

Prospectus

Federal National Mortgage Association



Guaranteed Mortgage Pass-Through Certificates

(Residential Mortgage Loans)

Principal and Interest payable on the 25th day of each month

THE OBLIGATIONS OF THE FEDERAL NATIONAL MORTGAGE ASSOCIATION UNDER ITS GUARANTY ARE OBLIGATIONS SOLELY OF THE CORPORATION AND ARE NOT BACKED BY THE FULL FAITH AND CREDIT OF THE UNITED STATES. THE CERTIFICATES ARE EXEMPT FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT OF 1933 AND ARE "EXEMPTED SECURITIES" WITHIN THE MEANING OF THE SECURITIES ACT OF 1934.

The Guaranteed Mortgage Pass-Through Certificates ("Certificates") are issued and guaranteed by the Federal National Mortgage Association (the "Corporation"), a corporation organized and existing under the laws of the United States, under the authority contained in Section 304(d) of the Federal National Mortgage Association Charter Act (12 U.S.C. §1716 *et seq.*).

Each Certificate offered hereby and by the Supplement related hereto will represent an undivided interest in a pool of mortgage loans (a "Pool") to be formed by the Corporation. Each Pool will consist of residential mortgage loans ("Mortgage Loans") either previously owned by the Corporation or purchased by it in connection with the formation of the Pool. Each Pool will consist entirely of one of the following: (i) fixed-rate level installment Mortgage Loans, (ii) fixed-rate growing equity Mortgage Loans that provide for scheduled annual increased payments, with the full amount of the increase applied to principal, (iii) fixed-rate graduated payment Mortgage Loans having deferred interest features, (iv) adjustable rate Mortgage Loans and (v) fixed-rate Mortgage Loans secured by multifamily projects consisting of five or more dwelling units, some of which Mortgage Loans may have balloon payments or other irregular features or characteristics

Interests in each Pool will be evidenced by a separate issue of Certificates. Information regarding the aggregate principal amount and characteristics of the related Pool (including, without limitation, the type of Mortgage Loans in the Pool) will be furnished in a Supplement to this Prospectus at the time of the identification of the Pool.

The Corporation will have certain contractual servicing responsibilities with respect to each Pool. In addition, the Corporation will be obligated to distribute scheduled monthly installments of principal and interest (adjusted to reflect the Corporation's servicing and guaranty fee) to Certificateholders, whether or not received. The Corporation also will be obligated to distribute to Certificateholders the full principal balance of any foreclosed Mortgage Loan, whether or not such principal balance is actually recovered.

The date of this Prospectus is July 27, 1984

Retain this Prospectus for future reference. This Prospectus may not be used to consummate sales of Certificates unless accompanied by a Prospectus Supplement

No salesman, dealer, bank or other person has been authorized to give any information or to make any representation other than those contained in this Prospectus and, if given or made, such information or representation must not be relied upon as having been authorized by the Corporation. This Prospectus does not constitute an offer to sell or a solicitation of an offer to buy any securities other than the Certificates offered hereby and by the related Supplement nor an offer of the Certificates to any person in any state or other jurisdiction in which such offer would be unlawful.

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SUMMARY OF PROSPECTUS

The following summary of certain pertinent information is qualified in its entirety by reference to the detailed information appearing elsewhere in this Prospectus and by reference to the information with respect to each pool of Mortgage Loans (a "Pool") contained in the supplement to this Prospectus (a "Prospectus Supplement") to be prepared in connection with the issue of Guaranteed Mortgage Pass-Through Certificates (the "Certificates") evidencing undivided interests in such Pool

Title of Security	Guaranteed Mortgage Pass-Through Certificates
Issuer and Guarantor ...	Federal National Mortgage Association (the "Corporation"), a corporation organized and existing under the laws of the United States. See "Federal National Mortgage Association" The obligations of the Corporation under its guaranty are obligations solely of the Corporation and are not backed by, nor entitled to, the full faith and credit of the United States
Description of Security . .	Each Certificate will represent a fractional undivided interest in a Pool of Mortgage Loans to be formed by the Corporation A Certificate will initially represent at least \$25,000 unpaid principal amount of Mortgage Loans. The Certificates will be in fully registered form only.
Interest	Interest on each Mortgage Loan will be passed through monthly to Certificateholders, commencing on the 25th day of the month following the month of initial issuance of the related Certificates For all Pools containing fixed-rate Mortgage Loans ("Fixed-Rate Pools"), interest will be passed through at a uniform Pass-Through Rate (or Accrual Rate in the case of Fixed-Rate Pools containing graduated payment mortgage loans) which will be specified in the Prospectus Supplement and will not be greater than the lowest annual interest rate borne by any Mortgage Loan in the related Pool, less a specified minimum annual percentage representing compensation for servicing and the Corporation's guaranty and less, in the case of Fixed-Rate Pools containing graduated payment Mortgage Loans, deferred interest which is added to the principal balances of the underlying Mortgage Loans For Pools containing adjustable rate Mortgage Loans ("ARM Pools"), interest will be passed through on each Mortgage Loan at the interest rate at the time applicable thereto less (i) the Corporation's fixed servicing and guaranty fee and (ii) any deferred interest which is added to the principal balance of such Mortgage Loan pursuant to its terms. See "Yield Considerations."
Principal (including pre-payments)	Passed through monthly, commencing on the 25th day of the month following the month of initial issuance of the related Certificates See "Maturity and Prepayment Assumptions" and "Description of Certificates."
Guaranty	The Corporation is obligated to distribute scheduled monthly installments of principal and interest (adjusted to reflect the Corporation's servicing and guaranty fee) on the Mortgage Loans in a Pool, whether or not received The Corporation is also obligated to distribute to Certificateholders the full principal balance of any foreclosed Mortgage Loan, whether or not such principal balance is actually recovered If the Corporation were unable to perform these guaranty obligations, distributions to Certificateholders would consist solely of payments and other recoveries on Mortgage Loans and, accordingly, delinquencies and defaults would affect monthly distributions to Certificateholders
Servicing	The Corporation will be responsible for servicing the Mortgage Loans and will contract with mortgage lenders to perform certain servicing functions on its behalf See "Description of Certificates—Servicing Through Lenders."
The Mortgage Pools ...	Each Pool will consist entirely of Mortgage Loans of only one of the following types (i) fixed-rate level installment Mortgage Loans, (ii) fixed-rate growing equity Mortgage Loans that provide for scheduled annual increased payments, with the full amount of the increase applied to principal, (iii) fixed-rate graduated payment Mortgage Loans with deferred interest features, (iv) adjustable rate Mortgage Loans, and (v) fixed-rate Mortgage Loans secured by multifamily projects consisting of five or more dwelling units, some of which may have balloon payments or other irregular features or characteristics The Mortgage Loans in each Pool will have unpaid principal balances aggregating not less than \$1,000,000 Each Mortgage Loan will be secured by a first lien on a residential property and each Mortgage Loan will meet the applicable standards set forth under "Purchase Program." Pool information as to the type of Mortgage Loans (including whether such Mortgage Loans are conventional Mortgage Loans or are insured by the Federal Housing Administration or guaranteed by the Veterans Administration), the aggregate principal balance of the Mortgage Loans as of the Issue Date, the Pass-Through Rate for Certificates evidencing interests in level installment Fixed-Rate Pools, the Accrual Rate for Certificates evidencing interests in graduated payment Fixed-Rate Pools, and the latest maturity date of any Mortgage Loan will be contained in the related Prospectus Supplement For an ARM Pool, the related Prospectus Supplement will also contain information respecting the index upon which adjustments are based, the frequency of interest rate and payment adjustments and any maximum or minimum limitations thereon, the Corporation's fixed guaranty and servicing fee and whether the underlying Mortgage Loans contain provisions for the deferral of interest
Financial Results	The Corporation was profitable in the first half of 1984 and in 1983, after experiencing losses in 1982 and 1981 The primary cause of the losses in 1982 and 1981 was the excess of the cost of outstanding debt over the yield on the mortgage portfolio (or "negative spread") In the first quarter of 1984 and in 1983 the negative spread was substantially narrower than the negative spread in 1982 and 1981, and its impact was more than offset by income from other sources. During the second quarter of 1984, interest rates rose, increasing the negative spread If interest rates remain at current levels, or increase further, the Corporation could experience unprofitable results of operations in the second half of 1984 and for 1984 as a whole See "Selected Financial Data," "Management's Discussion and Analysis of Financial Results—Annual Periods—Interim Period" and "Mortgage Portfolio Spread" herein

THE MORTGAGE POOLS

The Corporation has implemented a program for: (a) the setting aside of residential mortgage loans (the "Mortgage Loans") into separate pools (the "Pools") bearing distinctive identification and (b) the issuance and sale of trust certificates of beneficial interest evidencing pro rata undivided ownership interests in the Mortgage Loans comprising each separate Pool (the "Guaranteed Pass-Through Certificates" or "Certificates"). The Mortgage Loans may be purchased by the Corporation expressly for the Pools or may be Mortgage Loans that have been held by the Corporation in its own portfolio. Each Pool will consist of Mortgage Loans evidenced by promissory notes (the "Mortgage Notes") secured by first mortgages or deeds of trust (the "Mortgages") on either (i) one-family or two- to four-family residential properties or (ii) multifamily projects consisting of five or more dwelling units, (the "Mortgaged Properties"). A Pool will contain Mortgage Loans of only one of the following types: (i) fixed-rate level payment Mortgage Loans ("Level Payment Mortgage Loans"), (ii) fixed-rate growing equity Mortgage Loans that provide for scheduled annual increased payments, with the full amount of the increase applied to principal ("GEMs"), (iii) fixed-rate graduated payment Mortgage Loans with deferred interest features ("GPMs"), (iv) adjustable rate Mortgage Loans ("ARMs") and (v) fixed-rate Mortgage Loans secured by multifamily projects consisting of five or more dwelling units ("Multifamily Mortgage Loans"), some of which Mortgage Loans may have balloon payments or other irregular features or characteristics. The Mortgage Loans may be either conventional Mortgage Loans (i.e., not insured or guaranteed by any U.S. government agency) or Mortgage Loans which are either insured by the Federal Housing Administration or guaranteed by the Veterans Administration ("Conventional Mortgage Loans" and "FHA/VA Mortgage Loans," respectively). The Mortgage Loans purchased expressly for the Pools will be sold to the Corporation by eligible institutions that meet certain requirements set forth under "Purchase Program" and are referred to herein as "Lenders." No Pool will consist of Mortgage Loans having an aggregate unpaid principal balance of less than \$1,000,000 on the first day of the month of issuance of the related Certificates. See "Purchase Program—Mortgage Loan Eligibility" for a description of certain criteria applicable to the eligibility of Mortgage Loans for inclusion in Pools.

Interests in each Pool will be evidenced by a separate series of Certificates (an "Issue"). The Corporation will acquire the Mortgage Loans that it has purchased expressly for Pools under purchase contracts. By entering into such contracts, the Corporation will obligate itself to issue Certificates to, or to the order of, the Lenders named in the contracts, upon delivery to the Corporation of the required Mortgage Loans conforming to the Corporation's standards. **The Corporation will not insure or guarantee the performance by any Lender of its obligation to deliver Mortgage Loans and, correspondingly, does not insure or guarantee the performance by any person of any obligation to deliver Certificates.**

The Corporation will cause the Mortgage Loans in each Pool of fixed-rate Mortgage Loans other than GPMs to be held for the benefit of the holders of Certificates ("Certificateholders" or "Holders") pursuant to the combined terms of a trust indenture executed by the Corporation in its corporate capacity and in its capacity as Trustee (the Trust Indenture dated as of November 1, 1981, as modified and amended by a First Supplemental Indenture dated as of February 15, 1982, a Second Supplemental Indenture dated as of October 1, 1982, a Third Supplemental Indenture dated as of August 1, 1983, a Fourth Supplemental Indenture dated as of May 1, 1984, and a Fifth Supplemental Indenture dated as of July 1, 1984, being herein called the "Fixed-Rate Trust Indenture"), and a supplement thereto for the related Issue (the "Issue Supplement"). The Corporation will cause the Mortgage Loans in each Pool of GPMs and ARMs to be held for the benefit of the Certificateholders pursuant to the terms of a Trust Indenture dated as of July 1, 1984 (the "GPM Trust Indenture") and a Trust Indenture dated as of July 1, 1984 (the "ARM Trust Indenture"), respectively, each executed by the Corporation in its corporate capacity and in its capacity as Trustee. The Fixed-Rate Trust Indenture, the GPM Trust Indenture and the ARM Trust Indenture are herein, collectively, referred to as the "Trust Indenture" or "TI" where common terms and provisions are being referred to or described. Certain capitalized words or series of words in this Prospectus refer to and are further defined in the Trust Indenture. The Corporation will be responsible for the administration and servicing of the Mortgage Loans in the Pool, including the supervision of the servicing activities of Lenders, if appropriate, the collection and receipt of payments from Lenders, and the remittance of distributions and certain reports to Certificateholders. The Corporation will be entitled to

receive a fee for its guaranty obligations and its services pursuant to the Trust Indenture. The fee to the Corporation for any Mortgage Loan (out of which it will compensate Lenders for servicing the Mortgage Loans) will, as to any Pool containing fixed-rate Mortgage Loans (a "Fixed-Rate Pool"), be equal to the difference between the annual interest rate borne by the Mortgage Loan and the annual rate of interest paid to Certificateholders at the Pass-Through Rate for the related Fixed-Rate Pool or the Accrual Rate for Fixed-Rate Pools containing GPMs (a "GPM Pool"). For any Pool containing ARMs (an "ARM Pool"), the Corporation will similarly compensate itself from interest payments on the underlying ARMs in an amount, as to each ARM Pool, specified in the related Prospectus Supplement. The Corporation will reserve the right to remove the servicing responsibility from a Lender at any time if it considers such removal to be in the best interest of Certificateholders. In such event, the Corporation will meet its obligation to provide servicing either by directly servicing the Mortgage Loans itself or by finding a replacement Lender that meets the eligibility standards.

The Corporation's obligations with respect to the Mortgage Loans will be limited to the servicing responsibilities under the Trust Indenture, and, in the event of any delinquency in payment or loss on any Mortgage Loan, its obligation to make supplemental payments in amounts described herein under "Description of Certificates—The Corporation's Guaranty."

Because the principal amount of the Mortgage Loans in a Pool will decline (with the exception of Fixed-Rate Pools containing GPMs and certain ARM Pools which contain ARMs providing for deferred interest) monthly as principal payments, including prepayments, are received each Certificate Principal Balance (defined to be the principal amount appearing on the face of the related Certificate or, subsequent to the first Distribution Date, the last amount reported to the Holder of such Certificate by the Corporation as the principal balance thereof) will also decline over time. See "Maturity and Prepayment Assumptions."

YIELD CONSIDERATIONS

Fixed-Rate Pools Not Containing GPMs

Each Fixed-Rate Pool not containing GPMs will consist of Mortgage Loans that bear simple interest at fixed annual rates ("Mortgage Interest Rates"). Such a Fixed-Rate Pool may include Mortgage Loans that bear different Mortgage Interest Rates. The Pass-Through Rate of interest payable to Certificateholders of each such Issue, as set forth on the face of the Certificates, will be equal to the lowest Mortgage Interest Rate borne by any Mortgage Loan in the related Pool, less a specified minimum annual percentage representing compensation for servicing and the Corporation's guaranty. Since the Pass-Through Rate for an Issue will not be greater than the lowest Mortgage Interest Rate for the related Pool, any disproportionate principal prepayments among Mortgage Loans bearing different Mortgage Interest Rates will not affect the return to Certificateholders.

The effective yield to Certificateholders will be reduced slightly below the yield otherwise produced by the applicable Pass-Through Rate because the distribution of interest which accrues from the first day of each month will not be made until the 25th day of the month following the month of accrual.

When a Mortgage Loan is prepaid or otherwise liquidated, the proceeds of such prepayment or liquidation will, unless the Corporation elects in its discretion to make any distribution thereof in the following month, be passed through to Certificateholders in the second month following the month of such prepayment or other liquidation. Since the Corporation will agree in each Certificate to distribute on each Distribution Date to the Holder thereof an amount as to interest representing one month's interest at the Pass-Through Rate on the Certificate Principal Balance, any prepayment or other liquidation of a Mortgage Loan and the timing of the distribution of the proceeds thereof will have no effect on the interest return to Certificateholders.

Assuming performance by the Corporation of its obligations under its guaranty, the net effect of each distribution respecting interest will be the pass-through to each Certificateholder of an amount which is equal to one month's interest at the Pass-Through Rate on the Certificate Principal Balance of such Holder's Certificate. See "Description of Certificates—Payments on Mortgage Loans; Distributions on Certificates."

GPM Pools

A GPM Pool will consist of fixed-rate fully amortizing Mortgage Loans providing for monthly payments which increase annually for a period of years (generally between three to seven) and are level thereafter. During all or part of the period in which monthly payments are increasing, those payments will not be sufficient to cover the full amount of interest on the GPM at the Mortgage Interest Rate borne thereby. The amount of each such interest insufficiency will be added to the principal balance of the GPM, which will accrue interest thereafter on this new increased amount.

GPM Pools will have characteristics similar to Fixed-Rate Pools described above commencing with the time at which payments are sufficient to cover interest on the principal balances of the underlying GPMs. Prior to that time, the Certificates evidencing interests in GPM Pools will provide for the monthly distribution of the scheduled interest payment on each Mortgage Loan in the Pool less the Corporation's servicing and guaranty fee attributable thereto, the amount of any such fee being equal to the difference between the fixed Mortgage Interest Rate at which interest accrues on the GPM and the Accrual Rate borne by the related Certificates.

The Prospectus Supplement relating to a GPM Pool will set forth the period over which payments on the GPMs increase.

The Corporation's guaranty of Certificates evidencing interests in GPM Pools will cover the principal amount of each underlying GPM, including any portion thereof representing deferred interest. The Corporation will, following the period (the "Deferred Interest Period") during which such payments are insufficient to cover interest at the Mortgage Interest Rate on their then outstanding principal balances, including deferred interest which has been added thereto, also be obligated to distribute on each Distribution Date one month's interest at the Accrual Rate on the then outstanding principal balances of the underlying GPMs. During the Deferred Interest Period, the Corporation's guaranty will cover, as to each underlying GPM, the amount of each scheduled payment less the Corporation's servicing and guaranty fee applicable thereto.

ARM Pools

An ARM Pool will contain Mortgage Loans which bear interest at rates which will vary in response to a single specified index (such as then prevailing yields on five-year Treasury obligations) and will adjust periodically at uniform specified intervals. The actual Mortgage Interest Rate at any time borne by an ARM will be equal to a specified percentage, or Margin, over the index rate then applicable thereto. ARMs may or may not contain provisions limiting the amount by which rates may be adjusted upward or downward and may or may not limit the amount by which monthly payments may be increased or decreased to accommodate upward or downward adjustments in interest. Certain ARMs may provide for periodic adjustments of scheduled payments in order to fully amortize the Mortgage Loan by its stated maturity while other ARMs may permit that maturity to be extended or shortened in accordance with the portion of each payment which is applied to interest in accordance with the periodic interest rate adjustments.

Where an ARM provides for limitations on the amount by which monthly payments may be increased or changes to the Mortgage Interest Rate of the ARM are made more frequently than payment changes, it is possible that an increase in the rate of interest cannot be covered by the amount of the scheduled payment. In that case, the uncollected portion of interest will be deferred and added to the principal balance of the Mortgage Loan.

Since the interest rates borne by Mortgage Loans in an ARM Pool will vary and since a portion of the interest accrued thereon may be deferred and payable at a future time, Certificates evidencing interests in such Pools will not provide for the distribution of interest at a fixed Pass-Through Rate. Rather, each Certificate issued with respect to an ARM Pool will provide for the monthly pass-through of all interest payable on each Mortgage Loan in the Pool less the Corporation's servicing and guaranty fee. In some ARM Pools, the Corporation's servicing and guaranty fee may not be the same amount as to each ARM in the ARM Pool, but will rather be a percentage amount as to each such ARM which, when subtracted from the related Margin, will cause each ARM in the ARM Pool to float above the applicable index at a single

uniform "security spread" (the "Security Spread"). As a result, for such an ARM Pool, the rate at which interest accrues to Certificateholders (the "Accrual Rate") at any time (other than the period immediately following origination during which an initial rate having no relationship to the index may apply or during a period when a Mortgage Interest Rate minimum or maximum is applicable) on each Mortgage Loan included therein will be equal to the then applicable index plus the Security Spread.

The Prospectus Supplement relating to an ARM Pool will contain information respecting the index upon which adjustments are based, the Security Spread, if any, the frequency of interest rate and payment adjustments and any maximum and minimum limitations thereon. The Prospectus Supplement will also describe any provisions for deferred interest and will, to the extent applicable, set forth the original rates of interest borne by the underlying Mortgage Loans.

The Corporation's guaranty of Certificates evidencing interests in ARM Pools will cover the principal of each underlying Mortgage Loan, including any portion thereof representing deferred interest. Its guaranty of interest will cover all interest due and payable by the Mortgagor (net of the Corporation's servicing and guaranty fee). The Corporation will also agree to add to the amount of interest accompanying the prepayment of an underlying Mortgage Loan any amount by which such interest is less than one month's interest at the Accrual Rate on the prepaid principal balance thereof. As a consequence, the timing of the prepayment of a Mortgage Loan will have no effect on the interest return to Certificateholders.

MATURITY AND PREPAYMENT ASSUMPTIONS

The original maturities of substantially all of the Conventional Level Payment Mortgage Loans are expected to be between either 8 to 15 years or 20 to 30 years. The maturities of substantially all of the FHA/VA Level Payment Mortgage Loans at origination are expected to be 30 years. Each Level Payment Mortgage Loan with an original maturity of 30 years will provide for amortization of principal according to a schedule which, in the absence of prepayments, would result in repayment of one-half of the original principal amount of such Mortgage Loan by approximately the 23rd to 27th year, with higher Mortgage Interest Rates resulting in slower amortization of principal. A 15-year fully amortizing Level Payment Mortgage Loan would, in the absence of prepayments, result in repayment of one-half of the original principal amount by approximately the 10th to 12th year, with higher Mortgage Interest Rates resulting in slower amortization of principal.

A significant number of the Conventional Mortgage Loans may provide by their terms that in the event of the sale of all or some of the underlying property the full unpaid principal balance of the Mortgage Loan is due and payable at the option of the holder. FHA/VA Mortgage Loans contain no such "due-on-sale" provisions. As set forth under "Description of Certificates—Collection and Other Servicing Procedures," the Trust Indenture requires the Corporation to exercise its right to accelerate the maturity of a Conventional Mortgage Loan in such an event so long as acceleration is permitted under applicable law unless it elects to repurchase such Mortgage Loan.

The ability of mortgage lenders and their assignees and transferees to enforce "due-on-sale" clauses was addressed by the "Garn-St Germain Depository Institutions Act of 1982," which was passed by Congress and signed into law on October 15, 1982. This legislation, subject to certain exceptions, pre-empts state statutory and case law that prohibits the enforcement of "due-on-sale" clauses. Exempted from this pre-emption are mortgage loans (originated other than by Federally chartered lenders) that were made or assumed during the period beginning on the date a state, by statute or statewide court decision, prohibited the exercise of "due-on-sale" clauses and ending on October 15, 1982. Mortgage lenders, however, may require any successor or transferee of the borrower to meet customary credit standards. The exemption for such loans ends on October 15, 1985 unless the state acts to otherwise regulate these loans by that date. The legislation also enumerates nine circumstances under which a lender may not enforce "due-on-sale" clauses, *e.g.*, the creation of a subordinate encumbrance which does not relate to a transfer of rights of occupancy in the property, a transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety and the granting of a leasehold interest of three years or less not containing an option to purchase.

Conventional Mortgage Loans purchased by the Corporation from November 10, 1980 to October 15, 1982 in jurisdictions where, on the date of origination, the law substantially restricted lenders from enforcing "due-on-sale" provisions may provide that they are due and payable at the holder's option at the end of seven years. As described in "Description of Certificates—Collection and Other Servicing Procedures," the Trust Indenture provides that the Corporation will exercise or refrain from exercising any such "call option rider" in a manner that is consistent with then-current policies or practices employed by the Corporation respecting comparable mortgage loans held in its own portfolio.

Past experience of the Federal Housing Administration ("FHA") relating to government-insured single-family mortgage loans at various interest rates with original maturities of 26 to 30 years indicates that, while some of such mortgage loans remain outstanding until the scheduled maturity, a pool of 30-year FHA-insured single-family mortgage loans will produce an average loan life of 12 years. A 12-year prepayment assumption is the mortgage industry norm for quoting yields and is used in most generally accepted yield tables. Based upon published information and the Corporation's own experience, the rate of prepayments on 30-year single-family loans has fluctuated significantly in recent years, including a substantial reduction in the prepayment rate during 1980, 1981 and 1982, and a significant increase in the rate in 1983 and the first six months of 1984. The Corporation believes such fluctuation is due to a number of factors, including general economic conditions, mortgage market interest rates and homeowner mobility, and that such factors will affect the prepayment experience for the Mortgage Loans in Pools. Accordingly, the Corporation cannot estimate what such prepayment experience will be or how it might compare to the FHA 12-year prepayment assumption respecting insured mortgage loans. See "Description of Certificates—Termination" for a description of the Corporation's option to repurchase the Mortgage Loans in any Pool when the aggregate principal balance thereof becomes less than 10 percent of the aggregate principal balance of the Mortgage Loans in the Pool on the Issue Date.

A GEM provides for scheduled annual increases in the mortgagor's monthly payments. Since the additional scheduled portion of the monthly payments is applied to reduce the unpaid principal balance of a GEM, the scheduled maturity of a GEM will be significantly shorter than the 25- or 30-year term used as the basis for calculating the initial level installment of principal and interest applicable until the first adjustment. No GEM which matures by its terms more than 15 years subsequent to the Issue Date of the related Certificates will be eligible for inclusion in a Pool. Since GEMs have not, until recently, been originated in any appreciable volume, there are no reliable data available regarding their prepayment experience.

As set forth above under "Yield Considerations," GPMs provide for payments which increase annually for a period of years (generally between three and seven) and then amortize on a level payment basis to their stated maturity. Since the principal amount of a GPM will increase during its Deferred Interest Period, the time at which one-half of the principal amount of a GPM will be paid in accordance with its amortization schedule will be longer than for a Level Payment Mortgage Loan bearing a similar Mortgage Interest Rate. ARMs vary substantially as to their terms and it is impossible to generalize other than that, because of their adjustable feature, ARMs may be less subject to prepayment than fixed-rate Mortgage Loans should interest rates decline below levels prevailing at origination. Since both GPMs and ARMs have not been originated in quantity until recent periods, there is, like GEMs, no reliable data available regarding their prepayment experience.

PURCHASE PROGRAM

Set forth below is a description of certain aspects of the Corporation's purchase program for mortgage loans eligible for inclusion in a Pool (the "Program"). The Prospectus Supplement to be prepared with respect to each Issue will contain information on the Mortgage Loans in the Pool, including information as to the type of Mortgage Loans, the aggregate principal balance of the Mortgage Loans as of the Issue Date, for Fixed-Rate Pools the Pass-Through Rate or Accrual Rate, whichever is applicable, and the latest maturity date of any Mortgage Loan.

Lender Eligibility

The Corporation will purchase Mortgage Loans from eligible Federally and state-chartered savings and loan associations, mutual savings banks, commercial banks, credit unions and similar financial institutions, the deposits or accounts of which are insured by the Federal Savings and Loan Insurance Corporation ("FSLIC"), the Federal Deposit Insurance Corporation ("FDIC") or the National Credit Union Administration ("NCUA"), from certain other state-insured financial institutions and from certain institutions, principally mortgage bankers, that are mortgage sellers approved by the Corporation. The Corporation, on an individual institution basis, will determine whether such institutions will be approved as eligible Lenders for the Program by applying certain criteria, which may include depth of mortgage origination experience, servicing experience, and financial capacity. Approved Lenders will be party with the Corporation to a Mortgage Selling and Servicing Contract. Also, each Mortgage Loan purchased for inclusion in a Pool will be subject to and must comply with the terms of a Selling and Servicing Guide applicable to the Program. The Selling and Servicing Guide may be amended from time to time.

Mortgage Loan Eligibility

General

The Mortgage Loans to be included in each Pool will be Mortgage Loans on residential properties. These Mortgage Loans are permanent loans (as opposed to construction and land development loans) secured by Mortgages on properties comprised of (i) one- to four-family dwelling units, including units in condominium projects, planned unit developments, and *de minimis* planned unit developments or (ii) multifamily projects consisting of five or more dwelling units. The Prospectus Supplement to be prepared with respect to each Issue backed by Multifamily Mortgage Loans will describe the eligibility criteria for such loans, which will differ in certain respects from the criteria described below. Each Mortgage Loan will be documented by the appropriate FNMA/FHLMC Uniform Instrument in effect at the time of origination, FHA or VA mortgage instrument or other instrument acceptable to the Corporation, and will comply with all applicable Federal and local laws, including laws relating to usury, equal credit opportunity and disclosure.

There is no requirement that Mortgage Loans be payable on the first day of the month in order to be eligible for inclusion in a Pool. The Mortgage Loans must have had maturities of not more than 30 years from their date of origination.

Conventional Mortgage Loans

Pursuant to the requirements of the Selling and Servicing Guide, Conventional Mortgage Loans must be real estate loans secured by first Mortgages on residential properties, with principal balances which (when combined with the unpaid principal balance of any second mortgage in which the Corporation has an interest), at the time of purchase by the Corporation, did not exceed certain Federally imposed maximum principal balance limitations applicable to the Corporation. In 1984, the maximum dollar purchase limitations for Conventional Mortgage Loans are as follows: \$114,000 for mortgages secured by single-family residences (\$171,000 in Alaska and Hawaii); \$145,800 for mortgages secured by two-family residences (\$218,700 in Alaska and Hawaii); \$176,100 for mortgages secured by three-family residences (\$264,150 in Alaska and Hawaii); and \$218,900 for mortgages secured by four-family residences (\$328,350 in Alaska and Hawaii).

No Conventional Mortgage Loan with a loan-to-value ratio in excess of 95 percent will be included in any Pool. Conventional Mortgage Loans with loan-to-value ratios exceeding 80 percent must have the principal amount of the indebtedness in excess of 75 percent of the appraised value of the Mortgaged Property insured by a policy of primary mortgage guaranty insurance. Each mortgage insurer must be licensed to transact a mortgage guaranty insurance business in the state where the Mortgaged Property is located and be acceptable to the Corporation as a mortgage insurer. As an alternative to the requirement to obtain mortgage insurance for Conventional Mortgage Loans with loan-to-value ratios in excess of 80 percent, Lenders may contract with the Corporation to repurchase such Conventional Mortgage Loans at a

price equal to the unpaid principal balance thereof in the event of default before the loan-to-value ratio has been reduced to 80 percent of the original value.

The maximum loan-to-value ratio at the time of purchase for a Conventional Mortgage Loan secured by a first Mortgage on an owner-occupied property including the unpaid principal balances of all subordinate financing is 95 percent. In the case of a Conventional Mortgage Loan secured by a first Mortgage on a non-owner occupied property, the maximum loan-to-value ratio including the unpaid principal balances of all subordinate financing is 90 percent. The maximum loan-to-value ratio for Mortgage Loans secured by non-owner occupied properties is generally 80 percent but may vary based on the Corporation's evaluation of the age of a Mortgage Loan and its experience with the Lender from whom it purchases such Mortgage Loan.

Pursuant to the requirements of the Selling and Servicing Guide, each eligible Lender that sells a Conventional Mortgage Loan to the Corporation for the purposes of the Program must assume responsibility for underwriting such Conventional Mortgage Loan using the Corporation's published criteria for mortgage loan underwriting, as from time to time in effect, as guidelines. After delivery of the Conventional Mortgage Loans, the Corporation will conduct reviews of the quality of credit and property underwriting used in the origination of certain randomly selected Conventional Mortgage Loans.

FHA/VA Mortgage Loans

Pursuant to the requirements of the Selling and Servicing Guide, FHA/VA Mortgage Loans must be real estate loans with stated constant annual rates of interest, secured by first Mortgages on residential properties. The principal balance and loan-to-value ratio of each FHA Mortgage Loan must comply with the standards established by the FHA. In the case of VA Mortgage Loans, the Corporation has imposed a maximum principal balance limitation of \$135,000. In addition, the unguaranteed portion of the VA Mortgage Loan amount cannot be greater than 75 percent of the lesser of (i) the purchase price of the property or (ii) the VA's estimate of reasonable value. For two- to four-family properties, such unguaranteed portion cannot be greater than 75 percent of the least of (i) above, (ii) above or the appraiser's estimate of market value. Each FHA/VA Mortgage Loan must be insured or guaranteed by a valid and subsisting policy or guaranty in full force and effect. In addition, each FHA/VA Mortgage Loan must have been originated prior to the 12-month period preceding the Corporation's purchase of the Mortgage Loan for inclusion in a Pool.

DESCRIPTION OF CERTIFICATES

Each Issue of Certificates will be issued pursuant to the applicable Trust Indenture described above. The applicable Trust Indenture will, as to each Issue, be supplemented by an Issue Supplement, which will be prepared at the time of the creation of such Issue. The Issue Supplement will set forth the specific terms of the Issue, such as the Pass-Through Rate applicable thereto in the case of Fixed-Rate Pools (other than those containing GPMs) and the Issue Date. The Issue Supplement will also contain any variation from the basic Trust Indenture applicable to a particular Issue, any such variation also being described in the Prospectus Supplement relating to such Issue. As set forth under "Legal Opinion," the validity of each Issue of Certificates, the Trust Indenture and the applicable Issue Supplement will be passed upon by the General Counsel of the Corporation upon the request of any Holder of Certificates of such Issue.

Mortgage Loans not previously held in the Corporation's portfolio will be purchased pursuant to a Pool Purchase Contract for cash or in exchange for Certificates in the related Pool. Such Mortgage Loans will be serviced by one of the Corporation-approved Lenders, normally the same entity as the loan originator, pursuant to the terms of the Pool Purchase Contract, as supplemented by the Selling and Servicing Guide, which is incorporated therein by reference. Copies of the Trust Indenture and the Pool Purchase Contract, together with the Selling and Servicing Guide, may be obtained from the Corporation's Washington, D C office, from any of the Corporation's regional offices in Philadelphia, Atlanta, Chicago, Dallas, and Los Angeles, or from the Corporation's fiscal office in New York.

The following summaries describe certain provisions of the Trust Indenture. These summaries do not purport to be complete and are subject to, and qualified in their entirety by reference to, the more complete provisions of the Trust Indenture.

General

The Certificates will represent Fractional Undivided Interests in the Trust Fund created pursuant to the Trust Indenture and Issue Supplement for each Issue. The Fractional Undivided Interest represented by a particular Certificate will be equal to the initial principal denomination of such Certificate set forth on the face thereof divided by the aggregate Stated Principal Balance¹ of the Mortgage Loans in the Pool (the "Pool Principal Balance") as of the Issue Date, which also will be set forth on the face of the Certificate. The Trust Fund for an Issue consists of (i) such Mortgage Loans as from time to time are subject to the Trust Indenture and Issue Supplement, (ii) such payments or other recoveries on Mortgage Loans as from time to time may be considered to be held by the Corporation for Certificateholders, (iii) property acquired by foreclosure of Mortgage Loans or by deed in lieu of foreclosure, and (iv) the interest of Certificateholders in the obligation of the Corporation to supplement payments and other recoveries on Mortgage Loans to the extent necessary to make required distributions to Certificateholders.

The Certificates will be issued in fully registered form only unless the Corporation elects to establish a book-entry method for the registration of ownership of Certificates. In the event that such a system is established, Certificates which are presented for registration of transfer or exchange may be cancelled and, in lieu of the physical delivery of a new Certificate or Certificates, the ownership of such new Certificates will be entered in such book-entry system. Certificates will not be issued in initial principal denominations of less than \$25,000. (TI Section 7.01). In addition, Certificates may only be issued in integral multiples of \$5,000 in excess of \$25,000, with the exception of one odd denomination that may be issued for each Pool.

The Certificates will be freely transferable and exchangeable at the corporate trust office of Chemical Bank, New York, New York. A service charge may be imposed for any exchange or registration of transfer of Certificates and the Corporation may require payment of a sum sufficient to cover any tax or other governmental charge. (TI Section 7.02)

Distributions of principal and interest on each Issue of Certificates will be made by the Corporation on the 25th day of each month (the "Distribution Date") to the persons in whose names the Certificates are registered as of the close of business on the last day of the preceding month (the "Record Date"). The first distribution for each Issue of Certificates will be in the month following the month in which the Issue Date occurs. Distributions for each Issue will be made by check mailed to the address of the person entitled thereto as it appears on the Certificate Register not later than the 25th day of each month; provided, however, that the final distribution in retirement of Certificates of any Issue will be made only upon presentation and surrender of the Certificates at the office or agency of the Corporation specified in the notice to Certificateholders of such final distribution.

Transfer of Mortgage Loans to Pools

Each Mortgage Loan transferred to a Pool will be identified in a Mortgage Loan Schedule appearing as an exhibit to the Issue Supplement for the related Issue of Certificates. In addition, the Corporation, as Trustee of the Mortgage Loans, will retain on behalf of Certificateholders the original Mortgage Note, endorsed in blank, and a completed and executed assignment to the Corporation of the mortgage instrument in suitable form for recording but not recorded. At its option, the Corporation may choose to maintain such documents either with a custodian institution (the Lender or another institution) whose deposits or accounts are insured by the FDIC, FSLIC or a state agency, or with a subsidiary of the Lender. The Corporation will review the Mortgage Loan Schedule prior to the issuance of the Certificates and will conduct random spot checks to confirm the sufficiency of the documents after issuance of the Certificates.

Although the above procedures are intended to protect the interests of the Holders of Certificates in the Mortgage Loans in the related Pool, the law applicable to a liquidation, reorganization or similar

¹ All references herein to the Stated Principal Balance of a Mortgage Loan or to the aggregate Stated Principal Balance of all Mortgage Loans in a Pool are to the principal balance or aggregate principal balance, as the case may be, utilized by the Corporation in calculating the then outstanding principal balances of Certificates. Such Stated Principal Balances may differ from actual principal balances for a number of reasons, including supplemental payments by the Corporation on delinquent Mortgage Loans pursuant to its guaranty obligations and delays in the distribution of certain Mortgage Loan receipts

proceeding involving the assets of a Lender or of the Corporation is unclear and as a result no opinion can be rendered as to the status of Certificateholders' interests in the event of any such proceeding. The Corporation's guaranty would, however, by its terms be available in the event of any such proceeding involving the assets of a Lender.

As described herein under "Rights Upon Event of Default," Holders of Certificates will have the right under certain circumstances to appoint a successor Trustee.

Servicing Through Lenders

Pursuant to the Trust Indenture, the Corporation is responsible for servicing and administering the Mortgage Loans but, in its discretion, is permitted to contract with the originator of each Mortgage Loan, or another eligible servicing institution, to perform such functions under the supervision of the Corporation as more fully described herein. Any servicing contract or arrangement by the Corporation with a Lender for the direct servicing of Mortgage Loans is a contract solely between the Corporation and that Lender and the Certificateholders are not deemed to be parties thereto and have no claims, rights, obligations, duties or liabilities with respect to such Lender. (TI Section 5.01)

Lenders will be obligated pursuant to the Selling and Servicing Guide to perform diligently all services and duties customary to the servicing of mortgages, as well as those specifically prescribed by the Selling and Servicing Guide. The Corporation will monitor the Lender's performance and has the right to remove any Lender for cause at any time it considers such removal to be in the best interest of Certificateholders. The duties performed by Lenders include general loan servicing responsibilities, collection and remittance of principal and interest payments, administration of mortgage escrow accounts, collection of insurance claims and, if necessary, foreclosure.

The Corporation retains as to each Fixed-Rate Mortgage Loan the difference in interest between the annual Mortgage Interest Rate borne by the Mortgage Loan and the Pass-Through Rate or Accrual Rate on the Certificates. For example, if a Mortgage Loan with a 12.25 percent Mortgage Interest Rate is included in a Pool against which a Certificate with an 11.25 percent Pass-Through Rate is issued, the Corporation would be entitled to receive total compensation of one percent per annum on the Mortgage Loan. For ARMs, the Corporation will retain an amount equal to the percentage Spread applicable thereto applied to the outstanding principal balance as increased by any deferred interest that has been included therein. See "Yield Considerations." The Corporation is also entitled to retain prepayment fees, late charges, assumption fees, interest float on advance payments, and similar charges to the extent they are collected from borrowers. The Corporation will compensate Lenders in an amount up to, but never exceeding, the amount of interest retention described above, less a prescribed minimum amount to be retained by the Corporation for itself in consideration of its guaranty obligations and servicing responsibilities.

Payments on Mortgage Loans; Distributions on Certificates

On the twenty-fifth day of each month (beginning with the month following the month of the Issue Date), the Corporation will, respecting each Issue, distribute to Certificateholders an amount equal to the total of (i) the principal due on the Mortgage Loans in the related Pool during the period beginning on the second day of the month prior to the month of such distribution and ending on the first day of such month of distribution (the "Due Period"), (ii) the Stated Principal Balance of any such Mortgage Loan which was prepaid in full during the second month next preceding the month of such distribution (including as prepaid for this purpose any Mortgage Loan repurchased by the Corporation as described herein because of the Corporation's election to repurchase the Mortgage Loan after it is delinquent, in whole or in part, with respect to four consecutive installments of principal and interest, or because of the Corporation's election to repurchase such Mortgage Loan under the circumstances described in the last paragraph under "Collection and Other Servicing Procedures" below), (iii) the amount of any partial prepayment of a Mortgage Loan received in the second month next preceding the month of distribution, and (iv) in respect of all Fixed-Rate Mortgage Loans other than GPMs during their Deferred Interest Period, one month's interest at the Pass-Through Rate (or Accrual Rate in the case of GPMs) on the Pool Principal Balance as reported to Certificateholders in connection with the previous distribution (or, respecting the first distribution, the Pool Principal Balance on the Issue Date). For purposes of distributions, a Mortgage

Loan will be considered to have been prepaid in full if, in the Corporation's reasonable judgment, the full amount finally recoverable on account of such Mortgage Loan has been received, whether or not such full amount is equal to the Stated Principal Balance of the Mortgage Loan. The Corporation may, in its discretion, include with any distribution principal prepayments, both full and partial, received during the month prior to the month of distribution but is under no obligation to do so.

For each GPM during its Deferred Interest Period and each ARM, the Corporation will, on each monthly Distribution Date, distribute an amount as to interest equal to the amount of interest payable on such Mortgage Loan during the applicable Due Period (which will, in the case of GPMs during their Deferred Interest Period, and may, in the case of ARMs having deferred interest features, be less than one month's interest at the Mortgage Interest Rate) less the amount retained by the Corporation as described under "Servicing Through Lenders" above.

Distributions on any Distribution Date will be made to Certificateholders of record on the prior Record Date (the close of business on the last day of the immediately preceding month). Each Certificateholder will be entitled to receive an amount equal to the total amount distributed multiplied by the Fractional Undivided Interest evidenced by such Holder's Certificate.

The Corporation's Guaranty

The Corporation's obligation described above to distribute amounts representing scheduled principal and interest, whether or not received, and its obligation to distribute the full principal amount of any foreclosed or otherwise finally liquidated Mortgage Loan, whether or not such principal amount is actually recovered, constitute the Corporation's guaranty obligations in respect of the Certificates. If the Corporation were unable to perform such obligations, distributions to Certificateholders would consist solely of payments and other recoveries on Mortgage Loans and, accordingly, delinquencies and defaults would impact monthly distributions to Certificateholders

Reports to Certificateholders

With respect to each distribution, the Corporation will cause to be forwarded to each Certificateholder with respect to all Certificates held by such Certificateholder in each Pool, a statement setting forth, to the extent applicable, the following information:

- (i) the amount, if any, due on such Certificates on the related Distribution Date on account of total scheduled and unscheduled principal (including any Deferred Interest);
- (ii) the amount due on such Certificates on the related Distribution Date on account of interest;
- (iii) the total of the cash distribution on such Certificates on the related Distribution Date;
- (iv) the Certificate Principal Balances of such Certificates on the related Distribution Date after giving effect to any distribution of principal made on such date and to any Deferred Interest added to the principal balances of the underlying Mortgage Loans during the preceding Due Period;
- (v) the total amount of any Deferred Interest which was added to the principal balances of the underlying Mortgage Loans during the preceding Due Period;
- (vi) the amount, if any, of (i) above which is allocable to Deferred Interest;
- (vii) the amount, if any, of (iv) above which is allocable to Deferred Interest; and
- (viii) for ARM Pools, the Accrual Rate applicable to such Distribution Date (or, in the event the underlying Mortgage Loans have different Accrual Rates, the approximate weighted average Accrual Rate)

Within a reasonable period of time after the end of each calendar year, the Corporation will furnish to each Person who at any time during the calendar year was a Certificateholder a statement containing the information set forth in items (i), (ii), (v) and (vi) above, in summary form for such calendar year, or for any portion thereof during which such Person was a Certificateholder.

Servicing Compensation and Payment of Certain Expenses by the Corporation

As compensation for its activities and obligations under the Trust Indenture, the Corporation will be entitled to retain the amounts applicable to interest which are not required to be distributed to Certificateholders as described above. In addition, the Corporation is entitled to retain any amounts by

which the proceeds of the liquidation of a Mortgage Loan exceed (i) the Stated Principal Balance of that Mortgage Loan and (ii) interest thereon at the Pass-Through Rate in the case of a Fixed-Rate Mortgage Loan (other than a GPM) or interest thereon at the Accrual rate in the case of a GPM or an ARM. The Corporation will pay all expenses incurred by it in connection with its servicing activities, including, without limitation, the fees to Lenders, and is not entitled to reimbursement therefor out of the Trust Fund.

Additional servicing compensation in the form of prepayment charges, assumption fees, late payment charges or otherwise will be retained by the Corporation.

Collection and Other Servicing Procedures

The Corporation is responsible for servicing the Mortgage Loans in each Pool and may, as set forth above, conduct such servicing through Lenders or through other Corporation-approved mortgage servicers. In connection with its servicing activities, the Corporation has full power and authority to do or cause to be done any and all things as it may deem necessary or appropriate in its sole discretion, including the foreclosure or comparable conversion of a defaulted Mortgage Loan. In lieu of undertaking any such foreclosure, the Corporation may, in its discretion and without obligation, repurchase from the Trust Fund any Mortgage Loan which is delinquent, in whole or in part, as to four consecutive installments of principal and interest. The purchase price will be equal to the Stated Principal Balance of the delinquent Mortgage Loan together with accrued interest at the Pass-Through Rate (or the Accrual Rate in the case of a GPM or an ARM) and will be distributed to Certificateholders in the same manner as full prepayments of Mortgage Loans. See "Description of Certificates—Payments on Mortgage Loans; Distributions on Certificates." (TI Sections 5.01 and 5.03)

With respect to each Mortgage Loan in a Pool, the Lender makes certain warranties to the Corporation concerning such matters as the recordation of the original Mortgage, the validity of the Mortgage Loan as a first lien on the Mortgaged Property and compliance by such Mortgage Loan with applicable state and Federal laws. In the event of a material breach of any such warranty or a material defect in the Mortgage Loan documentation, the Corporation may withdraw such Mortgage Loan from the Trust Fund at a price equal to its Stated Principal Balance together with interest thereon at the Pass-Through rate (or the Accrual Rate in the case of a GPM or an ARM). Alternatively, the Corporation may, at its option, for all Pools other than Pools containing Multifamily Mortgage Loans, substitute a new Mortgage Loan for a defective Mortgage Loan; provided, however, that no such substitution may take place more than two years subsequent to the date of the original issue of the related Certificates and any such substitute Mortgage Loan must satisfy certain eligibility criteria designed to assure that the nature of the Pool will not be altered by any such substitution. Any amount by which the Stated Principal Balance of the defective Mortgage Loan exceeds the principal balance of the substitute Mortgage Loan (the substitute Mortgage Loan may not be larger than the Mortgage Loan it is replacing) will be passed through to Certificateholders.

Subject to the following paragraph and to the extent consistent with then-current policies of the Corporation respecting mortgage loans held in its own portfolio, the Corporation in its discretion may enforce or waive enforcement of any of the terms of any Mortgage Loan or enter into an agreement for the modification of any of the terms of any Mortgage Loan, or take any action or refrain from taking any action in servicing any Mortgage Loan. In such connection, the Corporation may waive any prepayment charge, assumption fee or late payment charge or may exercise or refrain from exercising any "call option rider"; provided, however, that any decision to exercise or refrain from exercising any "call option rider" must be consistent with then-current policies or practices employed by the Corporation respecting comparable mortgage loans held in its own portfolio and must be without consideration of the ownership status of the related Mortgage Loan.

In connection with the transfer or prospective transfer of title to a Mortgaged Property, the Corporation is obligated to accelerate the maturity of the related Mortgage Loan where that Mortgage Loan contains a "due-on-sale" clause permitting acceleration under those conditions unless the Corporation is restricted by law from enforcing the "due-on-sale" clause or the Corporation elects to withdraw such Mortgage Loan from the Pool. See "Maturity and Prepayment Assumptions."

In the event that, for any reason, the Corporation is not obligated to accelerate the maturity of a Conventional Mortgage Loan upon the transfer, or prospective transfer, of title to the underlying

Mortgaged Property, the Corporation may enter into a transaction by which the obligor is released from liability on the related Mortgage Loan and the transferee assumes such liability; provided, however, that no such transaction shall (i) be entered into which would not have been entered into had the Mortgage Loan been held in the Corporation's own portfolio or (ii) provide for reduction of the Mortgage Interest Rate or, in the case of any ARM, provide for any change in any interest rate adjustment provision or provision governing the calculation of scheduled payments if any such change would be adverse to the interests of Certificateholders.

The Trust Indenture provides that the Corporation may repurchase from the related Pool, at a price equal to the Stated Principal Balance thereof plus accrued interest thereon at the applicable Pass-Through Rate (or the applicable Accrual Rate in the case of a GPM or an ARM), any Mortgage Loan respecting which the underlying Mortgaged Property is transferred, or proposed to be transferred, under circumstances permitting the Corporation to accelerate the maturity of such Mortgage Loan pursuant to the terms of any "due-on-sale" clause contained therein.

Certain Matters Regarding the Corporation

The Trust Indenture provides that the Corporation may not resign from its obligations and duties thereunder, except upon determination that those duties are no longer permissible under applicable law. No such resignation will become effective until a successor has assumed the Corporation's obligations and duties under the Trust Indenture; provided, however, that no successor will succeed to the Corporation's guaranty obligations described above, the Corporation continuing to be responsible thereunder notwithstanding any termination of its other duties and responsibilities under the Trust Indenture. In the event that the Corporation is unable to fulfill its continuing guaranty obligations, the Trust Indenture may be modified to provide for monthly distributions to be made from then-available Mortgage Loan payments and other recoveries in a manner similar to practices and procedures followed in the servicing of whole loans for institutional investors. (TI Section 9.01)

The Trust Indenture also provides that neither the Corporation nor any director, officer, employee or agent of the Corporation will be under any liability to the Trust Fund or to Certificateholders for any action taken or for refraining from the taking of any action in good faith pursuant to such Trust Indenture, or for errors in judgment; provided, however, that neither the Corporation nor any such person will be protected against any liability which would otherwise be imposed by reason of willful misfeasance, bad faith or gross negligence or by reason of willful disregard of obligations and duties.

In addition, the Trust Indenture provides that the Corporation is not under any obligation to appear in, prosecute or defend any legal action which is not incidental to its responsibilities under the Trust Indenture and which in its opinion may involve it in any expense or liability. The Corporation may, however, in its discretion undertake any such legal action which it may deem necessary or desirable in the interests of the Certificateholders. In such event, the legal expenses and costs of such action and any liability resulting therefrom will be expenses, costs and liabilities of the Corporation which will not be reimbursable to the Corporation out of the Trust Fund. (TI Section 8.02)

Any corporation into which the Corporation may be merged or consolidated, or any corporation resulting from any merger, conversion or consolidation to which the Corporation is a party, or any corporation succeeding to the business of the Corporation, will be the successor of the Corporation under the terms of the Trust Indenture. (TI Section 9.02)

Events of Default

Events of Default under the Trust Indenture will consist of (i) any failure by the Corporation to distribute to Certificateholders any required payment which continues unremedied for 15 days after the giving of written notice of such failure to the Corporation by the Holders of Certificates evidencing Fractional Undivided Interests aggregating not less than five percent of the related Trust Fund; (ii) any failure by the Corporation duly to observe or perform in any material respect any other of its covenants or agreements in the Trust Indenture which failure continues unremedied for 60 days after the giving of written notice of such failure to the Corporation by the Holders of Certificates evidencing Fractional Undivided Interests aggregating not less than 25 percent of the related Trust Fund; and (iii) certain events

of insolvency, readjustment of debt, marshalling of assets and liabilities or similar proceedings and certain actions by or against the Corporation indicating its insolvency, reorganization or inability to pay its obligations. (TI Section 9.03)

Rights Upon Event of Default

As long as an Event of Default under the Trust Indenture for any Issue remains unremedied, the Holders of Certificates evidencing Fractional Undivided Interests aggregating not less than 25 percent of the related Trust Fund may, in writing, terminate all of the obligations and duties of the Corporation as Trustee and in its corporate capacity under the Trust Indenture in respect of such Issue (other than its guaranty obligations described above which continue notwithstanding any such termination) and name and appoint, in writing, a successor to succeed to all such responsibilities, duties and obligations of the Corporation thereunder (other than the Corporation's guaranty obligations) and to the legal title to the Mortgage Loans held in such Trust Fund. (TI Section 9.03)

Amendment

The Trust Indenture as it relates to any Issue may be amended by the Corporation without the consent of or notice to any of the Certificateholders, for one or more of the following purposes: (i) to add to the covenants of the Corporation; (ii) to evidence the succession of another party or parties to the Corporation and the assumption by such successor or successors of the obligations of the Corporation thereunder in its corporate capacity or in its capacity as Trustee or in both such capacities; (iii) to eliminate any right reserved to or conferred upon the Corporation in its corporate capacity; (iv) to make provisions for the purpose of curing any ambiguity or correcting or supplementing any provision in the Trust Indenture or any Issue Supplement, provided such provisions do not adversely affect the interests of any Certificateholder; or (v) to modify the Trust Indenture under the circumstances and for the purposes set forth in the final sentence of the first paragraph under "Certain Matters Regarding the Corporation" above. (TI Section 11.01)

The Trust Indenture as it relates to any Issue may also be amended by the Corporation with the consent of the Holders of Certificates evidencing Fractional Undivided Interests aggregating not less than 66 percent of the related Trust Fund so as to waive compliance by the Corporation with any terms of the Trust Indenture or related Issue Supplement, or to allow the Corporation to eliminate, change, add to, or modify the terms of the Trust Indenture or Issue Supplement. However, no such waiver or amendment may, without the consent of all Certificateholders, terminate or modify the guaranty obligations of the Corporation or reduce the percentages of Certificates the Holders of which are required to consent to any waiver or amendments. In addition, no waiver or amendment shall, without the consent of each Certificateholder affected thereby, reduce in any manner the amount of, or delay the timing of, payments received on Mortgage Loans which are required to be distributed on any Certificate. (TI Section 11.02)

List of Certificateholders

With respect to each Pool, in the event that Holders of Certificates evidencing Fractional Undivided Interests aggregating not less than five percent of the related Trust Fund notify the Corporation in writing that they desire to communicate with other Certificateholders of that Trust Fund, accompanied by a copy of the proposed communication, then, within five business days after receipt of such notification, the Corporation will afford access to such Certificateholders during normal business hours to the most recent list of Certificateholders in such Pool. (TI Section 12.02)

Termination

The Trust Indenture as it relates to each Issue terminates upon the final payment or liquidation of the last Mortgage Loan remaining in the related Pool and distribution of all proceeds thereof. The Trust Indenture as it relates to each Issue will terminate also upon repurchase by the Corporation, at its option, of all remaining Mortgage Loans in the related Pool at a price equal to 100 percent of the Stated Principal Balance of each such Mortgage Loan together with one month's interest thereon at the Pass-Through Rate (or, in the case of a GPM Pool or an ARM Pool, one month's interest on the Stated Principal Balance of each GPM or ARM, as the case may be, at the applicable Accrual Rate). (TI Section 10.01) The exercise

of such option will effect early retirement of the Certificates of that Issue, but the Corporation's right to repurchase is conditioned upon the Pool Principal Balance at the time of repurchase being less than ten percent of the Pool Principal Balance on the Issue Date. In addition, the Corporation has stated that it will be its policy not to exercise any such option in respect of any Pool if (i) it has knowledge that any related Certificate has been pledged to secure an issue of cash flow obligations and (ii) the exercise of such option would take place prior to the earliest date upon which the issuer of such cash flow obligations can exercise an option to redeem such obligations without premium. In no event, however, will the trust relating to each Pool as created by the Trust Indenture continue beyond the expiration of 21 years from the death of the last survivor of the persons named in the Trust Indenture. For each Issue, the Corporation will give written notice of termination of the Trust Indenture as it relates to such Issue to each affected Certificateholder, and the final distribution will be made only upon surrender and cancellation of the Certificates at an office of the Corporation specified in the notice of termination. (TI Section 10.01)

FEDERAL TAX ASPECTS

Taxation of Certificateholders

Set forth is a discussion of certain Federal income tax consequences to persons purchasing Certificates, including the impact of the recently enacted Deficit Reduction Act of 1984 (the "1984 Act"). The discussion does not purport to deal with all aspects of Federal taxation that may be relevant to particular investors. Prospective investors are advised to consult their own tax advisors regarding the federal income tax consequences of holding and disposing of Certificates as well as any tax consequences arising under the laws of any state or other taxing jurisdiction.

The Internal Revenue Service issued Revenue Ruling 84-10, 1984-3 I.R.B. 9, which sets forth certain Federal income tax consequences relating to investments in the Certificates issued with respect to a Pool. Pursuant to Revenue Ruling 84-10, a Pool will not be classified as an association taxable as a corporation, but will be classified as a trust of which the Certificateholders of the respective Pool are the owners under Subpart E of Part I of Subchapter J of the Internal Revenue Code of 1954, as amended (the "Code"). Each Certificateholder will be treated as the owner of a pro rata undivided interest in the ordinary income and corpus of the trust attributable to that particular Pool and will be considered to be the equitable owner of a pro rata undivided interest in each of the Mortgage Loans included therein.

Accordingly, Certificateholders of a particular series will be required to report on their Federal income tax returns, consistent with their methods of accounting, their pro rata share of the entire income from the Mortgage Loans in that particular Pool, including interest, prepayment penalties, assumption fees and late payment charges received by the Pool, plus any amount paid to the Pool by the Corporation as interest under its guaranty. It is expected that accrual basis Certificateholders of GPM or ARM Pools with respect to which interest payments are deferred will be required to include a substantial amount of interest in income earlier than they receive the cash relating to such interest income. Certificateholders will be entitled to deduct their pro rata share of the servicing fee paid to the Corporation, as provided in section 162 or section 212 of the Code, consistent with their methods of accounting.

Certificateholders must also report their pro rata share of any original issue discount on each of the Mortgage Loans as ordinary income, consistent with their methods of accounting. The special rules of section 1272 of the Code will be applicable to the Certificateholders' pro rata shares of such original issue discount on any Mortgage Loans in the Pool to the extent that the conditions for the application of that section are met. These special rules do not apply with respect to Mortgage Loans originated before March 2, 1984 if the Mortgagors of such Mortgage Loans were natural persons; however, these special rules may apply, pursuant to the 1984 Act, with respect to all such Mortgage Loans originated on or after March 2, 1984. To the extent these special rules apply, Certificateholders may be required to include amounts in income before the receipt of cash attributable to that income. With respect to any undivided interest in a Mortgage Loan purchased at a premium, the Certificateholder will not be entitled to a deduction for amortization under the special rules of section 171 of the Code unless the conditions for the application of

that section are met. However, such a premium may result in the inclusion by a Certificateholder of a lesser amount of original issue discount under the special rules of section 1272 of the Code. Certificateholders are advised to consult with their tax advisors as to whether premium or discount results from the acquisition of Certificates and the effect, if any, of such premium or discount upon any secondary market for Certificates. Such premium might be deductible only upon sale or final distribution in respect of the Certificates, and then only as a short- or long-term capital loss, depending upon how long the Certificates have been held. The long-term holding period is, pursuant to the 1984 Act, six months with respect to an undivided interest in a Mortgage Loan acquired by a Certificateholder after June 22, 1984 and on or before December 31, 1987 and will be one year with respect to all other undivided interests in Mortgage Loans.

The Internal Revenue Service also ruled in Revenue Ruling 84-10 as follows:

1. A Certificate owned by a domestic building and loan association is considered as representing "loans secured by an interest in real property" within the meaning of section 7701(a)(19)(C)(v) of the Code, provided the real property underlying the Mortgages is (or, from the proceeds of the Mortgage Loans, will become) the type of real property described in that section of the Code.

2. A Certificate owned by a real estate investment trust is considered as representing "real estate assets" within the meaning of section 856(c)(5)(A) of the Code, and the interest income is considered "interest on obligations secured by mortgages on real property" within the meaning of section 856(c)(3)(B) of the Code.

3. A Certificate is considered as representing "qualifying real property loans" within the meaning of section 593(d) of the Code, provided the real property underlying the Mortgages is (or, from the proceeds of the Mortgage Loans, will become) the type of real property described in that section of the Code. Thus, a Certificate owned by a domestic building and loan association or any other thrift institution described in section 593(a) of the Code will represent "qualifying real property loans" within the meaning of section 593(d) of the Code, provided the real property underlying the Mortgages is (or, from the proceeds of the Mortgage Loans, will become) the type of real property described in that section of the Code.

Pursuant to the 1984 Act, if a Certificateholder is considered as acquiring an undivided interest in a Mortgage Loan that constitutes a "market discount bond" and incurs or continues indebtedness to purchase or carry such undivided interest, the interest on such indebtedness for any taxable year that exceeds the interest (including original issue discount) on such undivided interest includable in the Holder's income for that year would not be allowed as a deduction in that year. A deduction would, at the election of the Holder, be allowed in a subsequent taxable year for any previously disallowed deduction to the extent that, for such subsequent taxable year, the interest (including original issue discount) includable in the Holder's gross income with respect to such undivided interest exceeds the interest paid or accrued with respect to the indebtedness. To the extent not previously deducted, the amount of any disallowed interest deduction will be allowed in the year of the disposition of such undivided interest. A market discount bond includes any undivided interest in a Mortgage Loan with respect to which the face amount exceeds the Certificateholder's basis in such undivided interest. In the case of an undivided interest in a Mortgage Loan issued at a discount, the face amount will be deemed to be the issue price (the original amount loaned by the lender of the Mortgage Loan) increased by the amount of original issue discount includable in the gross income of all Holders who owned such undivided interest for periods prior to its acquisition by the Certificateholder (without adjustment for any prior purchase premium). In addition, on the disposition of an undivided interest in a Mortgage Loan originated after July 18, 1984 that is a market discount bond, a Certificateholder will be required to include as interest income any gain realized on such disposition to the extent of any accrued market discount. If a Mortgage Loan was originated on or before July 18, 1984, any gain recognized by a Certificateholder on a disposition of an undivided interest in such Mortgage Loan shall be treated as ordinary income to the extent the amount of such gain does not exceed

the amount of the previously disallowed interest deduction which is allowable in the year of such disposition. An exception to the rules in this paragraph will apply if the Certificateholder elects to include in income in each taxable year the portion of the market discount attributable to such year (computed either on a straight line or a constant interest rate basis) with respect to all market discount bonds acquired by the Certificateholder on or after the first day of the first taxable year to which such election applies.

The Corporation will furnish to each Certificateholder with each distribution a statement setting forth the amount of such distribution allocable to principal and to interest. In addition, the Corporation will furnish or make available, within a reasonable time after the end of each calendar year, to each Certificateholder who at any time during such year held a Certificate, a statement setting forth such Certificateholder's pro rata share of interest income and administrative expense for such calendar year to assist the Certificateholder in the preparation of its tax return. The Corporation shall also furnish to the required persons such other forms as may be required to be filed under the Code and regulations thereunder with respect to Pools. In addition, the 1984 Act imposes certain reporting responsibilities on owners of mortgage loans relating to the receipt of interest income with respect to such mortgage loans and foreclosures and abandonments of the underlying mortgaged property. These reporting requirements are expected to apply to the Pools. However, the reporting of interest is the responsibility of the Trustee. Treasury regulations may impose the reporting of foreclosures and abandonments on the Trustee.

Backup Withholding

Section 3406 of the Code requires a payor of reportable interest and other reportable payments to solicit information from individuals, partnerships (not composed exclusively of corporations), trusts, estates, and certain other payees (not described below as exempt recipients). This solicitation must be made in connection with the payor's responsibility to report such payments to the Internal Revenue Service. If the information is not provided to the payor by a payee required to do so, the payor is required to withhold on all reportable payments. This withholding requirement is referred to as "backup withholding." Certificateholders exempt from backup withholding include corporations, organizations that are exempt from taxation under section 501(a) of the Code, individual retirement plans, the United States Government and any wholly owned agency or instrumentality thereof, state and local governments, foreign governments, international organizations, securities or commodities dealers who are required to register under the laws of the United States or a state, futures commission merchants, real estate investment trusts, entities registered at all times during the taxable year under the Investment Company Act of 1940, common trust funds under section 584 of the Code, nominees and custodians known generally in the investment community as nominees or listed in the most recent publication of the *Nominee List*, published by the American Society of Corporate Secretaries, Inc., financial institutions, and certain charitable trusts

Any amounts deducted and withheld from a distribution to a Certificateholder would be allowed as a credit against such Certificateholder's Federal income tax. Furthermore, certain penalties may be imposed by the Internal Revenue Service on a Certificateholder who is required to supply the information but who does not do so in the proper manner. The Corporation or its agent may decide that it must deduct and withhold from each distribution made or credited to a Certificateholder who has not provided the required information an amount equal to 20 percent of the reportable interest or other reportable component of such distribution.

LEGAL OPINION

Any purchaser of Certificates will be furnished upon request an opinion by Caryl S. Bernstein, Esq., Executive Vice President, General Counsel and Secretary of the Corporation, as to the validity of the Certificates, the applicable Trust Indenture and the relevant Issue Supplement.

ERISA CONSIDERATIONS

On May 13, 1982, the Department of Labor issued a final regulation (29 C.F.R. § 2550.401b-1), effective June 17, 1982, which provides that in the case where an employee benefit plan ("plan") subject to the Employee Retirement Income Security Act of 1974 ("ERISA") acquires a "guaranteed governmental mortgage pool certificate" then, for purposes of the fiduciary responsibility provisions of ERISA and the prohibited transaction provisions of the Code, the plan's assets include the certificate and all of its rights with respect to such certificate under applicable law, but do not, solely by reason of the plan's holding of such certificate, include any of the mortgages underlying such certificate. Under the regulation, the term "guaranteed governmental mortgage pool certificate" is specifically defined to include a mortgage pool certificate with respect to which interest and principal payable pursuant to the certificate are guaranteed by the Corporation. The effect of such regulation is to make clear that the sponsor (that is, the entity which organizes and services the pool, in this case the Corporation), the trustee, and other persons, in providing services with respect to the mortgages in the pool, would not be subject to the fiduciary responsibility provisions of Title I of ERISA, nor be subject to the prohibited transaction provisions of Section 4975 of the Code, merely by reason of the plan's investment in a certificate. The Corporation has been advised by its counsel, Brown, Wood, Ivey, Mitchell & Petty, that, on the basis of the final regulation and class exemptions previously issued by the Department of Labor, the acquisition from the Corporation and holding of the Certificates by plans are not prohibited either by ERISA or related provisions of the Code.

FEDERAL NATIONAL MORTGAGE ASSOCIATION

The Corporation is a federally chartered and privately owned corporation organized and existing under the Federal National Mortgage Association Charter Act (12 U.S.C. §1716 *et seq.*) (the "Charter Act"). It is the nation's largest supplier of residential mortgage funds, with a net portfolio of \$80.2 billion of mortgage loans as of June 30, 1984. The Corporation was originally established in 1938 as a United States government agency to provide supplemental liquidity to the mortgage market and was transformed into a stockholder-owned and privately managed corporation by legislation enacted in 1968.

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

The Corporation was profitable in the first six months of 1984 and in 1983, after experiencing losses in 1982 and 1981. The primary cause of the losses in 1982 and 1981 was the excess of the cost of outstanding debt over the yield on the mortgage portfolio (or "negative spread"). In the first quarter of 1984 and in 1983 the negative spread was substantially narrower than the negative spread in 1982 and 1981, and its impact on results of operations was more than offset by income from other sources. During the second quarter of 1984, interest rates rose, increasing the negative spread. If interest rates remain at current levels or increase further, the Corporation could experience unprofitable operating results in subsequent quarters of 1984 and for 1984 as a whole. See "Selected Financial Data," "Management's Discussion and Analysis of Financial Results" and "Mortgage Portfolio Spread."

Although the Secretary of the Treasury of the United States has discretionary authority to lend the Corporation up to \$2.25 billion outstanding at any time, neither the United States nor any agency thereof is obligated to finance the Corporation's operations or to assist the Corporation in any other manner.

The principal office of the Corporation is located at 3900 Wisconsin Avenue, N.W., Washington, D.C. 20016, and there are five regional offices located in Atlanta, Georgia; Chicago, Illinois; Dallas, Texas; Los Angeles, California; and Philadelphia, Pennsylvania. The Corporation also has a fiscal office at 100 Wall Street, New York, New York 10005.

Copies of the Corporation's annual report and quarterly financial statements, as well as other financial information, are available from John Meehan, Senior Vice President—Finance and Treasurer, Federal National Mortgage Association, 100 Wall Street, New York, New York 10005 (Telephone: 212-425-9002) or Paul Paquin, Director of Investor Relations, Federal National Mortgage Association, 3900 Wisconsin Avenue, N.W., Washington, D.C. 20016 (Telephone: 202-537-7115).

CAPITALIZATION

The following table sets forth the capitalization of the Corporation as of June 30, 1984.

	<u>Average Maturity</u>	<u>Average Annual Cost</u>	<u>Outstanding</u>
(Dollars in thousands)			
Bonds, notes and debentures (1):			
Due within one year			
Short-term notes, net of unamortized discount.....	4 mos.	10.77%	\$11,397,027
Master notes	4 mos.	10.39%	729,444
Investment notes (2).....		8.85%	7,625
Debentures	6 mos.	11.66%	17,022,245
Mortgage-backed bonds	3 mos	7.29%	23,230
Capital debentures	7 mos	11.77%	500,000
Total due within one year.....			<u>29,679,571</u>
Due after one year			
Debentures	3 yrs. 5 mos.	11.52%	48,173,435
Exchangeable debentures	6 yrs. 8 mos.	12.66%	450,000
Mortgage-backed bonds	5 yrs 4 mos.	8.28%	394,423
Capital debentures, net of unamortized discount.....	9 yrs.	9.98%	1,145,922
Convertible capital debentures	12 yrs. 3 mos	4.43%	27,465
Total due after one year			<u>50,191,245</u>
Total bonds, notes and debentures			<u>\$79,870,816</u>
Total stockholders' equity			<u>\$ 1,287,732</u>

(1) All of the outstanding short-term and long-term debt was issued under Section 304(b) of the Charter Act except the subordinated capital debentures and subordinated convertible capital debentures which were issued under Section 304(e) and the mortgage-backed bonds which were issued under Section 304(d). See "Corporate Indebtedness" for a description of certain limitations applicable to debt issued by the Corporation.

(2) Investment notes have fixed interest rates. The outstanding balance associated with each note will fluctuate over the life of the note agreement. The average term of the outstanding investment note agreements is 24 years.

SELECTED FINANCIAL DATA

The following selected financial data for the years 1979 through 1983 (which data are not covered by the report of independent certified public accountants) have been summarized or derived from the audited financial statements. The financial data for the six months ended June 30, 1983 and 1984 are unaudited and include, in the opinion of management, all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation. The results of operations for the six months ended June 30, 1984 are not necessarily indicative of the results expected for the entire year. These data should be read in conjunction with the audited financial statements and notes to financial statements which are presented elsewhere herein.

Condensed Statements of Operations (Dollars in millions, except per share amounts)

	Year Ended December 31,					Six Months Ended June 30,	
	1979	1980	1981(1)	1982	1983	1983	1984
Interest margin	\$ 322	\$ 21	\$ (463)	\$ (506)	\$ (62)	\$ (41)	\$ (17)
Commitment, guaranty and other fees	60	68	125	301	238	121	103
Gain (loss) on sales of mortgages	(2)	—	—	44	91	49	12
Other expenses	(81)	(63)	(22)	(96)	(129)	(60)	(67)
Income (loss) before Federal income taxes and extraordinary item	299	26	(360)	(257)	138	69	31
Provision for Federal income taxes	137	12	(170)	(123)	63	32	14
Income (loss) before extraordinary item	162	14	(190)	(134)	75	37	17
Extraordinary item: gain on early retirement of debt(2)	—	—	—	29	—	—	—
Net income (loss)	<u>\$ 162</u>	<u>\$ 14</u>	<u>\$ (190)</u>	<u>\$ (105)</u>	<u>\$ 75</u>	<u>\$ 37</u>	<u>\$ 17</u>
Earnings (loss) per share:							
Before extraordinary item:							
Primary	\$ 2.81	\$ 24	\$(3.22)	\$(2.20)	\$ 1.15	\$.57	\$.26
Fully diluted	2.68	.23	(3.22)	(2.20)	1.13	.56	.26
Net:							
Primary	2.81	.24	(3.22)	(1.72)	1.15	.57	.26
Fully diluted	2.68	.23	(3.22)	(1.72)	1.13	.56	.26
Cash dividends per share	1.28	1.12	.40	.16	.16	.08	.08

Condensed Balance Sheets (Dollars in millions)

	At December 31,					At June 30,	
	1979	1980	1981	1982	1983	1983	1984
Assets							
Mortgage portfolio, net	\$49,655	\$55,742	\$59,846	\$69,714	\$75,665	\$72,231	\$80,220
Other assets	1,424	2,426	2,052	3,753	3,253	3,350	4,207
Total assets	<u>\$51,079</u>	<u>\$58,168</u>	<u>\$61,898</u>	<u>\$73,467</u>	<u>\$78,918</u>	<u>\$75,581</u>	<u>\$84,427</u>
Liabilities							
Bonds, notes and debentures:							
Due within one year	\$13,087	\$15,542	\$17,365	\$25,781	\$26,860	\$22,567	\$29,680
Due after one year	35,116	39,338	41,186	43,833	47,734	48,736	50,191
Other liabilities	1,375	1,831	2,104	2,650	3,048	3,038	3,268
Total liabilities	49,578	56,711	60,655	72,264	77,642	74,341	83,139
Stockholders' equity	1,501	1,457	1,243	1,203	1,276	1,240	1,288
Total liabilities and stockholders' equity	<u>\$51,079</u>	<u>\$58,168</u>	<u>\$61,898</u>	<u>\$73,467</u>	<u>\$78,918</u>	<u>\$75,581</u>	<u>\$84,427</u>

(1) Results for the year ended December 31, 1981 include a \$42.0 million reduction in the allowance for loan losses effected in the second quarter. There was also a decrease in the rate of providing for losses on conventional loans which resulted in a reduction in the loss provision of \$8.3 million during the last three quarters of 1981. Exclusive of these reductions, the 1981 loss would have been \$217.0 million or \$3.67 per share.

(2) In September 1982, the Corporation entered into a nontaxable transaction which resulted in the issuance of 6.3 million shares of its common stock in exchange for \$101 million of its long-term debentures, which were retired.

Condensed Statements of Changes in Financial Position
(Dollars in millions)

	Six Months Ended June 30,	
	1983	1984
Funds Provided		
Operations	\$ 24	\$ (2)
Proceeds from issuance of debentures and bonds	11,074	11,981
Increase (decrease) in short-term notes	(2,147)	586
Mortgage repayments, less discount amortized	3,297	2,958
Sales of mortgages, excluding gains and losses	2,538	942
Other items	204	20
Total funds provided	14,990	16,485
Funds Applied		
Debentures and bonds retired	7,251	7,301
Mortgage purchases including refinancings, less discount	8,470	8,518
Mortgage refinancings	(91)	(26)
Dividends paid	5	5
Total funds applied	15,635	15,798
Increase (decrease) in cash and marketable securities	(645)	687
Beginning balance, cash and marketable securities	2,453	1,720
Ending balance, cash and marketable securities	\$ 1,808	\$ 2,407

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL RESULTS

ANNUAL PERIODS

General

The Corporation was profitable in 1983 after experiencing losses in 1982 and 1981. The primary cause of the Corporation's losses in 1982 and 1981 was the combination of high interest rates and the mismatch in the maturities of the Corporation's asset and debt portfolios. When interest rates rose to unprecedented levels in 1980 and 1981, large amounts of maturing debt had to be refinanced at much higher costs. Turnover of assets was much slower. Although the Corporation purchased substantial volumes of high-yielding assets, the increase in yield on portfolio did not keep pace with the sharp increase in the cost of outstanding debt.

Starting in 1981, a new management team implemented a wide range of strategic and operating changes designed to mitigate this problem. The effect of these changes, aided by a moderation in interest rates, produced a sharp improvement in operating results in 1983.

Since the new management team started in 1981, the Corporation has:

- Purchased substantial volumes of adjustable rate and second mortgages, which allow the Corporation to more closely match the maturity of its assets with that of its borrowings;
- Restructured the channels for acquiring mortgages and greatly expanded the types of mortgage instruments purchased, resulting in purchases of high-yielding assets in record volumes;
- Increased the amount of revenue which is derived from sources other than interest income on the mortgage portfolio—commitment fees, mortgage-backed security guaranty fees and gains on sales of mortgages; and
- Issued liabilities with extended maturities when there were opportunities to do so at favorable rates, while relying on lower-cost, short-term borrowings in periods of higher interest rates.

This discussion and analysis describes how these management initiatives helped produce a profit in 1983.

Results of Operations

The Corporation's net income for 1983 was \$75.5 million, compared with a net loss of \$104.9 million in 1982 (\$133.8 million excluding an extraordinary gain). In 1981, the Corporation incurred a net loss of \$190.4 million (\$217.0 million excluding the effect of a reduction in the provision and allowance for conventional loan losses). The per share net income in 1983 was \$1.13, fully diluted, compared with the 1982 per share loss of \$1.72 (\$2.20 before extraordinary item) and the 1981 per share loss of \$3.22 (\$3.67 before reduction in the provision and allowance for conventional loan losses).

In 1983, cash dividends were \$.16 per share, compared with per share cash dividends of \$.16 and \$.40 in 1982 and 1981, respectively.

Overall portfolio performance is measured by the "spread" between the average net yield on the mortgage portfolio and the average cost of outstanding debt. In 1983, average portfolio yield was 10.67 percent and the average cost of outstanding debt was 11.12 percent, producing a negative spread of .45 percent. In 1982, average portfolio yield was 10.29 percent and the average cost of outstanding debt was 11.59 percent, resulting in a negative spread of 1.30 percent. In 1981, the average portfolio yield was 9.45 percent and the average cost of outstanding debt was 10.81 percent, producing a negative spread of 1.36 percent. This substantial improvement in spread was the major cause of the decrease in negative interest margin to \$61.5 million in 1983 from \$506.5 million in 1982 and \$462.9 million in 1981.

Average portfolio yield was 10.70 percent during December 1983, compared with 10.69 percent during December 1982 and 9.82 percent during December 1981. The moderation in interest rates experienced in 1983 resulted in a significant increase in prepayments of many of the high-rate loans in the

Corporation's mortgage portfolio and also resulted in a downward adjustment of the net yield on its adjustable rate mortgages. These factors, combined with sales of mortgages in the form of mortgage-backed securities, reduced the favorable impact of 1983's record purchases and limited the improvement in yield to .01 percent during the year. The average cost of outstanding debt was 11.07 percent during December 1983, compared with 11.39 percent during December 1982 and 11.42 percent during December 1981.

Interest earned on marketable securities was \$221.7 million in 1983, compared with \$232.1 million in 1982 and \$140.0 million in 1981. This reflects the Corporation's decision to maintain an increased liquidity position in 1983 and 1982. The additional liquidity provides a temporary source of funding for mortgage purchases, which allows greater flexibility in structuring debt issues.

Other major sources of revenue are commitment fees, guaranty fees from mortgage-backed securities and gains on sales of mortgages. Commitment fees were \$151.2 million in 1983, compared with \$263.9 million in 1982 and \$112.6 million in 1981. The decline in commitment fees in 1983 resulted primarily from a decrease of \$2.9 billion or 21 percent in the volume of negotiated commitments and a decline of 45 percent in the average fee rate on negotiated transactions from 1.05 percent in 1982 to .58 percent in 1983. These declines reflect the increased competition in the mortgage market in 1983, which resulted from the lower interest rate environment.

Guaranty fees from mortgage-backed securities increased to \$54.3 million in 1983 from \$16.1 million in 1982 (the first full year of the program) and \$.3 million in 1981. This significant upward trend reflects the Corporation's success in marketing these securities. Mortgage-backed securities outstanding totaled \$25.1 billion at December 31, 1983, compared with \$14.5 billion and \$7.7 billion at December 31, 1982 and 1981, respectively. These fees are a stable source of revenue and help to insulate the Corporation's earnings from fluctuations in interest rates.

Gains on sales of mortgages more than doubled in 1983 compared to 1982, increasing from \$44.4 million in 1982 to \$90.7 million in 1983. Sales volume increased from \$3.0 billion in 1982 to \$4.5 billion in 1983.

The Mortgage Portfolio

In 1983, the Corporation issued \$18.6 billion in mortgage purchase commitments, compared with \$22.1 billion and \$9.5 billion in 1982 and 1981, respectively. Negotiated transactions comprised 58 percent of commitments issued in 1983, compared with 62 percent in 1982 and 16 percent in 1981. The Corporation further reduced its issuance of optional delivery commitments where the yield is fixed at the time of the commitment. In 1983, the Corporation eliminated all such optional delivery commitment programs (except for adjustable rate mortgages), including the Free Market System auctions which were the primary channel for acquisition of mortgages prior to 1982. Such optional delivery commitments result in mortgage deliveries primarily when interest rates increase, so that assets are generally purchased at yields below current market levels. When rates decline, lenders are free to sell the loans to other investors at a better price. Mandatory delivery commitments eliminate this risk, as lenders are required to deliver at the commitment yield whether this is above or below the current rate. They also allow the Corporation to plan its borrowings and risk management strategies more effectively. As of December 31, 1983, total commitments outstanding were \$5.5 billion, compared with \$7.6 billion and \$3.7 billion at December 31, 1982 and 1981, respectively.

The Corporation's purchase volume in 1983 was a record \$17.6 billion at an average net yield of 12.65 percent, compared with \$15.1 billion at 15.00 percent in 1982 and \$6.1 billion at 15.38 percent in 1981. The spread between the net yield on purchases and the cost of debt issued in 1983 was 2.58 percent, compared with 2.18 percent in 1982 and a negative .84 percent in 1981. Adjustable rate mortgages and second mortgages comprised 24 percent and 8 percent, respectively, of 1983's purchase volume. In 1982, adjustable rate mortgages and second mortgages were 21 percent and 10 percent of total purchases, respectively. Adjustable rate and second mortgages together comprised only 5 percent of purchases in 1981. On December 31, 1983, the net mortgage portfolio was \$75.7 billion, compared with \$69.7 billion and \$59.8 billion on December 31, 1982 and 1981, respectively.

Mortgage repayments increased substantially to \$6.2 billion in 1983 compared with \$2.1 billion in 1982 and \$1.9 billion in 1981. As noted above, the moderation in interest rates in 1983 resulted in an increase in prepayments of high rate loans.

Financing Activities

Since the Corporation's assets have considerably longer maturities than the debt financing them, the average cost of outstanding debt is more volatile than the average yield on portfolio and, as a result, earnings will continue to be sensitive to interest rate changes. In 1983, the Corporation sought to maintain a balance between reducing the average cost of outstanding debt by relying on lower cost shorter-term borrowings and lengthening the average maturity of outstanding debt by issuing longer-term debentures when rates were favorable. In addition, the Corporation took advantage of other financing opportunities in the market by reopening existing debentures, implementing a new master note program and continuing its residential financing security program. Beginning in 1982, the Corporation initiated a risk management program, which uses the interest rate futures and other financial markets to provide protection against increases in borrowing costs

In 1983, the Corporation raised a total of \$40.0 billion of debt at an average cost of 10.07 percent, compared with \$55.0 billion at 12.82 percent in 1982 and \$40.4 billion at 16.22 percent in 1981. The cost of debt issued in 1983, in addition to being substantially below that of 1982 and 1981, was also more stable throughout the year. In 1983, the cost of debt issued ranged from a monthly high of 10.41 percent in August to a low of 9.46 percent in January. The monthly high and low in 1982 were 15.41 percent in February and 9.72 percent in December, respectively.

The average maturity of outstanding debt increased from two years, three months at December 31, 1982 to two years, five months at December 31, 1983. The Corporation issued approximately \$6.7 billion of debentures with maturities of five years or more in 1983, compared with \$4.3 billion in this maturity range in 1982. Debt issued in 1983 included a \$250 million 30-year debenture offering with a 10-year par call provision.

The capital markets continued to be receptive to the Corporation's debt issues in 1983, as evidenced by narrower spreads between rates on the Corporation's securities and Treasury securities of similar maturities. Based on secondary market quotes of the comparative yields on the securities, the spread between the Corporation's six-month discount notes and six-month Treasury bills on a bond equivalent basis averaged .17 percent during 1983. This spread averaged .70 percent in 1982 and 1.09 percent in 1981. Measured similarly, the spread between the Corporation's five-year debentures and Treasury securities with a five-year maturity averaged .29 percent during 1983, compared with .64 percent in 1982 and .82 percent in 1981.

Mortgage-Backed Securities

In 1983, the Corporation issued \$13.3 billion of guaranteed mortgage-backed securities ("MBS"), compared with \$14.0 billion in 1982. The primary channel for issuance of MBS is "swap" transactions whereby participating lenders exchange pools of mortgages directly for securities. The Corporation also pools mortgages from its portfolio and issues securities for cash through public offerings and private placements. MBS issues from portfolio, which are treated as sales of assets, totaled \$4.4 billion in 1983 and \$3.0 billion in 1982. These portfolio sales increase market liquidity and also have produced substantial gains.

MBS guaranty fees grow in direct relation to the volume of MBS outstanding. The Corporation plans to continue being active in this market, which will provide it with a substantial stream of guaranty fee income that is not as interest rate sensitive as investing in mortgages for its own portfolio

INTERIM PERIOD

Six Months Ended June 30, 1984

Net income for the six months ended June 30, 1984 was \$17.0 million or \$.26 per share, compared with \$38.5 million or \$.57 per share for the six months ended December 31, 1983 and \$37.0 million or \$.56 per share for the six months ended June 30, 1983. The reduction in net income was due largely to the declines in gain on sales of mortgages and commitment fees.

Mortgage purchases were \$9.2 billion during the first half of 1984, compared with \$8.6 billion and \$9.0 billion in the second half and first half of 1983, respectively. For the six-month period ended June 30, 1984, adjustable rate mortgages comprised 38 percent of all purchases, compared with 24 percent of all purchases in 1983. The net yield on mortgage purchases during the first half of 1984 was 12.37 percent, compared with 12.64 percent and 12.65 percent for purchases during the second half of 1983 and the first half of 1983, respectively. The net yield on the mortgage portfolio was 10.81 percent at June 30, 1984, compared with 10.70 percent at December 31, 1983 and 10.66 percent at June 30, 1983.

Debt issued during the first half of 1984 had an average cost of 11.30 percent, compared with 10.25 percent and 9.84 percent for debt issued during the second half of 1983 and the first half of 1983, respectively. The cost of total debt outstanding increased to 11.41 percent at June 30, 1984, from 11.12 percent at December 31, 1983 and 11.10 percent at June 30, 1983.

During the first half of 1984, the average portfolio yield was 10.75 percent and the average cost of outstanding debt was 11.18 percent, producing a negative spread of 0.43 percent. In the second half of 1983, the average portfolio yield was 10.64 percent and the average cost of outstanding debt was 11.09 percent, resulting in a negative spread of 0.45 percent. In the first half of 1983, the average portfolio yield of 10.69 percent and the average cost of outstanding debt of 11.14 percent produced a negative spread of 0.45 percent. Interest margin, which includes income from short-term investments as well as net yield on the mortgage portfolio, was a negative \$17.2 million in the first half of 1984, compared with a negative \$20.1 million in the last half of 1983 and a negative \$41.4 million in the first half of 1983.

The Corporation issued \$10.1 billion in mortgage commitments in the first half of 1984, compared with \$9.6 billion in the second half of 1983 and \$9.0 billion in the first half of 1983. Commitment fees totaled \$52.0 million for the six months ended June 30, 1984. For the six-month periods ended December 31, 1983 and June 30, 1983, commitment fees were \$68.6 million and \$82.7 million, respectively. Commitment fees declined primarily because of a change in product mix and competition in the mortgage marketplace.

Mortgage-backed security guaranty fees were \$35.2 million for the first six months of 1984, compared with \$30.7 million for the six-month period ended December 31, 1983 and \$23.6 million for the six-month period ended June 30, 1983. The increase in fees is due to an increase in the amount of securities outstanding from \$20.9 billion at June 30, 1983 to \$25.1 billion at December 31, 1983, and to \$29.3 billion at June 30, 1984.

The gain on sales of mortgages was \$11.7 million for the first half of 1984 compared with \$41.9 million and \$48.8 million in the second half and first half of 1983, respectively. The decline largely results from a decrease in sales activity from \$2.6 billion in the first half of 1983 and \$1.9 billion in the second half of 1983 to \$1.0 billion in the first half of 1984.

Continuing high interest rates confront the Corporation with the prospect of refinancing debt in the third quarter of 1984 at a cost which is above the rates borne by the debt to be refinanced. If interest rates remain at current levels or increase further, the Corporation could experience unprofitable results of operations in the second half of 1984 and for 1984 as a whole. For information concerning historical spreads and the amount and cost of long-term debt maturing during the remainder of 1984 and the first half of 1985, see "Mortgage Portfolio Spread."

MORTGAGE PORTFOLIO SPREAD

The Corporation's portfolio profitability depends on the difference, or "spread," between the return it receives on its mortgage portfolio and the cost of money it borrows to finance that portfolio. The following table sets forth the spread on the portfolio during the periods indicated.

<u>For the Month</u>	<u>Net Portfolio at Month-End</u> (In millions)	<u>Average Yield(1)</u>	<u>Average Cost of Outstanding Indebtedness(1)</u>			<u>Spread</u>
			<u>Short-term Notes</u>	<u>Bonds and Debentures</u>	<u>Aggregate</u>	
December 1979	\$49,655	8.74%	11.90%	8.29%	8.72%	.02%
December 1980	55,742	9.20	13.93	9.29	9.87	(.67)
December 1981	59,846	9.82	16.10	10.63	11.42	(1.60)
December 1982	69,714	10.69	10.85	11.55	11.39	(.70)
1983						
July	72,220	10.63	9.48	11.34	11.06	(.43)
August	72,667	10.61	9.63	11.35	11.07	(.46)
September	72,789	10.62	9.63	11.37	11.11	(.49)
October	73,256	10.62	9.64	11.41	11.15	(.53)
November	74,291	10.65	9.59	11.34	11.07	(.42)
December	75,665	10.70	9.64	11.35	11.07	(.37)
1984						
January	76,438	10.71	9.67	11.36	11.08	(.37)
February	76,700	10.74	9.72	11.35	11.08	(.34)
March	78,224	10.75	9.86	11.36	11.11	(.36)
April	79,083	10.75	10.07	11.45	11.21	(.46)
May	79,736	10.76	10.36	11.46	11.27	(.51)
June	80,220	10.79	10.67	11.49	11.33	(.54)

(1) Average yield on portfolio is calculated for the month shown and converted to an annual interest rate using, as the numerator, the interest income plus the amortized discount less servicing fees and, as the denominator, the average outstanding unpaid principal balance of the mortgage portfolio less unamortized discount. Similarly, the average cost of bonds and debentures and aggregate indebtedness is calculated using actual expense and the average outstanding applicable indebtedness during the month. The average cost of short-term indebtedness is the average original issue cost computed on a 365-day basis.

Approximately \$16.0 billion principal amount of bonds and debentures (original term of one year or longer) matured or will mature during the twelve months following June 30, 1984.

<u>Maturity Date</u>	<u>Principal Amount</u> (In millions)	<u>Weighted Average Cost</u>	<u>Maturity Date</u>	<u>Principal Amount</u> (In millions)	<u>Weighted Average Cost</u>
1984			1985		
July 10	\$1,428	9.04%	January 10	\$1,050	9.95%
August 7	534	10.90	February 11	1,250	14.85
August 10	1,000	11.15	March 11	1,050	11.17
September 10	1,000	9.26	April 10	500	13.81
October 10	1,000	13.36	May 10	1,600	12.87
November 12	1,075	17.08	June 10	1,400	9.62
December 10	1,650	12.05	Other Dates	1,156	11.36
Other Dates	353	9.90			

An improvement in the spread and a return to a positive spread will depend upon the Corporation's ability to increase the yield on its mortgage portfolio and to refinance maturing borrowings at lower rates.

HISTORY AND BUSINESS

The Corporation was incorporated on February 10, 1938 pursuant to Title III of the National Housing Act. The Corporation was then a wholly owned government corporation that borrowed operating funds almost entirely from the United States Treasury. Its business primarily consisted of the purchase and resale of mortgages insured by the Federal Housing Administration ("FHA") and, since 1948, mortgages guaranteed by the Veterans Administration ("VA"), for the purpose of establishing and maintaining a secondary market for such mortgages. Title III was revised on August 2, 1954 and called the Federal National Mortgage Association Charter Act. Under the new Charter Act, the Corporation became a mixed-ownership corporate instrumentality of the United States. In connection with its secondary market operations, the Corporation issued non-voting common stock to the institutions from which it purchased mortgages.

From 1950 to 1965, the Corporation was a constituent agency of the Housing and Home Finance Agency and, from November 9, 1965 to September 1, 1968, the Corporation operated in the Department of Housing and Urban Development ("HUD"). The Charter Act, as in effect prior to September 1, 1968, empowered the Corporation to (1) conduct secondary market operations in FHA-insured and VA-guaranteed home mortgages consisting of purchases and sales of such mortgages ("Secondary Market Operations"), (2) perform special assistance functions in the purchase of mortgages as authorized by the President of the United States or by the Congress to assist in financing home mortgages in instances where established home financing facilities were inadequate ("Special Assistance Functions") and (3) manage and liquidate certain mortgages ("Management and Liquidating Functions")

Pursuant to amendments to the Charter Act enacted in the Housing and Urban Development Act of 1968 (the "1968 Act"), the Corporation was, as of September 1, 1968, partitioned into two separate and distinct corporations. One, the Government National Mortgage Association ("GNMA"), is a wholly owned corporate instrumentality of the United States within the Department of HUD. GNMA retained all of the assets and liabilities acquired and incurred under the Special Assistance Functions and Management and Liquidating Functions carried on by the predecessor corporation prior to the effective date of the 1968 Act

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The second, the Federal National Mortgage Association, now constituted as a federally chartered corporation, retained the assets and liabilities related to the Secondary Market Operations prior to the effective date of the 1968 Act. The 1968 Act changed each share of outstanding non-voting common stock of the Corporation, par value \$100 per share, into one share of voting common stock without par value and authorized the Corporation to issue its common stock to the public. The 1968 Act also provided for a transitional period for the Corporation's stockholders to assume control of the Corporation, and all preferred stock theretofore held by the Secretary of the Treasury was retired as of September 30, 1968. Accordingly, the entire equity interest in the Corporation became, and is now, publicly owned.

Government Supervision

Although the 1968 Act eliminated all federal ownership interest in the Corporation, it did not terminate the significant government regulation of the Corporation. Under the Charter Act, approval of the Secretaries of the Treasury and HUD is required for the Corporation's issuance of its obligations; however, the Secretary of HUD has delegated the authority to approve the issuance of the Corporation's debt instruments to the Secretary of the Treasury. The Secretaries of both the Treasury and HUD have approved the issuance and guaranty by the Corporation of the Certificates described herein and the Prospectus Supplement.

With regard to the Corporation's issuance of debt instruments, the Charter Act specifically provides that the aggregate amount of the Corporation's general obligations (under Section 304(b)) shall not exceed, at any one time, fifteen times the sum of capital, capital surplus, general surplus, reserves and undistributed earnings of the Corporation unless a greater ratio is fixed by the Secretary of HUD. The Secretary of HUD has increased this ratio to 30:1. Regulations adopted by HUD provide that, in the event

of a reduction in the capital of the Corporation, the Corporation's debt to capital ratio will automatically increase to such figure as is necessary to include all obligations outstanding pursuant to Section 304(b) of the Charter Act. The Certificates described herein and in the Prospectus Supplement are authorized by Section 304(d) of the Charter Act, and, as such, are not subject to any Charter Act limitations as to the maximum amount which may be issued or outstanding at any time.

In addition to specific enumerated powers, including those described above, the Secretary of HUD is granted general regulatory power over the Corporation under Section 309(h) of the Charter Act with authority to promulgate rules and regulations to carry out the purposes of the Charter Act. The Secretary also may require, pursuant to said Section 309(h), that a reasonable portion of the Corporation's mortgage purchases be related to the national goal of providing adequate housing for low- and moderate-income families, but with a reasonable economic return to the Corporation.

The Charter Act also gives the Secretary of HUD the authority to audit and examine financial transactions of the Corporation, but this authority has never been exercised.

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

In addition to placing the Corporation under significant federal supervision, the Charter Act also grants to the Corporation certain privileges and immunities that it would not otherwise enjoy. For instance, securities issued by the Corporation are deemed to be "exempt securities" under laws administered by the Securities and Exchange Commission to the same extent as securities that are obligations of, or guaranteed as to principal and interest by, the United States. Accordingly, no registration statement or other document with respect to the Certificates offered hereby and by the Prospectus Supplement has been filed with the Securities and Exchange Commission.

As described in "Corporate Indebtedness," the Corporation has the authority to borrow up to \$2.25 billion from the Secretary of the Treasury. Any such borrowing would be within the Secretary's discretion and the Corporation has not used this facility since its transition from government control.

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

MORTGAGE PORTFOLIO

General

The principal activity of the Corporation consists of the purchase of mortgages, primarily on residential properties, meeting certain eligibility requirements established by statute and by the Corporation. Substantially all of such purchases are made by the Corporation pursuant to forward purchase commitments issued by the Corporation. Under such commitments, the Corporation agrees in advance to purchase a specified dollar amount of loans at an agreed price. See "Mortgage Portfolio—Commitments" below.

Prior to 1972, all mortgages purchased were insured or guaranteed by the federal government, but since February 1972, under authority granted by the Emergency Home Finance Act of 1970, the Corporation has also purchased mortgages which are not federally insured or guaranteed (so-called "conventional mortgages") See "Mortgage Portfolio—Mortgage Purchase Activity" below

Commitments

The Corporation's mortgage loan purchases are based on its issuance of commitments by which the Corporation agrees in advance to purchase a specified dollar amount of loans. Lenders generally pay fees, typically from one-quarter of one percent to two percent of the amount of the commitment, for these commitments depending on market conditions, the type of mortgage loan and the length and characteristics of the commitment.

The Corporation purchases most of its mortgages pursuant to mandatory delivery commitments. Under such commitments, lenders are obligated to sell mortgages to the Corporation at the commitment yield.

The Corporation also issues standby commitments. Under these commitments, the Corporation commits to purchase a designated amount of mortgages. A yield on the mortgages is not established at the time the standby commitment is issued. To deliver the mortgages, the lender must convert the standby commitment to a mandatory delivery commitment. In such event, the lender generally pays an additional fee to the Corporation. The yield on the mortgages is established at the time of conversion.

In early 1984, the Corporation conducted a test program involving guaranteed rate convertible commitments. Under this program, the Corporation has committed to purchase adjustable rate and fixed rate mortgages at interest rates established during the offering period between January 23, 1984 and February 17, 1984. Mortgages can be delivered at the option of the lender against the commitment until October 17, 1984. To exercise the option, the lender must convert all or part of the optional delivery commitment to a mandatory delivery commitment according to a specified fee schedule. The Corporation has hedged commitments under the test program using a variety of financial instruments.

The following table sets forth the Corporation's mortgage commitment activity in connection with both the portfolio and mortgage-backed securities.

Mortgage Commitments
(Dollars in millions)

<u>Commitments Issued</u>	Year Ended December 31,					Six Months Ended June 30, 1984
	1979	1980	1981	1982	1983	1984
Portfolio						
Home: Government insured or guaranteed	\$ 5,698	\$5,570	\$2,971	\$ 923	\$ 141	\$ 20
Conventional: Fixed-rate	4,441	2,511	4,927	13,405	10,562	5,177
Adjustable rate	—	—	1,360	6,024	6,573	4,111
Second trust	—	—	213	1,745	1,325	317
Total home mortgages	<u>10,139</u>	<u>8,081</u>	<u>9,471</u>	<u>22,097</u>	<u>18,601</u>	<u>9,625</u>
Project: Fixed-rate	40	2	—	9	6	415
Adjustable rate	—	—	—	—	—	78
Total project mortgages	<u>40</u>	<u>2</u>	<u>—</u>	<u>9</u>	<u>6</u>	<u>493</u>
Total portfolio	<u>\$10,179</u>	<u>\$8,083</u>	<u>\$9,471</u>	<u>\$22,106</u>	<u>\$18,607</u>	<u>\$10,118</u>
Mortgage-backed securities	<u>\$ —</u>	<u>\$ —</u>	<u>\$3,259</u>	<u>\$15,517</u>	<u>\$15,722</u>	<u>\$32,879(1)</u>
<u>Commitments Outstanding</u>	At December 31,					At June 30, 1984
	1979	1980	1981	1982	1983	1984
Portfolio						
Home: Government insured or guaranteed	\$ 3,243	\$2,246	\$ 920	\$ 44	\$ 8	\$ 2
Conventional: Fixed-rate	3,111	1,008	1,468	4,016	1,554	1,461
Adjustable rate	—	—	1,279	3,331	3,828	4,016
Second trust	—	—	31	206	66	111
Total home mortgages	<u>6,354</u>	<u>3,254</u>	<u>3,698</u>	<u>7,597</u>	<u>5,456</u>	<u>5,590</u>
Project: Fixed-rate	55	24	19	9	4	48
Adjustable rate	—	—	—	—	—	2
Total project mortgages	<u>55</u>	<u>24</u>	<u>19</u>	<u>9</u>	<u>4</u>	<u>50</u>
Total portfolio	<u>\$ 6,409</u>	<u>\$3,278</u>	<u>\$3,717</u>	<u>\$ 7,606</u>	<u>\$ 5,460</u>	<u>\$ 5,640</u>
Mortgage-backed securities	<u>\$ —</u>	<u>\$ —</u>	<u>\$2,555</u>	<u>\$ 2,331</u>	<u>\$ 1,627</u>	<u>\$28,756(1)</u>

(1) The substantial increase in the commitment volume for mortgage-backed securities in the first six months of 1984 resulted from a marketing effort which included the elimination of commitment fees for a limited period on optional delivery mortgage-backed securities commitments. Because these optional delivery commitments were issued without charging any commitment fee, the Corporation expects that the delivery rate on these commitments will be lower than normal.

Mortgage Purchase Activity

As described above, the Corporation currently purchases conventional mortgages as well as mortgages that are insured by the FHA or guaranteed by the VA. Substantially all loans currently in the Corporation's portfolio are secured by first liens, but the Corporation also purchases second lien whole loans and participations in such loans. With the exception of \$5.6 billion of project loans held by the Corporation at June 30, 1984, all of the mortgage loans purchased by the Corporation and held in its portfolio are secured by residential one- to four-family properties. Since FHA-insured and VA-guaranteed loans are, because of their government backing, essentially risk-free from a credit standpoint, the Corporation's basic eligibility criterion for their purchase is simply the FHA insurance or the VA guaranty. Because conventional loans have no Federal government backing, the Corporation has established certain eligibility criteria for their purchase in an effort to reduce the risk of loss from mortgagor defaults. Because adjustable rate mortgages have been associated with significantly higher risk of default than fixed-rate mortgages, the Corporation has established special criteria for such mortgages. For information on the Corporation's loss and delinquency experience on conventional Mortgage Loans, see "Mortgage Portfolio—Conventional Mortgage (Whole Loan) Portfolio Loss and Delinquency Experience"

Generally, the Corporation requires that the unpaid principal amount of each conventional mortgage purchased by it (i) not be greater than 80 percent of the appraised value of the mortgaged property, or (ii) if it is greater than 80 percent, that the excess over 75 percent be insured by an acceptable mortgage insurance company for so long as the principal balance of the loan is greater than 80 percent of such original appraised value (or of the appraised value as determined by a subsequent appraisal). Mortgage insurance is not required on mortgages with loan-to-value ratios greater than 80 percent if the mortgage seller either retains a participation in the mortgage of not less than 10 percent or agrees to repurchase the loan in the event of default.

Sellers of mortgages to the Corporation generally retain, subject to the Corporation's supervision, the responsibility for servicing the loans sold to the Corporation. Servicers are compensated through the retention of a specified portion of each interest payment on a serviced mortgage loan. Servicing includes the collection and remittance of principal and interest payments, administration of escrow accounts, collection of insurance claims and, if necessary, foreclosure.

Conventional mortgage loans may not be purchased by the Corporation if their principal balance at the time of purchase exceeds \$114,000, except for loans secured by properties in Alaska and Hawaii or by two- to four-family dwelling units, where higher maximums apply. Loans eligible for insurance by the FHA are subject to statutory maximum amount limitations, and the Corporation imposes maximum amount limitations on loans guaranteed by the VA. Maximum principal balances applicable to the Corporation's conventional mortgage purchases can be increased annually to reflect the increasing cost of homes.

Generally, conventional mortgages purchased by the Corporation must conform to credit appraisal and underwriting guidelines established by the Corporation. These guidelines are designed to assess the creditworthiness of the mortgagor as well as to assure that the value of the mortgaged home is sufficient to secure the mortgage loan. These guidelines are changed from time to time by the Corporation, and the Corporation may deviate from them as to particular loans.

At June 30, 1984, the large majority of the Corporation's mortgage portfolio consisted of fixed-rate mortgage loans. Substantially all such loans provide for level monthly installments of principal and interest, such installments consisting primarily of interest during the early and middle years, with the major portion of the original principal balance being payable during the years immediately preceding maturity. The great majority of such loans had original maturities of not less than 25 years (generally 30 years for single-family loans and 40 years for project loans). At June 30, 1984, the weighted average dollar life (based on the underlying amortization schedules and assuming no prepayments) of the mortgage loans in the Corporation's mortgage portfolio was approximately 25 years, and the weighted average yield (net of servicing) was 10.81 percent.

The following table sets forth the composition of the Corporation's mortgage loan portfolio, purchase activity, principal repayments and mortgage sales, the weighted average yield (net of servicing) on the mortgage portfolio and the average net yield on mortgages purchased.

Mortgage Portfolio
(Dollars in millions)

	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>Six Months Ended June 30, 1984</u>
Unpaid Principal Balances at End of Period						
Home: Government insured or guaranteed....	\$29,381.7	\$33,416.7	\$34,550.7	\$33,742.3	\$30,999.9	\$29,615.9
Conventional: Fixed-rate.....	16,106.0	18,358.0	21,153.2	27,789.6	32,533.3	35,537.3
Adjustable rate.....	—	—	106.8	3,331.9	7,126.3	10,127.6
Second trust.....	—	—	175.3	1,635.5	2,385.4	2,352.4
Project: Fixed-rate.....	5,609.1	5,551.9	5,425.9	5,314.4	5,211.3	5,537.5
Adjustable rate.....	—	—	—	—	—	72.7
Total unpaid balance	<u>\$51,096.8</u>	<u>\$57,326.6</u>	<u>\$61,411.9</u>	<u>\$71,813.7</u>	<u>\$78,256.2</u>	<u>\$83,243.4</u>
Average yield net of servicing.....	8.75%	9.24%	9.85%	10.73%	10.70%	10.81%
Purchases During Period						
Home: Government insured or guaranteed....	\$ 5,387.8	\$ 5,272.5	\$ 2,284.0	\$ 901.1	\$ 186.1	\$ 91.3
Conventional: Fixed-rate.....	5,410.2	2,801.8	3,544.3	9,442.9	11,702.4	4,946.1
Adjustable rate.....	—	—	106.8	3,210.0	4,246.3	3,442.3
Second trust.....	—	—	175.9	1,552.3	1,407.9	270.1
Project: Fixed-rate.....	9.2	26.8	1.9	9.5	14.3	362.6
Adjustable rate	—	—	—	—	—	72.7
Total mortgages purchased.....	<u>\$10,807.2</u>	<u>\$ 8,101.1</u>	<u>\$ 6,112.9(1)</u>	<u>\$15,115.8(1)</u>	<u>\$17,557.0(1)</u>	<u>\$ 9,185.1(1)</u>
Average net yield on mortgages purchased....	10.11%	12.27%	15.38%	15.00%	12.65%	12.37%
Repayments During Period						
Home: Government insured or guaranteed....	\$ 2,060.7	\$ 1,343.3	\$ 1,252.1	\$ 1,263.6	\$ 2,045.5	\$ 946.5
Conventional: Fixed-rate.....	827.9	549.2	740.5	909.6	3,474.0	1,491.9
Adjustable rate.....	—	—	—	28.9	451.9	493.7
Second trust.....	—	—	.6	92.1	658.0	303.1
Project: Fixed-rate.....	115.3	84.0	127.1	121.0	117.4	36.4
Total mortgage repayments.....	<u>\$ 3,003.9</u>	<u>\$ 1,976.5</u>	<u>\$ 2,120.3(1)</u>	<u>\$ 2,415.2(1)</u>	<u>\$ 6,746.8(1)</u>	<u>\$ 3,271.6(1)</u>
Sales During Period						
Home: Government insured or guaranteed....	\$ —	\$ —	\$ —	\$ 518.2	\$ 907.2	\$ 528.8
Conventional: Fixed-rate.....	.7	.6	8.6	1,896.9	3,560.3	450.2
Adjustable rate.....	—	—	—	—	—	—
Second trust.....	—	—	—	—	—	—
Project: Fixed-rate.....	21.1	—	.8	—	—	—
Total sales.....	<u>\$ 21.8</u>	<u>\$.6</u>	<u>\$ 9.4</u>	<u>\$ 2,415.1</u>	<u>\$ 4,467.5</u>	<u>\$ 979.0</u>

(1) Includes \$630 million, \$617 million, \$126 million and \$26 million principal amount of mortgage loans which were refinanced under the Corporation's resale/refinance policy in 1981, 1982, 1983 and the first six months of 1984, respectively.

As shown by the table, the level of principal repayments as a percentage of the Corporation's mortgage portfolio in 1983 and the first six months of 1984 reflects a substantial increase from the unusually low levels of 1980-1982. Since all of the loans in the Corporation's portfolio are prepayable by the borrower (in some cases with a small penalty), the moderation in interest rates experienced since 1982 resulted in a significant increase in prepayments of the high rate loans in the Corporation's mortgage portfolio. This moderation in rates also affected the Corporation's yield on its adjustable rate mortgages.

The low level of principal repayments experienced in 1980-1982 contributed to the Corporation's losses in 1981 and 1982. As a result, the Corporation kept lower yielding mortgages on its books, which reduced significantly the increase in yield on its mortgage portfolio that, under more normal conditions, the Corporation would otherwise have expected to realize. In addition, the Corporation was forced to rely more heavily on high cost borrowings to finance new mortgage purchases and to refund maturing indebtedness.

The Corporation believes that the significant reduction in principal paydowns during 1980-1982 was due primarily to the high interest rate environment. Because of the high cost of new financing, a major portion of home sales was financed through so-called "creative" financing wherein the existing mortgage was assumed by the purchaser of the home (and generally coupled with second mortgage or purchase money financing) or "wrapped" by another loan from another lender. The Corporation currently enforces "due-on-sale" clauses in conventional fixed-rate mortgages purchased by the Corporation pursuant to commitments issued on and after November 10, 1980 and in conventional mortgages covering properties whose sale has been facilitated by "wraparound" or second mortgages made by institutional lenders. However, since approximately 60 percent of the Corporation's portfolio loans (including all FHA and VA loans) do not contain any such clause and a number of states substantially prohibit the enforcement of such clauses in mortgages originated or assumed during certain periods prior to October 15, 1982, the Corporation has been unable to prevent assumptions on a major portion of its portfolio. (See "Description of Certificates—Collection and Other Servicing Procedures" for a description of the Corporation's policy for Mortgage Loans in Pools.)

Conventional Mortgage (Whole Loan) Portfolio Loss and Delinquency Experience

The portfolio of conventional mortgages that the Corporation purchased on a whole loan basis (as opposed to participation interests) consists predominantly of loans made to owner-occupants and secured by first liens on residential real property. Since February 1972, the Corporation has purchased \$37.7 billion of such loans and on June 30, 1984 this portfolio approximated \$25.2 billion. The loss and delinquency experience on this conventional whole loan portfolio is summarized in the following tables. These tables exclude whole loans purchased and serviced by the Corporation in summary format for which such statistics are not currently available.

Conventional Loan Loss Experience

	Year Ended December 31,					Six Months Ended June 30, 1984
	1979	1980	1981	1982	1983	
	(Dollars in millions)					
Principal balance at end of period	\$15,864.5	\$18,060.3	\$20,268.9	\$24,567.1	\$25,080.9	\$25,154.6
Net losses during period(1)	\$.8	\$.9	\$ 8	\$ 16	\$ 38.4	\$ 42.8
Net loss ratio(2)	0.0050%	0.0050%	0.0039%	0.0065%	0.1531%	0.3403%
Total number of loans at end of period	395,903	435,355	472,414	539,465	538,470	539,147
Total number of foreclosures during period	219	368	606	1,270	2,963	2,458
Percent foreclosed(2)	0.0553%	0.0845%	0.1283%	0.2354%	0.5503%	0.9118%

(1) For 1979 through 1982, net losses were determined upon disposition of foreclosed properties by subtracting from the proceeds realized the sum of the book value of the foreclosed asset and related foreclosure costs, expenses, interest accrued but uncollected to the date of foreclosure and other carrying costs. Beginning in September 1983, estimated losses on acquired properties are charged to the allowance for losses when properties are acquired rather than at disposition. Write-downs to market for properties on hand produced a one-time charge to the

allowance for losses of \$20.1 million in September 1983. Also charged to the allowance in September 1983 was \$6.2 million related to below market financing on sales of acquired properties in all prior periods. The items had no effect on reported net income in 1983 because losses had been provided for previously.

(2) The ratios are annualized and based on amounts at the end of the period.

As indicated in the above table, the net loss ratio has increased to .153 percent in 1983 and .340 percent (annualized rate) for the six months ended June 30, 1984, from .004 percent in 1981 and .007 percent in 1982. The increase in the net losses charged off resulted both from an increase in the percent of mortgage loans foreclosed and from a higher average loss per foreclosure. As a result of the increased net losses, the Corporation's total allowance for conventional loan losses (including the allowance for losses on loans in summary format and participations) declined from \$112.6 million at December 31, 1983 to \$81.7 million at June 30, 1984. Loan losses may continue during the remainder of 1984 at a level that could result in a further reduction in the Corporation's allowance for loan losses by year-end.

Delinquency Experience
(Percent of Portfolio By Number of Loans)

Period of Delinquency	At December 31,					At
	1979	1980	1981	1982	1983	June 30, 1984
One month	2.9%	2.7%	2.9%	3.3%	3.5%	3.0%
Two months .....	.5	.5	.5	.7	.8	.7
Three or more months	2	.1	.2	.3	.5	.4
Total (1)	3.6%	3.3%	3.6%	4.3%	4.8%	4.1%
In foreclosure or under special lender forbearance (2)	4%	.8%	.8%	1.0%	1.4%	1.4%

(1) Delinquency percentages exclude loans in foreclosure or under special lender forbearance.

(2) A substantial percentage of loans in foreclosure or under special lender forbearance are reinstated.

While these delinquency and loss rates represent past experience, there can be no assurance that the experience on the mortgage loans in a pool serving as the basis for certificates will be comparable.

Mortgage Purchase Policies

Since 1981, the Corporation has instituted a number of policies designed to make the Corporation's mortgage portfolio more responsive to fluctuations in prevailing interest rates and to better match its borrowing costs. These policies have had a favorable short-term effect on the Corporation's operations and are expected to be of importance in the future in mitigating the risks associated with rising interest rates. They include:

- *Purchase of Adjustable Rate Mortgage Loans ("ARMs")*. The Corporation has developed standard plans applicable to the purchase of conventional mortgage loans that contain provisions for the automatic adjustment, both up and down, of their interest rates in accordance with changes in a specified index. Generally, such adjustments are limited by payment or interest rate caps on the mortgage. The Corporation also has entered into special negotiated purchases of ARMs that do not conform to its standard plans. As of June 30, 1984, the Corporation had purchased \$11.0 billion of ARMs, had outstanding commitments totaling \$4.0 billion, and expects that future purchases will be substantial. The Corporation believes that these ARM loans will enable it to reduce the risk that the interest cost on its debt will exceed the income realized on its mortgage portfolio.

- *Resale/Refinance Loans*. Since March 1981, to upgrade the yield on its portfolio, the Corporation has offered financing to persons purchasing or refinancing homes that secure the Corporation's existing portfolio loans. These new loans are offered at interest rates that result from combining the existing

balance at its original rate with an additional amount at a market rate. The resulting rate tends to be less than prevailing market rates but significantly greater than that applicable to the refinanced loan. Refinanced loans facilitate the complete financing of the sale and discourage the assumption of the existing loan as part of a financing package. As of June 30, 1984, \$2.5 billion resale/refinance loans had been made by the Corporation and, of that amount, \$1.1 billion, or 44 percent, represented newly loaned money

- *Second Mortgages.* Substantially all of the loans currently in the Corporation's portfolio are secured by first liens; however, the Corporation also purchases conventional loans secured by second mortgages and participations in such loans. Second mortgages generally bear higher interest rates than contemporaneous first mortgages, have shorter maturities, and are usually prepaid prior to maturity. At June 30, 1984, the Corporation had purchased \$3.4 billion of second mortgages and had commitments to purchase \$ 1 billion.

- *Guaranteed Mortgage Pass-Through Certificates.* In November 1981, the Corporation began issuing guaranteed mortgage pass-through certificates evidencing beneficial interests in pools of conventional loans that are generally sold to the Corporation by lenders in exchange for certificates. The Corporation began issuing similar certificates representing beneficial interests in FHA/VA mortgages and similar certificates representing beneficial interests in growing equity mortgages in October and November 1982, respectively. The Corporation intends to begin issuing similar certificates representing beneficial interests in ARMs and similar certificates representing beneficial interests in fixed-rate graduated payment mortgage loans with deferred interest features in July and August 1984, respectively.

As of June 30, 1984, \$33.4 billion of guaranteed mortgage pass-through certificates had been issued and \$29.3 billion were outstanding. The Corporation's lenders either hold the certificates or sell them to private investors. In addition, the Corporation pools mortgages from its own portfolio or purchases mortgages from lenders in exchange for cash, assembles the mortgages in a pool, and sells the related certificates pursuant to public offerings and private placements. These securities, which are modeled after the highly successful GNMA mortgage-backed security program (which applies only to U.S. government-backed mortgages), are playing a significant role in the Corporation's operations. The Corporation receives fees for its origination, servicing and guaranty of certificates, a portion of which is paid by the Corporation to institutions that directly service pooled loans on behalf of the Corporation. The Corporation expects that the guaranteed mortgage pass-through certificates will enable it to further its statutory purpose of increasing the liquidity of residential mortgages without requiring that the Corporation take the financing or "spread" risk on the pooled loans.

However, because the Corporation guarantees timely payment of loans in certificate pools, it absorbs the ultimate credit risk on all loans in these pools. This risk may be offset somewhat to the extent that sellers of pools of loans elect to remain at risk on the loans sold. If the loss rate on conventional loans in such pools should appreciably increase, the Corporation's losses could, to the extent not offset by recourse to sellers, become significant

CORPORATE INDEBTEDNESS

The Corporation borrows in the capital markets more than any other privately owned corporation in the United States. Although the Corporation is privately owned and its obligations (other than its outstanding mortgage-backed bonds guaranteed by GNMA) are not backed by the United States or any agency or instrumentality thereof other than the Corporation, the Corporation's debt has traditionally been treated as "U.S. Agency" debt in the marketplace. The Corporation, as a result, has historically enjoyed ready access to funds in the private credit markets at rates that are slightly higher than the yields on U.S. Treasury obligations of comparable maturities

The following table sets forth at June 30, 1984 the maturity profile of the Corporation's bonds and debentures that were originally issued with a maturity of one year or longer.

<u>Maturing Within</u>	<u>Principal Amount</u>	<u>Weighted Average Cost</u>
	(In millions)	
One year	\$16,045	11.78%
One to two years	12,977	12.12
Two to three years	15,311	11.40
Three to four years.....	10,011	11.24
Four to five years	5,393	11.73
Over five years	6,519	10.44

At June 30, 1984, the Corporation had short-term and master notes outstanding aggregating \$12.5 billion at face amount. Such notes had a weighted average term to maturity of 110 days at such date and a weighted average cost of 10.76 percent.

All of the outstanding indebtedness of the Corporation consists of general, unsecured obligations issued and outstanding under Section 304(b) of the Charter Act except the subordinated capital debentures (including the convertible capital debentures), which were issued under Section 304(e), and the mortgage-backed bonds, which were issued under Section 304(d). Section 304(b) provides that the aggregate amount of obligations outstanding thereunder shall not exceed, at any one time, fifteen times the sum of the capital (including, for this purpose, capital debentures), capital surplus, general surplus, reserves and undistributed earnings of the Corporation unless a greater ratio is fixed by the Secretary of HUD. On December 22, 1982 the Secretary of HUD increased this ratio to 30:1. Regulations adopted by HUD provide that this increased ratio is, in the event of a reduction in the Corporation's capital, further automatically increased to such ratio as shall be necessary to include all obligations outstanding pursuant to Section 304(b). At June 30, 1984, this debt to capital ratio was 25.5:1, as compared with a ratio of 24.9:1 at June 30, 1983.

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

Section 304(d) of the Charter Act, pursuant to which mortgage-backed bonds and guaranteed mortgage pass-through certificates are outstanding, contains no limitation on the amount of obligations that may be outstanding thereunder. Section 304(d) of the Charter Act provides, however, that the mortgages pledged or set aside must be sufficient at all times to make debt service payments on the securities. At June 30, 1984, the Corporation had \$417.7 million in mortgage-backed bonds outstanding, of which \$408.5 million were guaranteed by GNMA pursuant to Section 306(g) of the National Housing Act, and are thus backed by the full faith and credit of the United States.

Section 304(c) of the Charter Act authorizes the Secretary of the Treasury, as a public debt transaction, to purchase obligations of the Corporation up to a maximum of \$2.25 billion outstanding at any one time. The Corporation has not used such borrowing facility with the U.S. Treasury since its transition from government control. Although the Secretary of the Treasury is authorized to purchase the obligations of the Corporation, he is under no requirement to do so. Any borrowings from the Secretary of the Treasury would be made pursuant to Section 304(b) of the Charter Act and, accordingly, would be subject to the applicable limitations and restrictions described above.

The following table sets forth the Corporation's borrowing activity and outstanding borrowings at face amounts, the respective costs of borrowings and average maturities.

Debt
(Dollars in millions)

	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>Six Months Ended June 30, 1984</u>
Short-Term, Master Notes and Investment Notes						
Issued during period						
—Amount	\$10,567	\$17,654	\$30,185	\$34,196	\$20,262	\$11,642
—Cost	11.75%	14.29%	16.56%	12.31%	9.47%	10.71%
—Average Maturity—Days	198	152	98	129	161	188
Outstanding at end of period						
—Amount	\$ 6,593	\$ 8,578	\$ 9,189	\$11,752	\$11,841	\$12,494
—Cost	12.09%	14.68%	15.47%	10.48%	9.67%	10.76%
—Average Maturity—Days	108	92	57	141	106	110
Bonds and Debentures						
Issued during period						
—Amount	\$10,056	\$11,500	\$10,221	\$20,785	\$19,756	\$11,991
—Cost	9.71%	12.05%	15.26%	13.62%	10.66%	11.75%
—Average Maturity—Months	57	48	43	36	53	42
Outstanding at end of period						
—Amount	\$41,831	\$46,604	\$49,560	\$58,300	\$63,066	\$67,756
—Cost	8.33%	9.32%	10.71%	11.55%	11.38%	11.51%
—Average Maturity—Months	45	41	36	32	34	33
Total Debt						
Issued during period						
—Amount	\$20,623	\$29,154	\$40,406	\$54,981	\$40,018	\$23,633
—Cost	10.72%	13.37%	16.22%	12.82%	10.07%	11.30%
—Average Maturity—Months	31	22	13	16	29	26
Outstanding at end of period						
—Amount	\$48,424	\$55,182	\$58,749	\$70,052	\$74,907	\$80,250
—Cost	8.81%	10.11%	11.42%	11.38%	11.12%	11.41%
—Average Maturity—Months	39	35	31	27	29	29

RECENT LEGISLATIVE DEVELOPMENTS

The U.S. Senate passed the "Secondary Mortgage Market Enhancement Act of 1983" (S. 2040) on November 17, 1983. This legislation, if enacted, would remove certain technical impediments to trading and investing in mortgage-backed securities through the amendment of various securities laws and investment laws applicable to financial institutions. The bill passed by the Senate would also amend the Corporation's Charter Act to: (i) authorize the Corporation to confer such voting rights on the holders of the Corporation's preferred stock as are permitted by the rules of the New York Stock Exchange; (ii) require the Corporation to calculate, in the case of a participation interest purchased by the Corporation, the conventional mortgage limit with respect to the total principal obligation of the mortgage; (iii) require the Secretary of HUD to respond within 45 days to any request from the Corporation for approval of the Corporation's action authorized under the Charter Act, subject to a 15-day extension; (iv) remove the 80 percent loan-to-value ratio limitation on the Corporation's conventional mortgage purchases of multi-family mortgages; (v) increase the Corporation's Board of Directors to 18 by the addition of three new stockholder-elected directors; (vi) require the Secretary of HUD to report annually to Congress on the Corporation's activities; (vii) increase the maximum dollar purchase limitations for the Corporation to

purchase conventional multifamily mortgages from 125 percent to 240 percent of the FHA limitations for multifamily mortgages in areas determined by HUD to require an increase under Section 207(c)(3) of the National Housing Act; and (viii) limit the Corporation's authority to purchase, service, sell, lend on the security of, and otherwise deal in conventional mortgages that are secured by second liens on one- to four-family residences (1) by imposing a maximum dollar limitation of \$50,000 for a one-family residence and \$60,000 for a two- to four-family residence, (2) by requiring such mortgages to be upon the principal residence of the mortgagor, and (3) by restricting such authority to purchase money mortgage loans or refinancing of the remaining balance of purchase money loans (this second-lien authority would expire October 1, 1985), while retaining the requirement of HUD prior approval.

A companion bill to S. 2040, also entitled the "Secondary Mortgage Market Enhancement Act of 1983" (H.R. 4557), was introduced in the House of Representatives on November 18, 1983. Title II of H.R. 4557 was marked-up and reported by the Housing Subcommittee of the House Banking Committee on May 8, 1984. As so marked-up and reported, this bill would amend the Corporation's Charter Act to: (i) require the Corporation to calculate, in the case of a participation interest purchased by the Corporation, the conventional mortgage limit with respect to the total original principal obligation of the mortgage; (ii) limit the Corporation's authority to purchase, service, sell, lend on the security of, and otherwise deal in conventional mortgages that are secured by second liens on one- to four-family residences by imposing a maximum dollar limitation equal to 50 percent of the single-family first mortgage limit (currently \$114,000), but without restricting the Corporation's ability to purchase any type of second mortgage and eliminating the requirement for any prior HUD approval; (iii) increase the Corporation's Board of Directors to 18 by the addition of three new stockholder-elected directors; (iv) revise the requirement that the Secretary of HUD approve the issuance of the Corporation's instruments except as to the Corporation's stock and debt obligations convertible into stock; (v) require the Secretary of HUD to report annually to Congress on the Corporation's activities; (vi) require the Secretary of HUD to respond within 45 days to any request from the Corporation for approval of the Corporation's action authorized under the Charter Act, subject to a 15-day extension; (vii) increase the maximum dollar purchase limitations for the Corporation to purchase conventional multifamily mortgages from 125 percent to 240 percent of the FHA limitations for multifamily mortgages in areas determined by HUD to require an increase under Section 207(c)(3) of the National Housing Act; (viii) remove the 80 percent loan-to-value ratio limitation on the Corporation's conventional mortgage purchases of multifamily mortgages; and (ix) allow the Corporation to initiate a program to purchase mortgages secured by manufactured housing without prior HUD approval.

A bill (H.R. 3420) was introduced in the House of Representatives on June 27, 1983 that would raise the single-family conventional mortgage limits for both the Corporation and the Federal Home Loan Mortgage Corporation ("FHLMC") in HUD-designated high-cost areas. As of July 27, 1984 this bill was sponsored by 111 Representatives. An identical bill (S. 2130) was introduced in the Senate on November 17, 1983. This bill is sponsored by four Senators.

The ultimate effect of the above legislation on the Corporation's business and results of operations will depend upon the enactment and final provisions of this legislation.

The 1985 budget report of the President of the United States includes the following statement: "The Administration remains committed to the total privatization of two housing-related, Government-sponsored enterprises—the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation. An interagency cabinet-level group will continue to pursue this goal. Because they are sponsored by the Federal government, these two enterprises receive special advantages in the securities markets that completely private institutions do not have." Similar statements were included in the 1983 and 1984 budget reports. Any alteration of the relationship of the Corporation to the federal government would require legislation to be introduced in and passed by both Houses of Congress and signed by the President. No such legislation has been introduced to date. Alteration or elimination of the Corporation's relationship with the federal government could require the Corporation to change the manner in which it currently conducts business and could have a material adverse effect on its results of operations. Except for the particular bills summarized above, the Corporation is unaware of any specific legislative proposals that would alter in any material way its current status.

MANAGEMENT

The senior officers of the Corporation, their ages as of July 1, 1984 and business experience are as follows:

David O. Maxwell, 54, has been Chairman of the Board of Directors and Chief Executive Officer since May 1981. He served briefly as the Corporation's President and Chief Operating Officer from February 1981 until his election to his present position. Prior to his employment with the Corporation, Mr. Maxwell was Chairman of the Board and Chief Executive Officer of Ticor Mortgage Insurance Company.

Robert J. Mylod, 44, has been President and Chief Operating Officer since January 1983. Prior to his employment with the Corporation, Mr. Mylod was President of Advance Mortgage Corporation.

Caryl S. Bernstein, 50, has been Executive Vice President since February 1982; Secretary since July 1981; and General Counsel since May 1981. Mrs. Bernstein was Senior Vice President from May 1981 until her election as Executive Vice President. Prior to her employment with the Corporation, Mrs. Bernstein held a number of positions with the Overseas Private Investment Corporation ("OPIC"), a U.S. government agency that encourages private investment in less developed countries and insures against certain risks involved in such overseas investments. Mrs. Bernstein's most recent title at OPIC was Vice President for Insurance.

Stuart A. McFarland, 37, became Executive Vice President and Chief Financial Officer on October 31, 1983. From November 1982 until October 31, 1983, Mr. McFarland was Executive Vice President and Chief Planning Officer. From May 1981 until November 1982, Mr. McFarland was the Corporation's Executive Vice President—Operations. Prior to his employment with the Corporation, Mr. McFarland held a number of positions with Ticor Mortgage Insurance Company, most recently that of President.

Michael A. Smilow, 46, became Executive Vice President—Operations, on July 16, 1984. Prior to his employment with the Corporation, Mr. Smilow was with MGIC Investment Corporation—Capital Markets and Commercial Markets Groups since 1980, where he held the position of Senior Vice President. From 1978 to 1980, Mr. Smilow was Deputy Director, Office of State Agency and Bond Financed Programs, Department of Housing and Urban Development.

Richard R. Betchley, 34, has been Senior Vice President—Marketing and Regional Activities since February 1982. Prior to his employment with the Corporation, Mr. Betchley was the Manager of the Southern California Bond & Money Market Headquarters for Crocker National Bank. Mr. Betchley held a number of general management positions with Crocker National Bank, where he was employed from December 1975 until January 1982.

Douglas M. Bibby, 37, became Senior Vice President for Corporate Affairs on October 18, 1983. Prior to his employment with the Corporation, Mr. Bibby was Vice President of Russell Reynolds Associates, Inc., an executive recruiting firm. Mr. Bibby was previously employed by the J. Walter Thompson Company for twelve years, where his last position was as Senior Vice President.

Richard H. Daniel, 37, became Senior Vice President—Regional Activities on June 19, 1984. From April 1984 until June 19, 1984, Mr. Daniel was Vice President—Regional Activities. Mr. Daniel was the Corporation's Vice President—Marketing from March 1983 until April 1984. Prior to his employment with the Corporation, Mr. Daniel was employed by Wells Fargo & Company, where he was Vice President and Manager of the real estate division of the retail banking group.

Stephen Frank, 44, became Senior Vice President and Controller on October 18, 1983. From June 1981 until October 18, 1983, Mr. Frank was Vice President and Controller. Mr. Frank has been employed in the Corporation's Office of the Controller since 1970.

F. G. Gosling, 58, has been Senior Vice President—Administration since February 1982. From 1973 until assuming his present position, Mr. Gosling was the Corporation's Vice President for Administration.

John P. Harding, 39, became Senior Vice President for Planning and Financial Analysis on October 18, 1983. From November 1981 until October 18, 1983, Mr. Harding was Vice President for Corporate Planning. Mr. Harding has been in the Corporation's Office of Corporate Planning since June 1975.

J. Timothy Howard, 35, became Senior Vice President and Chief Economist on October 18, 1983. Mr. Howard has been the Corporation's Chief Economist since March 1982. Prior to his employment with the Corporation, Mr. Howard was Vice President and Senior Financial Economist for Wells Fargo Bank.

J. Donald Klink, 47, has been Senior Vice President for Mortgage-Backed Securities since October 18, 1983. From June 15, 1982 until October 18, 1983, Mr. Klink was Senior Vice President for Mortgage Securities and Negotiated Transactions. Mr. Klink was the Corporation's Vice President for Mortgage Marketing from August 1981 until February 1982, when he was elected Vice President for Mortgage Securities and Negotiated Transactions. Prior to his employment with the Corporation, Mr. Klink was employed by Coast Federal Savings and Loan Association for seven years, where he held the position of Senior Vice President in charge of mortgage banking.

Robert J. Mahn, 56, has been Senior Vice President—Mortgage Operations since February 1982. Mr. Mahn was the Corporation's Vice President and Controller from April 1969 until June 1981, when he was elected Vice President—Mortgage Operations.

John J. Meehan, 39, has been Senior Vice President—Finance and Treasurer since February 1982. Mr. Meehan was the Corporation's Vice President—Finance and Treasurer from May 1981 until his election to his present position. Prior to that, Mr. Meehan was Vice President and Fiscal Agent. Mr. Meehan has been with the Corporation since 1975.

Dale P. Riordan, 35, became Senior Vice President for Government Relations on October 18, 1983. Since 1981, Mr. Riordan has held various managerial positions with the Corporation, most recently that of Vice President for Government Relations. Prior to his employment with the Corporation, Mr. Riordan was Chief Economist of the National Savings and Loan League.

BOARD OF DIRECTORS

The age and background, as of July 1, 1984, of each of the members of the Board of Directors of the Corporation, and certain persons who served as members of the Board from the dates shown until their terms expired on May 17, 1984 (see footnote 2 to the table below) are as follow:

<u>Name and Age</u>	<u>Principal Occupation and Business Experience</u>	<u>First Became Director</u>	<u>Other Directorships (1)</u>
Eli Broad—51	Chairman of the Board and Chief Executive Officer of Kaufman and Broad, Inc., a housing and financial services corporation, 1976 to present; President and Chief Executive Officer, Sun Life Insurance Company of America, 1983 to present; Chairman of the Board, Sun Life Group of America, Inc., a life insurance-holding company, 1978 to present; Chairman of the Board of Sun Life Insurance Company of America, 1975 to 1979	1984	
Merrill Butler(2)—59	President, Chief Executive Officer and Chairman of the Board, The Butler Group, Inc., a home building company, January 1984 to present; President and Chairman of the Board, Butler Housing Corporation, a home building company, 1971-1983; Chairman of the Board, Bullard Homes Corporation, a home building company, 1976 to present; President and Chairman of the Board, BHC Housing, Inc., a home building corporate subsidiary of Butler Housing Corporation, 1972 to present, President, National Association of Homebuilders, 1980	1981	Commodore Corporation
James B. Coles(2)—42....	President and Chairman of the Board, James B. Coles, Inc., a framing contractor, 1972 to present; The Coles Development Company, Inc., a home building company, 1979 to present; C&C SunWest Contractors, Inc., 1982 to present, Pacific SunWest Marketing, Inc., 1983 to present	1981	
Bert A. Getz(2)—47.	President and Director, Globe Corporation, a banking, real estate and investment company, 1975 to present	1981	Arizona Bancwest Corporation

<u>Name and Age</u>	<u>Principal Occupation and Business Experience</u>	<u>First Became Director</u>	<u>Other Directorships(1)</u>
Joseph P. Hayden—54	Chairman of the Board and Chief Executive Officer, The Midland Company and its subsidiaries, financing and insuring of manufactured housing, December 1980 to present; President and Chief Executive Officer, 1961 to December 1980	1969	The Midland Company; First National Cincinnati Corporation
Carla A. Hills—50	Partner, Latham, Watkins & Hills, a law firm practicing in Washington, D.C., Illinois and California, 1978 to present; Secretary, U. S. Department of Housing & Urban Development, 1975 to 1977	1982	American Airlines, Inc., Corning Glass Works; International Business Machines Corporation; The Signal Companies, Inc., Chevron Corporation
Dianne E. Ingels(2)—42	Partner, The York Companies, a real estate development, acquisition and marketing firm, January 1984 to present; Principal, Dianne Ingels and Associates, an independent real estate broker, investor and consultant, 1977 to present; President, Ingels Company, 1976 to 1977; Chairman, Colorado Springs Urban Renewal Commission, 1974 to 1976	1981	
John E. Krout—64	Chairman of the Board, Germantown Savings Bank, a mutual savings bank, 1977 to present; President, Germantown Savings Bank, 1971 to 1977	1970	Chicago Title & Trust Co.; Trustee, PNB Mortgage & Realty Investors
James E. Lyon(2)—56	Chairman of the Board, River Oaks Bancshares, Inc., a bank holding company, April 1, 1984 to present; Chairman of the Board, River Oaks Financial Corporation, 1962 to present; Chairman of the Board, Ruska Instrument Corporation, November 1961 to present	1981	

<u>Name and Age</u>	<u>Principal Occupation and Business Experience</u>	<u>First Became Director</u>	<u>Other Directorships(1)</u>
David O Maxwell—54 ...	Chairman of the Board of Directors and Chief Executive Officer of the Corporation, May 1981 to present; President and Chief Operating Officer, Federal National Mortgage Association, February to May 1981; Chairman of the Board and Chief Executive Officer, Tigor Mortgage Insurance Company, private mortgage insurance, February 1973 to February 1981	1981	
Robert J. Mylod—44	President and Chief Operating Officer of the Corporation, January 1983 to present, President of Advance Mortgage Corporation, 1975 to 1982; Executive Vice President, Advance Mortgage Corporation, 1973 to 1975	1983	
John M O'Mara—56	Senior Vice President, Wertheim & Co, a securities business, July 1981 to present; Vice President, Merrill Lynch White Weld Capital Markets Group, a securities business, 1978 to July 1981; First Vice President, White Weld & Co, Inc, 1974 to 1978	1970	Baldwin & Lyons, Inc.
Samuel J Simmons—57. ...	President, National Caucus and Center on Black Aged, Inc, January 1982 to present, Housing and real estate consultant, May 1981 to present, President, National Center for Housing Management, a non-profit research and training organization, 1972 to May 1981	1978	
Richard C Van Dusen—57	Executive Partner, Dickinson, Wright, Moon, Van Dusen & Freeman, a Detroit law firm, 1977 to present	1981	Pennwalt Corporation, Tigor Mortgage Insurance Company; Primark Corporation
Mallory Walker—45	President, Walker & Dunlop, Inc., a mortgage banking and real estate company, 1976 to present	1981	

(1) Companies with a class of securities registered pursuant to Section 12 of the Securities Exchange Act of 1934 or subject to the requirements of Section 15(d) of that Act or any company registered as an investment company under the Investment Company Act of 1940

(2) These persons served as directors appointed by the President of the United States until their terms expired, pursuant to the Charter Act, on May 17, 1984. The Corporation has been informed that the President of the United States intends to appoint these individuals as directors of the Corporation for the term ending on the date of the 1985 annual meeting of stockholders

ACCOUNTANTS

The financial statements of the Corporation included herein have been examined by Peat, Marwick, Mitchell & Co., independent certified public accountants, to the extent and for the periods indicated in their report thereon. Such financial statements have been included in reliance upon the report of Peat, Marwick, Mitchell & Co. and given upon the authority of that firm as experts in accounting and auditing

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors and Stockholders
Federal National Mortgage Association:

We have examined the balance sheets of Federal National Mortgage Association as of December 31, 1983 and 1982, and the related statements of operations and changes in financial position for each of the years in the three-year period ended December 31, 1983. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned financial statements present fairly the financial position of Federal National Mortgage Association at December 31, 1983 and 1982 and the results of its operations and the changes in its financial position for each of the years in the three-year period ended December 31, 1983, in conformity with generally accepted accounting principles applied on a consistent basis.

PEAT, MARWICK, MITCHELL & CO

Washington, D.C.
January 25, 1984

FEDERAL NATIONAL MORTGAGE ASSOCIATION

BALANCE SHEETS

Assets

	<u>December 31,</u>	
	<u>1983</u>	<u>1982</u>
	(Dollars in thousands)	
Mortgage portfolio, net	\$75,664,817	\$69,713,984
Cash	30,115	22,622
U.S. Government and Federal Agency securities at cost (market value of \$227.7 million in 1983 and \$631.7 million in 1982)	227,163	630,869
Federal funds	1,462,259	1,799,100
Accrued interest receivable	770,328	687,709
Federal income taxes refundable	152,601	330,505
Accounts receivable and other assets	202,660	61,861
Acquired property and foreclosure claims, less allowance for losses of \$10.0 million in 1983 (\$4.1 million in 1982)	347,035	168,961
Unamortized debenture issue costs	60,559	51,092
Total Assets	<u>\$78,917,537</u>	<u>\$73,466,703</u>

Liabilities and Stockholders' Equity

Liabilities:

Bonds, notes and debentures, net:

Due within one year	\$26,859,533	\$25,780,576
Due after one year	47,734,289	43,833,062
	74,593,822	69,613,638
Accrued interest payable	1,904,645	1,724,274
Mortgagors' escrow deposits, exclusive of approximately \$609.6 million held by servicers in 1983 (\$548.3 million in 1982)	271,440	266,231
Deferred Federal income taxes	568,200	488,194
Other liabilities	303,519	171,037
Total liabilities	<u>77,641,626</u>	<u>72,263,374</u>

Stockholders' Equity:

Common stock, \$6.25 stated value, no maximum authorization—66,038,701 shares issued (65,650,117 shares in 1982)	412,742	410,313
Additional paid-in capital	310,913	305,750
Retained earnings	554,151	489,161
	1,277,806	1,205,224
Less Treasury stock, at cost—208,926 shares	1,895	1,895
Total stockholders' equity	<u>1,275,911</u>	<u>1,203,329</u>
Total Liabilities and Stockholders' Equity	<u>\$78,917,537</u>	<u>\$73,466,703</u>

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION
STATEMENTS OF OPERATIONS

	Year Ended December 31,		
	1983	1982	1981
	(Dollars in thousands, except per share amounts)		
Interest income:			
Mortgage portfolio	\$7,921,758	\$6,806,975	\$5,596,791
Less servicing fees	<u>216,262</u>	<u>217,984</u>	<u>202,622</u>
	7,705,496	6,588,991	5,394,169
Marketable securities	<u>221,666</u>	<u>232,123</u>	<u>139,998</u>
Total interest income	7,927,162	6,821,114	5,534,167
Interest on borrowings and related costs	<u>7,988,663</u>	<u>7,327,570</u>	<u>5,997,097</u>
Interest margin	<u>(61,501)</u>	<u>(506,456)</u>	<u>(462,930)</u>
Other income:			
Commitment fees	151,225	263,913	112,561
Gain on sales of mortgages	90,688	44,405	152
Guaranty fees	54,318	16,124	326
Other	<u>32,622</u>	<u>20,617</u>	<u>11,883</u>
Total other income	328,853	345,059	124,922
Other expenses:			
Administrative	80,760	60,067	49,462
Provision for losses	<u>47,900</u>	<u>35,700</u>	<u>(27,600)</u>
Total other expenses	128,660	95,767	21,862
Income (loss) before Federal income taxes and extraordinary item	<u>138,692</u>	<u>(257,164)</u>	<u>(359,870)</u>
Provision for Federal income taxes:			
Currently refundable	(15,200)	(200,900)	(271,300)
Deferred	<u>78,400</u>	<u>77,500</u>	<u>101,800</u>
	63,200	(123,400)	(169,500)
Income (loss) before extraordinary item	75,492	(133,764)	(190,370)
Extraordinary item: gain on early retirement of debt	<u>—</u>	<u>28,899</u>	<u>—</u>
Net income (loss)	<u>\$ 75,492</u>	<u>\$ (104,865)</u>	<u>\$ (190,370)</u>
Per share:			
Earnings (loss) before extraordinary item:			
Primary	\$ 1.15	\$ (2.20)	\$ (3.22)
Fully diluted	1.13	(2.20)	(3.22)
Net earnings (loss):			
Primary	1.15	(1.72)	(3.22)
Fully diluted	1.13	(1.72)	(3.22)
Cash dividends.....	.16	.16	.40
Average number of shares outstanding, in thousands	65,646	60,927	59,109

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION
STATEMENTS OF CHANGES IN FINANCIAL POSITION

	Year Ended December 31,		
	1983	1982	1981
	(Dollars in thousands)		
Funds Provided:			
Income (loss) before extraordinary item	\$ 75,492	\$ (133,764)	\$ (190,370)
Items not (providing) using funds:			
Interest capitalized on graduated payment mortgages, net	(99,841)	(116,342)	(102,111)
Provision for deferred Federal income taxes, net	78,400	77,500	101,800
Provision for losses	47,900	35,700	(27,600)
Funds provided by (applied to) operations before extraordinary item	101,951	(136,906)	(218,281)
Extraordinary gain—No funds effect	—	—	—
Proceeds from issuance of debentures and bonds ...	19,733,939	20,743,135	10,236,006
Increase in short-term notes	213,817	2,342,988	714,575
Mortgage repayments, less discount amortized	5,735,250	1,224,576	1,052,168
Foreclosure claims collected	425,440	289,063	230,684
Sales of mortgages, excluding gains and losses	4,370,300	2,071,297	9,340
Net increase in stockholders' equity resulting from debt exchange and debenture conversions	7,592	103,552	5
Increase in accrued interest payable/receivable, net	21,852	138,727	39,815
Other items, net	195,802	94,412	(86,185)
Total funds provided	30,805,943	26,870,844	11,978,127
Funds Applied:			
Debentures and bonds retired	14,991,082	12,044,363	7,265,815
Mortgage purchases including refinancings, less discount	16,663,040	14,047,268	5,903,936
Mortgage refinancings	(125,627)	(617,033)	(630,490)
Dividends paid	10,502	9,709	23,643
Total funds applied	31,538,997	25,484,307	12,562,904
Increase (decrease) in cash and marketable securities ...	(733,054)	1,386,537	(584,777)
Cash and marketable securities, beginning of year	2,452,591	1,066,054	1,650,831
Cash and marketable securities, end of year	\$ 1,719,537	\$ 2,452,591	\$ 1,066,054

See Notes to Financial Statements

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS

STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The Corporation operates in the residential mortgage finance industry. Its accounting policies conform to generally accepted accounting principles. The following is a description of significant accounting policies and practices:

Mortgage Portfolio and Purchase Discount

Mortgages acquired for investment are carried at their unpaid principal balances less unamortized discount. Discount is recognized as income using an amortization method which produces a level yield over the estimated life of the related mortgages.

Allowance for Losses

In order to recognize losses which may be sustained due to defaults on conventional mortgages acquired for portfolio, the Corporation maintains an allowance for losses which is established by charges to income when the mortgages are purchased. In 1981, the Corporation reduced the allowance for losses by \$42.0 million and also reduced the rate at which provisions are made for estimated losses on conventional loans.

Risk Management

In 1982, the Corporation began taking positions in financial markets to hedge against fluctuations in interest rates which affect the cost of planned borrowings. Results of hedging activity are deferred and amortized to interest expense over the lives of the protected borrowings. There were no open positions at December 31, 1983.

Commitment Fees

Commitment fees are generally recognized as income upon the execution of the commitment contract. However, commitment fees that are considered to be an adjustment to the yield on the related mortgages purchased are deferred and recognized as income using an amortization method which produces a level yield over the estimated life of the related mortgages.

Income Taxes

Certain income and expense items are recognized in different periods for financial and income tax reporting purposes. Provisions for deferred income taxes are made for such timing differences. Investment tax credits are recognized as deductions from income tax expense in the year the related assets are purchased (flow-through method)

Earnings Per Share

Earnings per share are computed on the weighted average number of shares outstanding. Fully diluted earnings per share are computed on the assumption that all outstanding convertible capital debentures were converted at the beginning of the year, after increasing earnings for the related interest expense, net of Federal income taxes.

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

MORTGAGE PORTFOLIO, NET

The mortgage portfolio balances consist of the following components:

	December 31,	
	1983	1982
	(Dollars in millions)	
Home mortgages:		
First mortgages:		
Government insured or guaranteed:		
Whole loans	\$30,970	\$33,730
Participations	30	12
	31,000	33,742
Conventional fixed-rate:		
Whole loans	28,108	24,662
Participations	4,425	3,127
	32,533	27,789
Conventional adjustable rate:		
Whole loans	6,120	2,775
Participations	1,006	557
	7,126	3,332
Second mortgages:		
Whole loans	989	382
Participations	1,397	1,254
	2,386	1,636
Project mortgages:		
Government insured	5,148	5,284
Conventional	63	31
	5,211	5,315
Total unpaid principal balance	78,256	71,814
Less:		
Unamortized discount	2,474	1,972
Allowance for losses	117	128
	\$75,665	\$69,714

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

BONDS, NOTES AND DEBENTURES, NET

Bonds, notes and debentures consist of the following:

	December 31,	
	1983	1982
	(Dollars in millions)	
Due within one year:		
Short-term notes—net of \$293 million discount in 1983 (\$418 million in 1982)	\$10,833	\$11,334
Master notes	715	—
Debentures	15,289	14,434
Mortgage-backed bonds	23	13
Total due within one year	26,860	25,781
Due after one year:		
Debentures	45,794	41,825
Mortgage-backed bonds	402	464
Capital debentures—net of \$20 million discount in 1983 (\$21 million in 1982)	1,510	1,509
Convertible capital debentures	28	35
Total due after one year	47,734	43,833
	\$74,594	\$69,614

Short-term notes are general obligations of the Corporation. These notes are issued in both discount and interest-bearing form. Maturities range up to 360 days, and denominations range from \$5,000 to \$1,000,000 with a minimum original purchase of \$50,000. Master notes are individually negotiated, variable principal amount short-term notes. These notes, which have varying maturities, carry a floating interest rate tied to 91-day U.S. Treasury bill rates which is adjusted weekly. Investors have the option of increasing or decreasing the principal amount outstanding on these notes on a daily basis, usually within a range of 80 to 120 percent of the original principal balance. The Corporation had short-term and master notes outstanding of \$11.8 billion (face amount) at December 31, 1983 and December 31, 1982. The largest amount of notes outstanding at any month-end was \$11.8 billion in 1983, in 1982, \$11.9 billion. The average cost to the Corporation of notes outstanding at December 31, 1983 and 1982 was 9.7 percent and 10.5 percent, respectively. These rates represent the effective average cost computed on a 365-day basis, including commission and the effect of related hedging activity. The average remaining terms were approximately 106 and 141 days at December 31, 1983 and 1982, respectively. The average aggregate amount of notes outstanding during 1983 was \$10.1 billion at an average cost of 9.67 percent; during 1982, it was \$9.0 billion at an average cost of 13.27 percent.

The Corporation has a \$322 million line of credit with a group of commercial banks. The total amount is available to the Corporation on the same day. Interest on any borrowings is calculated at the prime rate used by Continental Bank. The credit agreement is terminable by either party on the anniversary date with 45 days prior written notice.

Section 304(c) of the Federal National Mortgage Association Charter Act authorizes the Secretary of the Treasury, as a public debt transaction, to purchase obligations of the Corporation up to a maximum of \$2.25 billion outstanding at any one time. The interest rate on such obligations is to be based upon the average rate on outstanding marketable obligations of the United States as of the last day of the month preceding the date of making such purchases.

The Corporation did not utilize the commercial line of credit or the Treasury borrowing authority in 1983 or 1982.

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

A summary of bonds and debentures due after one year follows:

(Dollars in millions)	December 31,			
	1983		1982	
	<u>Weighted Average Interest Rates</u>	<u>Amount Outstanding</u>	<u>Weighted Average Interest Rates</u>	<u>Amount Outstanding</u>
<u>Maturity</u>				
Debentures:				
1984	—%	\$ —	11.53%	\$12,225
1985	12.37	12,600	12.42	12,350
1986	11.46	10,850	11.72	7,600
1987	11.16	10,650	11.59	5,150
1988	11.00	6,345	11.55	2,100
1989-1993	10.26	4,945	9.61	2,246
1994-1998	7.10	154	7.10	154
2013	12.35	250	—	—
	11.44	45,794	11.72	41,825
Mortgage-backed Bonds:				
1984	—	—	7.30	24
1985	6.70	34	6.76	34
1986	6.39	76	6.33	77
1987	9.01	12	9.08	13
1988	9.01	12	9.11	13
1989-1993	8.70	243	8.77	251
1994-1998	9.58	17	10.91	28
1999-2002	12.05	8	12.84	24
	8.22	402	8.50	464
Capital Debentures:				
1985	11.70	500	11.70	500
1986	8.15	300	8.15	300
1989	15.25	200	15.25	200
1997	7.40	250	7.40	250
2002	8.20	280	8.20	280
		1,530		1,530
Less Discount		(20)		(21)
	10.12	1,510	10.12	1,509
Convertible Capital Debentures:				
1996	4.38	28	4.38	35
Total	11.36%	\$47,734	11.62%	\$43,833

The convertible capital debentures are convertible into 1.4 million shares of common stock at a price of \$19.63 per share, subject to adjustment in certain events. Such debentures are redeemable, at the option of the Corporation, at par.

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

The 12.35 percent debentures, due in 2013, are redeemable at par, in whole or in part, at the option of the Corporation, on any interest payment date commencing December 10, 1993.

The 7.40 percent and 8.20 percent capital debentures, due in 1997 and 2002, are redeemable at par, in whole or in part, at the option of the Corporation, on any interest payment date commencing October 1, 1982 and July 10, 1988, respectively.

Pursuant to the Corporation's Charter Act and related regulations, approval of the Secretary of Housing and Urban Development is required prior to a change in the stockholding requirements for lenders or the issuance of any stock of the Corporation. In addition, no debt instrument may be issued without the approval of the Secretary of the Treasury. The maximum amount of the Corporation's general obligations (those neither subordinated nor secured) outstanding at any one time may not exceed 30 times the sum of its stockholders' equity and outstanding subordinated obligations. Subordinated obligations include the capital debentures and the convertible capital debentures. The secured obligations, mortgage-backed bonds, of which \$425 million were outstanding at December 31, 1983 and \$477 million at December 31, 1982, were issued pursuant to authority contained in the Charter Act to issue and sell securities based upon mortgages set aside from the Corporation's portfolio. There is no limitation on the amount of such obligations that may be outstanding. Under the provisions of a Trust Indenture entered into as of May 15, 1970 with Government National Mortgage Association (GNMA), as amended, \$416 million of the mortgage-backed bonds outstanding at December 31, 1983 and \$428 million of the mortgage-backed bonds outstanding at December 31, 1982 are guaranteed as to principal and interest by GNMA. Trust assets of approximately \$898 million at December 31, 1983 and \$867 million at December 31, 1982, consisting of the aggregate unpaid principal balances of specified mortgages, and U.S. government and Federal Agency securities, are restricted for the payment of principal and interest on the mortgage-backed bonds and are included in the accompanying balance sheets. Interest earned on trust assets exceeds bond interest requirements.

Annual maturities of all debt for the years 1985-1989 are \$13.1, \$11.2, \$10.7, \$6.4 and \$1.4 billion, respectively.

STOCKHOLDERS' EQUITY

Transactions in common stock, additional paid-in capital, retained earnings, and treasury stock accounts for the years 1981, 1982 and 1983 are summarized as follows:

	<u>Common Stock</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Treasury Stock</u>	<u>Total Stockholders' Equity</u>
	(Dollars in Thousands)				
Balance, January 1, 1981	\$370,735	\$270,670	\$817,748	\$(1,895)	\$1,457,258
Conversion of convertible debentures.....	2	3	—	—	5
Net loss.....	—	—	(190,370)	—	(190,370)
Dividends.....	—	—	(23,643)	—	(23,643)
Balance, December 31, 1981	370,737	270,673	603,735	(1,895)	1,243,250
Conversion of convertible debentures.....	259	565	—	—	824
Shares issued in exchange for outstanding debentures.....	39,317	34,512	—	—	73,829
Net loss.....	—	—	(104,865)	—	(104,865)
Dividends.....	—	—	(9,709)	—	(9,709)
Balance, December 31, 1982	410,313	305,750	489,161	(1,895)	1,203,329
Conversion of convertible debentures	2,429	5,163	—	—	7,592
Net income.....	—	—	75,492	—	75,492
Dividends.....	—	—	(10,502)	—	(10,502)
Balance, December 31, 1983	<u>\$412,742</u>	<u>\$310,913</u>	<u>\$554,151</u>	<u>\$(1,895)</u>	<u>\$1,275,911</u>

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

In 1982, the Corporation adopted a performance share plan that makes awards to officers for three four-year periods starting in 1982, 1983 and 1984, provided certain financial goals are attained. Generally, contingent shares will be issued, if earned, half in cash and half in stock, but no more than 200,000 shares of common stock will be distributed under the plan. Accordingly, as of December 31, 1983, 175,000 contingent performance shares are outstanding for the 1982-85 period, and 64,200 for the 1983-86 period.

In September 1982, the Corporation entered into a nontaxable transaction which resulted in the issuance of 6.3 million shares of its common stock in exchange for \$101 million of its long-term debentures, which were retired. Had this transaction and all conversions of convertible debentures during the year taken place on January 1, 1982, the net loss per share for 1982 would have been \$1.56 (\$2.00 before extraordinary item), compared with a loss of \$1.72 per share (\$2.20 before extraordinary item) as reported in the Statements of Operations.

INCOME TAXES

Deferred Federal income tax expense relating to timing differences consists of the following:

	<u>1983</u>	<u>1982</u>	<u>1981</u>
	(Dollars in millions)		
Amortization of purchase discount	\$52.9	\$71.3	\$ 48.9
Losses on dispositions of mortgages	44.5	(3.9)	35.9
Provision for losses—conventional mortgages	(7.9)	0.8	19.7
Risk management activities	(9.4)	6.3	—
Other items, net	<u>(1.7)</u>	<u>3.0</u>	<u>(2.7)</u>
Total deferred Federal income tax expense	<u>\$78.4</u>	<u>\$77.5</u>	<u>\$101.8</u>

The Internal Revenue Service has completed its examinations of the Corporation's Federal income tax returns for the years 1979-1982, and has proposed certain adjustments. The Corporation has filed a protest contesting these adjustments, and has filed a claim for refund for \$124.9 million relating to losses on sales of participation interests in mortgages. In addition, the Corporation plans to file amended returns for 1981 and 1982 to claim losses sustained on mortgages exchanged pursuant to the Corporation's resale/refinance program. Such amended returns will result in a claim for refund of an additional \$15.2 million for losses carried back to 1979. Losses claimed in excess of the amount carried back are sufficient to offset all 1983 taxable income. Remaining losses would be carried forward to reduce future taxable income.

All disputed amounts relate to items for which deferred taxes have been provided. It is management's opinion that any unfavorable determinations would have no material adverse impact on the results of operations.

The Corporation is exempt from state and local taxes, with the exception of real estate taxes.

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

RETIREMENT PLANS

All permanent, full-time employees of the Corporation are covered by the non-contributory Federal National Mortgage Association Retirement Plan or the contributory Civil Service Retirement Law. Pension expenses for these plans were \$.6 million and \$.2 million, respectively, for the year ended December 31, 1983 (\$.8 million and \$.2 million in 1982, and \$2.5 million and \$.3 million in 1981). The Corporation makes annual contributions to the plans equal to the amounts accrued for pension expense, which includes, as to the Corporation's defined benefit pension plan, amortization over 10 years of unfunded past service costs. Accumulated plan benefits, total actuarial liabilities and plan assets for the Corporation's defined benefit pension plan at January 1 are presented below:

	<u>1983</u>	<u>1982</u>
	(Dollars in millions)	
Actuarial present value of accumulated plan benefits:		
Vested	\$ 5.8	\$ 4.1
Nonvested	<u>1.7</u>	<u>1.8</u>
Total accumulated benefits	<u>\$ 7.5</u>	<u>\$ 5.9</u>
Total actuarial liability	<u>\$19.4</u>	<u>\$16.7</u>
Net assets available for benefits	<u>\$28.4</u>	<u>\$23.1</u>

The annual rate of return and the actuarial present value rate for determining accumulated plan benefits were 7.5 percent in 1983 and 1982. The rates were changed to 7.5 percent in 1982 from 6.0 percent in 1981. The changes had the effect of reducing the annual pension expense for 1982 by \$1.6 million.

COMMITMENTS AND CONTINGENCIES

Portfolio

The Corporation had outstanding at December 31, 1983 mandatory delivery commitments for the purchase of \$1.7 billion of mortgages at an average net yield of 12.36 percent compared with \$3.3 billion at 12.85 percent at December 31, 1982.

The Corporation also issues standby commitments, which must be converted to mandatory delivery commitments in order for the seller to deliver mortgages. The yield is set on the date of conversion. The Corporation had \$3.7 billion of such commitments outstanding at December 31, 1983, compared with \$3.9 billion at December 31, 1982.

Further, the Corporation issues certain commitments under which delivery is optional at the discretion of the seller, and the yield is set on the date of the commitment. The Corporation had \$0.1 billion of such commitments at an average net yield of 12.29 percent outstanding at December 31, 1983, compared with \$0.4 billion (including \$0.1 billion relating to mortgages to be refinanced) at 13.43 percent at December 31, 1982.

Mortgage-Backed Securities

The Corporation packages pools of mortgages in pass-through securities (Federal National Mortgage Association Mortgage-Backed Certificates) and guarantees the payment of principal and interest. The outstanding principal balance of the pools was \$25.1 billion at December 31, 1983 compared with \$14.5 billion at December 31, 1982. These securities represent interests primarily in fixed-rate mortgages held in trust by the Corporation. The pools of mortgages are not assets of the Corporation, nor are the

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

outstanding securities liabilities of the Corporation. The Corporation as issuer and guarantor of the mortgage-backed securities is obligated to disburse scheduled monthly installments of principal and interest, whether or not such amounts have actually been received, unscheduled principal payments when received, and the full principal balance upon liquidation of any foreclosed mortgage whether or not such principal balance is recovered. Either the Corporation or the participating lender from whom the mortgages were acquired can assume the foreclosure loss risk on the mortgages in a pool. The Corporation establishes by charges to income a liability for estimated foreclosure losses for the securities on which the Corporation has assumed the risk of loss. The outstanding principal balance of mortgage-backed securities on which the Corporation has the foreclosure loss risk was \$7.2 billion at December 31, 1983 compared with \$3.1 billion at December 31, 1982. The amount of the related liability for estimated foreclosure losses was \$15.6 million at December 31, 1983 and \$4.7 million at December 31, 1982.

At December 31, 1983, the Corporation had commitments outstanding to issue and guarantee \$1.6 billion of mortgage-backed securities when the related mortgages are delivered by participating lenders at their option, compared with \$2.2 billion at December 31, 1982. At December 31, 1982 the Corporation also had \$0.1 billion in outstanding mandatory delivery commitments to issue guaranteed mortgage-backed securities. There were no such commitments outstanding at December 31, 1983.

UNAUDITED INTERIM PERIOD RESULTS OF OPERATIONS

The following unaudited results of operations include, in the opinion of management, all adjustments (consisting only of normal recurring accruals) necessary for a fair statement of the results of operations for such periods.

	1983 Quarter Ended			
	December	September	June	March
	(Dollars in thousands, except per share amounts)			
Interest margin	\$ (1,386)	\$ (18,730)	\$ (11,974)	\$ (29,411)
Commitment fees	23,890	44,680	42,862	39,793
Gain on sales of mortgages	13,476	28,454	18,445	30,313
Guaranty fees	16,125	14,585	13,003	10,605
Other income	8,000	9,656	8,657	6,309
Other expenses	(35,994)	(32,792)	(30,197)	(29,677)
Income before Federal income taxes	24,111	45,853	40,796	27,932
Federal income taxes	10,500	21,000	18,800	12,900
Net income	<u>\$ 13,611</u>	<u>\$ 24,853</u>	<u>\$ 21,996</u>	<u>\$ 15,032</u>
Per share:				
Net earnings:				
Primary(a)	\$.21	\$.38	\$.34	\$.23
Fully diluted .....	.20	.37	.34	.22
Cash dividends .....	.04	.04	.04	.04

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Continued

	1982 Quarter Ended			
	December	September	June	March
	(Dollars in thousands, except per share amounts)			
Interest margin	\$(77,464)	\$(144,514)	\$(147,454)	\$(137,024)
Commitment fees	57,070	56,845	80,333	69,665
Gain on sales of mortgages	18,259	22,943	2,398	805
Guaranty fees	7,613	4,624	2,611	1,276
Other income	5,539	6,950	4,400	3,728
Other expenses	(31,083)	(24,771)	(22,233)	(17,680)
Loss before Federal income taxes and extraordinary item	(20,066)	(77,923)	(79,945)	(79,230)
Federal income taxes	(14,400)(b)	(35,800)	(36,800)	(36,400)
Loss before extraordinary item	(5,666)	(42,123)	(43,145)	(42,830)
Extraordinary item: Gain on early retirement of debt	—	28,899(c)	—	—
Net loss	<u>\$ (5,666)</u>	<u>\$ (13,224)</u>	<u>\$ (43,145)</u>	<u>\$ (42,830)</u>
Per share:				
Loss before extraordinary item(a)	\$ (.09)	\$ (.71)	\$ (.73)	\$ (.72)
Net loss(a)	(.09)	(.22)	(.73)	(.72)
Cash dividends .....	.04	.04	.04	.04

(a) The total of the four quarters does not equal the amount for the year since the amount for each period is independently calculated based on the weighted average number of shares outstanding during that period. In 1982, there were no differences between primary and fully diluted loss per share.

(b) Federal legislation that alters the Corporation's tax status to give it a tax loss carryback and carryforward treatment for operating losses comparable to that of other financial institutions (10-year carryback and 5-year carryforward) was enacted in October 1982. This legislation gives the Corporation access to refunds not otherwise available. Federal income taxes recorded in the fourth quarter of 1982 include an appropriate adjustment for this change in circumstances.

(c) In September 1982, the Corporation entered into a nontaxable transaction which resulted in the issuance of 6.3 million shares of its common stock in exchange for \$101 million of its long-term debentures, which were retired.

UNAUDITED FINANCIAL DATA ADJUSTED FOR EFFECTS OF CHANGING PRICES

The Corporation is subject to a requirement, promulgated by the Financial Accounting Standards Board (FASB), that it provide supplementary financial information which is intended to disclose the impact of changing prices (inflation) on its financial condition and the results of operations. As a financial institution, the Corporation does not maintain inventories or significant amounts of plant and equipment. Accordingly, the adjustments to income required by the statement are not material and need not be reported.

The FASB statement provides that the impact of inflation on the Corporation's financial condition be shown by reporting the loss from decline in purchasing power of its net monetary assets. For the Corporation, the definition of net monetary assets includes virtually all assets and liabilities of the Corporation. Net monetary assets are, therefore, approximately equivalent to stockholders' equity. The loss from decline in purchasing power is required to be measured by restating net monetary assets in constant dollars using the Consumer Price Index for All Urban Consumers.

FEDERAL NATIONAL MORTGAGE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS—Concluded

In accordance with the FASB statement, an unaudited five-year comparison of the impact of changing prices on certain financial data is shown below:

Financial Data Adjusted for Effects of Changing Prices

	<u>1983</u>	<u>1982</u>	<u>1981</u>	<u>1980</u>	<u>1979</u>
	(Dollars in millions, except per share amounts)				
Interest margin:					
As reported	\$ (62)	\$ (506)	\$ (463)	\$ 21	\$ 322
In constant dollars(1)	(62)	(523)	(507)	25	442
Net income (loss):					
As reported	75	(105)	(190)	14	162
In constant dollars(1)	75	(108)	(209)	17	222
Net monetary assets at end of year:					
As reported	1,233	1,164	1,204	1,419	1,461
In constant dollars(1)	1,207	1,184	1,272	1,636	1,892
Loss in purchasing power for the year of average net monetary assets	46	46	129	204	239
Per share:					
Fully diluted earnings(loss):					
As reported	1.13	(1.72)	(3.22)	.23	2.68
In constant dollars(1)	1.13	(1.78)	(3.53)	.28	3.68
Cash dividends:					
As reported .....	.16	.16	.40	1.12	1.28
In constant dollars(1) .....	.16	.17	.44	1.35	1.76
Year-end market price:					
As reported	23.00	24.50	8.50	11.88	16.13
In constant dollars(1)	22.52	24.93	8.98	13.70	20.88
Average consumer price index	298.5	289.1	272.4	246.8	217.4

(1) Constant dollars are computed by reference to the Consumer Price Index for All Urban Consumers and are expressed in average 1983 dollars