected cash flows due to higher expected defaults and loss severties on the underlying mortgages, which resulted in the recognition of other-than-temporary impairment on these securities totaling $492 million in the second quarter of 2008.

An increase in losses resulting from lower-of-cost-or-market adjustments on HFS loans primarily, attributable to higher interest rates during the second quarter of 2008.

A decrease in gains on the sale of AFS securities, net. The investment gains recorded during the first six months of 2007 were attributable to the recovery in value of securities we sold that we had previously written down due to other-than-temporary impairment.

Fair Value Gains (Losses), Net

Beginning in mid-April 2008, we implemented fair value hedge accounting with respect to a portion of our derivatives to hedge, for accounting purposes, the interest rate risk related to some of our mortgage assets. Under fair value hedge accounting, we offset the fair value gains or losses on some of our derivative instruments against the corresponding fair value losses or gains attributable to changes in interest rates on the specific hedged mortgage assets. Although our implementation of hedge accounting does not affect our exposure to volatility in our financial results that is attributable to changes in spreads on the fair value of securities designated as trading, we believe this hedging strategy will reduce the level of volatility in our earnings, attributable to changes in interest rates, for our interest rate risk management derivatives. In addition, we generally expect that gains and losses on our trading securities, to the extent they are attributable to changes in interest rates, will offset a portion of the losses and gains on our derivatives because changes in the fair value of our trading securities typically move inversely to changes in the fair value of our derivatives. We also seek to eliminate our exposure to fluctuations in foreign exchange rates by entering into foreign currency swaps that effectively convert debt denominated in a foreign currency to debt denominated in U.S. dollars. The foreign currency exchange gains and losses on our foreign-denominated debt are offset in part by corresponding losses and gains on foreign currency swaps.

Table 7 summarizes the components of fair value gains (losses), net for the three and six months ended June 30, 2008 and 2007. Fair value gains and losses, net consists of (1) derivatives fair value gains and losses, including gains and losses on derivatives designated as accounting hedges; (2) trading securities gains and losses; (3) fair value adjustments to the carrying value of mortgage assets designated for hedge accounting that are attributable to changes in interest rates; (4) foreign exchange gains and losses on our foreign-denominated debt and (5) fair value gains and losses on certain debt securities carried at fair value. By presenting these items together in our condensed consolidated results of operations, we are able to show the net impact of mark-to-market adjustments that generally result in offsetting gains and losses attributable to changes in interest rates. We provide additional information below on the most significant components of the fair value gains (losses), net line item.

Table 7: Fair Value Gains (Losses), Net

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Derivatives fair value gains (losses), net	$ 2,293	$ 1,916	$ (710)	$ 1,353
Trading securities losses, net	(965)	(501)	(2,192)	(440)
Hedged mortgage assets losses, net[1]	(803)		(803)	
Fair value gains (losses) on derivatives, trading securities and hedged mortgage assets, net	525	1,415	(3,705)	913
Debt foreign exchange gains (losses), net	(12)	9	(169)	(55)
Debt fair value gains, net	4		14	
Fair value gains (losses), net	$ 517	$ 1,424	$ (3,860)	$ 858

(1) Represents adjustments to the carrying value of mortgage assets designated for hedge accounting that are attributable to changes in interest rates.

We recorded net fair value gains of $517 million for the second quarter of 2008, attributable to an increase in swap interest rates and a tightening of spreads. The increase in swap interest rates resulted in fair value gains on our derivatives and losses on our trading securities and hedged mortgage assets. The decrease in value of our trading securities from the increase in interest rates was partially offset by gains that resulted from the tightening of spreads during the quarter. The net fair value gains of $1.4 billion for the second quarter of 2007 were attributable to an increase in swap interest rates during the second quarter of 2007, which resulted in fair value gains on our derivatives.

We recorded net fair value losses of $3.9 billion for the first six months of 2008. The net losses for the first six months reflected the impact of the decrease in swap interest rates during the first quarter of 2008, which resulted in net fair value losses on our derivatives that more than offset net fair value gains on our derivatives during the second quarter of 2008 that resulted from the increase in swap interest rates. We also experienced fair value losses on our trading securities that were attributable to the significant widening of spreads during the first quarter of 2008 and the increase in interest rates during the second quarter of 2008. In addition, we recorded losses on hedged mortgage assets during the second quarter of 2008 in connection with our implementation of fair value hedge accounting. In contrast, we recorded fair value gains of $858 million for the first six months of 2007, due to an increase in swap interest rates during the period, which resulted in net fair value gains on our derivatives. We did not apply hedge accounting during this period.

The fair value of our trading securities may not always move inversely to changes in the fair value of our derivatives because the fair values of these financial instruments are affected not only by interest rates, but also by other factors such as spreads and changes in implied volatility. Consequently, the gains and losses on our trading securities may not result in partially offsetting losses and gains on our derivatives.

Derivatives Fair Value Gains (Losses), Net

Table 8 presents, by type of derivative instrument, the fair value gains and losses on our derivatives for the three and six months ended June 30, 2008 and 2007. Table 8 also includes an analysis of the components of derivatives fair value gains and losses attributable to net contractual interest accruals on our interest rate swaps, the net change in the fair value of terminated derivative contracts through the date of termination and the net change in the fair value of outstanding derivative contracts.

Table 8: Derivatives Fair Value Gains (Losses), Net

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Risk management derivatives:				
Swaps:				
Pay-fixed	$ 15,782	$ 6,206	$ (113)	$ 5,720
Receive-fixed	(11,092)	(3,241)	1,700	(2,878)
Basis	(73)	(111)	(68)	(125)
Foreign currency[1]	(20)	(63)	126	(43)
Swaptions:				
Pay-fixed	270	392	81	269
Receive-fixed	(2,499)	(1,356)	(2,226)	(1,659)
Interest rate caps	4	7	3	8
Other[2]	(13)	2	51	1
Total risk management derivatives fair value gains (losses), net	2,359	1,836	(446)	1,293
Mortgage commitment derivatives fair value gains (losses), net	(66)	80	(264)	60

Total derivatives fair value gains (losses), net	$ 2,293	$ 1,916	$ (710)	$ 1,353
Risk management derivatives fair value gains (losses) attributable to:				
Net contractual interest income (expense) on interest rate swaps	$ (304)	$ 64	$ (330)	$ 98
Net change in fair value of terminated derivative contracts from end of prior period to date of termination	(108)	(29)	174	(93)
Net change in fair value of outstanding derivative contracts, including derivative contracts entered into during the period	2,771	1,801	(290)	1,288
Risk management derivatives fair value gains, net[3]	$ 2,359	$ 1,836	$ (446)	$ 1,293

	2008	2007
5-year swap rate:		
As of January 1	4.19%	5.10%
As of March 31	3.31	4.99
As of June 30	4.26	5.50

(1) Includes the effect of net contractual interest income of approximately $6 million and interest expense of $16 million for the three months ended June 30, 2008 and 2007, respectively, and interest income of $3 million and interest expense of $34 million for the six months ended June 30, 2008 and 2007, respectively. The change in fair value of foreign currency swaps excluding this item resulted in a net loss of $26 million and a net loss of $47 million for the three months ended June 30, 2008 and 2007, respectively, and a net gain of $123 million and a net loss of $9 million for the six months ended June 30, 2008 and 2007, respectively.

(2) Includes MBS options, swap credit enhancements and mortgage insurance contracts.

(3) Reflects net derivatives fair value losses, excluding mortgage commitments, recognized in the condensed consolidated statements of operations.

The derivatives fair value gains of $2.3 billion for the second quarter of 2008, which includes $754 million of gains on pay-fixed swaps designated as fair value hedges, reflected the impact of an increase in swap interest rates during the quarter. The 5-year swap interest rate, which is presented in Table 8, rose by 95 basis points to 4.26% as of June 30, 2008 from 3.31% as of March 31, 2008. This increase in swap interest rates resulted in fair value gains on our pay-fixed swaps that exceeded the fair value losses on our receive-fixed swaps. The derivatives fair value gains of $1.9 billion for the second quarter of 2007 also was attributable to an increase in swap interest rates during the quarter, which resulted in fair value gains on our pay-fixed swaps.

The derivatives fair value losses of $710 million for the first six months of 2008 was largely attributable to losses resulting from a combination of the time decay of our purchased options and rebalancing activities. These losses were partially offset by net fair value gains on our swaps. The derivatives fair value gains of $1.4 billion for the first six months of 2007 was attributable to an increase in swap interest rates during the period, which resulted in fair value gains on our pay-fixed swaps.

For additional discussion of the effect of our derivatives on our consolidated financial statements, see Consolidated Balance Sheet Analysis Derivative Instruments. For information on changes in our derivatives activity and the outstanding notional amounts of our derivatives, see Risk Management Interest Rate Risk Management and Other Market Risks Derivatives Activity.

Trading Securities Gains (Losses), Net

Our portfolio of trading securities increased to $99.6 billion as of June 30, 2008, from $64.0 billion as of December 31, 2007. We recorded net losses on trading securities of $965 million and $2.2 billion for the second quarter and first six months of 2008, respectively. The losses for the second quarter of 2008 were primarily due to an increase in long-term interest rates during the quarter, partially offset by gains resulting from the tightening of spreads during the quarter relative to the first quarter of 2008. The losses for the first six months of 2008 were attributable to the significant widening of spreads during the first quarter of 2008, particularly related to private-label mortgage-related securities backed by Alt-A and subprime loans and commercial mortgage-backed securities (CMBS)

backed by multifamily mortgage loans, and the increase in interest rates during the second quarter of 2008. In comparison, we recorded losses of $501 million and $440 million for the second quarter and first six months of 2007, respectively, which were attributable to the combined effect of an increase in long-term interest rates and widening of spreads during the second quarter of 2007.

We provide additional information on our trading and AFS securities in Consolidated Balance Sheet Analysis Trading and Available-for-Sale Investment Securities and disclose the sensitivity of changes in the fair value of our trading securities to changes in interest rates in Risk Management Interest Rate Risk Management and Other Market Risks Measuring Interest Rate Risk.

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Hedged Mortgage Assets Losses, Net

Our hedge accounting relationships during the second quarter of 2008 consisted of pay-fixed interest rate swaps designated as fair value hedges of changes in the fair value, attributable to changes in the LIBOR benchmark interest rate, of specified mortgage assets. As of June 30, 2008, we had a notional amount of $68.6 billion of pay-fixed swaps designated as fair value hedges of specified mortgage assets. We include changes in fair value of hedged mortgage assets attributable to changes in the benchmark interest rate in our assessment of hedge effectiveness. These fair value accounting hedges resulted in losses on the hedged mortgage assets for the three and six months ended June 30, 2008 of $803 million, which were partially offset by gains of $789 million on the pay-fixed swaps designated as hedging instruments. The gains on these pay-fixed swaps are included as a component of derivatives fair value gains (losses), net. We also record as a component of derivatives fair value gains (losses), net the ineffectiveness, or the portion of the change in the fair value of our derivatives that was not effective in offsetting the change in the fair value of the designated hedged mortgage assets. Included in our derivatives fair value gains (losses), net was a loss of $14 million for the second quarter and first six months of 2008 representing the ineffectiveness of our fair value hedges. We provide additional information on our application of hedge accounting in Notes to Condensed Consolidated Financial Statements, Note 1 Summary of Significant Accounting Policies and Note 9 Derivative Instruments and Hedging Activities.

Losses from Partnership Investments

Losses from partnership investments decreased to $195 million and $336 million for the second quarter and first six months of 2008, respectively, from $215 million and $380 million for the second quarter and first six months of 2007. The decrease in losses during each period was due to a reduction in net operating losses attributable to a decrease in our tax-advantaged partnership investments and gains from the sale of some of our low income housing tax credit (LIHTC) investments, which was partially offset by increases in losses from our non-tax-advantaged investments.

Administrative Expenses

Administrative expenses decreased to $512 million and $1.0 billion for the second quarter and first six months of 2008, respectively, from $660 million and $1.4 billion for the second quarter and first six months of 2007, respectively, reflecting significant reductions in restatement and related regulatory expenses and a reduction in our ongoing operating costs due to efforts we undertook in 2007 to increase productivity and lower our administrative costs. We are actively managing our administrative expenses with the intent to maintain our ongoing operating costs for 2008, which exclude costs associated with our restatement, such as regulatory examinations and litigation related to the restatement, near the $2.0 billion level that we achieved in 2007.

Credit-Related Expenses

Credit-related expenses included in our condensed consolidated statements of operations consist of the provision for credit losses and foreclosed property expense. We detail the components of our credit-related expenses in Table 9. The significant increase in credit-related expenses for the second quarter and first six months of 2008 compared with the second quarter and first six months of 2007 was driven by a substantial increase in our provision for credit losses due to higher charge-offs and to build our loss reserves and an increase in foreclosed property expense.

Table 9: Credit-Related Expenses

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Provision attributable to guaranty book of business	$ 4,591	$ 368	$ 6,927	$ 548
Provision attributable to SOP 03-3 and HomeSaver Advance fair value losses	494	66	1,231	135
Total provision for credit losses[1]	5,085	434	8,158	683
Foreclosed property expense	264	84	434	156
Credit-related expenses	$ 5,349	$ 518	$ 8,592	$ 839

[1] Reflects total provision for credit losses reported in Table 10 below under Combined loss reserves.

Provision Attributable to Guaranty Book of Business

Our allowance for loan losses and reserve for guaranty losses, which we collectively refer to as our combined loss reserves, provide for probable credit losses inherent in our guaranty book of business as of each balance sheet date. The change in our combined loss reserves each period is driven by the provision for credit losses recognized in our condensed consolidated statements of operations and the net charge-offs recorded against our loss reserves. Table 10 below summarizes changes in our combined loss reserves for the three and six months ended June 30, 2008 and 2007.

Table 10: Allowance for Loan Losses and Reserve for Guaranty Losses

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Changes in loss reserves:				
Allowance for loan losses:				
Beginning balance	$ 993	$ 312	$ 698	$ 340
Provision	880	73	1,424	90
Charge-offs[1]	(495)	(64)	(774)	(126)
Recoveries	98	16	128	33

Ending balance[2]	$ 1,476	$ 337	$ 1,476	$ 337
Reserve for guaranty losses:				
Beginning balance	$ 4,202	$ 618	$ 2,693	$ 519
Provision	4,205	361	6,734	593
Charge-offs[3]	(989)	(168)	(2,026)	(321)
Recoveries	32	10	49	30
Ending balance	$ 7,450	$ 821	$ 7,450	$ 821
Combined loss reserves:				
Beginning balance	$ 5,195	$ 930	$ 3,391	$ 859
Provision	5,085	434	8,158	683
Charge-offs[1][3]	(1,484)	(232)	(2,800)	(447)
Recoveries	130	26	177	63
Ending balance[2]	$ 8,926	$ 1,158	$ 8,926	$ 1,158

	As of	
	June 30, 2008	December 31, 2007
Allocation of combined loss reserves:		
Balance at end of each period attributable to:		
Single-family	$ 8,866	$ 3,318
Multifamily	60	73
Total	$ 8,926	$ 3,391
Single-family and multifamily loss reserve ratios:[4]		
Single-family loss reserves as % of single-family guaranty book of business	0.32%	0.13%
Multifamily loss reserves as % of multifamily guaranty book of business	0.04	0.05
Combined loss reserves as a percentage of:		
Total guaranty book of business	0.31	0.12
Total nonperforming loans[5]	19.4	9.5

(1) Includes accrued interest of $161 million and $27 million for the three months ended June 30, 2008 and 2007, respectively, and $239 million and $52 million for the six months ended June 30, 2008 and 2007, respectively.

(2) Includes $114 million and $28 million as of June 30, 2008 and 2007, respectively, for acquired loans subject to the application of SOP 03-3.

(3) Includes charges recorded at the date of acquisition of $380 million and $66 million for the three months ended June 30, 2008 and 2007, respectively, and $1.1 billion and $135 million for the six months ended June 30, 2008 and 2007, respectively, for acquired loans subject to the application of SOP 03-3 where the acquisition cost exceeded the fair value of the acquired loan. Also includes charges recorded for our HomeSaver Advance initiative of $114 million and $123 million for the three and six months ended June 30, 2008, respectively.

(4) Represents loss reserves amount attributable to each loan type as a percentage of the guaranty book of business for each loan type.

(5) Loans are classified as nonperforming at the earlier of when payment of principal and interest is three months or more past due according to the loan s contractual terms (unless we have recourse against the seller of the loan in the event of default) or when, in our opinion, collectability of interest or principal on the loan is not reasonably assured. See Table 39: Nonperforming Single-Family and Multifamily Loans for detail on nonperforming loans as of June 30, 2008 and December 31, 2007.

We have continued to build our combined loss reserves through provisions that have been well in excess of our charge-offs. The provision for credit losses attributable to our guaranty book of business totaled $4.6 billion and $6.9 billion for the second quarter and first six months of 2008, respectively. These amounts consisted of charge-offs, net of recoveries, totaling $860 million and $1.4 billion for the second quarter and first six months of 2008, respectively, and an incremental provision of $3.7 billion and $5.5 billion, respectively, to build our combined loss reserves. In comparison, we recorded a provision for credit losses attributable to our guaranty book of business of $368 million and $548 million for the second quarter and first six months of 2007. As a result of our higher loss provisioning levels, we have substantially increased our combined loss reserves both in absolute terms and as a

percentage of our guaranty book of business, to $8.9 billion, or 0.31% of our guaranty book of business, as of June 30, 2008, from $3.4 billion, or 0.12% of our guaranty book of business, as of December 31, 2007.

The increase in our loss provisioning levels and combined loss reserves reflects our current estimate of inherent losses in our guaranty book of business as of June 30, 2008. The increased estimate of inherent losses is due to the continued decline in home prices, which worsened during the second quarter of 2008 and resulted in higher delinquencies and defaults and an increase in the average loan loss severity or charge-off per default. Our conventional single-family serious delinquency rate has doubled over the past year, increasing to 1.36% as of June 30, 2008, from 0.98% as of December 31, 2007 and 0.64% as of June 30, 2007. The average default rate and loan loss charge-off severity, excluding fair value losses related to SOP 03-3 loans, was 0.13% and 23%, respectively, for the second quarter of 2008, compared with 0.07% and 9% for the second quarter of 2007. These worsening credit performance trends have been most notable in certain states, certain higher risk loan categories and our 2006 and 2007 loan vintages. The Midwest, which has experienced prolonged

economic weakness, and California, Florida, Arizona and Nevada, which previously experienced rapid home price increases and are now experiencing steep home price declines, have accounted for a disproportionately large share of our seriously delinquent loans and charge-offs. Our Alt-A book, particularly the 2006 and 2007 loan vintages, has exhibited early stage payment defaults and represented a disproportionate share of our seriously delinquent loans and charge-offs for the first six months of 2008.

We expect our credit-related expenses to peak during 2008. In addition, we expect that the majority of the credit-related expenses that we will realize from our 2006 and 2007 vintages will be recognized by the end of 2008 through a combination of charge-offs, foreclosed property expense and increases to our combined loss reserves, although we expect that the total amount of our credit-related expenses will be significant in 2009. We also expect that a significant portion of the anticipated charge-offs from the 2006 and 2007 vintages will be provided for in our combined loss reserves by the end of 2008.

Provision Attributable to SOP 03-3 and HomeSaver Advance Fair Value Losses

We experienced a substantial increase in the SOP 03-3 fair value losses recorded upon the purchase of seriously delinquent loans from MBS trusts for the second quarter and first six months of 2008 relative to the second quarter and the first six months of 2007, due to the significant disruption in the mortgage market and severe reduction in market liquidity for certain mortgage products, such as delinquent loans, that has persisted since July 2007. As indicated in Table 9 above, SOP 03-3 and HomeSaver Advance fair value losses increased to $494 million and $1.2 billion for the second quarter and first six months of 2008, respectively, from $66 million and $135 million for the second quarter and first six months of 2007, respectively. We describe how we account for SOP 03-3 fair value losses and the process we use to value loans subject to SOP 03-3 in Part II Item 7 MD&A Critical Accounting Policies and Estimates Fair Value of Financial Instruments Fair Value of Loans Purchased with Evidence of Credit Deterioration Effect on Credit-Related Expenses of our 2007 Form 10-K.

Seriously Delinquent Loans Purchased from MBS Trusts

Table 11 provides a quarterly comparison of the average market price, as a percentage of the unpaid principal balance and accrued interest, of seriously delinquent loans subject to SOP 03-3 purchased from MBS trusts and additional information related to these loans. Beginning in November 2007, we decreased the number of optional delinquent loan purchases from our single-family MBS trusts in order to preserve capital in compliance with our regulatory capital requirements. HomeSaver Advance, which is a loss mitigation tool discussed below that we implemented in the first quarter of 2008, has affected our optional delinquent loan purchases. The significant reduction in liquidity in the mortgage markets, along with the increase in mortgage credit risk, that was observed in the second half of 2007 has persisted and continued to exert downward pressure on the valuations of these loans.

Table 11: Statistics on Seriously Delinquent Loans Purchased from MBS Trusts Subject to SOP 03-3

	2008		2007			
	Q2	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**
Average market price[1]	53%	60%	70%	72%	93%	94%
Unpaid principal balance and accrued interest of loans purchased (dollars in millions)	$ 807	$ 1,704	$ 1,832	$ 2,349	$ 881	$ 1,057
Number of seriously delinquent loans purchased	4,618	10,586	11,997	15,924	6,396	8,009

(1) The value of primary mortgage insurance is included as a component of the average market price.

Table 12 presents activity related to seriously delinquent loans subject to SOP 03-3 purchased from MBS trusts under our guaranty arrangements for the three months ended March 31, 2008 and June 30, 2008.

Table 12: Activity of Seriously Delinquent Loans Purchased from MBS Trusts Subject to SOP 03-3

	Contractual Amount[1]	Market Discount	Allowance for Loan Losses	Net Investment
	(Dollars in millions)			
Balance as of December 31, 2007	$ 8,096	$ (991)	$ (39)	$ 7,066
Purchases of delinquent loans	1,704	(728)		976
Provision for credit losses			(35)	(35)
Principal repayments	(180)	46	1	(133)
Modifications and troubled debt restructurings	(915)	331	5	(579)
Foreclosures, transferred to REO	(619)	169	18	(432)
Balance as of March 31, 2008	$ 8,086	$ (1,173)	$ (50)	$ 6,863
Purchases of delinquent loans	807	(380)		427
Provision for credit losses			(86)	(86)
Principal repayments	(192)	28	2	(162)
Modifications and troubled debt restructurings	(582)	240	5	(337)
Foreclosures, transferred to REO	(471)	129	15	(327)
Balance as of June 30, 2008	$ 7,648	$ (1,156)	$ (114)	$ 6,378

(1) Reflects contractually required principal and accrued interest payments that we believe are probable of collection.

Tables 13 and 14 provide information about the re-performance, or cure rates, of seriously delinquent single-family loans we purchased from MBS trusts during the first and second quarters of 2008, each of the quarters for 2007 and each of the years 2004 to 2007, as of both (1) June 30, 2008 and (2) the end of each respective period in which the loans were purchased. Table 13 includes all seriously delinquent loans we purchased from our MBS trusts, while Table 14 includes only those seriously delinquent loans that we purchased from our MBS trusts because we intended to modify the loan.

We believe there are inherent limitations in the re-performance statistics presented in Tables 13 and 14, both because of the significant lag between the time a loan is purchased from an MBS trust and the conclusion of the delinquent loan resolution process and because, in our experience, it generally takes at least 18 to 24 months to assess the ultimate re-performance of a delinquent loan. Accordingly, these re-performance statistics, particularly those for more recent loan purchases, are likely to change, perhaps materially. As a result, we believe the re-performance rates as of June 30, 2008 for delinquent loans purchased from MBS trusts during 2008 and 2007, and, to a lesser extent, the latter half of 2006, may not be indicative of the ultimate long-term performance of these loans. In addition, our cure rates may be affected by changes in our loss mitigation efforts and delinquent loan purchase practices.

Table 13: Re-performance Rates of Seriously Delinquent Single-Family Loans Purchased from MBS Trusts[1]

	Status as of June 30, 2008									
	2008		2007							
	Q2	Q1	Q4	Q3	Q2	Q1	2007	2006	2005	2004
Cured without modification[2]	10%	15%	16%	19%	18%	25%	20%	37%	45%	43%
Cured with modification[3]	35	45	32	18	34	29	26	29	16	15
Total cured	45	60	48	37	52	54	46	66	61	58
Defaults[4]	2	5	16	31	21	26	24	23	32	37
90 days or more delinquent	53	35	36	32	27	20	30	11	7	5
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

	Status as of the End of Each Respective Period									
	2008		2007							
	Q2	Q1	Q4	Q3	Q2	Q1	2007	2006	2005	2004
Cured without modification[2]	10%	7%	11%	10%	11%	17%	16%	32%	31%	33%
Cured with modification[3]	35	37	26	12	31	26	26	29	12	12
Total cured	45	44	37	22	42	43	42	61	43	45
Defaults[4]	2	2	4	6	3	3	13	9	12	14
90 days or more delinquent	53	54	59	72	55	54	45	30	45	41
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

(1) Re-performance rates calculated based on number of loans.

(2) Loans classified as cured without modification consist of the following: (1) loans that are brought current without modification; (2) loans that are paid in full; (3) loans that are repurchased by lenders; (4) loans that have not been modified but are returned to accrual status because they are less than 90 days delinquent; (5) loans for which the default is resolved through long-term forbearance; and (6) loans for which the default is resolved through a repayment plan. We do not extend the maturity date, change the interest rate or otherwise modify the principal amount of any loan that we resolve through long-term forbearance or a repayment plan unless we first purchase the loan from the MBS trust.

(3) Loans classified as cured with modification consist of loans that are brought current or are less than 90 days delinquent as a result of resolution of the default under the loan through the following: (1) a modification that does not result in a concession to the borrower; or (2) a modification that results in a concession to a borrower, which is referred to as a troubled debt restructuring. Concessions may include an extension of the time to repay the loan beyond its original maturity date or a temporary or permanent reduction in the loan s interest rate.

(4) Consists of foreclosures, preforeclosure sales, sales to third parties and deeds in lieu of foreclosure.

Table 14 below presents cure rates only for seriously delinquent single-family loans that have been modified after their purchase from MBS trusts. The cure rates for these modified seriously delinquent loans differ substantially from those shown in Table 13, which presents the information for all seriously delinquent loans purchased from our MBS trusts. Loans that have not been modified tend to start with a lower cure rate than those of modified loans, and the cure rate tends to rise over time as loss mitigation strategies for those loans are developed and then implemented. In contrast, modified loans tend to start with a high cure rate, and the cure rate tends to decline over time. For example, as shown below in Table 14, the initial cure rate for modified loans as of the end of 2007 was 85%, compared with 72% as of June 30, 2008.

Table 14: Re-performance Rates of Seriously Delinquent Single-Family Loans Purchased from MBS Trusts and Modified[1]

	Status as of June 30, 2008									
	2008		2007							
	Q2	Q1	Q4	Q3	Q2	Q1	2007	2006	2005	2004
Cured	99%	90%	77%	70%	68%	70%	72%	79%	76%	73%
Defaults[2]			1	3	5	6	3	8	12	17
90 days or more delinquent	1	10	22	27	27	24	25	13	12	10
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

	Status as of the End of Each Respective Period									
	2008		2007							
	Q2	Q1	Q4	Q3	Q2	Q1	2007	2006	2005	2004
Cured	99%	99%	100%	100%	99%	99%	85%	91%	87%	88%
Defaults[2]							1	1	1	1
90 days or more delinquent	1	1			1	1	14	8	12	11
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

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(1) Re-performance rates calculated based on number of loans.

(2) Consists of foreclosures, preforeclosure sales, sales to third parties and deeds in lieu of foreclosure.

The substantial majority of the loans reported as cured in Tables 13 and 14 above represent loans for which we believe it is probable that we will collect all of the original contractual principal and interest payments because one or more of the following has occurred: (1) the borrower has brought the loan current without servicer intervention; (2) the loan has paid off; (3) the lender has repurchased the loan; or (4) we have resolved the loan through modification, long-term forbearances or repayment plans. The variance in the cumulative cure rates as of June 30, 2008, compared with the cure rates as of the end of each period in which the loans were purchased from the MBS trust, as displayed in Tables 13 and 14, is primarily due to the amount of time that has elapsed since the loan was purchased to allow for the implementation of a workout solution if necessary.

A troubled debt restructuring is the only form of modification in which we do not expect to collect the full original contractual principal and interest amount due under the loan, although other resolutions and modifications may result in our receiving the full amount due, or certain installments due, under the loan over a period of time that is longer than the period of time originally provided for under the loan. Of the percentage of loans reported as cured as of June 30, 2008 for the second and first quarters of 2008 and for the years 2007, 2006, 2005 and 2004, approximately 74%, 67%, 39%, 15%, 4% and 2%, respectively, represented troubled debt restructurings where we have provided a concession to the borrower.

Required and Optional Purchases of Single Family Loans from MBS Trusts

Table 15 presents information on our required and optional purchases of single-family loans from MBS trusts.

Table 15: Required and Optional Purchases of Single-Family Loans from MBS Trusts

	Serious Delinquency Rate[1]	Approximate Number of Loans Purchased	Aggregate Unpaid Principal Balance[2]	Required Purchases[3]	Optional Purchases[4]
		(Dollars in billions)			
For the quarter ended:					
December 31, 2007	0.67%	13,200	$ 2.0	74%	26%
March 31, 2008	0.85	11,400	1.8	97	3
June 30, 2008	1.10	5,000	0.9	91	9

(1) Represents serious delinquency rates for conventional single-family loans in Fannie Mae MBS trusts.

(2) Represents unpaid principal balance and accrued interest for single-family loans purchased from MBS trusts during the quarter.

(3) Calculated based on the number of loans purchased that we were required to purchase, including purchases of loans we plan to modify, divided by the total number of loans we purchased from MBS trusts during the quarter.

(4) Calculated based on the number of loans purchased on an optional basis divided by the total number of loans we purchased from MBS trusts during the quarter.

The proportion of delinquent loans purchased from MBS trusts for the purpose of modification varies from period to period, driven primarily by factors such as changes in our loss mitigation efforts, as well as changes in interest rates and other market factors. HomeSaver Advance, which serves as a loss mitigation tool earlier in the delinquency cycle than a modification can be offered due to our MBS trust constraints, allows borrowers to cure their payment defaults without requiring modification of their mortgage loans. HomeSaver Advance allows servicers to provide qualified borrowers with a 15-year unsecured personal loan in an amount equal to all past due payments relating to their mortgage loan, up to the lesser of $15,000 or 15% of the unpaid principal balance of the delinquent first lien loan. Because HomeSaver Advance does not require modification of the first lien loan, we are not required to purchase the delinquent loans from the MBS trusts. We purchased 17,901 unsecured, outstanding HomeSaver Advances with an unpaid principal balance of $127 million as of June 30, 2008. The average advance made was approximately $7,100. We record these loans, which we report in our condensed consolidated balance sheets as a component of Other assets, at their estimated fair value at the date of purchase and assess for impairment subsequent to the date of purchase. The

carrying value of our HomeSaver Advances was $4 million as of June 30, 2008. The fair value of these loans is less than the outstanding unpaid principal balance for several reasons, including the lack of underlying collateral to secure the loans, the large discount that market participants have placed on mortgage-related financial assets, and the uncertainty about how these loans will perform given the current housing market and insufficient amount of time to adequately assess their performance. Although several months of payment history is generally required to fully assess loan performance, approximately 59% of the first lien mortgage loans associated with the HomeSaver Advances made through the end of May 2008 were current as of June 30, 2008.

We expect HomeSaver Advance to continue to reduce the number of delinquent loans that we otherwise would have purchased from our MBS trusts for the remainder of 2008. Although our optional loan purchases have decreased since the end of 2007, we expect that our SOP 03-3 fair value losses for 2008 will be higher than the losses recorded for 2007, based on the number of required and optional loans we purchased from MBS trusts during the first six months of 2008 and the continued weakness in the housing market, which has reduced the price of these loans.

Credit Loss Performance Metrics

Management views our credit loss performance metrics, which include our historical credit losses and our credit loss ratio, as significant indicators of the effectiveness of our credit risk management strategies. Management uses these metrics together with other credit risk measures to assess the credit quality of our existing guaranty book of business, make determinations about our loss mitigation strategies, evaluate our historical credit loss performance and determine the level of our loss reserves. These 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 exclude SOP 03-3 and HomeSaver Advance fair value losses that have not yet produced an economic loss from our credit loss performance metrics. However, we include in our credit loss performance metrics the impact of any credit losses we experience on loans subject to SOP 03-3 or first lien loans associated with HomeSaver Advance loans that result in foreclosure.

We believe that our credit loss performance metrics are useful to investors because they reflect how management evaluates our credit performance and the effectiveness of our credit risk management strategies and loss mitigation efforts. They also provide a consistent treatment of credit losses for on- and off-balance sheet loans. Moreover, by presenting credit losses with and without the effect of SOP 03-3 and HomeSaver Advance fair value losses, investors are able to evaluate our credit performance on a more consistent basis among periods.

Table 16 below details the components of our credit loss performance metrics, which exclude the effect of SOP 03-3 and HomeSaver Advance fair value losses, for the three and six months ended June 30, 2008 and 2007.

Table 16: Credit Loss Performance Metrics

	For the Three Months Ended June 30,				**For the Six Months Ended June 30,**			
	2008		**2007**		**2008**		**2007**	
	Amount	**Ratio[(1)]**	**Amount**	**Ratio[(1)]**	**Amount**	**Ratio[(1)]**	**Amount**	**Ratio[(1)]**
	(Dollars in millions)							
Charge-offs, net of recoveries	$ 1,354	18.9bp	$ 206	3.3bp	$ 2,623	18.6bp	$ 384	3.1bp
Foreclosed property expense	264	3.7	84	1.4	434	3.1	156	1.3
	(494)	(6.9)	(66)	(1.1)	(1,231)	(8.7)	(135)	(1.1)

Less: SOP 03-3 and HomeSaver Advance fair value losses[2]								
Plus: Impact of SOP 03-3 on charge-offs and foreclosed property expense[3]	129	1.8	26	0.4	298	2.1	51	0.4
Credit losses[4]	$ 1,253	17.5bp	$ 250	4.0bp	$ 2,124	15.1bp	$ 456	3.7bp

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(1) Based on the annualized amount for each line item presented divided by the average guaranty book of business during the period. We previously calculated our credit loss ratio based on annualized credit losses as a percentage of our mortgage credit book of business, which includes non-Fannie Mae mortgage-related securities held in our mortgage investment portfolio that we do not guarantee. Because losses related to non-Fannie Mae mortgage-related securities are not reflected in our credit losses, we revised the calculation of our credit loss ratio to reflect credit losses as a percentage of our guaranty book of business. Our credit loss ratio calculated based on our mortgage credit book of business would have been 16.7 basis points and 3.8 basis points for the three months ended June 30, 2008 and 2007, respectively. Our charge-off ratio calculated based on our mortgage credit book of business would have been 18.0 basis points and 3.1 basis points for the three months ended June 30, 2008 and 2007, respectively. Our credit loss ratio calculated based on our mortgage credit book of business would have been 14.3 basis points and 3.5 basis points for the six months ended June 30, 2008 and 2007, respectively. Our charge-off ratio calculated based on our mortgage credit book of business would have been 17.7 basis points and 3.0 basis points for the six months ended June 30, 2008 and 2007, respectively.

(2) Represents the amount recorded as a loss when the acquisition cost of a seriously delinquent loan purchased from an MBS trust exceeds the fair value of the loan at acquisition. Also includes the difference between the unpaid principal balance of HomeSaver Advance loans at origination and the estimated fair value of these loans that we record in our condensed consolidated balance sheets.

(3) For seriously delinquent loans purchased from MBS trusts that are recorded at a fair value amount at acquisition that is lower than the acquisition cost, any loss recorded at foreclosure would be less than it would have been if we had recorded the loan at its acquisition cost instead of at fair value. Accordingly, we have added back to our credit losses the amount of charge-offs and foreclosed property expense that we would have recorded if we had calculated these amounts based on the purchase price.

(4) Interest forgone on nonperforming loans in our mortgage portfolio, which is presented in Table 39, reduces our net interest income but is not reflected in our credit losses total. In addition, other-than-temporary impairment losses resulting from deterioration in the credit quality of our mortgage-related securities and accretion of interest income on loans subject to SOP 03-3 are excluded from credit losses.

Our credit loss ratio increased to 17.5 basis points and 15.1 basis points for the second quarter and first six months of 2008, respectively, from 4.0 basis points and 3.7 basis points for the second quarter and first six months of 2007, respectively. The substantial increase in our credit losses reflected the impact of a further deterioration of conditions in the housing and credit markets. The decline in national home prices and the economic weakness in the Midwest have continued to contribute to higher default rates and loan loss severities, particularly for certain higher risk loan categories, loan vintages and loans within certain states that have had the greatest home price depreciation from their recent peaks. Our credit loss ratio including the effect of SOP 03-3 and HomeSaver Advance fair value losses was 22.6 basis points and 21.7 basis points for the second quarter and first six months of 2008, respectively, and 4.7 basis points and 4.4 basis points for the second quarter and first six months of 2007, respectively.

Certain higher risk loan types, such as Alt-A loans, interest-only loans, loans to borrowers with low credit scores and loans with high loan-to-value (LTV) ratios, many of which were originated in 2006 and 2007, represented approximately 29% of our single-family conventional mortgage credit book of business as of June 30, 2008, but accounted for approximately 72% and 70% of our credit losses for the second quarter and first six months of 2008, respectively, compared with 52% and 51% for the second quarter and first six months of 2007, respectively.

The states of California, Florida, Arizona and Nevada, which represented approximately 27% of our single-family conventional mortgage credit book of business as of June 30, 2008, accounted for 48% and 42% of our credit losses

for the second quarter and first six months of 2008, respectively, compared with 8% and 5% for the second quarter and first six months of 2007, respectively. Michigan and Ohio, two key states driving credit losses in the Midwest, represented approximately 6% of our single-family conventional mortgage credit book of business as of June 30, 2008, but accounted for 18% and 23% of our credit losses for the second quarter and first six months of 2008, respectively, compared with 46% and 44% for the second quarter and first six months of 2007, respectively.

In light of our experience during the second quarter and our credit performance in July, we are increasing our forecast for our credit loss ratio (which excludes SOP 03-3 and HomeSaver Advance fair value losses) of 23 to 26 basis points for 2008, as compared with our previous guidance of 13 to 17 basis points. We continue to anticipate that our credit loss ratio will increase further in 2009 compared with 2008.

We provide more detailed credit performance information, including serious delinquency rates by geographic region, statistics on nonperforming loans and foreclosed property activity, in Risk Management Credit Risk Management Mortgage Credit Risk Management Mortgage Credit Book of Business.

Credit Loss Sensitivity

Pursuant to our September 2005 agreement with OFHEO, we 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. Table 17 shows the credit loss sensitivity before and after consideration of projected credit risk sharing proceeds, such as private mortgage insurance claims and other credit enhancement, as of June 30, 2008 and December 31, 2007 for first lien single-family whole loans we own or that back Fannie Mae MBS. The sensitivity results represent the difference between our base case scenario of the present value of expected credit losses and credit risk sharing proceeds, derived from our internal home price path forecast, and a scenario that assumes an instantaneous nationwide 5% decline in home prices. The increase in the credit loss sensitivities since December 31, 2007 reflects the decline in home prices during the first half of 2008 and the current negative near-term outlook for the housing and credit markets. These higher sensitivities also reflect the impact of updates to our underlying credit loss estimation models to capture the credit risk associated with the rapidly changing and worsening of conditions in the housing market. An environment of continuing lower home prices affects the frequency and timing of defaults and increases the level of credit losses, resulting in greater loss sensitivities. Although the anticipated credit risk sharing proceeds have increased as home prices have declined, the expected amount of proceeds resulting from a 5% home price shock are lower. As home prices decline, the number of loans without mortgage insurance that are projected to default increases and the losses on loans with mortgage insurance that default are more likely to increase to a level that exceeds the level of mortgage insurance.

Table 17: Single-Family Credit Loss Sensitivity[1]

	As of	
	June 30, 2008	December 31, 2007
	(Dollars in millions)	
Gross single-family credit loss sensitivity[2]	$ 11,300	$ 9,644
Less: Projected credit risk sharing proceeds	(3,933)	(5,102)
Net single-family credit loss sensitivity[2]	$ 7,367	$ 4,542
Outstanding single-family whole loans and Fannie Mae MBS	$ 2,660,098	$ 2,523,440
Single-family net credit loss sensitivity as a percentage of outstanding single-family whole loans and Fannie Mae MBS	0.28%	0.18%

(1) For purposes of this calculation, we assume that, after the initial 5% shock, home price growth rates return to the average of the possible growth rate paths used in our internal credit pricing models. The present value change reflects the increase in future expected credit losses under this shock scenario.

(2) Represents total economic credit losses, which consists of credit losses and forgone interest. Calculations are based on approximately 97% of our total single-family guaranty book of business as of both June 30, 2008 and December 31, 2007. The mortgage loans and mortgage-related securities that are included in these estimates

consist of: (i) single-family Fannie Mae MBS (whether held in our mortgage portfolio or held by third parties), excluding certain whole loan real estate mortgage investment conduits (REMICs) and private-label wraps; (ii) single-family mortgage loans, excluding mortgages secured only by second liens, subprime mortgages, manufactured housing chattel loans and reverse mortgages; and (iii) 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.

We generated these sensitivities using the same models that we use to estimate fair value. Because these sensitivities represent hypothetical scenarios, they should be used with caution. They are limited in that they assume an instantaneous uniform 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 basis. In addition, these sensitivities are calculated independently without considering changes in other interrelated

assumptions, such as unemployment rates or other economic factors, which would likely have a significant impact on our credit losses.

Other Non-Interest Expenses

Other non-interest expenses increased to $286 million and $791 million for the second quarter and first six months of 2008, respectively, from $60 million and $164 million for the second quarter and first six months of 2007, respectively. The increase in expenses for each period was predominately due to a reduction in the amount of net gains recognized on the extinguishment of debt and interest expense related to an increase in our unrecognized tax benefit.

Federal Income Taxes

We recorded a tax benefit of $476 million and $3.4 billion for the second quarter and first six months of 2008, respectively, which resulted in an effective tax rate, excluding the provision or benefit related to extraordinary amounts of 17% and 43%, respectively. The tax benefit for each period was due in part to the pre-tax loss for the period as well as the tax credits generated from our LIHTC partnership investments. The reduction of our tax benefit as a percentage of pre-tax loss in the three months ended June 30, 2008 as compared with the three months ended March 31, 2008, was due in part to an increase in our projected credit losses for 2008 which is used in computing our annual effective tax rate. In comparison, we recorded a tax provision of $187 million and $114 million for the second quarter and first six months of 2007, respectively, and our effective tax rate was 9% and 4%, respectively.

In calculating our interim provision for income taxes, we use an estimate of our annual effective tax rate, which we update each quarter based on actual historical information and forward-looking estimates. The estimated annual effective tax rate may fluctuate each period based upon changes in facts and circumstances, if any, as compared with those forecasted at the beginning of the year and each interim period thereafter.

BUSINESS SEGMENT RESULTS

The presentation of the results of each of our three business segments is intended to reflect each segment as if it were a stand-alone business. We describe the management reporting and allocation process that we use to generate our segment results in our 2007 Form 10-K in Notes to Consolidated Financial Statements Note 15, Segment Reporting. We summarize our segment results for the three and six months ended June 30, 2008 and 2007 in the tables below and provide a discussion of these results. We include more detail on our segment results in Notes to Condensed Consolidated Financial Statements Note 13, Segment Reporting.

Single-Family Business

Our Single-Family business recorded a net loss of $2.4 billion and $3.4 billion for the second quarter and first six months of 2008, respectively, compared with net income of $136 million and $491 million for the second quarter and first six months of 2007, respectively. Table 18 summarizes the financial results for our Single-Family business for the periods indicated.

Table 18: Single-Family Business Results

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		Quarterly Variance		Year-to-Date Variance	
	2008	2007	2008	2007	$	%	$	%
			(Dollars in millions)					
ment of operations								
anty fee income	$ 1,819	$ 1,304	$ 3,761	$ 2,591	$ 515	39%	$ 1,170	4
management income	74	141	179	295	(67)	(48)	(116)	(3
r income(1)(2)	197	184	385	360	13	7	25	
es on certain guaranty acts		(451)		(731)	451	100	731	10
t-related expenses(3)	(5,339)	(519)	(8,593)	(845)	(4,820)	(929)	(7,748)	(91
r expenses(1)(4)	(461)	(454)	(994)	(922)	(7)	(2)	(72)	(
ne (loss) before al income taxes	(3,710)	205	(5,262)	748	(3,915)	(1,910)	(6,010)	(80
fit (provision) for al income taxes	1,304	(69)	1,848	(257)	1,373	1,990	2,105	81
ncome (loss)	$ (2,406)	$ 136	$ (3,414)	$ 491	$ (2,542)	(1,869)%	$ (3,905)	(79
r key performance								
age single-family anty book of ess(5)	$ 2,704,345	$ 2,349,006	$ 2,668,099	$ 2,318,897	$ 355,339	15%	$ 349,202	1

(1) Certain prior period amounts have been reclassified to conform with the current period presentation in our condensed consolidated statements of operations.

(2) Consists of net interest income, investment gains and losses, and fee and other income.

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

(4) Consists of administrative expenses and other expenses.

(5) The single-family guaranty book of business consists of single-family mortgage loans held in our mortgage portfolio, single-family Fannie Mae MBS held in our mortgage portfolio, single-family Fannie Mae MBS held by third parties, 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.

Key factors affecting the results of our Single-Family business for the second quarter and first six months of 2008 compared with the second quarter and first six months of 2007 included the following.

Increased guaranty fee income, attributable to growth in the average single-family guaranty book of business, coupled with an increase in the average effective single-family guaranty fee rate.

We experienced an increase of 15% in our average single-family guaranty book of business for the second quarter and first six months of 2008 over the second quarter and first six months of 2007, reflecting the significant increase in our market share since the end of the second quarter of 2007. Our single-family guaranty book of business increased to $2.7 trillion as of June 30, 2008, from $2.4 trillion as of June 30, 2007. Our estimated market share of new single-family mortgage-related securities issuances, which is based on publicly available data and excludes previously securitized mortgages, increased to approximately 45.4% and 47.6% for the second quarter and first six months of 2008, respectively, from 27.9% and 26.5% for the second quarter and first six months of 2007, respectively.

Our average effective single-family guaranty fee rate increased to 26.9 basis points and 28.2 basis points for the second quarter and first six months of 2008, respectively, from 22.2 basis points and 22.3 basis points for the second quarter and first six months of 2007, respectively. The growth in our average effective single-family guaranty fee rate for the second quarter and first six months of 2008 over the comparable periods in 2007 reflects the accelerated recognition of deferred amounts into income as interest rates were lower in the second quarter and first six months of 2008, relative to the

level of interest rates during the comparable prior year periods. Our average effective single-family guaranty fee rate for the second quarter and first six months of 2008 also reflects the impact of guaranty fee pricing changes and a shift in the composition of our guaranty book of business to a greater proportion of higher-quality, lower risk and lower guaranty fee mortgages, as we reduced our acquisitions of higher risk, higher fee product categories, such as Alt-A loans.

The elimination of losses on certain guaranty contracts due to the change in measuring the fair value of our guaranty obligation upon adoption of SFAS 157 on January 1, 2008.

A substantial increase in credit-related expenses, primarily due to an increase in the provision for credit losses due to higher charge-offs, as well as a higher incremental provision to build our loss reserves, reflecting worsening credit performance trends, including significant increases in delinquencies, default rates and average loan loss severities, particularly in certain states and higher risk loan categories. We also experienced an increase in SOP 03-3 fair value losses, which are recorded as a component of our provision for credit losses.

A relatively stable effective income tax rate of approximately 35%, which represents our statutory tax rate.

HCD Business

Our HCD business recorded net income of $72 million and $222 million for the second quarter and first six months of 2008, respectively, compared with net income of $110 million and $273 million for the second quarter and first six months of 2007, respectively. Table 19 summarizes the financial results for our HCD business for the periods indicated.

Table 19: HCD Business Results

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		Quarterly Variance		Year-to-Date Variance	
	2008	2007	2008	2007	$	%	$	%
	(Dollars in millions)							
Statement of operations data:								
Guaranty fee income	$ 134	$ 110	$ 282	$ 211	$ 24	22%	$ 71	34%
Other income[1]	52	106	116	200	(54)	(51)	(84)	(42)
Losses on partnership investments	(195)	(215)	(336)	(380)	20	9	44	12
Credit-related income (expenses)[2]	(10)	1	1	6	(11)	(1,100)	(5)	(83)
Other expenses[3]	(225)	(263)	(479)	(510)	38	14	31	6
Loss before federal income taxes	(244)	(261)	(416)	(473)	17	7	57	12

Benefit for federal income taxes	316	371	638	746	(55)	(15)	(108)	(14)
Net income	$ 72	$ 110	$ 222	$ 273	$ (38)	(35)%	$ (51)	(19)%
Other key performance data:								
Average multifamily guaranty book of business[4]	$ 158,444	$ 126,575	$ 155,173	$ 124,818	$ 31,869	25%	$ 30,355	24%

[1] Consists of trust management income and fee and other income (expense).

[2] Consists of provision for credit losses and foreclosed property income (expense).

[3] Consists of net interest expense, losses on certain guaranty contracts, administrative expenses, minority interest in earnings of consolidated subsidiaries and other expenses.

[4] The multifamily guaranty book of business consists of multifamily mortgage loans held in our mortgage portfolio, multifamily Fannie Mae MBS held in our mortgage portfolio, multifamily Fannie Mae MBS held by third parties 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.

Key factors affecting the results of our HCD business for the second quarter and first six months of 2008 compared with the second quarter and first six months of 2007 included the following.

Increased guaranty fee income, attributable to growth in the average multifamily guaranty book of business and an increase in the average effective multifamily guaranty fee rate. These increases reflect the increased investment and liquidity that we are providing to the multifamily mortgage market.

A decrease in other income, attributable to lower multifamily fees due to a reduction in multifamily loan liquidations for the first six months of 2008.

A decrease in losses on partnership investments, primarily due to a decline in tax-advantaged investments and gains on the sales of some of our LIHTC investments, partially offset by increases in our non-tax advantaged investments.

A tax benefit of $316 million and $638 million for the second quarter and first six months of 2008, respectively, driven primarily by tax credits of $229 million and $490 million, respectively. In comparison, we recorded a tax benefit of $371 million and $746 million for the second quarter and first six months of 2007, respectively, driven by tax credits of $277 million and $577 million, respectively.

Capital Markets Group

Our Capital Markets group recorded net income of $34 million and a net loss of $1.3 billion for the second quarter and first six months of 2008, respectively, compared with net income of $1.7 billion and $2.1 billion for the second quarter and first six months of 2007, respectively. Table 20 summarizes the financial results for our Capital Markets group for the periods indicated.

Table 20: Capital Markets Group Results

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		Quarterly Variance		Year-to-Date Variance	
	2008	2007	2008	2007	$	%	$	%
	(Dollars in millions)							
Statement of operations data:								
Net interest income	$ 2,003	$ 1,182	$ 3,662	$ 2,391	$ 821	69%	$ 1,271	53%
Investment losses, net[1]	(846)	(86)	(909)	201	(760)	(884)	(1,110)	(552)
Fair value gains (losses), net[1]	517	1,424	(3,860)	858	(907)	(64)	(4,718)	(550)
Fee and other income[1]	82	83	145	187	(1)	(1)	(42)	(22)
Other expenses[2]	(545)	(410)	(1,216)	(884)	(135)	(33)	(332)	(38)

Income (loss) before federal income taxes and extraordinary losses, net of tax effect	1,211	2,193	(2,178)	2,753	(982)	(45)	(4,931)	(179)
Benefit (provision) for federal income taxes	(1,144)	(489)	918	(603)	(655)	(134)	1,521	252
Extraordinary losses, net of tax effect	(33)	(3)	(34)	(6)	(30)	(1,000)	(28)	(467)
Net income (loss)	$ 34	$ 1,701	$ (1,294)	$ 2,144	$ (1,667)	(98)%	$ (3,438)	(160)%

(1) Certain prior period amounts have been reclassified to conform with the current period presentation in our condensed consolidated statements of operations.

(2) Includes debt extinguishment losses, allocated guaranty fee expense, administrative expenses and other expenses.

Key factors affecting the results of our Capital Markets group for the second quarter and first six months of 2008 compared with the second quarter and first six months of 2007 included the following.

An increase in net interest income, primarily attributable to an expansion of our taxable-equivalent net interest yield driven by the reduction in short-term interest rates, which reduced the average cost of our debt, and wider mortgage-to-debt spreads on acquisitions. The reversal of accrued interest expense on step-rate debt that we redeemed during the first quarter of 2008 also reduced the average cost of our debt.

A decrease in fair value gains for the second quarter of 2008 compared with the second quarter of 2007, largely due to adjustments on hedged mortgage assets attributable to the increase in interest rates during the quarter. The fair value losses recorded for the first six months of 2008 were primarily attributable to losses on our trading securities resulting from the significant widening of spreads during the first quarter of 2008 and the decrease in interest rates during the first quarter of 2008.

A significant increase in investment losses due to other-than-temporary impairment on AFS securities, principally for Alt-A and subprime private-label securities, reflecting a reduction in expected cash flows due to higher expected defaults and loss severities on the underlying mortgages.

An effective tax rate of 94% and 42% for the second quarter and first six months of 2008, respectively, compared with an effective tax rate of 22% for both the second quarter and first six months of 2007. Fluctuations in our effective tax rate and variances between the effective tax rate and statutory rate reflect fluctuations in our pre-tax earnings and the relative benefit of tax-exempt income generated from our investments in mortgage revenue bonds. In addition, the effective tax rate for the second quarter of 2008 reflected an adjustment during the quarter to our estimated annual 2008 corporate effective tax rate, which was due in part to the increase in our projected credit losses for 2008.

CONSOLIDATED BALANCE SHEET ANALYSIS

Total assets of $885.9 billion as of June 30, 2008 increased by $6.5 billion, or 1%, from December 31, 2007. Total liabilities of $844.5 billion increased by $9.3 billion, or 1%, from December 31, 2007. Stockholders equity of $41.2 billion reflected a decrease of $2.8 billion, or 6%, from December 31, 2007. Following is a discussion of material changes in the major components of our assets and liabilities since December 31, 2007.

Mortgage Investments

Table 21 summarizes our mortgage portfolio activity for the three and six months ended June 30, 2008 and 2007.

Table 21: Mortgage Portfolio Activity[1]

	For the Three Months Ended June 30,		Variance		For the Six Months Ended June 30,		Variance	
	2008	2007	$	%	2008	2007	$	%
	(Dollars in millions)							
Purchases[2]	$ 60,315	$ 48,287	$ 12,028	25%	$ 95,815	$ 84,004	$ 11,811	14%
Sales	9,051	8,048	1,003	12	22,580	25,039	(2,459)	(10)
Liquidations[3]	25,020	32,671	(7,651)	(23)	48,591	64,908	(16,317)	(25)

(1) Excludes unamortized premiums, discounts and other cost basis adjustments.

(2) Excludes advances to lenders and mortgage-related securities acquired through the extinguishment of debt.

(3) Includes scheduled repayments, prepayments and foreclosures.

For the first two months of 2008, we were subject to an OFHEO-directed limitation on the size of our mortgage portfolio. OFHEO s mortgage portfolio cap requirement, which is described in our 2007 Form 10-K, was eliminated by OFHEO effective March 1, 2008. OFHEO s reduction in our capital surplus requirement provided us with more flexibility to take advantage of purchase opportunities. As a result, we were able to increase our portfolio purchases during the first six months of 2008, particularly in the second quarter of 2008, as mortgage-to-debt spreads reached historic highs, which presented more opportunities for us to purchase mortgage assets at attractive prices and spreads. We experienced a decrease in mortgage liquidations during the second quarter and first six months of 2008 relative to the second quarter and first six months of 2007, reflecting a decline in refinancing activity due to the continuing deterioration in the housing market and tightening of credit standards in the primary mortgage market, as well as higher mortgage interest rates.

Table 22 shows the composition of our net mortgage portfolio by product type and the carrying value as of June 30, 2008 and December 31, 2007. Our net mortgage portfolio totaled $737.5 billion as of June 30, 2008, reflecting an increase of 2% from December 31, 2007.

Table 22: Mortgage Portfolio Composition[1]

	As of	
	June 30, 2008	December 31, 2007
	(Dollars in millions)	
Mortgage loans:[2]		
Single-family:		
Government insured or guaranteed	$ 36,009	$ 28,202
Conventional:		
Long-term, fixed-rate	191,351	193,607
Intermediate-term, fixed-rate[3]	44,124	46,744
Adjustable-rate	43,758	43,278
Total conventional single-family	279,233	283,629
Total single-family	315,242	311,831
Multifamily:		
Government insured or guaranteed	753	815
Conventional:		
Long-term, fixed-rate	5,537	5,615
Intermediate-term, fixed-rate[3]	83,296	73,609
Adjustable-rate	16,164	11,707
Total conventional multifamily	104,997	90,931
Total multifamily	105,750	91,746
Total mortgage loans	420,992	403,577
Unamortized premiums (discounts) and other cost basis adjustments, net	(1,050)	726
Lower of cost or market adjustments on loans held for sale	(235)	(81)
Allowance for loan losses for loans held for investment	(1,476)	(698)
Total mortgage loans, net	418,231	403,524
Mortgage-related securities:		
Fannie Mae single-class MBS	118,069	102,258
Fannie Mae structured MBS	75,052	77,905
Non-Fannie Mae single-class mortgage securities	28,599	28,129
Non-Fannie Mae structured mortgage securities[4]	92,524	96,373
Mortgage revenue bonds	15,788	16,315

Other mortgage-related securities	3,092	3,346
Total mortgage-related securities	333,124	324,326
Market value adjustments[5]	(11,531)	(3,249)
Other-than-temporary impairments	(1,189)	(603)
Unamortized discounts and other cost basis adjustments, net[6]	(1,147)	(1,076)
Total mortgage-related securities, net	319,257	319,398
Mortgage portfolio, net[7]	$ 737,488	$ 722,922

(1) Mortgage loans and mortgage-related securities are reported at unpaid principal balance.

(2) Mortgage loans include unpaid principal balance totaling $82.4 billion and $81.8 billion as of June 30, 2008 and December 31, 2007, respectively, related to mortgage-related securities that were consolidated under Financial Accounting Standards Board Interpretation (FIN) No. 46R (revised December 2003), *Consolidation of Variable Interest Entities (an interpretation of ARB No. 51)* (FIN 46R), and mortgage-related securities created from

securitization transactions that did not meet the sales criteria under SFAS No. 140, *Accounting for Transfer and Servicing of Financial Assets and Extinguishments of Liabilities (a replacement of FASB Statement No. 125)* (SFAS 140), which effectively resulted in mortgage-related securities being accounted for as loans.

(3) Intermediate-term, fixed-rate consists of mortgage loans with contractual maturities at purchase equal to or less than 15 years.

(4) Includes private-label mortgage-related securities backed by Alt-A or subprime mortgage loans totaling $57.8 billion and $64.5 billion as of June 30, 2008 and December 31, 2007, respectively. Refer to Trading and Available-for-Sale Investment Securities Investments in Private-Label Mortgage-Related Securities for a description of our investments in Alt-A and subprime securities.

(5) Includes unrealized gains and losses on mortgage-related securities and securities commitments classified as trading and available-for-sale.

(6) Includes the impact of other-than-temporary impairments of cost basis adjustments.

(7) Includes consolidated mortgage-related assets acquired through the assumption of debt. Also includes $736 million and $538 million as of June 30, 2008 and December 31, 2007, respectively, of mortgage loans and mortgage-related securities that we have pledged as collateral and which counterparties have the right to sell or repledge.

Liquid Investments

Our liquid assets consist of cash and cash equivalents, funding agreements with our lenders, including advances to lenders and repurchase agreements, and non-mortgage investment securities. Our liquid assets, net of cash equivalents pledged as collateral, decreased to $82.7 billion as of June 30, 2008 from $102.0 billion as of December 31, 2007, as we used funds to redeem a significant amount of higher cost long-term debt.

Trading and Available-for-Sale Investment Securities

Our mortgage investment securities are classified in our condensed consolidated balance sheets as either trading or AFS and reported at fair value. In conjunction with our January 1, 2008 adoption of SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159), we elected to reclassify all of our non-mortgage investment securities from AFS to trading. Table 23 shows the composition of our trading and AFS securities at amortized cost and fair value as of June 30, 2008, which totaled $356.7 billion and $344.8 billion, respectively. We also disclose the gross unrealized gains and gross unrealized losses related to our AFS securities as of June 30, 2008, and a stratification of these losses based on securities that have been in a continuous unrealized loss position for less than 12 months and for 12 months or longer.

Table 23: Trading and AFS Investment Securities

	As of June 30, 2008							
					Less Than 12 Consecutive Months		12 Consecutive Months or Longer	
	Amortized Cost[1]	Gross Unrealized Gains	Gross Unrealized Losses	Total Fair Value	Gross Unrealized Losses	Total Fair Value	Gross Unrealized Losses	Total Fair Value
	(Dollars in millions)							
Trading:								
Fannie Mae single-class MBS	$ 42,604	$	$	$ 42,908	$	$	$	$
Fannie Mae structured MBS	10,992			10,945				
Non-Fannie Mae single-class mortgage-related securities	1,122			1,123				
Non-Fannie Mae structured mortgage-related securities	20,772			18,338				
Mortgage revenue bonds	799			717				
Asset-backed securities	13,077			12,843				
Corporate debt securities	10,193			10,049				
Other non-mortgage-related securities	2,638			2,639				
Total trading	$ 102,197	$	$	$ 99,562	$	$	$	$
Available for sale:								
Fannie Mae single-class MBS	$ 74,659	$ 572	$ (1,100)	$ 74,131	$ (795)	$ 42,373	$ (305)	$ 7,143
Fannie Mae structured MBS	63,828	670	(700)	63,798	(397)	26,331	(303)	7,568
Non-Fannie Mae single-class mortgage-related securities	27,267	371	(153)	27,485	(126)	7,806	(27)	1,172
Non-Fannie Mae structured mortgage-related	71,045	102	(8,380)	62,767	(2,359)	24,757	(6,021)	32,812

securities								
Mortgage revenue bonds	14,989	64	(736)	14,317	(258)	6,237	(478)	3,900
Other mortgage-related securities	2,711	110	(93)	2,728	(78)	1,025	(15)	93
Total available for sale	$ 254,499	$ 1,889	$ (11,162)	$ 245,226	$ (4,013)	$ 108,529	$ (7,149)	$ 52,688
Total investments in securities	$ 356,696	$ 1,889	$ (11,162)	$ 344,788	$ (4,013)	$ 108,529	$ (7,149)	$ 52,688

(1) Amortized cost includes unamortized premiums, discounts and other cost basis adjustments, as well as other-than-temporary impairment write downs.

The estimated fair value of our AFS securities decreased to $245.2 billion as of June 30, 2008 from $293.6 billion as of December 31, 2007. Gross unrealized losses related to these securities totaled $11.2 billion as of June 30, 2008, compared with $4.8 billion as of December 31, 2007. The increase in gross unrealized losses during the first six months of 2008 was primarily due to significantly wider spreads during the period, which reduced the fair value of substantially all of our mortgage-related securities, particularly our private-label mortgage-related securities backed by Alt-A, subprime, and commercial multifamily loans. We discuss our process for assessing our AFS investment securities for other-than-temporary impairment below.

Investments in Private-Label Mortgage-Related Securities

The non-Fannie Mae mortgage-related security categories presented in Table 23 above include agency mortgage-related securities issued or guaranteed by Freddie Mac or Ginnie Mae and private-label mortgage-related securities backed by Alt-A, subprime, multifamily, manufactured housing or other mortgage loans. We do not have any exposure to collateralized debt obligations, or CDOs. We classify private-label securities as Alt-A, subprime, multifamily or manufactured housing if the securities were labeled as such when issued. We also have invested in private-label Alt-A and subprime mortgage-related securities that we have resecuritized to include our guaranty (wraps), which we report in Table 23 above as a component of Fannie Mae structured MBS. We generally have focused our purchases of these securities on the highest-rated tranches available at the time of acquisition. Higher-rated tranches typically are supported by credit enhancements to reduce the exposure to losses. The credit enhancements on our private-label security investments generally are in the form of initial subordination provided by lower level tranches of these securities, prepayment proceeds within the trust and secondary guarantees from monoline financial guarantors based on specific performance

triggers. The characteristics of the subprime securities that we hold are different than the securities underlying the ABX indices. For example, the pass-through securities in our portfolio reflect the entirety of the underlying AAA cash flows, while only a portion of the underlying AAA cash flows backs the securities in the ABX indices.

We owned $104.9 billion of private-label mortgage-related securities backed by Alt-A, subprime, multifamily, manufactured housing and other mortgage loans and mortgage revenue bonds as of June 30, 2008, down from $111.1 billion as of December 31, 2007, reflecting a reduction of $6.2 billion due to principal payments. Table 24 summarizes, by loan type, the composition of our investments in private-label securities and mortgage revenue bonds as of June 30, 2008 and the average credit enhancement. The average credit enhancement generally reflects the level of cumulative losses that must be incurred before we experience a loss of principal on the tranche of securities that we own. Table 24 also provides information on the credit ratings of our private-label securities as of July 31, 2008. The credit rating reflects the lowest rating as reported by Standard & Poor s (Standard & Poor s), Moody s Investors Service (Moody s), Fitch Ratings (Fitch) or Dominion Bond Rating Service Limited (DBRS, Limited), each of which is a nationally recognized statistical rating organization.

Table 24: Investments in Private-Label Mortgage-Related Securities and Mortgage Revenue Bonds

	As of June 30, 2008		As of July 31, 2008			
	Unpaid Principal Balance	Average Credit Enhancement[1]	% AAA[2]	% AA to BBB-[2]	% Below Investment Grade[2]	Current % Watchlist[3]
	(Dollars in millions)					
Private-label mortgage-related securities backed by:						
Alt-A mortgage loans	$ 29,507	24%	96%	4%	%	14%
Subprime mortgage loans	28,276	37	42	48	10	22
Multifamily mortgage loans	25,880	30	100			
Manufactured housing mortgage loans	3,065	37	6	39	55	1
Other mortgage loans	2,411	6	96	1	3	
Total private-label mortgage-related securities	89,139					
Mortgage revenue bonds[4]	15,788	35	48	50	2	27
Total	$ 104,927					

(1) 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 a securitization structure before any losses are allocated to securities that we own. Percentage calculated based on the quotient of the total unpaid principal balance of all credit enhancement 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.

(2) Reflects credit ratings as of July 31, 2008, calculated based on unpaid principal balance as of June 30, 2008. Investment securities that have a credit rating below BBB- or its equivalent or that have not been rated are classified as below investment grade.

(3) Reflects percentage of investment securities, calculated based on unpaid principal balance as of June 30, 2008, that have been placed under review by either Standard & Poor s, Moody s, Fitch or DBRS, Limited.

(4) Reflects that 35% of the outstanding unpaid principal balance of our mortgage revenue bonds are guaranteed by third parties.

Investments in Alt-A and Subprime Private-Label Mortgage-Related Securities

As indicated in Table 24, the unpaid principal balance of our investments in private-label mortgage-related securities backed by Alt-A and subprime loans totaled $57.8 billion as of June 30, 2008. For our investments in Alt-A and subprime private-label securities, including wraps, classified as trading, we recognized fair value gains of $316 million for the second quarter of 2008 and fair value losses of $763 million for the first six months of 2008. These amounts are included in our condensed consolidated results of operations as a component of Fair value gains (losses), net. The gross unrealized losses on our Alt-A and subprime securities, including wraps, classified as AFS were $7.6 billion as of June 30, 2008, compared with $3.3 billion as of December 31, 2007.

The substantial majority of our Alt-A private-label mortgage securities, or 96%, continued to be rated AAA as of July 31, 2008, and the remaining 4% were rated AA to BBB- as of July 31, 2008. Approximately $4.1 billion, or 14%, of our Alt-A private-label mortgage-related securities had been placed under review for possible credit downgrade or on negative watch as of July 31, 2008.

The percentages of our subprime private-label mortgage-related securities rated AAA and rated AA to BBB- were 42% and 48%, respectively, as of July 31, 2008, compared with 97% and 3%, respectively, as of December 31, 2007. The percentage of our subprime private-label mortgage-related securities rated below investment grade was 10% as of July 31, 2008. None of these securities were rated below investment grade as of December 31, 2007. Approximately $6.2 billion, or 22%, of our subprime private-label mortgage-related securities had been placed under review for possible credit downgrade or on negative watch as of July 31, 2008.

Other-than-temporary Impairment Assessment

Our policy for determining whether an impairment is other-than-temporary is based on an analysis of our AFS securities in an unrealized loss position as of the end of each quarter. As discussed in our 2007 Form 10-K in Item 7 MD&A Critical Accounting Policies and Estimates Other-than-temporary Impairment of Investment Securities, the determination that a security has suffered an other-than-temporary decline in value requires management judgment and consideration of various factors, including, but not limited to, the severity and duration of the impairment, recent events specific to the issuer and/or the industry to which the issuer belongs, and external credit ratings, as well as the probability that we will not collect all of the contractual amounts due and our ability and intent to hold the security until recovery. Although external rating agency actions or changes in a security s external credit rating is one criterion in our assessment of other-than-temporary impairment, a rating action alone is not necessarily indicative of other-than-temporary impairment.

We employ models to assess the expected performance of our Alt-A and subprime private-label securities under hypothetical scenarios. These models incorporate particular attributes of the loans underlying our securities and assumptions about changes in the economic environment, such as home prices and interest rates, to predict borrower behavior and the impact on default frequency, loss severity and remaining credit enhancement. We use these models to estimate the expected cash flows (recoverable amount) from our securities as part of our process in assessing whether it is probable that we will not collect all of the contractual amounts due. If the recoverable amount is less than the contractual principal and interest due, we may determine, based on this factor in combination with our assessment of other relevant factors, that the security is other-than-temporarily impaired. If we make that determination, the amount of other-than-temporary impairment is determined by reference to the security s current fair value, rather than the expected cash flows of the security. We write down any other-than-temporarily impaired AFS security to its current fair value, record the difference between the cost basis and the fair value as an other-than-temporary loss in our consolidated statements of operations and establish a new cost basis for the security based on the current fair value. The fair value measurement we use to determine the amount of other- than-temporary impairment to record

may be less than the actual amount we expect to realize by holding the security to maturity.

The performance of the loans underlying our Alt-A and subprime private-label securities has been adversely impacted by the significant deterioration of conditions in the mortgage and credit markets during the second quarter of 2008, including the rapid acceleration and deepening of home price declines. These conditions have

contributed to a sharp rise in expected defaults and loss severities and slower voluntary prepayment rates, particularly for the 2006 and 2007 loan vintages. Following is a comparison, based on data provided by Intex, where available, of the 60-plus days or more delinquency rates as of June 30, 2008 for Alt-A and subprime loans backing securities owned or guaranteed by Fannie Mae.

Loan Categories	**60+ Day Delinquencies[(1)] As of June 30, 2008**
Option ARM Alt-A loans:	
2004 and prior	15.95%
2005	17.35
2006	21.44
2007	10.79
Other Alt-A loans:	
2004 and prior	3.36
2005	8.78
2006	15.40
2007	17.55
Subprime loans:	
2004 and prior	21.51
2005	36.51
2006	36.13
2007	23.87

(1) For purposes of consistency, where appropriate, we have adjusted the delinquency data obtained from Intex to include in the delinquency rates all bankruptcies, foreclosures and real estate owned.

Our other-than-temporary impairment assessment as of the end of the second quarter of 2008, including an evaluation of the individual performance of the securities and the potential for continued adverse developments, indicated an increased level of uncertainty as to whether we would collect all principal and interest amounts due in accordance with the contractual terms. As a result, we determined that we did not have sufficient persuasive evidence to conclude that the impairment of certain AFS securities was temporary. For these securities, we recognized other-than-temporary impairment totaling $492 million in the second quarter of 2008, of which $116 million related to Alt-A securities with an unpaid principal balance of $449 million as of June 30, 2008, and $376 million related to subprime securities with an unpaid principal balance of $2.4 billion as of June 30, 2008. As of June 30, 2008, we had recognized cumulative other-than-temporary impairment totaling $714 million on our investments in Alt-A and subprime securities classified as AFS, including the $492 million that was recognized in the second quarter of 2008.

The current market pricing of Alt-A and subprime securities, which reflects a significant discount to cost, has been adversely affected by a significant reduction in the liquidity of these securities and market perceptions that defaults on the mortgages underlying these securities will increase significantly. As a result, the current fair value of some of these is substantially less than what we believe is indicated by the performance of the collateral underlying the securities and our calculation of the expected cash flows of the securities. Accordingly, although we have recognized other-than-temporary impairment equal to the difference between the cost basis and the fair value of the security, we anticipate at this time, based on the expected cash flows of the securities, that we will recover some of these impairment amounts. For the AFS Alt-A securities for which we recognized other-than-temporary impairment during

the second quarter of 2008, the average credit enhancement was approximately 16% and the expected average collateral loss was approximately 17%, resulting in projected expected credit losses of $51 million. For the AFS subprime securities for which we recognized other-than-temporary impairment during the second quarter of 2008, the average credit enhancement was approximately 24% and the expected average collateral loss was approximately 37%, resulting in projected expected credit losses of $172 million. However, the other-than-temporary impairment we recorded on our Alt-A and subprime securities totaled $116 million and $376 million, respectively. We will accrete into interest income the portion of the amounts we expect to recover that exceeds the cost basis of these securities over the remaining life of the securities. The amount accreted into earnings on our Alt-A and subprime securities for which we have recognized other-than-temporary impairment totaled $26 million and $48 million for the three and six months ended June 30, 2008, respectively.

We will continue to monitor and analyze the performance of these securities to assess the collectability of principal and interest as of each balance sheet date. If there is further deterioration in the housing and mortgage markets and the decline in home prices exceeds our current expectations, we may recognize significant other-than-temporary impairment amounts in the future. See Part II Item 1A Risk Factors of this report for a discussion of the risks related to potential future write-downs of our investment securities.

Hypothetical Performance Scenarios

Tables 25, 26 and 27 present additional information as of June 30, 2008 for our investments in Alt-A and subprime private-label mortgage-related securities, stratified by year of issuance (vintage) and by credit enhancement quartile for securities issued in 2005, 2006 and 2007. The 2006 and 2007 vintages of loans underlying these securities have experienced significantly higher delinquency rates than other vintages. Accordingly, the year of issuance or origination of the collateral underlying these securities is a significant factor in projecting expected cash flow performance and evaluating the ongoing credit performance. The credit enhancement quartiles presented range from the lowest level of credit enhancement to the highest. A higher level of credit enhancement generally reduces the exposure to loss.

We have disclosed for information purposes the net present value of projected losses (NPV) of our securities under four hypothetical scenarios, which assume specific cumulative constant default and loss severity rates against the loans underlying our Alt-A and subprime private-label securities. The projected loss results under these scenarios, which are considered stressful based on historical mortgage loan performance, are calculated based on the projected cash flows from each security and include the following additional key assumptions: (i) discount rate, (ii) expected constant prepayment rates (CPR) and (iii) average life of the securities. These scenarios assume a discount rate based on LIBOR and constant default and loss severity rates experienced over a six-year period. We assume CPRs of 15% for our Alt-A securities and 10% to 15% for our subprime securities, which vary in each scenario based on the loan age. We experienced a decrease in the NPV loss amounts as of June 30, 2008 from the NPV loss amounts previously disclosed as of March 31, 2008, which was attributable to the reduction in the outstanding principal balance of our securities from principal payments and better than expected performance of the loans underlying the securities.

Table 25: Investments in Alt-A Private-Label Mortgage-Related Securities, Excluding Wraps*

	As of June 30, 2008											
	Unpaid Principal Balance				Credit Enhancement Statistics				Hypothetical Scenarios[6]			
ntage and E Quartile[1]	Trading Securities[2]	AFS Securities[3]	Average Price	Fair Value	Average Current[4]	Original[4]	Minimum Current[4]	Monoline Financial Guaranteed Amount[5]	20d/40s NPV	20d/50s NPV	30d/40s NPV	50d/50s NPV
	(Dollars in millions)											
vestments in t-A curities:[7]												
otion ARM t-A securities:												
04 and prior	$	$ 704	$ 82.09	$ 578	22%	9%	16%	$	$	$	$	$ 31
05-1(1)		105	78.65	83	19	7	19					4
05-1(2)		109	78.43	85	20	7	20					4
05-1(3)		198	80.00	158	24	12	20					6
05-1(4)		165	78.09	129	42	33	33					
05-1 subtotal		577	78.91	455	27	16	19					14
05-2(1)		255	78.84	201	34	24	33					5
05-2(2)		256	79.10	203	39	32	39					3
05-2(3)		375	79.64	298	48	36	45					1
05-2(4)		337	84.76	286	100	100	100	337				
05-2 subtotal		1,223	80.77	988	58	51	33	337				9
06-1(1)		135	66.57	90	21	19	11					30
06-1(2)		419	75.43	316	41	38	40					3
06-1(3)		389	75.14	292	45	42	45					
06-1(4)		434	75.61	328	88	88	49	335				
06-1 subtotal		1,377	74.54	1,026	55	53	11	335				33
06-2(1)												
06-2(2)		215	76.70	165	37	35	37					
06-2(3)		100	76.43	77	42	40	42					
06-2(4)		224	82.22	184	69	68	47	92				
06-2 subtotal		539	78.95	426	51	50	37	92				

07-1(1)	209		76.06	159	25	24	24					10
07-1(2)	371		75.54	280	46	45	45					
07-1(3)	264		72.75	192	48	47	48					
07-1(4)	529		71.02	376	100	100	100	530				
07-1 subtotal	1,373		73.34	1,007	64	64	24	530				10
07-2(1)	296		77.40	229	33	32	25					10
07-2(2)	216		77.60	167	47	47	47					
07-2(3)	311		78.04	243	48	47	48					
07-2(4)	422		76.74	324	100	100	100	422				
07-2 subtotal	1,245		77.37	963	62	62	25	422				10
08-1(1)												
08-1(2)												
08-1(3)												
08-1(4)												
08-1 subtotal												
tal Option rm Alt-A curities	$ 2,618	$ 4,420	$ 77.34	$ 5,443	53%	49%	11%	$ 1,716	$	$	$	$ 10
ading curities with pothetical PV losses:(9)												
ir Value									$	$	$	$ 30
PB												39
fference									$	$	$	$ (9
FS securities th pothetical PV losses:(9)												
ir Value									$	$	$ 46	1,73
PB											66	2,21
fference									$	$	$ (20)	(47

	As of June 30, 2008										
	Unpaid Principal Balance				Credit Enhancement Statistics				Hypothetical Scenarios(6		
d e(1)	Trading Securities(2)	AFS Securities(3)	Average Price	Fair Value	Average Current(4)	Original(4)	Minimum Current(4)	Monoline Financial Guaranteed Amount(5)	20d/40s NPV	20d/50s NPV	30d/40s NPV
	(Dollars in millions)										
in ities:(7)											
ior	$	$ 9,195	$ 87.97	$ 8,089	12%	6%	4%	$ 29	$ 22	$ 75	$ 170
		387	87.28	338	9	5	6		1	4	9
		471	87.19	410	13	7	12			1	3
		363	91.27	331	14	11	14			1	5
		523	87.35	457	17	12	15				3
otal		1,744	88.11	1,536	14	9	6		1	6	20
		1,022	87.82	898	6	5	4		17	35	54
		1,023	85.51	875	11	8	8			6	20
		933	82.74	772	16	14	14				2
		1,194	81.45	972	21	17	18				
otal		4,172	84.29	3,517	14	11	4		17	41	76
	34	1,110	91.85	1,051	5	4	5		28	49	71
		1,103	86.97	959	10	8	9		5	16	30
	51	1,324	85.93	1,182	15	12	12				2
		1,351	76.54	1,034	22	17	19				
otal	85	4,888	84.97	4,226	13	11	5		33	65	103
		518	77.89	404	11	10	6				3
		284	74.16	210	17	16	17				
		343	77.67	266	18	16	18				
otal		1,145	76.90	880	15	13	6				3
	76		77.12	59	7	5	7				
	189		76.55	145	8	7	7		1	3	4
	109		79.08	86	12	11	8				
	236		77.84	183	17	16	16				

otal	610		77.57	473	12	11	7		1	3	4
	457		83.26	381	100	100	100	457			
otal	457		83.26	381	100	100	100	457			
		173	93.02	161	20	20	20				
otal[10]		173	93.02	161	20	20	20				
Alt-A	$ 1,152	$ 21,317	$ 85.73	$ 19,263	15%	11%	4%	$ 486	$ 74	$ 190	$ 376
urities etical [9]											
									$ 98	$ 98	$ 157
									113	113	189
									$ (15)	$ (15)	$ (32)
ies with l NPV											
									$ 5,254	$ 8,150	$ 11,496
									5,832	9,135	13,016
									$ (578)	$ (985)	$ (1,520)

* The footnotes to this table are presented following Table 26.

Table 26: Investments in Subprime Private-Label Mortgage-Related Securities, Excluding Wraps

	As of June 30, 2008											
	Unpaid Principal Balance				Credit Enhancement Statistics				Hypothetical Scenarios[6]			
e and artile[1]	Trading Securities[2]	AFS Securities[3]	Average Price	Fair Value	Average Current[4]	Original[4]	Minimum Current[4]	Monoline Financial Guaranteed Amount[5]	50d/50s NPV	50d/60s NPV	60d/50s NPV	60 N
	(Dollars in millions)											
nents in ne es:[8]												
d prior	$	$ 3,109	$ 86.75	$ 2,697	74%	54%	13%	$ 1,398	$ 2	$ 4	$ 6	$
(1)												
(2)		26	94.68	25	69	36	69					
(3)												
(4)		44	83.37	37	78	29	78					
subtotal		70	87.55	62	75	31	69					
(1)		95	95.44	91	41	23	37					
(2)		96	90.00	86	54	32	54					
(3)		225	91.23	205	60	32	57					
(4)		166	91.86	153	80	63	65	69				
subtotal		582	91.90	535	62	39	37	69				
(1)		1,428	81.35	1,162	26	19	24					
(2)		1,770	82.67	1,463	29	20	28					
(3)		1,794	85.33	1,531	36	22	33					
(4)		1,692	82.81	1,401	49	32	40	52				
subtotal		6,684	83.14	5,557	35	23	24	52				
(1)		2,810	79.69	2,240	22	18	19				2	
(2)		3,060	80.27	2,456	25	19	24					
(3)		3,273	79.20	2,592	29	23	27					
(4)		3,167	81.25	2,573	35	28	31					
subtotal		12,310	80.10	9,861	28	22	19				2	
(1)	613		48.17	295	17	16	9		66	162	208	
(2)	741		81.23	602	27	24	25					

(3)	629		81.06	510	28	24	28					
(4)	840		78.71	661	50	45	30	228				
subtotal	2,823		73.27	2,068	32	29	9	228	66	162	208	
(1)	485		64.67	314	25	23	14		8	37	56	
(2)	399	394	84.72	671	30	28	28					
(3)		516	86.76	448	35	33	34					
(4)	904		85.95	777	62	60	42	317				
subtotal	1,788	910	81.92	2,210	41	39	14	317	8	37	56	
(1)												
(2)												
(3)												
(4)												
subtotal												
ubprime es	$ 4,611	$ 23,665	$ 81.30	$ 22,990	37%	28%	9%	$ 2,064	$ 76	$ 203	$ 272	$
g es with etical sses:(9)												
lue									$ 33	$ 66	$ 207	$
									223	371	558	
nce									$ (190)	$ (305)	$ (351)	$
curities												
etical sses:(9)												
lue									$ 36	$ 298	$ 834	$
									39	335	1,002	
nce									$ (3)	$ (37)	$ (168)	$ (

(1) Reported based on half-year vintages for 2005, 2006 and 2007, with each half-year vintage stratified based on credit enhancement quartiles.

(2) For the second quarter 2008, we recognized net fair value gains on our investments in private-label Alt-A securities classified as trading of $5 million and net fair value losses on our private-label subprime securities classified as trading of $118 million. For the first six months of 2008, we recognized net fair value losses on our investments in private-label Alt-A securities and subprime classified as trading of $565 million and $575 million, respectively.

(3) Gross unrealized losses as of June 30, 2008 related to our investments in Alt-A private-label securities and subprime private-label securities classified as AFS totaled $3.9 billion and $3.6 billion, respectively.

(4) Average current, original and minimum credit enhancement percentages reflect both subordination and financial guarantees. Reflects the ratio of the current amount of the securities that will incur losses in a securitization structure before any losses are allocated to securities that we own. Percentage calculated based on the quotient of the total unpaid principal balance of all credit enhancement in the form of subordination or financial guaranty 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.

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

(6) Reflects the present value of projected losses based on the disclosed hypothetical cumulative default and loss severity rates against the outstanding collateral balance.

(7) Consists of private-label securities backed by Alt-A mortgage loans that are reported in our mortgage portfolio as a component of non-Fannie Mae structured securities.

(8) Consists of private-label securities backed by subprime loans that are reported in our mortgage portfolio as a component of non-Fannie Mae structured securities. Excludes guaranteed resecuritizations of private-label securities backed by subprime loans held in our mortgage portfolio totaling $8.0 billion as of June 30, 2008, which are presented in Table 27 Alt-A and Subprime Private Label Wraps.

(9) Reflects the unpaid principal balance and fair value amounts of all securities for which the expected cash flows of the security under the specified hypothetical scenario were less than the unpaid principal balance of the security as of June 30, 2008.

(10) The 2008-1 vintage for other Alt-A securities consists entirely of a security from a resecuritized REMIC transaction whose underlying bonds represent senior bonds from 2007 residential mortgage-backed securities (RMBS) transactions backed by Alt-A loans. These bonds have a weighted average credit enhancement of 5.03% as of June 30, 2008 and an original weighted average credit enhancement of 4.68%.

The projected loss results for the scenarios presented above are for indicative purposes only and should not be construed as a prediction of our future results, market conditions or actual performance of these securities. These scenarios, which are based on numerous assumptions, including specific constant default and severity rates, are not the only way to analyze the performance of these securities. For example, as discussed above, we consider various factors in our assessment of other-than-temporary impairment, the most critical of which is whether it is probable that we will not collect all of the contractual amounts due. This assessment is not based on specific constant default and severity rates, but instead involves assumptions including, but not limited to the following: actual default, prepayment or loss severity rates; the effectiveness of subordination and credit enhancement; the level of interest rates; changes in loan characteristics; the level of losses covered by monoline financial guarantors; the financial condition of other transaction participants; and changes in applicable legislation and regulation that may impact performance.

Alt-A and Subprime Private-Label Wraps

In addition to Alt-A and subprime private-label mortgage-related securities included in our mortgage portfolio, we also have exposure to private-label Alt-A and subprime mortgage-related securities that have been resecuritized (or wrapped) to include our guaranty. The unpaid principal balance of these Fannie Mae guaranteed securities held by third parties is included in outstanding and unconsolidated Fannie Mae MBS held by third parties, which we discuss in Off-Balance Sheet Arrangements and Variable Interest Entities. Table 27 presents the unpaid principal balance of our Alt-A and subprime private-label wraps as of June 30, 2008 and additional information to evaluate our potential loss exposure. We held $8.0 billion of these securities in our mortgage portfolio as of June 30, 2008.

Table 27: Alt-A and Subprime Private-Label Wraps

	As of June 30, 2008								
		Credit Enhancement Statistics				Hypothetical Scenarios[5]			
Vintage and CE Quartile[1]	**Unpaid Principal Balance[2]**	**Average Current[3]**	**Original[3]**	**Minimum Current[3]**	**Monoline Financial Guaranteed Amount[4]**	**20d/40s NPV**	**20d/50s NPV**	**30d/40s NPV**	**30d/50s NPV**
	(Dollars in millions)								
Alt-A wraps:									
2005-1(1)	$	%	%	%	$	$	$	$	$
2005-1(2)									
2005-1(3)									
2005-1(4)	240	6	4	6					
2005-1 subtotal	240	6	4	6					
2007-1(1)									
2007-1(2)									
2007-1(3)									
2007-1(4)	319	9	7	9					
2007-1 subtotal	319	9	7	9					
2008-1(1)									
2008-1(2)									
2008-1(3)									
2008-1(4)									
2008-1 subtotal									
Total Alt-A wraps	$ 559	8%	6%	6%	$	$	$	$	$

	As of June 30, 2008								
		Credit Enhancement Statistics				Hypothetical Scenarios[5]			
Vintage and CE Quartile[1]	Unpaid Principal Balance[2]	Average Current[3]	Original[3]	Minimum Current[3]	Monoline Financial Guaranteed Amount[4]	50d/50s NPV	50d/60s NPV	60d/50s NPV	60d/60s NPV
	(Dollars in millions)								
Subprime wraps:									
2004 and prior	$ 885	37%	14%	14%	$ 15	$	$	$	$
2005-1(1)	89	58	22	58					
2005-1(2)									
2005-1(3)	319	61	18	59					
2005-1(4)	141	84	31	73					
2005-1 subtotal	549	66	22	58					
2005-2(1)	438	39	25	26				1	7
2005-2(2)	709	46	32	46					
2005-2(3)	595	50	26	46					
2005-2(4)	611	79	56	55	203				
2005-2 subtotal	2,353	54	35	26	203			1	7
2007-1(1)	1,531	19	17	19			1	30	139
2007-1(2)	1,797	23	20	22				1	70
2007-1(3)	1,705	25	22	24					29
2007-1(4)	1,943	32	26	28				1	33
2007-1 subtotal	6,976	25	21	19			1	32	271
2007-2(1)	289	27	24	24					10
2007-2(2)									
2007-2(3)	439	32	30	32					11
2007-2(4)	497	33	30	33					
2007-2 subtotal	1,225	31	29	24					21
2008-1(1)									
2008-1(2)									
2008-1(3)									
2008-1(4)									
2008-1 subtotal									
Total subprime wraps	$ 11,988	34%	24%	14%	$ 218	$	$ 1	$ 33	$ 299

Total Alt-A and subprime wraps	$ 12,547	33%	24%	6%	$ 218	$	$ 1	$ 33	$ 299

(1) Reported based on half-year vintages for 2005, 2006 and 2007, with each half-year vintage stratified based on credit enhancement quartiles.

(2) For the second quarter and first six months of 2008, we recognized net fair value gains on our investments in subprime private-label wraps classified as trading of $428 million and $377 million, respectively. We did not recognize any fair value gains or losses on our investments in Alt-A private-label wraps during this period. Gross unrealized losses related to our investments in subprime private-label wraps classified as AFS totaled $14 million as of June 30, 2008. We did not have any gross unrealized gains or losses on our investments in Alt-A private-label wraps as of June 30, 2008.

(3) Average current, original and minimum credit enhancement percentages reflect both subordination and financial guarantees. Reflects the ratio of the current amount of the securities that will incur losses in a securitization structure before any losses are allocated to securities that we own. Percentage calculated based on the quotient of the total unpaid principal balance of all credit enhancement in the form of subordination or financial guaranty 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.

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

(5) Reflects the present value of projected losses based on the disclosed hypothetical cumulative default and loss severity rates against the outstanding collateral balance.

Debt Instruments

We issue debt instruments as the primary means to fund our mortgage investments and manage our interest rate risk exposure. Table 28 below provides a summary of our debt activity for the three and six months ended June 30, 2008 and 2007.

Table 28: Debt Activity

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
	(Dollars in millions)			
Issued during the period:[1]				
Short-term:[2]				
Amount:[3]	$ 404,431	$ 346,473	$ 840,884	$ 783,167
Weighted average interest rate	2.07%	5.11%	2.50%	5.13%
Long-term:[4]				
Amount:[3]	$ 83,589	$ 54,160	$ 171,867	$ 113,291
Weighted average interest rate	3.71%	5.58%	3.88%	5.57%
Total issued:				
Amount:[3]	$ 488,020	$ 400,633	$ 1,012,751	$ 896,458
Weighted average interest rate	2.35%	5.17%	2.73%	5.19%
Redeemed during the period:[1][5]				
Short-term:[2]				
Amount:[3]	$ 380,417	$ 340,874	$ 836,047	$ 784,222
Weighted average interest rate	2.58%	5.12%	3.07%	5.12%
Long-term:[4]				
Amount:[3]	$ 65,730	$ 43,576	$ 171,869	$ 97,248
Weighted average interest rate:	4.90%	4.75%	5.00%	4.54%
Total redeemed:				
Amount:[3]	$ 446,147	$ 384,450	$ 1,007,916	$ 881,470
Weighted average interest rate	2.92%	5.08%	3.40%	5.06%

(1) Excludes debt activity resulting from consolidations and intraday loans.

(2) Short-term debt consists of borrowings with an original contractual maturity of one year or less. Includes Federal funds purchased and securities sold under agreements to repurchase.

(3) Represents the face amount at issuance or redemption.

(4) Long-term debt consists of borrowings with an original contractual maturity of greater than one year.

(5) Represents all payments on debt, including regularly scheduled principal payments, payments at maturity, payments as the result of a call and payments for any other repurchases.

Despite the significant volatility in the financial markets during the first six months of 2008, including historically high credit spreads, we remained an active issuer of short-term and long-term debt securities to meet our consistent need for funding and rebalancing our portfolio. We issued and redeemed a higher amount of debt during the first six months of 2008 relative to the first six months of 2007, as we continued to rebalance our portfolio.

Table 29 summarizes our outstanding short-term borrowings and long-term debt as of June 30, 2008 and December 31, 2007. We provide additional detail on our outstanding short-term and long-term debt in Notes to Condensed Consolidated Financial Statements Note 8, Short-term Borrowings and Long-term Debt.

Table 29: Outstanding Debt[1]

	June 30, 2008		December 31, 2007	
	Outstanding	Weighted Average Interest Rate	Outstanding	Weighted Average Interest Rate
	(Dollars in millions)			
Federal funds purchased and securities sold under agreements to repurchase	$ 443	1.84%	$ 869	3.48%
Short-term debt[2]	240,223	2.43	234,160	4.45
Long-term debt[3]	559,279	4.86	562,139	5.25

(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 as of June 30, 2008 include fair value gains and losses associated with debt that we elected to carry at fair value pursuant to our January 1, 2008 adoption of SFAS 159. The unpaid principal balance of outstanding debt, which excludes unamortized discounts, premiums and other cost basis adjustments and amounts related to debt from consolidation, totaled $809.4 billion and $804.3 billion as June 30, 2008 and December 31, 2007, respectively.

(2) Short-term debt consists of borrowings with an original contractual maturity of one year or less.

(3) Long-term debt consists of borrowings with an original contractual maturity of greater than one year. Reported amounts include net discount and cost basis adjustments of $14.6 billion and $11.6 billion as of June 30, 2008 and December 31, 2007, respectively. The unpaid principal balance of long-term debt, which excludes unamortized discounts, premiums and other cost basis adjustments and amounts related to debt from consolidation, totaled $567.4 billion and $567.2 billion as June 30, 2008 and December 31, 2007, respectively.

Our short-term and long-term debt includes callable debt that can be redeemed in whole or in part at our option at any time on or after a specified date. The amount of our outstanding debt that was callable totaled $212.8 billion and had an average interest rate of 4.93% as of June 30, 2008, compared with $215.6 billion and an average interest rate of 5.35% as of December 31, 2007.

Derivative Instruments

We supplement our issuance of debt with interest rate-related derivatives to manage the prepayment and duration risk inherent in our mortgage investments. We present, by derivative instrument type, the estimated fair value of derivatives recorded in our condensed consolidated balance sheets and the related outstanding notional amount as of June 30, 2008 and December 31, 2007 in Notes to Condensed Consolidated Financial Statements Note 9, Derivative Instruments and Hedging Activities.

Table 30 provides an analysis of changes in the estimated fair value of the net derivative asset (liability) amounts, excluding mortgage commitments, recorded in our condensed consolidated balance sheets between December 31, 2007 and June 30, 2008.

Table 30: Changes in Risk Management Derivative Assets (Liabilities) at Fair Value, Net[(1)]

	For the Six Months Ended June 30, 2008 (Dollars in millions)
Net derivative liability as of December 31, 2007[(2)]	$ (1,321)
Effect of cash payments:	
Fair value at inception of contracts entered into during the period[(3)]	713
Fair value at date of termination of contracts settled during the period[(4)]	(573)
Net collateral posted	794
Periodic net cash contractual interest payments (receipts)[(5)]	204
Total cash payments (receipts)	1,138
Income statement impact of recognized amounts:	
Periodic net contractual interest income (expense) accruals on interest rate swaps	(330)
Net change in fair value of terminated derivative contracts from end of prior year to date of termination	174
Net change in fair value of outstanding derivative contracts, including derivative contracts entered into during the period	(290)
Derivatives fair value losses, net[(6)]	(446)
Net derivative liability as of June 30, 2008[(2)]	$ (629)

(1) Excludes mortgage commitments.

(2) Reflects the net amount of Derivative assets at fair value and Derivative liabilities at fair value recorded in our condensed consolidated balance sheets, excluding mortgage commitments, and reflects our adoption of FASB Staff Position No. 39-1, *Amendment of FASB Interpretation No. 39*.

(3) Cash payments made to purchase derivative option contracts (purchased options premiums) increase the derivative asset recorded in the condensed consolidated balance sheets. Primarily includes upfront premiums paid or received on option contracts. Also includes upfront cash paid or received on other derivative contracts.

(4) Cash payments to terminate and/or sell derivative contracts reduce the derivative liability recorded in the condensed consolidated balance sheets. Primarily represents cash paid (received) upon termination of derivative

contracts.

(5) We accrue interest on our interest rate swap contracts based on the contractual terms and recognize the accrual as an increase to the net derivative liability recorded in the condensed consolidated balance sheets. The corresponding offsetting amount is recorded as an expense and included as a component of derivatives fair value losses in the condensed consolidated statements of operations. Periodic interest payments on our interest rate swap contracts reduce the derivative liability.

(6) Reflects net derivatives fair value losses recognized in the condensed consolidated statements of operations, excluding mortgage commitments.

The decrease in the net derivative liability to $629 million as of June 30, 2008, from $1.3 billion as of December 31, 2007 was primarily attributable to an increase in the aggregate net fair value of our interest rate swaps due to the increase in swap interest rates during the first six months of 2008. We present, by derivative instrument type, our risk management derivative activity for the six months ended June 30, 2008, along with the stated maturities of our derivatives outstanding as of June 30, 2008, in Table 43 in Risk Management Interest Rate Risk Management and Other Market Risks.

Table 31 provides information on our option activity for the first six months of 2008 and the amount of outstanding options as of June 30, 2008 based on the original premiums paid.

Table 31: Purchased Options Premiums

	Original Premium Payments	Original Weighted Average Life to Expiration	Remaining Weighted Average Life
	(Dollars in millions)		
Outstanding options as of December 31, 2007	$ 7,843	8.4 years	4.6 years
Purchases[1]	723		
Exercises	(1,601)		
Terminations	(54)		
Expirations	(219)		
Outstanding options as of June 30, 2008	$ 6,692	7.6 years	4.3 years

[1] Amount of purchases is included in Table 30 as a component of the line item Fair value at inception of contracts entered into during the period.

SUPPLEMENTAL NON-GAAP INFORMATION FAIR VALUE BALANCE SHEETS

Each of the non-GAAP supplemental consolidated fair value balance sheets presented below in Table 32 reflects all of our assets and liabilities at estimated fair value. The non-GAAP estimated fair value of our net assets (net of tax effect) is derived from our non-GAAP fair value balance sheet. This measure is not a defined term within GAAP and may not be comparable to similarly titled measures reported by other companies. The estimated fair value of our net assets (net of tax effect) presented in the non-GAAP supplemental consolidated fair value balance sheets is not intended as a substitute for amounts reported in our consolidated financial statements prepared in accordance with GAAP. We believe, however, that the non-GAAP supplemental consolidated fair value balance sheets and the fair value of our net assets, when used in conjunction with our consolidated financial statements prepared in accordance with GAAP, can serve as valuable incremental tools for investors to assess changes in our overall value over time relative to changes in market conditions. In addition, we believe that the non-GAAP supplemental consolidated fair value balance sheets are useful to investors because they provide consistency in the measurement and reporting of all of our assets and liabilities. Management uses this information to gain a clearer picture of changes in our assets and liabilities from period to period, to understand how the overall value of the company is changing from period to period and to measure the performance of our investment activities.

Cautionary Language Relating to Supplemental Non-GAAP Financial Measures

In reviewing our non-GAAP supplemental 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 and does not incorporate other factors that may have a significant impact on that value, most notably any value from future business activities in which we expect to engage. As a result, the estimated fair value of our net assets presented in our non-GAAP supplemental 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 significantly from the estimated fair values presented in our non-GAAP supplemental consolidated fair value balance sheets. Because temporary changes in market conditions can substantially affect the fair value of our net assets, we do not believe that short-term fluctuations in the fair value of our net assets attributable to mortgage-to-debt OAS or changes in the fair value of our net guaranty assets are necessarily representative of the effectiveness of our investment strategy or the long-term underlying value of our business. We believe the long-term value of our business depends primarily on our ability to acquire new assets and funding at attractive prices and to effectively manage the risks of these assets and

liabilities over time. However, we believe that focusing on the factors that affect near-term changes in the estimated fair value of our net assets helps us evaluate our long-term value and assess whether temporary market factors have caused our net assets to become overvalued or undervalued relative to the level of risk and expected long-term fundamentals of our business.

As discussed in Critical Accounting Policies and Estimates Fair Value of Financial Instruments, when quoted market prices or observable market data are not available to estimate fair value, we rely on level 3 inputs to estimate fair value. Because assets and liabilities classified as level 3 are generally based on unobservable inputs, the process to determine fair value is generally more subjective and involves a high degree of management judgment and assumptions. These assumptions may have a significant effect on our estimates of fair value, and the use of different assumptions as well as changes in market conditions could have a material effect on our results of operations or financial condition.

Table 32: Supplemental Non-GAAP Consolidated Fair Value Balance Sheets

	As of June 30, 2008			As of December 31, 2007		
	GAAP Carrying Value	Fair Value Adjustment[1]	Estimated Fair Value	GAAP Carrying Value	Fair Value Adjustment[1]	Estimated Fair Value[2]
	(Dollars in millions)					
Assets:						
Cash and cash equivalents	$ 13,681	$	$ 13,681(3)	$ 4,502	$	$ 4,502(3)
Federal funds sold and securities purchased under agreements to resell	35,694		35,694(3)	49,041		49,041(3)
Trading securities	99,562		99,562(3)	63,956		63,956(3)
Available-for-sale securities	245,226		245,226(3)	293,557		293,557(3)
Mortgage loans:						
Mortgage loans held for sale	6,931	79	7,010(4)	7,008	75	7,083(4)
Mortgage loans held for investment, net of allowance for loan losses	411,300	(2,526)	408,774(4)	396,516	70	396,586(4)
Guaranty assets of mortgage loans held in portfolio		3,925	3,925(4)(5)		3,983	3,983(4)(5)
Guaranty obligations of mortgage loans held in portfolio		(9,074)	(9,074)(4)(5)		(4,747)	(4,747)(4)(5)
Total mortgage loans	418,231	(7,596)	410,635(3)(4)	403,524	(619)	402,905(3)(4)
Advances to lenders	9,459	(223)	9,236(3)	12,377	(328)	12,049(3)
Derivative assets at fair value	1,013		1,013(3)	885		885(3)
Guaranty assets and buy-ups, net	11,402	5,167	16,569(3)(5)	10,610	3,648	14,258(3)(5)

Total financial assets	834,268	(2,652)	831,616(3)	838,452	2,701	841,153(3)
Master servicing assets and credit enhancements	1,561	5,607	7,168(5)(6)	1,783	2,844	4,627(5)(6)
Other assets	50,089	16,121	66,210(6)(7)	39,154	5,418	44,572(6)(7)
Total assets	$ 885,918	$ 19,076	$ 904,994	$ 879,389	$ 10,963	$ 890,352
Liabilities:						
Federal funds purchased and securities sold under agreements to repurchase	$ 443	$ (5)	$ 438(3)	$ 869	$	$ 869(3)
Short-term debt	240,223(8)	33	240,256(3)	234,160	208	234,368(3)
Long-term debt	559,279(8)	13,267	572,546(3)	562,139	18,194	580,333(3)
Derivative liabilities at fair value	1,712		1,712(3)	2,217		2,217(3)
Guaranty obligations	16,441	43,336	59,777(3)	15,393	5,156	20,549(3)
Total financial liabilities	818,098	56,631	874,729(3)	814,778	23,558	838,336(3)
Other liabilities	26,430	(8,781)	17,649(9)	20,493	(4,383)	16,110(9)
Total liabilities	844,528	47,850	892,378	835,271	19,175	854,446
Minority interests in consolidated subsidiaries	164		164	107		107
Stockholders Equity (Deficit):						
Preferred	21,725	(3,883)	17,842(10)	16,913	(1,565)	15,348(10)
Common	19,501	(24,891)	(5,390)(11)	27,098	(6,647)	20,451(11)
Total stockholders equity/non-GAAP fair value of net assets	**$ 41,226**	**$ (28,774)**	**$ 12,452**	**$ 44,011**	**$ (8,212)**	**$ 35,799**
Total liabilities and stockholders equity	$ 885,918	$ 19,076	$ 904,994	$ 879,389	$ 10,963	$ 890,352

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) Certain prior period amounts have been reclassified to conform to the current period presentation.

(3) We determined the estimated fair value of these financial instruments in accordance with the fair value guidelines outlined in SFAS No. 157, as described in Notes to Condensed Consolidated Financial Statements Note 17, Fair Value of Financial Instruments. In Note 17, we also disclose the carrying value and estimated fair value of our total financial assets and total financial liabilities as well as discuss the methodologies and assumptions we use in estimating the fair value of our financial instruments.

(4) We have separately presented the estimated fair value of Mortgage loans held for sale, Mortgage loans held for investment, net of allowance for loan losses, Guaranty assets of mortgage loans held in portfolio and Guaranty obligations of mortgage loans held in portfolio, which, taken together, represent total mortgage loans reported in our GAAP condensed consolidated balance sheets. In order to present the fair value of our guarantees in these non-GAAP consolidated fair value balance sheets, we have separated (i) the embedded fair value of the guaranty assets, based on the terms of our intra-company guaranty fee allocation arrangement, and the embedded fair value of the obligation from (ii) the fair value of the mortgage loans held for sale and the mortgage loans held for investment. We believe this presentation provides transparency into the components of the fair value of the mortgage loans associated with the activities of our guaranty businesses and the components of the activities of our capital markets business, which is consistent with the way we manage risks and allocate revenues and expenses for segment reporting purposes. While the carrying values and estimated fair values of the individual line items may differ from the amounts presented in Note 17 of the condensed consolidated financial statements, the combined amounts together equal the carrying value and estimated fair value amounts of total mortgage loans in Note 17.

(5) In our GAAP condensed consolidated balance sheets, we report the guaranty assets associated with our outstanding Fannie Mae MBS and other guarantees as a separate line item and include buy-ups, master servicing assets and credit enhancements associated with our guaranty assets in Other assets. The GAAP carrying value of our guaranty assets reflects only those guaranty arrangements entered into subsequent to our adoption of FIN No. 45, *Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others (an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FIN No. 34)* (FIN 45), on January 1, 2003. On a GAAP basis, our guaranty assets totaled $10.3 billion and $9.7 billion as of June 30, 2008 and December 31, 2007, respectively. The associated buy-ups totaled $1.1 billion and $944 million as of June 30, 2008 and December 31, 2007, respectively. In our non-GAAP supplemental consolidated fair value balance sheets, we also disclose the estimated guaranty assets and obligations related to mortgage loans held in our portfolio. The aggregate estimated fair value of the guaranty asset-related components totaled $18.6 billion and $18.1 billion as of June 30, 2008 and December 31, 2007, respectively. These components represent the sum of the following line items in this table: (i) Guaranty assets of mortgage loans held in portfolio; (ii) Guaranty obligations of mortgage loans held in portfolio, (iii) Guaranty assets and buy-ups; and (iv) Master servicing assets and credit enhancements. See Critical Accounting Policies and Estimates Change in Measuring the Fair Value of Guaranty Obligations.

(6) The line items Master servicing assets and credit enhancements and Other assets together consist of the assets presented on the following five line items in our GAAP condensed consolidated balance sheets: (i) Accrued

interest receivable; (ii) Acquired property, net; (iii) Deferred tax assets; (iv) Partnership investments; and (v) Other assets. The carrying value of these items in our GAAP condensed consolidated balance sheets together totaled $52.8 billion and $41.9 billion as of June 30, 2008 and December 31, 2007, respectively. We deduct the carrying value of the buy-ups associated with our guaranty obligation, which totaled $1.1 billion and $944 million as of June 30, 2008 and December 31, 2007, respectively, from Other assets reported in our GAAP condensed consolidated balance sheets because buy-ups are a financial instrument that we combine with guaranty assets in our SFAS 107 disclosure in Note 17. We have estimated the fair value of master servicing assets and credit enhancements based on our fair value methodologies discussed in Note 17.

(7) With the exception of partnership investments and deferred tax assets, the GAAP carrying values of other assets generally approximate fair value. While we have included partnership investments at their carrying value in each of the non-GAAP supplemental consolidated fair value balance sheets, the fair values of these items are generally different from their GAAP carrying values, potentially materially. Our LIHTC partnership investments had a carrying value of $7.0 billion and $8.1 billion and an estimated fair value of $7.9 billion and $9.3 billion as of June 30, 2008 and December 31, 2007, respectively. We assume that certain other assets, consisting primarily of prepaid expenses, have no fair value. Our GAAP-basis deferred tax assets are described in Notes to Condensed Consolidated Financial Statements Note 10, Income Taxes. In addition to the GAAP-basis deferred income tax amounts included in Other assets, we include in our non-GAAP supplemental consolidated fair value balance sheets the estimated income tax effect related to the fair value adjustments made to derive the fair value of our net assets. Because our adjusted deferred income taxes are a net asset in each year, the amounts are included in our non-GAAP fair value balance sheets as a component of other assets.

(8) Includes certain short-term debt and long-term debt instruments reported in our GAAP condensed consolidated balance sheet at fair value as of June 30, 2008 of $4.5 billion and $22.5 billion, respectively.

(9) The line item Other liabilities consists of the liabilities presented on the following four line items in our GAAP condensed consolidated balance sheets: (i) Accrued interest payable; (ii) Reserve for guaranty losses; (iii) Partnership liabilities; and (iv) Other liabilities. The carrying value of these items in our GAAP condensed consolidated balance sheets together totaled $26.4 billion and $20.5 billion as of June 30, 2008 and December 31, 2007, respectively. The GAAP carrying values of these other liabilities generally approximate fair value. We assume that certain other liabilities, such as deferred revenues, have no fair value. Although we report the Reserve for guaranty losses as a separate line item on our 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 condensed consolidated fair value balance sheets.

(10) Preferred stockholders equity is reflected in our non-GAAP supplemental condensed consolidated fair value balance sheets at the estimated fair value amount.

(11) Common stockholders equity consists of the stockholders equity components presented on the following five line items in our GAAP consolidated balance sheets: (i) Common stock; (ii) Additional paid-in capital; (iii) Retained earnings; (iv) Accumulated other comprehensive loss; and (v) Treasury stock, at cost. Common stockholders equity is the residual of the excess (deficit) of the estimated fair value of total assets over the estimated fair value of total liabilities, after taking into consideration preferred stockholders equity and minority interest in consolidated subsidiaries.

Changes in Non-GAAP Estimated Fair Value of Net Assets

We expect periodic fluctuations in the estimated fair value of our net assets due to our business activities, as well as due to changes in market conditions, including changes in interest rates, changes in relative spreads between our mortgage assets and debt, and changes in implied volatility. As discussed in Critical Accounting Policies and Estimates Fair Value of Financial Instruments Change in Measuring the Fair Value of Guaranty Obligations, beginning January 1, 2008, as part of the implementation of SFAS 157, we changed our approach to measuring the fair value of our guaranty obligations. We believe that this change, which increased the previously reported fair value of our net assets as of December 31, 2007 by $1.6 billion to $37.4 billion, provides a more meaningful presentation of the guaranty obligations by better aligning the revenue we recognize for providing our guaranty with the compensation we receive. Table 33 summarizes the changes in the fair value of our net assets for the first six months of 2008.

Table 33: Non-GAAP Estimated Fair Value of Net Assets (Net of Tax Effect)

	For the Six Months Ended June 30, 2008 (Dollars in millions)
Balance as of December 31, 2007, as reported	$ 35,799
Effect of change in measuring fair value of guaranty obligations[1]	1,558
Balance as of December 31, 2007, as adjusted to include effect of change in measuring fair value of guaranty obligations	37,357

Capital transactions:[2]	
Common dividends, common stock repurchases and issuances, net	1,869
Preferred dividends and issuances, net	4,060
Capital transactions, net	5,929
Change in estimated fair value of net assets, excluding effect of capital transactions	(30,834)
Decrease in estimated fair value of net assets, net	(24,905)
Balance as of June 30, 2008[3]	$ 12,452

(1) Represents the estimated after-tax impact of the change in our approach to measuring the fair value of our guaranty obligations as part of our January 1, 2008 implementation of SFAS 157. Amount reflects the difference of $2.3 billion ($1.6 billion after-tax) between the estimated fair value of our guaranty obligations based on our current valuation approach of $18.2 billion as of December 31, 2007, and the previously reported fair value of our guaranty obligations of $20.5 billion as of December 31, 2007.

(2) Represents net capital transactions, which are reflected in the condensed consolidated statements of changes in stockholders equity.

(3) Represents estimated fair value of net assets (net of tax effect) presented in Table 32: Supplemental Non-GAAP Consolidated Fair Value Balance Sheets.

Table 34 presents selected market information that impacts changes in the fair value of our net assets.

Table 34: Selected Market Information(1)

	As of		
	June 30, 2008	**December 31, 2007**	**Change**
10-year U.S. Treasury note yield	3.97%	4.03%	(0.06)%
Implied volatility(2)	21.9	20.4	1.5
30-year Fannie Mae MBS par coupon rate	5.84	5.51	0.33
Lehman U.S. MBS Index OAS (in basis points) over LIBOR yield curve	59.2bp	26.2bp	33.0bp
Lehman U.S. Agency Debt Index OAS (in basis points) over LIBOR yield curve	(12.3)	(20.2)	7.9

(1) Information obtained from Lehman Live, Lehman POINT and Bloomberg.

(2) Implied volatility for an interest rate swaption with a 3-year option on a 10-year final maturity.

The estimated fair value of our net assets, excluding capital transactions, decreased by $30.8 billion during the first six months of 2008. This decrease was offset by net proceeds of $5.9 billion from capital transactions, resulting in a net decrease in the estimated fair value of our net assets of $24.9 billion to $12.5 billion as of June 30, 2008, from an adjusted $37.4 billion as of December 31, 2007. The primary factors driving the $30.8 billion decline were: (i) a decrease of approximately $25.2 billion in the fair value of our net guaranty assets, net of tax, reflecting the significant increase in the fair value of our guaranty obligations attributable to an increase in expected credit losses as well as an increase in risk premium due to our current guaranty fee pricing and (ii) a decrease in the fair value of the net portfolio for our capital markets business, largely attributable to the significant widening of mortgage-to-debt OAS during the first six months of 2008, which had an estimated effect of approximately $5.9 billion.

The $25.2 billion decline in the fair value of our net guaranty assets, net of tax, was driven by the substantial increase in the estimated fair value of our guaranty obligations (approximately $25.5 billion net of tax), which we now measure based on the compensation we currently require to provide our guaranty and assume the credit risk associated with the mortgage loans underlying the guaranteed Fannie Mae MBS, or mortgage credit risk. This increase in the fair value of our guaranty obligations resulted from both an increase in the underlying risk in our guaranty book of business, as delinquencies increased and declining home prices continued to adversely affect mark-to-market LTV ratios, and an increase in the estimated mortgage credit risk premium required to take mortgage credit risk in the current market, as indicated by the pricing of our new guaranty business. Although we continue to measure the estimated fair value of our guaranty obligations using the models and inputs we used prior to January 1, 2008, since January 1, 2008, we have calibrated these models to our current guaranty fee compensation, which includes our March 2008 and June 2008 guaranty fee price increases. As a result, the estimated fair value of our guaranty obligations as of June 30, 2008 takes into account the guaranty fees we currently charge, regardless of the date on which we actually issued any of our guarantees. Because we measure the fair value of our guaranty obligations based on our pricing as of the fair value

measurement date, the fair value of these obligations generally will increase when our risk-adjusted guaranty fees increase, resulting in a reduction in the fair value of our net assets. Similarly, the fair value of the guaranty obligations generally will decrease when our risk-adjusted guaranty fees decrease, resulting in an increase in the fair value of our net assets. The total fair value of our guaranty obligations presented in our non-GAAP supplemental consolidated fair value balance sheets is not reflective of our expected credit losses because it consists of not only future expected credit losses but also an estimated market risk premium that is based on our current risk pricing. For more information about how we measure the fair value of our guaranty obligations, refer to Critical Accounting Policies and Estimates Fair Value of Financial Instruments Change in Measuring the Fair Value of Guaranty Obligations.

The widening of mortgage-to-debt spreads during the first six months of 2008 contributed to approximately $5.9 billion of the decline in the fair value of our net assets. As indicated in Table 34 above, the Lehman U.S. MBS index, which primarily includes 30-year and 15-year mortgages, reflected a further widening of

OAS during the first six months of 2008. The OAS on securities held by us that are not in the index, such as AAA-rated 10-year CMBS and AAA-rated private-label mortgage-related securities, widened even more dramatically, resulting in an overall decrease in the fair value of our mortgage assets. Debt OAS based on the Lehman U.S. Agency Debt Index to LIBOR fell by 7.9 basis points during the first six months of 2008 to minus 12.3 basis points as of June 30, 2008, which resulted in a decrease in the fair value of our debt from December 31, 2007.

LIQUIDITY AND CAPITAL MANAGEMENT

We actively manage our liquidity and capital position with the objective of preserving stable, reliable and cost-effective sources of cash to meet all of our current and future operating financial commitments and regulatory capital requirements. We obtain the funds we need to operate our business primarily from the proceeds we receive from the issuance of debt. We seek to maintain sufficient excess liquidity in the event that factors, whether internal or external to our business, temporarily prevent us from issuing debt in the capital markets.

Liquidity

Sources and Uses of Cash

Our sources of cash include:

- proceeds from the issuance of our debt;
- principal and interest payments received on our mortgage portfolio assets;
- principal and interest payments received on our liquid investments;
- borrowings under secured and unsecured intraday funding lines of credit we have established with several large financial institutions;
- sales of mortgage loans, mortgage-related securities and liquid assets;
- borrowings against mortgage-related securities and other investment securities we hold pursuant to repurchase agreements and loan agreements;
- guaranty fees earned on Fannie Mae MBS;
- mortgage insurance counterparty payments; and
- net receipts on derivative instruments.

Our uses of cash include:

- the repayment of matured, redeemed and repurchased debt;
- the purchase of mortgage loans, mortgage-related securities and other investments;
- interest payments on outstanding debt;
- net payments on derivative counterparty agreements;

the pledging of collateral under derivative instruments;

administrative expenses;

the payment of federal income taxes;

losses incurred in connection with our Fannie Mae MBS guaranty obligations; and

the payment of dividends on our common and preferred stock.

Funding

Because our primary source of cash is proceeds from the issuance of our debt securities, we depend on our ability to issue debt securities in the capital markets on an ongoing basis to meet our cash requirements. During the first six months of 2008, we issued $840.9 billion in short-term debt and $171.9 billion in long-term debt. We also redeemed $1.0 trillion of debt securities during the first six months of 2008. As of June 30, 2008, we had $240.2 billion in outstanding short-term debt and $559.3 billion in outstanding long-term debt, compared with $234.2 billion in outstanding short-term debt and $562.1 billion in outstanding long-term debt as of December 31, 2007. For information about our debt activity for the three and six months ended June 30, 2008 and 2007, and our outstanding short-term and long-term debt as of June 30, 2008 and December 31, 2007, refer to Consolidated Balance Sheet Analysis Debt Instruments and Notes to Condensed Consolidated Financial Statements Note 8, Short-term Borrowings and Long-term Debt.

Our sources of liquidity remain adequate to meet our short-term and long-term needs for funding. During the first six months of 2008, we did not experience limitations on our ability to borrow funds through the issuance of debt securities at attractive rates in the capital markets, and we remained an active issuer of short-term and long-term debt securities to meet our continual need for funding and rebalancing our portfolio.

From July 2007 though June 2008, the company was able to raise short-term funds at unusually attractive yields relative to market benchmarks, such as LIBOR. In the first three weeks of July 2008 the secondary market yields of our outstanding short term debt increased in response to market concerns about the U.S. housing market and its impact on the company s capital position and future profitability. As an example, our auction of three-month debt on July 2, 2008 resulted in a spread-to-LIBOR of -44 basis points whereas the auction on July 23, 2008 resulted in a spread of -16 basis points. On July 13, 2008 the U.S. Department of Treasury and the Board of Governors of the Federal Reserve announced actions designed to support our continued operation, including making proposals for legislative authority that would permit the government to support our financial position by lending funds to us or taking an equity position in the company. Those proposed legislative provisions were enacted into law on July 30, 2008. These announcements and actions have helped to reduce market concerns and strengthen our access to the debt markets and have had a positive impact on the cost of our debt. Our auction of three-month debt on July 30, 2008 resulted in a spread-to-LIBOR of -37 basis points, an improvement of 21 basis points from the prior week.

The company historically has issued most of its long-term debt in the form of fixed-rate callable medium term notes. The notes are distributed through broker-dealers who negotiate the terms of this debt with the company via a process known as reverse inquiry . In July, we noted a significant decrease in demand for such issuances, as has happened in past periods of market stress. Heightened market concerns about housing market conditions and their potential impact on the GSEs characterized this most recent period.

Throughout the second quarter and July, the company maintained its access to liquidity. During July, we increased our net issuance of short-term debt which resulted in an increase of our outstanding short-term debt by an estimated $31 billion. The incremental proceeds were invested primarily in federal funds and short-term bank deposits. In addition, during July, our new issuance of long-term debt exceeded the total of redemptions, maturities, and repurchases of previously issued long-term debt, resulting in an increase in our outstanding long-term debt by an estimated $3 billion. We have not needed to trigger any of the contingency plans, as described below in Liquidity Risk Management to generate liquidity through other means.

The U.S. Treasury and Federal Reserve announcements have had some positive impacts on the market for our debt. We continue to believe that the short-term debt markets provide superior pricing and liquidity than the long-term debt markets. To the extent that the liquidity and pricing in the long-term debt market does not improve, we could have

increased reliance on short-term debt funding versus our historical issuance pattern. If at some point in the future, our outstanding short-term debt increases significantly from its current level, it could result in an increase of the cost of issuing that debt and the risk associated with rolling over short-term debt on a frequent basis. In extreme cases, limited investor demand for our short-term debt securities at reasonable yields could require us to use contingent sources of liquidity, such as using our mortgage assets as collateral for financing. To date, investor demand has been sufficient to meet our liquidity requirements. We continue to carefully monitor the current volatile market conditions to determine the impact of these

conditions on our funding and liquidity. Further disruptions and continued turmoil in the financial markets could result in changes in the amount, mix and cost of funds we obtain and could have a material adverse impact on our financial condition.

See Part I Item 1A Risk Factors of our 2007 Form 10-K and Part II Item 1A Risk Factors of this report for a discussio of the risks related to our ability to obtain funds through the issuance of debt securities, and the cost at which we are able to obtain these funds. The U.S. government does not guarantee our debt and our debt does not constitute a debt or obligation of the U.S. government or of any of its agencies or instrumentalities.

We also obtained funds in the second quarter of 2008 through the issuance of common and preferred stock. We had not previously issued common stock in a public offering since February 1987. As described in Capital Management Capital Activity below, we issued a total of $7.4 billion in common stock, non-cumulative mandatory convertible preferred stock, and non-cumulative, non-convertible preferred stock in the second quarter of 2008, in order to preserve and further build our capital. These stock issuances increased our core capital and resulted in a material change in the mix of our capital resources and increased the relative cost of those resources. We cannot be certain whether, or at what terms, we will have access to this kind of funding in the future. To the extent we were able to access this form of funding, any new issuance could be dilutive to existing shareholders and/or may result in further downgrades from the ratings agencies.

Under the Regulatory Reform Act, the Secretary of the U.S. Treasury has additional temporary authority to purchase our obligations and other securities on terms that Treasury may determine, subject to our agreement. As of August 7, 2008, Fannie Mae has not entered into any specific agreement with Treasury to obtain such funds nor have terms been defined as to the cost and conditions of any such investment. Any investment by Treasury could materially adversely affect our business and our ability to access the private capital markets in the future. See Part II Item 1A Risk Factors of this report for information on how any use of this facility could materially adversely affect our business and liquidity.

Liquidity Risk Management

We define liquidity risk as the risk that would arise from an inability to meet our cash obligations in a timely manner. We have met, and continue to meet, our cash obligations in a timely manner. Our liquidity position could be adversely affected by many causes, both internal and external to our business, including elimination of Fannie Mae s GSE status, a sustained period of negative coverage of Fannie Mae in the media, an unexpected systemic event leading to the withdrawal of liquidity from the market, a sudden catastrophic operational failure in the financial sector due to a terrorist attack or other event, an extreme market-wide widening of credit spreads, a downgrade of our credit ratings from the major ratings organizations, loss of demand for Fannie Mae debt from a major group of investors or a significant credit event involving one of our major institutional counterparties. See Part II Item 1A Risk Factors of this report for a description of factors that could adversely affect our liquidity.

Liquidity Risk Policy

Our liquidity risk policy governs our management of liquidity risk and outlines our methods for measuring and monitoring liquidity risk.

We conduct daily liquidity management activities to achieve the goals of our liquidity risk policy. The primary tools that we employ for liquidity management include the following:

- daily monitoring and reporting of our liquidity position;

- daily monitoring of market and economic factors that may impact our liquidity;

daily forecasting of our ability to meet our liquidity needs over a 90-day period without relying upon the issuance of long-term or short-term unsecured debt securities;

daily forecasting and statistical analysis of our daily cash needs over a 28 business day period;

maintaining an investment portfolio of liquid non-mortgage assets that are readily marketable or have short-term maturities so that we can quickly and easily convert these assets into cash;

routine testing of our ability to rely upon identified sources of liquidity, such as mortgage repurchase agreements;

periodic reporting to management and the Board of Directors regarding our liquidity position;

periodic review and testing of our liquidity management controls by our Internal Audit department; and

maintaining of a portfolio of unencumbered mortgage assets that can be sold or can be pledged as collateral for secured borrowings.

Liquidity Contingency Plan

We maintain a liquidity contingency plan in the event that factors, whether internal or external to our business, temporarily compromise our ability to access funds in the unsecured agency debt market. Our contingency plan provides for alternative sources of liquidity that we believe would allow us to meet all of our cash obligations for 90 days without relying upon the issuance of unsecured debt.

In the event of a liquidity crisis in which our access to the unsecured debt funding market becomes impaired, our primary source of potential liquidity is the unencumbered mortgage portfolio. These assets could be used to raise cash through outright sale or as collateral for secured borrowing. In the event of such a liquidity crisis, haircuts for secured borrowing may be in excess of historical levels, and any sale of assets could be made at valuation levels below historical norms. Our ability to raise funds through the sale or pledge of mortgage assets in the event that we cannot access unsecured funding could be limited if the markets for the sale and financing of mortgage-related assets experience significant disruption or reduced levels of liquidity.

Pursuant to our September 2005 agreement with OFHEO, we periodically test our liquidity contingency plan. We believe we were in compliance with our agreement with OFHEO to maintain and test our liquidity contingency plan as of June 30, 2008.

Liquid Investment Portfolio

Another source of liquidity in the event of a liquidity crisis is the sale or maturation of assets in our liquid investment portfolio (LIP). Our LIP is designed to provide a pool of funds that, if drawn upon, should provide sufficient time for us to implement fully a large scale secured financing program with the mortgage assets in our portfolio. Our LIP contains cash, bank deposits, and other highly-rated non-mortgage securities that are readily marketable or have short-term maturities. Our ability to sell assets from our liquid investment portfolio could be limited in the event of a significant market disruption. As described in Consolidated Balance Sheet Analysis Liquid Investments, we had approximately $82.7 billion and $102.0 billion in liquid assets, net of cash equivalents pledged as collateral, as of June 30, 2008 and December 31, 2007, respectively.

Credit Ratings

Our ability to borrow at attractive rates is highly dependent upon our credit ratings from the major nationally recognized statistical ratings organizations. Our senior unsecured debt (both long-term and short-term), benchmark subordinated debt and preferred stock are rated and continuously monitored by Standard & Poor s, Moody s and Fitch.

In May 2008, for example, Standard & Poor s lowered our risk-to-the-government rating to A+ from AA- with a negative outlook and subsequently, in July 2008, placed it on CreditWatch Negative. In addition, during July 2008, all three rating agencies affirmed or updated our ratings, as follows.

Long-Term and Short-Term Senior Unsecured Debt Ratings. Standard & Poor s, Moody s and Fitch each affirmed their ratings on our long-term and short-term senior unsecured debt, with Standard & Poor s at AAA / A-1+ with a stable outlook; Moody s at Aaa / P-1 with a stable outlook; and Fitch at AAA / F1+ .

Long Term Issuer Default Rating. Fitch affirmed our long-term Issuer Default Rating of AAA with a stable outlook.

Subordinated Debt Ratings. Both Moody s and Fitch affirmed our subordinated debt ratings, with: Moody s at Aa2 with a stable outlook; and Fitch at AA- , while Standard & Poor s placed our AA- subordinated debt rating on CreditWatch Negative.

Preferred Stock Ratings. Moody s downgraded our preferred stock rating to A1 from Aa3 and placed it on review for possible downgrade; Fitch downgraded it to A+ from AA- and maintained it on Rating Watch Negative; and Standard & Poor s placed our AA- rating on CreditWatch Negative.

Bank Financial Strength Rating. Moody s lowered our bank financial strength rating to B− from B and placed it on review for possible downgrade in July 2008; Moody s had previously downgraded this rating in May 2008 to B from B+ with a negative outlook.

Table 35 below sets forth the credit ratings issued by each of these rating agencies of our long-term and short-term senior unsecured debt, subordinated debt and preferred stock as of August 7, 2008. Table 35 also sets forth our risk to the government rating and our Bank Financial Strength Rating as of August 7, 2008.

Table 35: Fannie Mae Credit Ratings

	Senior Long-Term Unsecured Debt	Senior Short-Term Unsecured Debt	Subordinated Debt	Preferred Stock	Risk to the Government[1]	Bank Financial Strength[1]
Standard & Poor s[2]	AAA	A-1+	AA−	AA−	A+	
Moody s[3]	Aaa	P-1	Aa2	A1		B−
Fitch[4]	AAA	F1+	AA−	A+		

(1) Pursuant to our September 2005 agreement with OFHEO, we agreed to seek to obtain a rating that assesses the independent financial strength or risk to the government of Fannie Mae operating under its authorizing legislation but without assuming a cash infusion or extraordinary support of the government in the event of a financial crisis.

(2) In July 2008, Standard & Poor s affirmed our senior debt ratings with stable outlooks and placed on CreditWatch Negative our subordinated debt, preferred stock and risk to the government ratings. In May 2008, they lowered our risk-to-the-government rating to A+ from AA− .

(3) In July 2008, Moody s affirmed our senior debt and subordinated debt ratings with stable outlooks. They downgraded our preferred stock rating to A1 from Aa3 and our bank financial strength rating to B− from B (which was downgraded from B+ to B in May 2008); they placed both ratings on review for possible downgrade.

(4) In July 2008, Fitch affirmed our debt ratings and downgraded our preferred stock rating to A+ from AA− ; they maintained our preferred stock on Rating Watch Negative. Fitch affirmed our long term Issuer Default Rating at AAA with a stable outlook.

Cash Flows

Six Months Ended June 30, 2008. Cash and cash equivalents of $13.5 billion as of June 30, 2008 increased by $9.6 billion from December 31, 2007. Net cash generated from operating activities totaled $29.9 billion, resulting primarily from the proceeds from maturities or sales of our short-term, liquid investments, which are classified as trading securities. We also generated net cash from financing activities of $3.7 billion, reflecting the proceeds from the issuance of common and preferred stock, which was partially offset by the redemption of a significant amount of long-term debt as interest rates fell during the period. Net cash used in investing activities was $24.1 billion, attributable to our purchases of AFS securities and loans held for investment.

Six Months Ended June 30, 2007. Cash and cash equivalents of $5.8 billion as of June 30, 2007 increased by $2.6 billion from December 31, 2006, primarily due to net cash provided by financing activities of $4.2 billion generated from the issuance of debt and net cash of $1.5 billion from investing activities, attributable to net mortgage asset liquidations. These increases were partially offset by net cash used in operating activities of $3.1 billion attributable to an increase in the purchase of HFS mortgage loans.

Capital Management

Regulatory Capital Requirements

On March 19, 2008, OFHEO reduced from 30% to 20% the amount of capital we are required to hold in excess of our statutory minimum capital requirement. On June 9, 2008, OFHEO announced that we were classified as adequately capitalized as of March 31, 2008 (the most recent date for which results have been published by OFHEO). With the completion of our capital raise in May 2008, OFHEO further reduced the amount of capital we are required to hold in excess of our statutory minimum capital requirement to 15%. OFHEO had also indicated its intention to reduce our excess capital requirement to 10% in September 2008, based upon our continued maintenance of excess capital well above OFHEO s regulatory requirement and no material adverse change to our ongoing regulatory compliance. As our new safety, soundness and mission regulator under the Regulatory Reform Act, FHFA will have responsibility for making this determination in September. Under the Regulatory Reform Act, FHFA has the authority to increase our minimum capital levels and to establish additional capital and reserve requirements with respect to any product or activity. FHFA also has the authority to increase our minimum capital levels temporarily if the Director of FHFA determines it necessary and the authority to adjust our capital classification at any time.

On June 10, 2008, OFHEO announced a final rule that changes the mortgage loan loss severity formulas used in our regulatory risk-based capital stress test. This new risk-based capital stress test will be formally applied beginning with the third quarter 2008 capital classification and is expected to increase the risk-based capital requirement. We estimate that our statutory risk-based capital requirement of $23.1 billion as of March 31, 2008, would have instead been $30.4 billion using the new stress test loss severity formulas and assuming no other change. With total capital holdings of $47.7 billion as of March 31, 2008, our estimated $24.6 billion surplus would have instead totaled $17.3 billion or 57% higher than the risk-based capital requirement estimated under the new standard. Under the Regulatory Reform Act, the Director of FHFA has responsibility for establishing our risk-based capital requirements.

For information about our regulatory capital classification measures as of June 30, 2008, refer to Notes to Condensed Consolidated Financial Statements Note 15, Regulatory Capital Requirements. For more information on the authority of our new regulator, refer to Legislation Relating to Our Regulatory Framework.

Amendments being considered by the FASB to SFAS 140 and FIN 46R could affect the amount of capital we would be required to maintain, but would be effective no earlier than January 2010. For a description of these amendments being considered by the FASB, refer to Off-Balance Sheet Arrangements and Variable Interest Entities.

Capital Activity

Capital Management Actions

As described in Consolidated Results of Operations above, we recorded a net loss of $4.5 billion for the first six months of 2008. Because our retained earnings are a component of our core capital, this loss reduced the amount of our core capital. Our losses for the first six months of 2008 were due to continuing market challenges that have adversely affected our results of operations. During the period, we have taken aggressive management actions to preserve and further build our capital, including:

- issuing equity securities. In May and June 2008, we completed public offerings totaling $7.4 billion in common stock, non-cumulative mandatory convertible preferred stock, and non-cumulative, non-convertible preferred stock. For more information on these issuances, refer to Notes to Condensed Consolidated Financial Statements Note 14, Stockholders Equity;

managing the size of our investment portfolio;

selling assets to reduce the amount of capital that we were required to hold and to realize investment gains;

reducing our common stock dividend;

electing not to purchase mortgage assets at attractive prices;

slowing growth of our guaranty business; and

applying other changes to our business practices to reduce our losses and expenses during the period.

Management continues to carefully monitor our capital and dividend positions and the trends impacting those positions and, if necessary, intends to take actions designed to help mitigate the impacts of a worsening environment on those positions. We have already taken some actions, such as:

further reducing our common stock dividend;

further increasing our guaranty fee pricing on new acquisitions; and

evaluating our costs and expenses with the expectation to reduce administrative costs.

Additional steps we could take include: reducing or eliminating our dividends; slowing growth; decreasing the size of our balance sheet; further raising guaranty fees; and raising additional capital (which could be dilutive). Some of these actions could have negative consequences, including decreased revenue due to growth limitations, or increased mark-to-market charges associated with the decreased liquidity for mortgage assets that could arise from a reduction in our market activity. If our capital fails to meet standards set by FHFA, FHFA could require us to enter into a capital restoration plan or take other actions. Refer to Part II Item 1A Risk Factors of this report for a more detailed discussion of how continued declines in our earnings could negatively impact our regulatory capital position.

Dividends

We paid common stock dividends of $0.35 per share, which totaled $343 million, for the second quarter of 2008. Our Board of Directors previously announced its intent to reduce our quarterly common stock dividend, and on August 7, 2008, our Board of Directors declared common stock dividends of $0.05 per share for the third quarter of 2008, payable on August 29, 2008. Our Board of Directors will continue to assess dividend payments for each quarter based upon the facts and conditions existing at the time.

We paid an aggregate of $303 million in preferred stock dividends in the second quarter of 2008 on 16 of our 17 outstanding series of preferred stock. The first dividend on the Mandatory Convertible Preferred Stock Series 2008-1 that was issued on May 14, 2008 will be paid on September 30, 2008. On August 7, 2008, our Board of Directors declared total preferred stock dividends in aggregate of $413 million for the third quarter of 2008, payable on September 30, 2008.

On June 27, 2008, the dividend rate for our Series P Preferred Stock was reset to 4.50% per year. The new dividend rate for the Series P Preferred Stock will be in effect from and including June 30, 2008 to but excluding September 30, 2008.

Subordinated Debt

In September 2005, we agreed with OFHEO to issue and maintain a specified amount of qualifying subordinated debt. As of June 30, 2008, we were in compliance with our OFHEO subordinated debt requirement. The sum of our total capital plus the outstanding balance of our qualifying subordinated debt exceeded our subordinated debt requirement by an estimated $15.7 billion, or 34%, as of June 30, 2008, compared with an estimated $10.3 billion, or 23%, as of December 31, 2007. As of June 30, 2008, we had $9.0 billion in outstanding qualifying subordinated debt.

OFF-BALANCE SHEET ARRANGEMENTS AND VARIABLE INTEREST ENTITIES

We enter into certain business arrangements that are not recorded in our condensed consolidated balance sheets or may be recorded in amounts that are different from the full contract or notional amount of the transaction. These arrangements are commonly referred to as off-balance sheet arrangements, and expose us to potential losses in excess of the amounts recorded in the condensed consolidated balance sheets.

The Financial Accounting Standards Board (FASB) is considering amendments to SFAS No. 140, *Accounting for Transfer and Servicing of Financial Assets and Extinguishments of Liabilities (a replacement of FASB Statement No. 125)* (SFAS 140) to eliminate qualifying special purpose entities (QSPEs). Additionally, the FASB is considering amendments to FIN 46R (revised December 2003), *Consolidation of*

Variable Interest Entities (an interpretation of ARB No. 51) (FIN 46R) that would replace the current consolidation model with a qualitative evaluation that requires consolidation of an entity when the reporting enterprise both (a) has the power to direct matters which significantly impact the activities and success of the entity, and (b) has exposure to benefits and/or losses that could potentially be significant to the entity. If an enterprise is not able to reach a conclusion through the qualitative analysis, it would then proceed to a quantitative evaluation. As of August 7, 2008, the FASB had not formally issued proposed amendments to SFAS 140 or FIN 46R.

Our most significant off-balance sheet arrangements result from the mortgage loan securitization and resecuritization transactions that we routinely enter into as part of the normal course of our guaranty business operations. Currently, most trusts used in our guaranteed securitizations are not consolidated by the company for financial reporting purposes because the trusts are QSPEs under SFAS 140. Because the trusts are not consolidated, the assets and liabilities of the trusts are not reported on our balance sheet, and the amount of capital that we must hold for the guaranties that we provide to these QSPEs is significantly lower than the capital we must hold for assets reported on our balance sheet.

As of June 30, 2008, we had over $2 trillion of assets held in QSPEs. If we are required to consolidate incremental assets and liabilities of these trusts, the amount of capital we would be required to maintain could increase. Under certain circumstances, these changes could have a material adverse impact on our earnings, financial condition and capital position. Since the amendments to SFAS 140 and FIN 46R are not final and the FASB s proposals will be subject to a public comment period, we are unable to predict the impact that the amendments may have on our consolidated financial statements or capital position.

We also enter into other guaranty transactions, liquidity support transactions and hold partnership interests that may involve off-balance sheet arrangements.

Fannie Mae MBS Transactions and Other Financial Guarantees

As described in our 2007 Form 10-K, our maximum potential exposure to credit losses relating to our outstanding and unconsolidated Fannie Mae MBS held by third parties and our other financial guarantees is significantly higher than the carrying amount of the guaranty obligations and reserve for guaranty losses that are reflected in the consolidated balance sheets. In the case of outstanding and unconsolidated Fannie Mae MBS held by third parties, our maximum potential exposure arising from these guaranty obligations is primarily represented by the unpaid principal balance of the mortgage loans underlying these Fannie Mae MBS, which was $2.3 trillion and $2.1 trillion as of June 30, 2008 and December 31, 2007, respectively. In the case of the other financial guarantees that we provide, our maximum potential exposure arising from these guarantees is primarily represented by the unpaid principal balance of the underlying bonds and loans, which totaled $31.8 billion and $41.6 billion as of June 30, 2008 and December 31, 2007, respectively.

Partnership Interests

We had a recorded investment in LIHTC partnerships of $7.0 billion as of June 30, 2008, compared with $8.1 billion as of December 31, 2007. For additional information regarding our holdings in off-balance sheet limited partnerships, refer to Notes to Condensed Consolidated Financial Statements Note 2, Consolidations.

RISK MANAGEMENT

This section updates the information set forth in our 2007 Form 10-K and our 2008 Q1 Form 10-Q relating to our management of risk. For further discussion of the primary risks to our business and how we seek to manage those risks, refer to Part I Item 1A Risk Factors and Part II Item 7 MD&A Risk Management of our 2007 Form 10-K, Part I Item 2 MD&A Risk Management of our 2008 Q1 Form 10-Q and Part II Item 1A Risk Factors of this report.

Credit Risk Management

We are generally subject to two types of credit risk: mortgage credit risk and institutional counterparty credit risk. The deterioration in the mortgage and credit markets, including the national decline in home prices, rating agency downgrades of mortgage-related securities and counterparties, increased level of institutional insolvencies and higher levels of delinquencies and foreclosures, has increased our exposure to both mortgage credit and institutional counterparty credit risks.

Mortgage Credit Risk Management

In order to manage our mortgage credit risk in the shifting market environment, we have significantly reduced our participation in riskier loan product categories and taken steps to ensure that our pricing and our eligibility and underwriting criteria more accurately reflect the current risks in the housing market. Effective June 1, 2008, we implemented Desktop Underwriter 7.0®, a more comprehensive risk assessment model. We believe our new model will significantly improve the credit profile of our single-family acquisitions, particularly for higher risk product segments that have been large drivers of our credit losses. We recently took additional steps that we believe further our ability to manage our mortgage credit risk. These steps include discontinuing the purchase of newly originated Alt-A loans effective January 1, 2009, increasing the adverse market delivery charge announced earlier in the year to 50 basis points from 25 basis points and updating our standard pricing adjustments for mortgage loans with certain risk characteristics. These pricing changes are effective October 1, 2008. In addition, we are continuing to enhance our loss mitigation strategy to minimize the frequency of foreclosure, including increasing our focus on problem loan workouts and developing and implementing new loss mitigation tools such as our HomeSaver Advance initiative.

Mortgage Credit Book of Business

Table 36 displays the composition of our entire mortgage credit book of business, which consists of both on- and off-balance sheet arrangements, as of June 30, 2008 and December 31, 2007. Our single-family mortgage credit book of business accounted for approximately 93% of our entire mortgage credit book of business as of June 30, 2008 and 94% as of December 31, 2007.

Table 36: Composition of Mortgage Credit Book of Business

	As of June 30, 2008					
	Single-Family[1]		Multifamily[2]		Total	
	Conventional[3]	Government[4]	Conventional[3]	Government[4]	Conventional[3]	Government[4]
	(Dollars in millions)					
Mortgage portfolio:[5]						
Mortgage loans[6]	$ 279,233	$ 36,009	$ 104,997	$ 753	$ 384,230	$ 36,762

Fannie Mae MBS[6]	190,695	1,969	353	104	191,048	2,073
Agency mortgage-related securities[6][7]	33,506	1,542		28	33,506	1,570
Mortgage revenue bonds	3,079	2,651	7,898	2,160	10,977	4,811
Other mortgage-related securities[8]	61,222	2,011	25,880	26	87,102	2,037
Total mortgage portfolio	567,735	44,182	139,128	3,071	706,863	47,253
Fannie Mae MBS held by third parties[9]	2,198,519	14,068	38,762	933	2,237,281	15,001
Other credit guarantees[10]	14,752		17,014	46	31,766	46
Mortgage credit book of business	$ 2,781,006	$ 58,250	$ 194,904	$ 4,050	$ 2,975,910	$ 62,300
Guaranty book of business	$ 2,683,199	$ 52,046	$ 161,126	$ 1,836	$ 2,844,325	$ 53,882

	As of December 31, 2007					
	Single-Family[1]		Multifamily[2]		Total	
	Conventional[3]	Government[4]	Conventional[3]	Government[4]	Conventional[3]	Government[4]
	(Dollars in millions)					
Mortgage portfolio:[5]						
Mortgage loans[6]	$ 283,629	$ 28,202	$ 90,931	$ 815	$ 374,560	$ 29,017
Fannie Mae MBS[6]	177,492	2,113	322	236	177,814	2,349
Agency mortgage-related securities[6][7]	31,305	1,682		50	31,305	1,732
Mortgage revenue bonds	3,182	2,796	8,107	2,230	11,289	5,026
Other mortgage-related securities[8]	68,240	1,097	25,444	30	93,684	1,127
Total mortgage portfolio	563,848	35,890	124,804	3,361	688,652	39,251
Fannie Mae MBS held by third parties[9]	2,064,395	15,257	38,218	1,039	2,102,613	16,296
Other credit guarantees[10]	24,519		17,009	60	41,528	60
Mortgage credit book of business	$ 2,652,762	$ 51,147	$ 180,031	$ 4,460	$ 2,832,793	$ 55,607
Guaranty book of business	$ 2,550,035	$ 45,572	$ 146,480	$ 2,150	$ 2,696,515	$ 47,722

(1) The amounts reported above reflect our total single-family mortgage credit book of business. Of these amounts, the portion of our single-family mortgage credit book of business for which we have access to detailed loan-level information represented approximately 96% and 95% of our total conventional single-family mortgage credit book of business as of June 30, 2008 and December 31, 2007, respectively. Unless otherwise noted, the credit statistics we provide in the discussion that follows relate only to this specific portion of our conventional single-family mortgage credit book of business. The remaining portion of our conventional single-family mortgage credit book of business consists of Freddie Mac securities, Ginnie Mae securities, private-label mortgage-related securities, Fannie Mae MBS backed by private-label mortgage-related securities, housing-related municipal revenue bonds, other single-family government related loans and securities, and credit enhancements that we provide on single-family mortgage assets. See Consolidated Balance Sheet Analysis Trading and Available-For-Sale Investment Securities Investments in Private-Label Mortgage-Related Securities for additional information on our private-label mortgage securities.

(2) The amounts reported above reflect our total multifamily mortgage credit book of business. Of these amounts, the portion of our multifamily mortgage credit book of business for which we have access to detailed loan-level information represented approximately 81% and 80% of our total multifamily mortgage credit book of business as of June 30, 2008 and December 31, 2007, respectively. Unless otherwise noted, the credit statistics we provide in the discussion that follows relate only to this specific portion of our multifamily mortgage credit book of business.

(3) Refers to mortgage loans and mortgage-related securities that are not guaranteed or insured by the U.S. government or any of its agencies.

(4) Refers to mortgage loans and mortgage-related securities guaranteed or insured by the U.S. government or one of its agencies.

(5) Mortgage portfolio data is reported based on unpaid principal balance.

(6) Includes unpaid principal balance totaling $82.4 billion and $81.8 billion as of June 30, 2008 and December 31, 2007, respectively, related to mortgage-related securities that were consolidated under FIN 46 and mortgage-related securities created from securitization transactions that did not meet the sales criteria under SFAS 140, which effectively resulted in these mortgage-related securities being accounted for as loans.

(7) Includes mortgage-related securities issued by Freddie Mac and Ginnie Mae. We held mortgage-related securities issued by Freddie Mac with both a carrying value and fair value of $33.4 billion and $31.2 billion as of June 30, 2008 and December 31, 2007, respectively, which exceeded 10% of our stockholders equity as of each respective date.

(8) Includes mortgage-related securities issued by entities other than Fannie Mae, Freddie Mac or Ginnie Mae.

(9) Includes Fannie Mae MBS held by third-party investors. The principal balance of resecuritized Fannie Mae MBS is included only once in the reported amount.

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

Single-Family

Table 37 presents our conventional single-family business volumes for the six months ended June 30, 2008 and 2007 and our conventional single-family mortgage credit book of business as of June 30, 2008 and December 31, 2007 based on certain key risk characteristics that we use to evaluate the risk profile and credit quality of our loans.

Table 37: Risk Characteristics of Conventional Single-Family Business Volume and Mortgage Credit Book of Business[1]

	Percent of Conventional Single-Family Business Volume[2]				Percent of Conventional Single-Family Book of Business[3]	
			For the Six Months Ended June 30,		As of	
	Q2 2008	Q1 2008	2008	2007	June 30, 2008	December 31, 2007
Original LTV ratio:[4]						
<= 60%	24%	21%	22%	18%	23%	23%
60.01% to 70%	17	16	17	14	16	16
70.01% to 80%	38	37	38	48	43	43
80.01% to 90%	11	12	11	7	8	8
90.01% to 100%	10	14	12	13	10	10
Greater than 100%						
Total	100%	100%	100%	100%	100%	100%
Weighted average	71%	73%	72%	74%	72%	72%
Average loan amount	$ 206,205	$ 209,086	$ 207,593	$ 194,252	$ 146,503	$ 142,747
Estimated mark-to-market LTV ratio:[5]						
<= 60%					41%	46%
60.01% to 70%					15	15
70.01% to 80%					18	19
80.01% to 90%					12	12
90.01% to 100%					8	6
Greater than 100%					6	2
Total					100%	100%
Weighted average					65%	61%
Product type:						
Fixed-rate:[6]						
Long-term	72%	79%	75%	74%	72%	71%

Intermediate-term	15	11	13	6	14	15
Interest-only	1	3	2	10	3	3
Total fixed-rate	88	93	90	90	89	89
Adjustable-rate:						
Interest-only	5	5	5	7	5	5
Negative-amortizing					1	1
Other ARMs	7	2	5	3	5	5
Total adjustable-rate	12	7	10	10	11	11
Total	100%	100%	100%	100%	100%	100%

	Percent of Conventional Single-Family Business Volume[2]				Percent of Conventional Single-Family Book of Business[3]	
			For the Six Months Ended June 30,		As of	
	Q2 2008	Q1 2008	2008	2007	June 30, 2008	December 31, 2007
Number of property units:						
1 unit	97%	97%	97%	96%	96%	96%
2-4 units	3	3	3	4	4	4
Total	100%	100%	100%	100%	100%	100%
Property type:						
Single-family homes	90%	90%	90%	89%	91%	91%
Condo/Co-op	10	10	10	11	9	9
Total	100%	100%	100%	100%	100%	100%
Occupancy type:						
Primary residence	90%	90%	90%	88%	90%	90%
Second/vacation home	5	4	5	5	5	4
Investor	5	6	5	7	5	6
Total	100%	100%	100%	100%	100%	100%
FICO credit score:						
< 620	3%	5%	3%	6%	5%	5%
620 to < 660	5	8	7	11	10	10
660 to < 700	15	17	16	20	18	18
700 to < 740	22	22	22	23	23	23
>= 740	55	48	52	40	44	43
Not available						1
Total	100%	100%	100%	100%	100%	100%
Weighted average	738	728	733	717	722	721
Loan purpose:						
Purchase	34%	34%	34%	47%	40%	41%
Cash-out refinance	34	33	34	34	32	32
Other refinance	32	33	32	19	28	27
Total	100%	100%	100%	100%	100%	100%
Geographic concentration:[7]						

Midwest	16%	16%	16%	15%	16%	17%
Northeast	18	17	18	18	19	19
Southeast	23	25	24	26	25	25
Southwest	16	16	16	18	16	16
West	27	26	26	23	24	23
Total	100%	100%	100%	100%	100%	100%

	Percent of Conventional Single-Family Business Volume[2]				Percent of Conventional Single-Family Book of Business[3]	
			For the Six Months Ended June 30,		As of	
	Q2 2008	**Q1 2008**	**2008**	**2007**	**June 30, 2008**	**December 31, 2007**
Origination year:						
<=1998					2%	2%
1999						1
2000						
2001					2	2
2002					6	7
2003					20	22
2004					11	12
2005					14	16
2006					15	17
2007					21	21
2008					9	
Total					100%	100%

(1) As noted in Table 36 above, we generally have access to detailed loan-level statistics only on conventional single-family mortgage loans held in our portfolio and backing Fannie Mae MBS (whether held in our portfolio or held by third parties).

(2) Percentages calculated based on unpaid principal balance of loans at time of acquisition. Single-family business volume refers to both single-family mortgage loans we purchase for our mortgage portfolio and single-family mortgage loans we securitize into Fannie Mae MBS.

(3) Percentages calculated based on unpaid principal balance of loans as of the end of each period.

(4) The original LTV ratio generally is based on the appraised property value reported to us at the time of acquisition of the loan and the original unpaid principal balance of the loan. Excludes loans for which this information is not readily available.

(5) The aggregate estimated mark-to-market LTV ratio is based on the estimated current value of the property, calculated using an internal valuation model that estimates periodic changes in home value, and the unpaid principal balance of the loan as of the date of each reported period. Excludes loans for which this information is not readily available.

(6) Long-term fixed-rate consists of mortgage loans with maturities greater than 15 years, while intermediate-term fixed-rate have maturities equal to or less than 15 years.

(7) Midwest consists of IL, IN, IA, MI, MN, NE, ND, OH, SD and WI. Northeast includes CT, DE, ME, MA, NH, NJ, NY, PA, PR, RI, VT and VI. Southeast consists of AL, DC, FL, GA, KY, MD, MS, NC, SC, TN, VA and WV. Southwest consists of AZ, AR, CO, KS, LA, MO, NM, OK, TX and UT. West consists of AK, CA, GU, HI, ID, MT, NV, OR, WA and WY.

Credit risk profile summary. Our conventional single-family mortgage credit book of business continues to consist mostly of traditional fixed-rate mortgage loans. As a result of changes we made in our underwriting and eligibility criteria to reduce our credit risk, we experienced a shift in the risk profile of our new business for the first six months of 2008 relative to the first six months of 2007. We believe the change in the composition of our new business, including a significant increase in the weighted average FICO credit score and a reduction in the proportion of higher risk, interest-only loans to more traditional, fully amortizing fixed-rate mortgage loans, reflects an improvement in the overall credit quality of our new business. The increase in the estimated weighted average mark-to-market LTV ratio of our conventional single-family mortgage credit book of business to 65% as of June 30, 2008, from 61% as of December 31, 2007 was largely due to the national decline in home prices.

Alt-A and Subprime Loans. We provide information below on our exposure to Alt-A and subprime mortgage loans. Our Alt-A loans have recently accounted for a significant portion of our credit losses.

Alt-A Loans: Alt-A mortgage loans, whether held in our portfolio or backing Fannie Mae MBS, represented approximately 4% of our single-family business volume for the first six months of 2008, compared with approximately 22% for the first six months of 2007. The significant decline in Alt-A volume is due in part to our recent and continued tightening of eligibility standards and price increases, as well as the overall decline in the Alt-A market. As a result of these recent eligibility restrictions and price increases, we expect our Alt-A mortgage loan acquisitions to be significantly limited in future periods. In addition, we are discontinuing the purchase of newly originated Alt-A loans effective January 1, 2009. Alt-A mortgage loans held in our portfolio or Alt-A mortgage loans backing Fannie Mae MBS, excluding resecuritized private-label mortgage-related securities backed by Alt-A mortgage loans, represented approximately 11% of our total single-family mortgage credit book of business as of June 30, 2008, compared with approximately 12% as of December 31, 2007.

Subprime Loans: Subprime mortgage loans, whether held in our portfolio or backing Fannie Mae MBS, represented less than 1% of our single-family business volume for the first six months of 2008 and 2007. We estimate that subprime mortgage loans held in our portfolio or subprime mortgage loans backing Fannie Mae MBS, excluding resecuritized private-label mortgage-related securities backed by subprime mortgage loans, represented approximately 0.3% of our total single-family mortgage credit book of business as of both June 30, 2008 and December 31, 2007.

See Consolidated Results of Operations Credit-Related Expenses Credit Loss Performance Metrics for information on the portion of our credit losses attributable to Alt-A and subprime loans. See Consolidated Balance Sheet Analysis Trading and Available-for-Sale Investment Securities Investments in Private-Label Mortgage-Related Securities for information on our investments in Alt-A and subprime private-label mortgage-related securities, including other-than-temporary impairment losses recognized on these investments.

Jumbo-Conforming Loans. We began acquiring jumbo-conforming loans in April 2008 in response to the Economic Stimulus Act of 2008. We believe we have priced these loans to compensate us for the related risk. As of June 30, 2008, we had 1,619 outstanding jumbo-conforming loans with an unpaid principal balance of $947 million.

Multifamily

The weighted average original LTV ratio for our multifamily mortgage credit book of business was 67% as of both June 30, 2008 and December 31, 2007. The percentage of our multifamily mortgage credit book of business with an original LTV ratio greater than 80% was 5% as of June 30, 2008, compared with 6% as of December 31, 2007.

Mortgage Credit Book of Business Performance

Key statistical metrics that we use to measure credit risk in our mortgage credit book of business and evaluate credit performance include: (1) the serious delinquency rate; (2) nonperforming loans; and (3) foreclosure activity. We provide information below on these metrics. We provide information on our credit loss performance, another key metric we use to evaluate credit performance, in Consolidated Results of Operations Credit-Related Expenses Credit Loss Performance Metrics.

Serious Delinquency

Table 38 below compares the serious delinquency rates, by geographic region, for all conventional single-family loans and multifamily loans with credit enhancement and without credit enhancement as of June 30, 2008, December 31, 2007 and June 30, 2007.

Table 38: Serious Delinquency Rates

	June 30, 2008		December 31, 2007		June 30, 2007	
	Book Outstanding[1]	Serious Delinquency Rate[2]	Book Outstanding[1]	Serious Delinquency Rate[2]	Book Outstanding[1]	Serious Delinquency Rate[2]
Conventional single-family delinquency rates by geographic region:[3]						
Midwest	16%	1.57%	17%	1.35%	17%	0.98%
Northeast	19	1.21	19	0.94	19	0.68
Southeast	25	1.80	25	1.18	24	0.68
Southwest	16	1.08	16	0.86	16	0.60
West	24	0.97	23	0.50	24	0.23
Total conventional single-family loans	100%	1.36%	100%	0.98%	100%	0.64%
Conventional single-family loans:						
Credit enhanced	21%	3.74%	21%	2.75%	20%	1.81%
Non-credit enhanced	79	0.74	79	0.53	80	0.35
Total conventional single-family loans	100%	1.36%	100%	0.98%	100%	0.64%
Multifamily loans:						
Credit enhanced	87%	0.09%	88%	0.06%	90%	0.09%
Non-credit enhanced	13	0.22	12	0.22	10	0.04
Total multifamily loans	100%	0.11%	100%	0.08%	100%	0.09%

(1) Reported based on unpaid principal balance of loans, where we have detailed loan-level information.

(2) Calculated based on number of loans for single-family and unpaid principal balance for multifamily. We include all of the conventional single-family loans that we own and that back Fannie Mae MBS in the calculation of the single-family delinquency rate. We include the unpaid principal balance of all multifamily loans that we own or that back Fannie Mae MBS and any housing bonds for which we provide credit enhancement in the calculation of the multifamily serious delinquency rate.

(3) See footnote 7 to Table 37 for states included in each geographic region.

In the first six months of 2008, our serious delinquency rates, which are a leading indicator of potential foreclosures, increased across our entire conventional single-family mortgage credit book of business to 1.36% as of June 30, 2008, from 0.98% as of December 31, 2007 and 0.64% as of June 30, 2007. We experienced the most notable increases in serious delinquency rates in California, Florida, Arizona and Nevada, which previously experienced rapid increases in home prices and are now experiencing sharp declines in home prices. In addition, we continued to experience significant increases in the serious delinquency rates in some higher risk loan categories: Alt-A loans, adjustable-rate loans, interest-only loans, negative amortization loans, loans made for the purchase of condominiums and loans with second liens. Many of these higher risk loans were originated in 2006 and 2007. As a result of tightening our eligibility standards and underwriting criteria, we expect that the loans we are now acquiring will have a lower credit risk relative to the loans we acquired in 2006 and 2007.

The conventional single-family serious delinquency rates for California and Florida, which represent the two largest states in our conventional single-family mortgage credit book of business in terms of unpaid principal balance, climbed to 1.05% and 3.21%, respectively, as of June 30, 2008, from 0.50% and 1.59%, respectively, as of December 31, 2007, and 0.20% and 0.65% as of June 30, 2007. The serious delinquency rates for Alt-A

and subprime loans was 3.79% and 9.08%, respectively, as of June 30, 2008, compared with 2.15% and 5.76%, respectively, as of December 31, 2007 and 1.05% and 4.80% as of June 30, 2007. The multifamily serious delinquency rate was 0.11% as of June 30, 2008, compared with 0.08% as of December 31, 2007 and 0.09% as of June 30, 2007.

We expect the housing market to continue to deteriorate and home prices to continue to decline in these states and on a national basis. Accordingly, we expect our single-family serious delinquency rate to continue to increase during 2008 and 2009.

Nonperforming Loans

Table 39 provides statistics on nonperforming single-family and multifamily loans as of June 30, 2008 and December 31, 2007. The increase in the nonperforming loans during the first six months of 2008 reflects the increase in our serious delinquency rates.

Table 39: Nonperforming Single-Family and Multifamily Loans

	As of	
	June 30, 2008	December 31, 2007
	(Dollars in millions)	
On-balance sheet nonperforming loans:		
Nonaccrual loans	$ 8,273	$ 8,343
Troubled debt restructurings[1]	2,422	1,765
HomeSaver Advance first-lien loans[2]	646	
Total on-balance sheet nonperforming loans	11,341	10,108
Off-balance sheet nonperforming loans:[3]		
Other off-balance sheet nonperforming loans, excluding HomeSaver Advance first lien loans[4]	32,856	25,700
HomeSaver Advance first-lien loans[2]	1,931	
Total off-balance sheet nonperforming loans	34,787	25,700
Total nonperforming loans	$ 46,128	$ 35,808
Accruing on-balance sheet loans past due 90 days or more[5]	$ 205	$ 204
Interest related to on-balance sheet nonperforming loans:[6]		
Interest income forgone[7]	$ 192	$ 215
Interest income recognized for the period[8]	223	328

(1) Troubled debt restructurings include loans whereby the contractual terms have been modified that result in concessions to borrowers experiencing financial difficulties.

(2) Represents total unpaid principal balance of first-lien loans associated with unsecured HomeSaver Advance loans, including first-lien loans that are not seriously delinquent.

(3) Represents unpaid principal balance of nonperforming loans in our outstanding and unconsolidated Fannie Mae MBS held by third parties.

(4) Represents total unpaid principal balance of loans that are seriously delinquent as of June 30, 2008.

(5) Recorded investment of loans as of the end of each period that are 90 days or more past due and continuing to accrue interest include loans insured or guaranteed by the U.S. government and loans where we have recourse against the seller of the loan in the event of a default.

(6) Amounts reported for June 30, 2008 relate to the six months ending June 30, 2008. Amounts reported for December 31, 2007 relate to the twelve months ended December 31, 2007.

(7) Forgone interest income represents the amount of interest income that would have been recorded during the period for on-balance sheet nonperforming loans as of the end of each period had the loans performed according to their contractual terms.

(8) Represents interest income recognized during the period for on-balance sheet loans classified as nonperforming as of the end of each period.

Foreclosure and REO Activity

Table 40 below provides information, by region, on our foreclosure activity for the six months ended June 30, 2008 and 2007.

Table 40: Single-Family and Multifamily Foreclosed Properties

	For the Six Months Ended June 30,	
	2008	**2007**
Single-family foreclosed properties (number of properties):		
Beginning of period inventory of single-family foreclosed properties (REO)[1]	33,729	25,125
Acquisitions by geographic area:[2]		
Midwest	15,265	9,532
Northeast	2,916	1,798
Southeast	11,347	5,436
Southwest	8,377	4,675
West	6,166	804
Total properties acquired through foreclosure	44,071	22,245
Dispositions of REO	(23,627)	(20,226)
End of period inventory of single-family foreclosed properties (REO)[1]	54,173	27,144
Carrying value of single-family foreclosed properties (dollars in millions)[3]	$ 5,808	$ 2,484
Single-family foreclosure rate[4]	0.24%	0.13%
Multifamily foreclosed properties (number of properties):		
Ending inventory of multifamily foreclosed properties (REO)	20	13
Carrying value of multifamily foreclosed properties (dollars in millions)[3]	$ 85	$ 78

(1) Includes deeds in lieu of foreclosure.

(2) See footnote 7 to Table 37 for states included in each geographic region.

(3) Excludes foreclosed property claims receivables, which are reported in our condensed consolidated balance sheets as a component of Acquired property, net.

(4) Estimated based on the total number of properties acquired through foreclosure as a percentage of the total number of loans in our conventional single-family mortgage credit book of business as of the end of each

respective period.

Our single-family foreclosure rate increased to 0.24% for the first six months of 2008, from 0.13% for the first six months of 2007, reflecting the near doubling of the number of single-family properties we acquired through foreclosure during the first six months of 2008 relative to the first six months of 2007. This increase was attributable to the impact of the housing market downturn and continued decline in home prices throughout much of the country, particularly in California, Florida, Arizona and Nevada, and continued weak economic conditions in the Midwest, particularly in Michigan and Ohio. We also experienced an increase in the number of multifamily properties acquired during the first six months of 2008 due primarily to the economic weakness in the Midwest. As discussed in Consolidated Results of Operations Credit-Related Expenses Credit Loss Performance Metrics, we have experienced a significant increase in our single-family default rates, particularly within certain states that have had significant home price depreciation, for certain higher risk loan categories, such as Alt-A, and for loans originated in 2006 and 2007.

The states of California, Florida, Arizona and Nevada, which represented approximately 27% of the loans in our conventional single-family mortgage credit book of business as of June 30, 2008, accounted for 22% of single-family properties acquired through foreclosure for the first six months of 2008, reflecting the sharp declines in home prices that these states are now experiencing. The Midwest, which represented approximately 20% of the loans in our conventional single-family mortgage credit book of business as of June 30, 2008, accounted for approximately 35% of the single-family properties acquired through foreclosure for the first six months of 2008, reflecting the continued impact of weak economic conditions in this region. Alt-A mortgage

loans backing Fannie Mae MBS, excluding resecuritized private-label mortgage-related securities backed by Alt-A mortgage loans, represented approximately 11% of our total single-family mortgage credit book of business as of June 30, 2008, but accounted for 30% of single-family properties acquired through foreclosure for the first six months of 2008.

The severe housing market downturn and decline in home prices on a national basis have resulted in a higher percentage of our mortgage loans that transition from delinquent to foreclosure status and a significant reduction in the sales prices of our foreclosed single-family properties. Based on these factors as well as the sharp rise in our serious delinquency rates during the first six months of 2008, we expect the level of foreclosures to increase further in 2008 compared with both 2007 and the first six months of 2008.

Institutional Counterparty Credit Risk Management

Mortgage Servicers

Our ten largest single-family mortgage servicers serviced 73% and 74% of our single-family mortgage credit book of business as of June 30, 2008 and December 31, 2007, respectively. On July 1, 2008, Bank of America Corporation announced the completion of its purchase of Countrywide Financial Corporation, our largest single-family mortgage servicer through June 30, 2008, making Bank of America our largest single-family mortgage servicer. Countrywide and its affiliates serviced approximately 23% of our single-family mortgage credit book of business as of June 30, 2008 and December 31, 2007. Together, Bank of America, Countrywide, and their respective affiliates serviced approximately 28% of our single-family mortgage credit book of business as of December 31, 2007 and June 30, 2008. As a result of the merger, we will experience an increase in our concentration of mortgage servicers.

Many of our mortgage servicers are experiencing weak financial conditions and performance. Due to the challenging market conditions, several of these servicers have experienced ratings downgrades and liquidity constraints, including IndyMac, Federal Bank F.S.B., formerly IndyMac Bank, F.S.B,, which was closed by the Office of Thrift Supervision in July 2008, with the Federal Deposit Insurance Corporation named as conservator. The financial difficulties that a number of our mortgage servicers are currently experiencing, coupled with growth in the number of delinquent loans on their books of business, may negatively affect the ability of these counterparties to meet their obligations to us, including their ability to service mortgage loans adequately and their ability to meet their obligations to repurchase delinquent mortgages due to a breach of the representations and warranties they provided upon delivery of the mortgages to us. We have taken steps to mitigate our risk with servicers with whom we have material counterparty exposure. Our risk management strategies have included collateral posting by servicers, guaranty of obligations by a higher-rated entity, reduction or elimination of exposures, reduction or elimination of certain business activities, transfer of exposures to third parties and suspension or termination of the servicing relationship.

Mortgage Insurers

We had total mortgage insurance coverage of $116.0 billion on the single-family mortgage loans in our guaranty book of business as of June 30, 2008, of which $106.1 billion represented primary mortgage insurance and $9.9 billion was pool mortgage insurance. We had total mortgage insurance coverage of $104.1 billion on the single-family mortgage loans in our guaranty book of business as of December 31, 2007, of which $93.7 billion represented primary mortgage insurance and $10.4 billion was pool mortgage insurance.

Eight mortgage insurance companies provided over 99% of our mortgage insurance as of both June 30, 2008 and December 31, 2007. We received proceeds of $830 million and $547 million for the six months ended June 30, 2008 and 2007, respectively, from our primary and pool mortgage insurance policies on our single-family loans for those respective periods. We had outstanding receivables from mortgage insurers of $625 million and $293 million as of

June 30, 2008 and December 31, 2007, respectively, related to amounts claimed on foreclosed properties.

Table 41 presents our maximum potential loss recovery for the primary and pool mortgage insurance coverage on single-family loans in our guaranty book of business by mortgage insurer for our top eight mortgage insurer counterparties as of June 30, 2008, as well as the insurer financial strength ratings of each of these counterparties as of August 1, 2008.

Table 41: Mortgage Insurance Coverage

	As of August 1, 2008 Insurer Financial Strength Ratings			As of June 30, 2008 Maximum Coverage[2] (Dollars in millions)		
Counterparty:[1]	**Moody s**	**S&P**	**Fitch**	**Primary**	**Pool**	**Total**
Mortgage Guaranty Insurance Corporation	A1	A	A+	$ 25,057	$ 2,629	$ 27,686
Genworth Mortgage Insurance Corporation	Aa3	AA	AA	17,387	439	17,826
PMI Mortgage Insurance Co.	A3	A+	A+	14,373	2,515	16,888
United Guaranty Residential Insurance Company	Aa3	AA+	AA+	16,140	295	16,435
Radian Guaranty, Inc.	A2	A	N/R	15,062	919	15,981
Republic Mortgage Insurance Company	A1	AA-	AA-	11,676	1,706	13,382
Triad Guaranty Insurance Corporation	B1	N/R	BB	4,379	1,433	5,812
CMG Mortgage Insurance Company[3]	N/R	AA-	AA	1,948		1,948

(1) Insurance coverage amounts provided for each counterparty may include coverage provided by consolidated subsidiaries of the counterparty.

(2) Maximum coverage refers to the aggregate dollar amount of insurance coverage (*i.e.*, risk in force) on single-family loans in our guaranty book of business and represents our maximum potential loss recovery under the applicable mortgage insurance policies.

(3) CMG Mortgage Insurance Company is a joint venture owned by PMI Mortgage Insurance Co. and CUNA Mutual Investment Corporation.

Recent increases in mortgage insurance claims due to higher credit losses in recent periods have adversely affected the financial results and condition of many mortgage insurers. In various actions since December 31, 2007, Standard & Poor s, Fitch and Moody s downgraded the insurer financial strength ratings of seven of our top eight primary mortgage insurer counterparties. As of June 30, 2008, these seven mortgage insurers provided $114.0 billion, or 98%, of our total mortgage insurance coverage on single-family loans in our guaranty book of business.